Company Number 05375156

VERONA PHARMA plc

ANNUAL REPORT AND ACCOUNTS

YEAR ENDED DECEMBER 31, 2019

VERONA PHARMA PLC
CONTENTS

Directors	David Ebsworth (Non-Executive Chairman) David Zaccardelli (Chief Executive Officer) (appointed February 1, 2020) Ken Cunningham Martin Edwards (appointed April 1, 2019) Rishi Gupta Mahendra Shah Andrew Sinclair Vikas Sinha Anders Ullman
Company Secretary	Ben Harber
Registered Office	One Central Square Cardiff CF10 1FS
Company Number	05375156
Auditors	PricewaterhouseCoopers LLP 3 Forbury Place 23 Forbury Road Reading Berkshire, RG1 3JH
Nominated Adviser and Broker	N+1 Singer One Bartholomew Lane London, EC2N 2AX
Solicitors	Latham & Watkins LLP 99 Bishopsgate London EC2M 3XF
Principal Banker	Lloyds Bank plc 33 Old Broad Street London, EC2N 1HZ
Registrars	Computershare Investor Services plc The Pavilions Bridgewater Road Bristol BS99 6ZZ

Verona Pharma is a clinical-stage biopharmaceutical company focused on developing and commercializing innovative therapies for the treatment of respiratory diseases. The company's first-in-class development candidate, ensifentrine, is an inhaled, dual inhibitor of the enzymes phosphodiesterase 3 and 4 that has been shown to act both as a bronchodilator and anti-inflammatory agent in a single compound. Verona Pharma has recently reported positive top-line Phase 2b clinical data with nebulized ensifentrine for the maintenance treatment of COPD and is plathe nning to enter Phase 3 clinical trials for this indication in the third quarter of 2020, subject to FDA feedback and to funding. Dry powder inhaler and pressurized metered-dose inhaler formulations of ensifentrine are in Phase 2 clinical trials. Verona Pharma is considering developing ensifentrine for the treatment of cystic fibrosis and asthma.

OPERATIONAL AND DEVELOPMENT HIGHLIGHTS

Solid clinical progress with ensifentrine, demonstrating efficacy and tolerability in COPD.

Nebulizer formulation:

In January 2020 the Company reported positive top-line data from a Phase 2b clinical study in symptomatic patients with moderate to severe COPD. The study met the primary endpoint at all doses, as well as meeting clinically relevant secondary endpoints:

- The 4 week, 416 patient, Phase 2b dose-ranging study evaluated nebulized ensifentrine (0.375 mg, 0.75 mg, 1.5 mg and 3.0 mg) or placebo as an add-on treatment to tiotropium (Spiriva® Respimat®), a long acting anti-muscarinic ("LAMA").
- The primary endpoint of improved lung function as measured by increase in morning peak forced expiratory volume in one second (FEV_1)[1] at week 4 was met at all doses. Statistically significant and clinically meaningful improvements ranged from 78 mL for the 0.375 mg dose (p=0.0368) to 124 mL for the 3.0 mg dose (p=0.0008). Effects were maintained over 4 weeks.
- Dose-dependent improvements in lung function were observed on both peak forced expiratory volume in one second (FEV_1)[1] and $FEV_{1\ AUC\ 0\text{-}12\ hours}$[2].
- Statistically significant improvement in average $FEV_{1\ AUC\ 0\text{-}12\ hours}$ of 87 mL for the 3.0 mg dose (p=0.0111) is supportive of twice daily dosing.
- Clinically meaningful improvements in health-related quality of life (mean SGRQ-C[3]) were observed when added to tiotropium treatment, exceeding the minimal clinically important difference ("MCID") of 4 units compared to placebo at week 4, with the two highest doses also achieving statistical significance.
- Ensifentrine was well tolerated at all doses with an adverse event profile similar to placebo.
- These data provide support for dose selection in Phase 3 trials.

In January 2019, the Company reported top-line data from an exploratory Phase 2a clinical trial in patients with moderate to severe COPD. While the study did not meet the primary endpoint of an increase in morning peak FEV_1, ensifentrine did produce additional bronchodilation when added to an inhaled long acting anti-muscarinic antagonist/long acting beta2 agonist ("LAMA/LABA") therapy.

- The three-day, 79 patient, Phase 2a trial, evaluated nebulized ensifentrine (1.5 mg or 6.0 mg) or placebo as an add-on treatment to tiotropium/olodaterol (Spiriva® Respimat®), a LAMA/LABA therapy.
- The primary endpoint of statistically significant improvement in peak FEV_1 (over 4 hours) on day 3 of treatment was not met, although the morning dose of ensifentrine 1.5 mg improved peak FEV_1 by 46 mL, compared to placebo.
- In a post hoc analysis, greater lung function improvements were observed in patients less responsive to existing dual bronchodilator therapy. More than 40% of patients observed improved morning peak FEV_1 by >100 mL.

- Statistically significant improvements in evening peak FEV_1 after the evening dose of ensifentrine were observed with both the 1.5 mg and 6 mg dose groups, with ensifentrine 1.5 mg showing a 130 mL improvement ($p<0.001$) and ensifentrine 6.0 mg showing an 81 mL improvement ($p=0.002$), compared to placebo.

Inhaler formulations:

In 2019 positive Phase 2 clinical data with a dry powder inhaler ("DPI") formulation for the maintenance treatment of COPD met all primary and secondary lung function endpoints.

- The two-part, 35 patient, Phase 2 trial evaluated DPI ensifentrine compared to placebo. In Part A, patients received a single dose of ensifentrine (150 μg[4], 500 μg, 1500 μg, 3000 μg, or 6000 μg) or placebo. In Part B, patients were randomized to receive one of four dose levels (150 μg, 500 μg, 1500 μg, or 3000 μg) of ensifentrine or placebo, administered twice daily over one week.
- The primary endpoint of improvement in peak bronchodilator effect of repeat doses of ensifentrine, as measured by FEV_1, was met. Peak FEV_1 corrected for placebo demonstrated improvements over baseline of 102 mL for the 150 μg dose, 175 mL for the 500 μg dose, 180 mL for the 1500 μg dose and 260 mL for the 3000 μg dose, ($p<0.0001$ for all doses), all highly statistically significant.
- Statistically significant improvements in average FEV_1 over 12 hours (average FEV_1 $AUC_{(0\text{-}12hr)}$) corrected for placebo were observed over 7 days with all doses : 36 mL for the 150 μg dose, 90 mL for the 500 μg dose, 80 mL for the 1500 μg dose and 147 mL for the 3000 μg dose ($p<0.05$ for all doses).
- Ensifentrine in a handheld dry powder format was well tolerated at all doses with an adverse event profile similar to placebo. The safety profile was comparable to that observed in clinical studies with nebulized ensifentrine.

We have initiated a Phase 2 clinical trial with a pMDI formulation of ensifentrine. Single dose data are expected early in the second quarter of 2020, and multiple dose data are expected in the second half of 2020.

ORGANISATION

Major organization changes:

Dr. David Zaccardelli, Pharm. D., appointed President and Chief Executive Officer, and Mark W. Hahn appointed Chief Financial Officer, following the end of the period.

Strengthened the management team through the additions of Kathleen Rickard, MD, as Chief Medical Officer, and Tara Rheault, PhD, MPH, as Vice President of Research and Development Operations and Global Project Management. Expanded the clinical team through the addition of senior experts with many years of experience in late-stage clinical development of COPD therapies.

KEY PRESENTATIONS

Scientific presentations and Investor/Analyst R&D forums.

- Oral and poster presentations on the development of ensifentrine for COPD maintenance treatment at major scientific meetings, including the American Thoracic Society 2019 International Conference, the European Respiratory Society International Congress 2019, and CHEST Annual Meeting 2019.
- Investor and Analyst R&D Forums in London and New York, featuring COPD Key Opinion Leaders, as well as a COPD patient from the British Lung Foundation, providing insight into the unmet medical need, challenges of treating COPD and the requirement for a novel mechanism of action such as ensifentrine.
- Published overview of clinical milestones for a candidate COPD treatment in MedNous, the medical research publication.
- Published full results from an ensifentrine Phase 2 clinical study in asthma in Pulmonary Pharmacology & Therapeutics.

[1]FEV_1: Forced Expiratory Volume in one second, a standard measure of lung function

[2]FEV_1 $AUC_{(0\text{-}12hr)}$: Area Under the Curve 0-12 hours calculated using the trapezoidal rule, divided by the observation time (12 hours) to report in mL, a measure of the aggregate effect over 12 hours

[3]SGRQ-C: St. George's Respiratory Questionnaire is a validated instrument that measures impact on overall health, daily life, and perceived well-being in patients with COPD (i.e. change in frequency and severity of COPD symptoms, and impact on activities, social functioning and psychological disturbances related to airways disease).

[4]µg: microgram, or mcg

FINANCIAL HIGHLIGHTS

- Cash, cash equivalents and short-term investments at December 31, 2019 amounted to £30.8 million (December 31, 2018: £64.7 million);
- For the year ended December 31, 2019, reported operating loss of £41.1 million (full year 2018: £25.6 million) and reported loss after tax of £31.9 million (full year 2018: loss after tax of £19.9 million), reflecting the preparation and initiation of clinical trials and pre-clinical activities;
- Reported loss per share of 30.3 pence for the year ended December 31, 2019 (full year 2018: loss per share 18.9 pence);
- Net cash used in operating activities for the year ended December 31, 2019 of £33.8 million (full year 2018: £18.1 million).

CHAIRMAN AND CHIEF EXECUTIVE OFFICER'S JOINT STATEMENT

OVERVIEW

Verona Pharma is a clinical-stage biopharmaceutical company developing life enhancing treatments for respiratory diseases with significant unmet medical needs. We are focused on the development of our first-in-class inhaled candidate, ensifentrine, for the treatment of chronic obstructive pulmonary disease (COPD). Ensifentrine has a unique dual mode of action. It acts as a bronchodilator and an anti-inflammatory in the same molecule. We are in Phase 2 development with three formulations of ensifentrine for COPD: nebulized, dry powder inhaler (DPI) and pressurized metered-dose inhaler (MDI).

During the year and post year-end, we made significant clinical progress, reporting positive Phase 2 clinical data from trials with nebulized and DPI formulations. In addition, we expanded our understanding of the market opportunities, retaining our focus on the US as the initial market for nebulized ensifentrine.

OUTLOOK AND STRATEGY

We intend to become a leading biopharmaceutical company focused on the treatment of respiratory diseases with significant unmet medical needs. Our key 2020 goals are:

- Rapidly advance the development of nebulized ensifentrine for the maintenance treatment of COPD in moderate and severe patients.
- Raise funding to advance the development of ensifentrine and supporting business activities
- Agree an End of Phase 2 meeting with the FDA to provide guidance on the design of the Phase 3 program with nebulized ensifentrine
- Start our Phase 3 program with nebulized ensifentrine in moderate to severe COPD patients
- Report results from a Phase 2 trial with a pressured metered dose inhaler (MDI) formulation of ensifentrine for the treatment of COPD
- Longer term we aim to develop ensifentrine for acute exacerbations of COPD as well as additional respiratory indications such as CF and severe asthma, and to seek strategic collaborations with market leading biopharmaceutical companies.

We would like to thank the staff and Board members for all their contributions and shareholders for their continued support during a successful year.

Significant progress in development and identification of compelling market opportunities

We are initially developing ensifentrine as a nebulized formulation for the maintenance treatment of uncontrolled, symptomatic, moderate to severe COPD patients. Our market research shows that nebulized delivery is the preferred route of administration for more severe COPD patients, especially in the US. The regulatory pathway for the development of nebulized drug products is well-established.

COPD is a progressive respiratory disease with no cure. Our market research demonstrates that, in the US alone, approximately two million patients remain uncontrolled and symptomatic despite taking currently available medications. Few therapeutic alternatives are available for these patients.

Ensifentrine is potentially a treatment alternative for these symptomatic COPD patients. The past year has seen significant clinical progress with the successful completion in January 2020 of our second four-week Phase 2b clinical trial with nebulized ensifentrine in over 400 patients with COPD. In this trial ensifentrine demonstrated statistically and clinically meaningful improvements in lung function when dosed on top of tiotropium, a LAMA which is a mainstay of current COPD chronic maintenance therapy.

Ensifentrine produced both a clinically meaningful bronchodilator effect and a progressive improvement in symptoms, suggesting an anti-inflammatory effect in these COPD patients. A further exploratory Phase 2 study that reported in January 2019 demonstrated that ensifentrine provides additional bronchodilation when added on top of what was formerly presumed to be maximum bronchodilator treatment with dual or triple COPD standard-of-care treatment.

In our clinical program, which has enrolled over 1,300 human subjects, we have demonstrated that ensifentrine is an effective bronchodilator in COPD patients with or without concurrent bronchodilator therapy. In addition, many Key Opinion Leaders in the field of COPD support our view that the progressive improvement in COPD symptoms observed over a four-week treatment period with ensifentrine is due to an anti-inflammatory effect, attesting to its dual activity.

We believe that nebulized ensifentrine could potentially be used to treat symptomatic COPD patients who already take either a single bronchodilator or dual or triple therapy. This is an attractive market opportunity estimated to be about 3 million patients in the US alone.

The successful development of DPI and MDI formulations of ensifentrine and the completion last year of the DPI Phase 2 clinical trial in COPD patients are further important development milestones. In August 2019, we announced positive results from our Phase 2 clinical trial evaluating a DPI formulation of ensifentrine for the maintenance treatment of patients with COPD. The magnitude of improvement in lung function, as measured by FEV1, was highly statistically significant and we believe this supports twice daily dosing of ensifentrine for COPD treatment.

In June 2019, we announced the initiation of a Phase 2 trial to evaluate a pressurized MDI formulation of ensifentrine in patients with moderate-to-severe COPD. We anticipate reporting data from the single-dose portion of this trial (Part A) early in the second quarter of 2020, and reporting results from the second portion of the trial (Part B), which evaluates multiple doses of the MDI formulation of ensifentrine, in the second half of 2020.

In the US, our market research shows that about 5.5 million moderate to severe COPD patients currently use these types of devices. We expect that developing DPI and MDI formulations would open up another attractive market opportunity. We anticipate that we would partner the DPI/MDI formulations later in development in order to realize the potential of this multi-billion dollar opportunity.

In addition to COPD, we believe ensifentrine could become an attractive development candidate in cystic fibrosis and severe asthma.

Senior executive changes bring substantial leadership, operational and clinical expertise

With effect from February 1, 2020, Verona Pharma appointed Dr. David Zaccardelli as President and Chief Executive Officer (CEO) and executive director. He succeeded Dr. Jan-Anders Karlsson following his retirement after 8 years of dedicated service to the Company. Dr. Zaccardelli brings substantial specialty pharmaceutical leadership and operational expertise, including most notably, serving as President and CEO of Dova Pharmaceuticals, Inc. until its acquisition by Swedish Orphan Biovitrum AB (Sobi) in November 2019. Previously, Dr. Zaccardelli held several senior management roles including Chief Operating Officer at United Therapeutics Corporation.

We have also appointed Mark Hahn, a seasoned pharmaceutical finance executive, as Chief Financial Officer (CFO), with effect from March 1, 2020. Mr. Hahn previously served as the CFO of Dova Pharmaceuticals, Inc. and Cempra, Inc. and raised over $600 million to support product development and commercialization activities

of those companies. Mr. Piers Morgan will continue to serve as CFO of Verona Pharma through February 28, 2020 to ensure a smooth transition and continue support on financial reporting, before leaving to pursue other interests. We are grateful to Dr. Karlsson and Mr. Morgan for their contributions to the Company.

To support the later stage development of ensifentrine, in early 2019, we strengthened our team with the appointment of Kathleen Rickard, MD, as Chief Medical Officer (CMO,) and Tara Rheault, PhD, MPH, as VP Research and Development Operations and Global Project Management. Together they have extensive expertise in respiratory drug development, regulatory affairs and commercialization. We also expanded our team hiring experts with significant experience of late-stage clinical trials in COPD.

Ensifentrine - first-in-class bronchodilator and anti-inflammatory agent

We are a clinical-stage biopharmaceutical company focused on developing and commercializing innovative therapeutics for the treatment of respiratory diseases with significant unmet medical need. Our product candidate, ensifentrine (RPL554) is an investigational, potential first-in-class, inhaled, dual inhibitor of the enzymes phosphodiesterase 3 and 4, or PDE3 and PDE4, that is designed to act as both a bronchodilator and an anti-inflammatory agent. We are not aware of any other single compound in clinical development or approved by the U.S. Food and Drug Administration, or FDA, nor the European Medicines Agency, or EMA, for the treatment of respiratory diseases that acts as both a bronchodilator and anti-inflammatory agent. We believe ensifentrine has the potential to be the first novel class of bronchodilator in over 40 years. A nebulized formulation of ensifentrine has currently completed Phase 2 clinical development for the treatment of chronic obstructive pulmonary disease, or COPD, and we are preparing to meet with the FDA to discuss plans for Phase 3 clinical trials, which we expect to commence in the third quarter of 2020, subject to FDA feedback and to funding.

Successful Phase 1 and 2 studies have been completed with nebulized ensifentrine in healthy volunteers and in patients with cystic fibrosis, or (CF), chronic asthma and allergic rhinitis, in addition to COPD. A Phase 2 study in COPD with ensifentrine formulated in a dry powder inhaler, or DPI, has been completed, with positive clinical results reported in August 2019. A Phase 2 study in COPD with ensifentrine formulated in a pressurized metered dose inhaler, or MDI, is ongoing with clinical results expected in the second half of 2020. We intend to develop ensifentrine as a nebulized therapy for the treatment of COPD.

For the past 40 years, the treatment of COPD has been dominated by three classes of inhaled therapies approved for use by the FDA or EMA: antimuscarinic agents and beta2-agonists, both available as either short-acting or long-acting bronchodilators, and inhaled corticosteroids, or ICS, known for their anti-inflammatory effects. However, despite existing treatment with one or multiple combinations of these therapies, and owing to the progressive and incurable nature of COPD, many COPD patients on maximum inhaled therapy still experience significant lung function impairment and symptoms for which limited further approved treatment options are available. One such treatment is an oral formulation of a PDE4 inhibitor (roflumilast) with anti-inflammatory properties, although frequency of adverse events has limited its use in COPD patients. Clinicians have expressed desire to use this oral PDE4 inhibitor in more patients were it not for the adverse events. We believe this suggests that ensifentrine has potential to become an important treatment for COPD and other respiratory diseases if our late-stage clinical program demonstrates favorable efficacy, safety and tolerability results for the compound.

In our clinical trials, treatment with ensifentrine has been repeatedly observed to result in statistically significant improvements in lung function as compared to placebo, whether dosed alone or in combination with commonly used short- and long-acting classes of bronchodilators, with or without ICS. Statistically significant means that there is a low statistical probability, typically less than 5%, that the observed results in a study or a trial occurred

by chance alone. In two Phase 2b clinical trials of nebulized ensifentrine as a maintenance treatment for COPD, patients with moderate-to-severe COPD treated with ensifentrine showed clinically meaningful and statistically significant improvements in reported COPD symptom scores. In addition, our clinical trials have also shown clinically meaningful and statistically significant improvements in certain measures of lung function following combined treatment with ensifentrine as add-on to other approved bronchodilators; COPD patients experienced a marked reduction in residual lung volume, which is believed to be related to one of the most debilitating symptoms, breathlessness. The rapid onset of action observed when adding ensifentrine on top of tiotropium, a commonly used LAMA, was also notable, and may be particularly helpful to those patients suffering from morning breathlessness. We believe that the clinical effects observed with ensifentrine are driven by its bronchodilator, anti-inflammatory and mucociliary clearance mechanisms.

High unmet medical need in symptomatic COPD patients despite treatment with current standard-of-care

We believe there is an urgent and unmet medical need for new and more effective treatments for COPD to reduce the number and burden of symptoms, acute periods of worsening symptoms, or exacerbations, and establish a consistent and durable response to treatment.

According to the World Health Organization (WHO), over one billion people suffer from chronic respiratory diseases. Among the most common of these afflictions is COPD, which is a progressive respiratory disease for which there is no cure. COPD damages the airways and the lungs and leads to shortness of breath, impacting a person's ability to perform daily activities. Chronic inflammation plays a central role in the pathology of the disease and is particularly prominent in the airways of COPD patients. COPD includes chronic bronchitis, which refers to the inflammation of the lung and airways that results in coughing and sputum production, and emphysema, which refers to a destruction of distal lung tissue, or air sacs.

In some cases, patients with COPD experience exacerbations, which are estimated to cause approximately 1.5 million emergency department visits, 687,000 hospitalizations and 129,000 deaths per year in the United States alone. According to the WHO, COPD is expected to become the third leading cause of death globally by 2030, with 384 million people worldwide suffering from the disease. It is estimated that there are 24 million people with COPD in the United States, only half of whom have been diagnosed. Of those diagnosed with COPD in the United States, more than 2 million suffer from severe or very severe forms of the disease. Total annual medical costs relating to COPD in the United States are projected to rise to $49 billion in 2020. Whereas the number of patients diagnosed with COPD in the United States continues to increase annually, the growth in numbers in more developing countries, like China, is significantly higher. The prevalence of COPD in China is expected to be about 8% of patients over 40 years of age and is expected to increase in coming years. Global sales of drugs used for chronic maintenance therapy of COPD were $13.6 billion in 2019, of which $9.6 billion were in the US.

Cystic fibrosis and severe asthma

In CF, a fatal inherited disease, we believe the bronchodilatory and anti-inflammatory effects of ensifentrine may be beneficial and, if approved, has the potential to become an additional important and novel treatment for patients. Furthermore, we aim to explore, alone or with a collaborator, the development of ensifentrine to treat severe asthma and other respiratory diseases.

CF is the most common fatal inherited disease in the United States and Europe. CF causes impaired lung function and is commonly associated with repeat and persistent lung infections often resulting in frequent exacerbations and hospitalizations. There is no cure for CF and although current therapies are leading to longer lifespans the median age of death for CF patients is still only around 40 years.

CF is considered a rare, or orphan, disease by both the FDA and the EMA. According to the Cystic Fibrosis Foundation, more than 30,000 people in the United States and more than 70,000 people worldwide are living with CF and approximately 1,000 new cases of CF are diagnosed each year. The FDA and the EMA provide incentives for sponsors to develop products for orphan diseases, and we may seek orphan drug designation for ensifentrine from both regulators in treating CF. CF patients take an average of seven medications daily. Global sales of drugs used for the treatment of CF were $3.5 billion in 2019, of which $2.0 billion were in the US.

Asthma is widely seen as a result of chronic inflammation in the lungs. Worldwide 300 million people suffer from asthma with about 25 million diagnosed in the US alone. Global sales of drugs used for the treatment of asthma were $16.5 billion in 2019, with $9.7 billion in the US alone. Established treatments include those adopted from the treatment of COPD (for example, bronchodilators and ICS), anti-IgE agents and leukotriene inhibitors. Approximately 1 million patients in the United States are refractory asthmatic patients who remain uncontrolled on established therapies. These patients are the target for injectable biologic anti-IL-5 agents. Annual sales of biologics in the United States for the treatment of asthma exceed $1.0 billion. We see potential for ensifentrine as an inhaled product for such patients.

We may also explore the development of ensifentrine in MDI and/or DPI formulations for the treatment of asthma and other respiratory diseases.

DEVELOPMENT OF ENSIFENTRINE

Clinical development of ensifentrine in COPD

In January 2020, we reported top-line results from our 4 week 416-patient Phase 2b dose-ranging clinical trial. This trial evaluated four doses of nebulized ensifentrine (0.375 mg, 0.75 mg, 1.5 mg and 3.0 mg) or placebo as an add-on treatment to tiotropium (Spiriva® Respimat®), a commonly used LAMA bronchodilator, in symptomatic patients with moderate-to-severe COPD who required additional treatment. The trial met its primary endpoint of improved lung function, with ensifentrine plus tiotropium producing a clinically and statistically significant dose-dependent improvement in FEV_1 at week 4, compared to placebo plus tiotropium. Additionally, clinically meaningful improvements in health-related quality of life (mean SGRQ-C) were observed on top of tiotropium. Ensifentrine was well tolerated at all doses with an adverse event profile similar to placebo. We believe that these data support dose selection for our planned Phase 3 program, which we anticipate initiating in the third quarter of 2020, subject to FDA feedback and funding.

In January 2019, we announced results from our exploratory pharmacological Phase 2 clinical trial evaluating nebulized ensifentrine administered twice daily on top of treatment with tiotropium and olodaterol. Although we did not meet the primary endpoint, treatment with ensifentrine showed statistically significant improvements in FEV_1, including when measured over 24 hours, and after the second dose in the evening. We believe this suggests that ensifentrine could be an effective addition to dual bronchodilator therapy, in particular during the second half of the day following treatment, when patients may derive less benefit from their LAMA/LABA dual bronchodilator therapy.

COPD – successful development of DPI and pMDI formulations

In addition to our nebulized formulation of ensifentrine, we have developed both MDI and DPI formulations of ensifentrine for the maintenance treatment of COPD.

Delivery of orally inhaled drugs by pMDI or DPI is a mainstay of maintenance treatment for patients with moderate to severe COPD. We believe that over 90% of patients with diagnosed COPD use inhalers, such as a pMDI or DPI, rather than a nebulizer.It is estimated that, in the United States, approximately 5.5 million patients

with moderate to severe COPD use inhalers for maintenance therapy. Successful development of a pMDI or DPI formulation of ensifentrine for moderate disease would greatly expand the addressable market for the drug and represents a multi-billion dollar potential opportunity.

In August 2019, we announced results from our Phase 2 clinical trial evaluating a DPI formulation of ensifentrine for the maintenance treatment of patients with COPD. The magnitude of improvement in lung function, as measured by FEV_1 was highly statistically significant and we believe this supports twice daily dosing of ensifentrine for COPD treatment. Secondary lung function endpoints were also met, and ensifentrine was well tolerated at all dose levels. We believe that delivery of ensifentrine with a hand-held inhalation device, such as the DPI format, could substantially expand the clinical utility and commercial opportunity in COPD treatment.

In June 2019, we announced the initiation of a Phase 2 dose-ranging trial to evaluate the pharmacokinetic, or PK profile, efficacy, and safety of a pressurized MDI formulation of ensifentrine in patients with moderate-to-severe COPD. We anticipate reporting data from the single-dose portion of this trial (Part A) early in the second quarter of 2020, and reporting results from the second portion of the trial (Part B), which evaluates multiple doses of the MDI formulation of ensifentrine, in the second half of 2020.

We may also explore the development of ensifentrine in pMDI and/or DPI formulations for the treatment of asthma and other respiratory diseases.

CORPORATE

Ensifentrine is protected by granted and pending patents. We believe that medicinal products containing ensifentrine are protected by our IP beyond 2035. We have worldwide commercialization rights for ensifentrine. We raised $90 million in gross proceeds from investors from our April 2017 global offering comprising an initial public offering (“IPO”) on the Nasdaq Global Market (“Nasdaq”), and a concurrent European private placement, together with a shareholder private placement. Members of our management team, which we have strengthened and expanded during the year, and our board of directors have extensive experience in large pharmaceutical and biotechnology companies, particularly in respiratory product development from drug discovery through commercialization and have played important roles in the development and commercialization of several approved respiratory treatments, including Symbicort, Daliresp/Daxas, Flutiform, Advair, Breo Ellipta and Anoro Ellipta.

FINANCIALS

The operating loss for the year ended December 31, 2019 was £41.1 million (2018: £25.6 million) and the loss after tax for the year ended December 31, 2019 was £31.9 million (2018: £19.9 million).

Research and Development Costs

Research and development costs were £33.5 million for the year ended December 31, 2019 as compared to £19.3 million for the year ended December 31, 2018, an increase of £14.2 million. The cost of clinical trials increased by £12.7 million as there were two active trials in the year ended December 31, 2018, compared to four clinical trials in the year ended December 31, 2019. Pre-clinical costs increased by £0.3 million which was offset by a reduction in Chemistry, Manufacturing, and Controls of £0.4 million. Personnel related costs increased by £1.3 million in the year ended December 31, 2019, compared to the prior year.

General and Administrative Costs

General and administrative costs were £7.6 million for the year ended December 31, 2019 as compared to £6.3 million for the year ended December 31, 2018, an increase of £1.3 million. The increase was primarily attributable to a £0.9 million increase in costs relating to commercial market research, a £0.3 million increase in personnel

related costs and a £0.6 million increase in other overhead costs. This was offset by a £0.5 million decrease in share based payments.

Finance Income and Expense

Finance income was £2.4 million for the year ended December 31, 2019 and £2.8 million for the year ended December 31, 2018. The decrease was due to a loss in foreign exchange on cash and short term investments (recorded as a finance expense) compared to £1.9 million gain in the prior year. This was offset by a £1.6 million decrease in the fair value of the warrant liability in the year ended December 31, 2019 compared to a increase in the liability in the year ended December 31, 2018 (which is a non-cash item, recorded as a finance expense).

Finance expense was £0.5 million for the year ended December 31, 2019, as compared to £1.3 million for the year ended December 31, 2018. The movement was due to a decrease in the fair value of the warrant liability (recorded in finance income), compared to an increase of £1.2 million December 31, 2018, both non-cash items. In addition, there was a foreign exchange loss on cash and short-term investments in December 31, 2019 of £0.3 million. In the year ended December 31, 2018, there was a foreign exchange gain (recorded in finance income).

As at December 31, 2019, there was approximately £22.9 million in cash and cash equivalents (2018: £19.8 million) and £7.8 million in short-term investments (2018: £44.9 million).

Taxation

Taxation for the year ended December 31, 2019 amounted to a credit of £7.3 million as compared to a credit of £4.2 million for the year ended December 31, 2018, an increase in the credit amount of £3.1 million. The credits are obtained at a rate of 14.5% of 230% of our qualifying research and development expenditure, and the increase in the credit amount was primarily attributable to our increased expenditure on research and development.

We would like to thank the staff and Board members for all their contributions and shareholders for their continued support during a successful year.

Dr. David Ebsworth	**Dr. David Zaccardelli**
Chairman	**Chief Executive Officer**
February 27, 2020	**February 27, 2020**

STRATEGIC REPORT

The Directors present their strategic report together with the audited consolidated financial statements, audited company financial statements and auditors' report for the year ended December 31, 2019.

Principal activity

The Company was incorporated on February 24, 2005. On September 18, 2006 the Company successfully acquired all the shares of Rhinopharma Limited, a private company incorporated in Canada, and changed its name to Verona Pharma plc (the "Company" or the "Parent"). On December 12, 2014, the Company established a U.S subsidiary, Verona Pharma, Inc., in the state of Delaware. The Company, Rhinopharma Limited and Verona Pharma, Inc. are collectively referred to as the "Group".

The principal activity of the Group is the development of novel, "first-in-class" drugs for the treatment of chronic respiratory diseases, such as chronic obstructive pulmonary disease (COPD), cystic fibrosis and asthma.

Section 172(1) Companies Act 2006

The Directors are required by law to act in good faith to promote success of the Company for the benefit of the shareholders as a whole and are also required to have regard for the following:

- the likely long term consequences of any decision;
- the interests of the Company's employees;
- the need to foster the Company's business relationships with suppliers, customers and others;
- the impact of the Company's operations on the community and the environment;
- the desirability of the Company maintaining a reputation for high standards of business conduct; and
- the need to act fairly as between shareholders of the Company.

In 2018 the Group adopted the Corporate Governance Code for Small and Mid-Size Quoted Companies from The Quoted Companies Alliance (the "QCA Code"). The QCA Code is an appropriate code of conduct for the Group's size and stage of development. There is a discussion of how the Group applies the ten principles of the QCA Code in support of its growth on the Group website.

Outlook and Strategy in the Chairman and Chief Executive Officer's joint statement describes the Group's activities, strategy and future prospects, including the considerations for long term decision making on pages 6 to 10.

The Group intends to initiate its Phase 3 program for the maintenance treatment of COPD once it believes it has alignment with the FDA on its planned design for the Phase 3 clinical program. The Group will require significant additional funding to initiate and complete this Phase 3 program and will need to secure the required capital to fund the program. The Group will seek additional funding through public or private financings, debt financing, collaboration or licensing agreements and other arrangements. However, there is no guarantee that the Group will be successful in securing additional finance on acceptable terms, or at all, and should the Group be unable to raise sufficient additional funds it will be required to defer the initiation of Phase 3 clinical trials, until such funding can be obtained. This could also force the Group to delay, reduce or eliminate some or all of its research and development programs, product portfolio expansion or commercialization efforts, or pursue alternative development strategies that differ significantly from its current strategy, which could have a material adverse effect on the Group's business, results of operations and financial condition.

The Board has a good relationship with the Group's employees. The Board maintains constructive dialogue with employees through the Chief Executive Officer. Appropriate remuneration and incentive schemes are maintained to align employees' objectives with those of the Group. More detail on how the board has regard to the interests of employees can be found on pages 35 to 36 of the Corporate Governance report.

The Group endeavours to maintain good relationships with its suppliers by contracting on their standard business terms and paying them promptly, within agreed and reasonable terms. We meet with our significant suppliers regularly, using steering and operational committees to ensure that our research program is planned

and delivered effectively in a timely and cost-efficient manner. This ensures that the Group's and our significant suppliers' interests are aligned.

The Group has few employees and most operations are outsourced. Its reportable greenhouse gas emissions are therefore nil. This is discussed further within "Greenhouse Gas Emissions" on page 17 in the Strategic Report.

The Board recognizes the importance of maintaining high standards of business conduct. The Group operates Codes of Business Conduct and Ethics and provides mechanisms for whistle blowing and complaints, described in detail on the Group's website, under Corporate Governance. Employees are required to read and acknowledge these codes annually and to follow them at all times.

The Board endeavors to maintain good relationships with its shareholders and treat them equally. This is described in more details in "Relations with shareholders" in the Corporate Governance Report on page 32.

Review of the business strategy and future prospects

The Chairman and Chief Executive Officer's joint statement on pages 6 to 12 describes the Group's activities, strategy and future prospects. The Directors' report describes the Group's results for the year ended December 31, 2019.

Key Performance Indicators ("KPIs")

The Company is a development stage business and does not yet generate significant revenues or other operating cash inflows. The Company therefore uses a mix of Financial and Non-financial KPIs to monitor its activities. Financial KPIs can typically be compared over a period of years; Non-financial KPIs may change from year to year depending on the development stage of the Company's programs.

1. Research and development spend during the year

Strategic objective: Investment in R&D to generate future revenue for the Group.

Key Performance Indicator: R&D expenditure of £33.5 million (2018: £19.3 million).

Definition*:* Costs including labour, materials and other expenditure incurred by the Group on research and development.

			£'m		
Year ended December 31,	***2015***	***2016***	***2017***	***2018***	***2019***
Research and development	7.3	4.5	23.7	19.3	*33.5*

2. Cash and short-term investments held at year end

Strategic objective: Availability of financial resources to progress the development of the Group's research and development activities.

Key Performance Indicator: Year end cash and short-term investments of £30.8 million (2018: £64.7 million).

Definition: Cash and cash equivalents plus term deposits with maturities over three months at date of investment.

			£'m		
Year ended December 31,	***2015***	***2016***	***2017***	***2018***	***2019***
Short-term investments, cash and equivalents	3.5	39.8	80.3	64.7	*30.8*

3. Demonstration of activity of ensifentrine when dosed in addition to dual bronchodilator therapy

Strategic objective: Show that ensifentrine provides a significant and clinically meaningful benefit when added to existing bronchodilator therapies (LAMA and LABA), when used in combination (LAMA/LABA).

Key Performance Indicator: Improvement in FEV1 and residual volume.

Definition: Statistically significant improvement in FEV1 (additional bronchodilation) on the third day of dosing, compared to placebo, when used as add-on to dual bronchodilator therapy (LAMA/LABA). Statistically significant improvements in reduction in residual volume.

Progress during year ended December 31, 2019: Completed an exploratory three-day pharmacology study of ensifentrine as add-on to LAMA/LABA therapy. On January 14, 2019 the Company announced that a 1.5 mg dose of ensifentrine produced a statistically significant additional improvement in FEV1 of 52 mL compared to placebo 0-4 hours post morning dose ($p<0.05$). Peak FEV1 and Residual Volume after evening dose on day 2 showed statistically significant improvement with both 1.5 mg and 6 mg doses (1.5 mg dose $p<0.001$; 6 mg dose $p=0.002$).

4. Demonstration of activity of ensifentrine when dosed in addition to single bronchodilator therapy in a 4-week Phase 2b dose-ranging clinical trial in US in approximately 400 patients

Strategic objective: Show that ensifentrine provides a significant and clinically meaningful benefit when added to existing LAMA bronchodilator therapy in a dose dependent manner.

Key Performance Indicator: Sustained improvement in FEV_1 (supporting bronchodilator activity) and progressive improvement in symptom scores (supporting anti-inflammatory activity).

Definition: statistically significant improvement in peak FEV_1 (additional bronchodilation) at the end of 4 weeks of dosing, compared to placebo, and statistically significant improvement in total COPD symptoms measured using SGRQ by the end of week 4 for ensifentrine treated patients compared to placebo.

Progress during year ended December 31, 2019: Conducted a 4 week Phase 2b study of ensifentrine as add-on to LAMA therapy. Following the year end, on January 13, 2020 the Company announced that all doses of ensifentrine (0.375mg, 0.75mg, 1.5mg and 3mg) produced a dose-ordered, statistically significant and clinically meaningful additional improvement in peak FEV1 compared to placebo post morning dose ($p<0.05$). The top two doses (1.5mg and 3mg) also showed statistically and clinically significant improvements in symptom scores, measured using SGRQ.

5. Maintain a dual-listing on Nasdaq and AIM

Strategic objective: to maintain a broad and stable pool of investors, both existing and potential, in the Company.

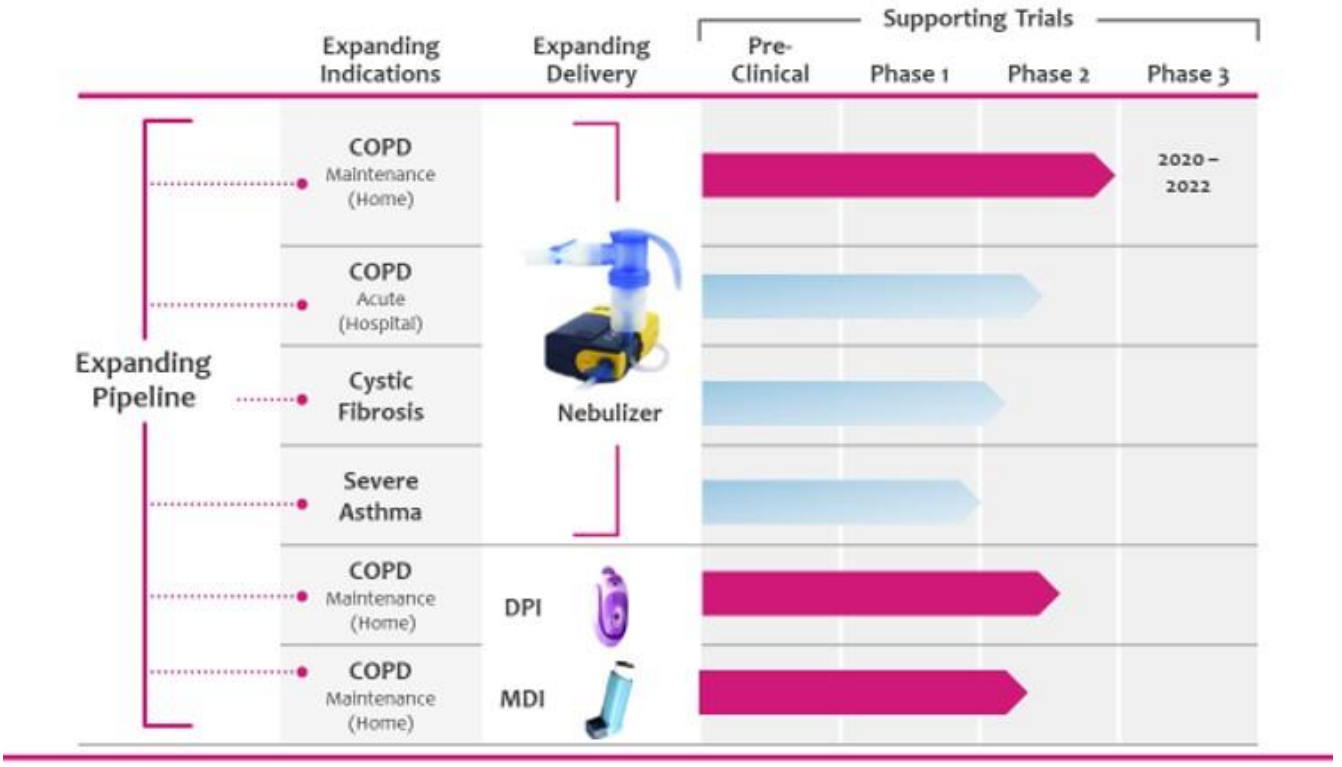
Key Performance Indicator: Maintenance of Verona Pharma ADSs trading on Nasdaq and Verona Pharma shares on AIM.

Definition*:* to comply with market and regulatory requirements to maintain trading facilities for the Company's American Depositary Shares (ADSs) on Nasdaq and ordinary shares on AIM.

Progress during the year ended December 31, 2019: the Company's ADSs are traded on Nasdaq with the symbol VRNA; each ADS represents 8 ordinary shares in the Company. The Company's shares are traded on AIM with the symbol VRP.

Pipeline

The following table depicts the potential indications for ensifentrine and their current development status:



Gender of Directors and employees

We recruit individuals who have the skills, experience and integrity needed to perform the roles to make Verona Pharma a successful company. We note that there are no women on the board but that we recruit without regard to sex or ethnic origin, appointing and thereafter promoting staff based upon merit.

The profile of the Group's employees at December 31, 2019, was as follows:

	Male	Female	Total
	December 31, 2019	**December 31, 2019**	**December 31, 2019**
Number of persons who were Directors of the Company	9	—	9
Number of persons who were other employees of the Company	10	14	24
Total employees at December 31, 2019	**19**	**14**	**33**

Environmental matters

We currently outsource our research, development, testing and manufacturing activities. These activities are subject to various environmental, health and safety laws and regulations, which govern, among other things, the controlled use, handling, release and disposal of and the maintenance of a registry for, hazardous materials and biological materials. If we or our partners fail to comply with such laws and regulations, we could be subject to fines or other sanctions.

As with other companies engaged in activities similar to ours, we face a risk of environmental liability inherent in our current and historical activities, including liability relating to releases of or exposure to hazardous or biological materials. Environmental, health and safety laws and regulations are becoming more stringent. We may be required to incur substantial expenses in connection with future environmental compliance or remediation activities, in which case, our production and development efforts may be interrupted or delayed.

Greenhouse Gas Emissions

We have used the Greenhouse Gas ("GHG") Protocol Corporate Accounting and Reporting Standard (revised edition) data gathered to fulfil our requirements under the CRC Energy Efficiency scheme, and emission. Our greenhouse gas emission estimates for 2019 and 2018 have been prepared in accordance with the UK government's Department for Environment, Food and Rural Affairs (DEFRA) guidance document Environmental Reporting Guidelines: Including Mandatory GHG emissions reporting guidance from June 2013.

	Tonnes carbon dioxide equivalent (tCO2-e)	
	2019	**2018**
Estimated greenhouse gas emissions from our own activities, including the combustion of fuel and the operation of our facilities	—	—
Estimated greenhouse gas emissions from purchased electricity, heat, steam or cooling for own use	—	—
Total estimated greenhouse gas emissions	—	—
Intensity ratio:	N/A	N/A

We are a company with a small number of employees. We have serviced offices and we currently outsource our research, development, testing and manufacturing activities. As a result we do not emit greenhouse gases from our own activities, nor do we purchase electricity, heat or steam for our own use. (Scope 1 and Scope 2 disclosures).

However, we are aware that our activities do have an impact on GHG emissions through the work of our partners and our activities such as business travel (Scope 3 disclosures). We have discussed with our partners the impact of our operations on emissions but they have not been able to provide the information for us to provide a meaningful analysis.

Whilst we have few employees, we have activities in the US and Europe and we need to fly our employees, directors and consultants to effectively manage our business and operations. We recognize that we have control over business travel and have chosen to disclose our estimated related greenhouse gas emissions. For 2019, we estimate that our business travel resulted in the emission of 590 tCO2-e (2018: 430 tCO2-e).

Strategy, Business Model and Approach to Risk

We intend to become a leading biopharmaceutical company focused on the treatment of respiratory diseases with significant unmet medical needs. We are focused on developing ensifentrine for the treatment of patients with COPD. We believe there is an urgent and unmet medical need for new and more effective treatments for COPD to reduce the number and burden of symptoms, reduce acute periods of worsening symptoms, exacerbations, and establish a consistent and durable treatment response. We may also develop ensifentrine for the treatment of CF, a fatal inherited disease where the bronchodilatory and anti-inflammatory effects of ensifentrine may be beneficial. We believe ensifentrine, if approved, has the potential to become an important,

novel treatment and standard of care for COPD and CF patients. We may also explore, alone or with a collaborator, the development of ensifentrine to treat asthma and other respiratory diseases.

We are developing ensifentrine in a nebulized formulation for the maintenance treatment of COPD patients as a single agent and add-on therapy and potentially for the treatment of CF. We are also developing ensifentrine in a nebulized formulation as an add-on therapy to short-acting bronchodilators and other commonly used therapies for the treatment of hospitalized patients with acute exacerbations of COPD.

In addition to our nebulized formulation of ensifentrine, we are developing ensifentrine in both dry powder inhaler, (DPI), and metered dose inhaler (pMDI) formulations for the maintenance treatment of COPD. We may explore the development of ensifentrine in these formulations for the treatment of asthma and other respiratory diseases.

According to the World Health Organization, over one billion people suffer from chronic respiratory diseases. Among the most common of these afflictions is COPD, which is a progressive respiratory disease for which there is no cure. COPD damages the airways and the lungs and leads to shortness of breath, impacting a person's ability to perform daily activities. In some cases, patients experience acute exacerbations, which are estimated to cause approximately 1.5 million emergency departments, 687,000 hospitalizations and 129,000 deaths per year in the United States alone. According to the World Health Organization, COPD is the third leading cause of death globally, with 384 million people worldwide suffering from the disease. Global sales of drugs currently indicated for COPD are expected to grow to $15.6 billion in 2019.

According to the Cystic Fibrosis Foundation, more than 30,000 people in the United States and more than 70,000 people worldwide are living with CF and approximately 1,000 new cases of CF are diagnosed each year. CF is the most common fatal inherited disease in the United States and Europe. CF causes impaired lung function and is commonly associated with repeat and persistent lung infections due to the inability to clear thickened phlegm, or mucus, from the lung. This condition often results in frequent exacerbations and hospitalizations. There is no cure for CF and the median age of death for CF patients is 37 years. CF is considered a rare, or orphan, disease by both the U.S. Food and Drug Administration and the European Medicines Agency.

Drug development is inherently risky. There is no certainty that ensifentrine will progress successfully through development, obtain regulatory approval and become a marketable product. Verona Pharma's internal development expertise and knowledge of respiratory diseases should however allow it to develop ensifentrine in a manner that will substantially reduce, but which cannot eliminate, this risk in the future. All of the Group's activities involve an ongoing assessment of risks and the Group seeks to mitigate such risks where possible. The Board has undertaken an assessment of the principal risks and uncertainties facing the Group, including those that would threaten its business model, future performance, solvency and liquidity. In addition, the Board has considered the longer-term viability of the Group including factors such as the prospects of the Group and its ability to continue in operation for the foreseeable future. The Board considers that the disclosures outlined in the Group's Strategic Report on pages 13-19, and the further detailed risk factors included in Form 20-F filed with the SEC, are appropriate given the stage of development of the business. The Board considers that these disclosures provide the information necessary for shareholders to assess the Group's future viability and potential requirements for further capital to fund its operations.

Having carried out a review of the level of risks that the Group is taking in pursuit of its strategy, the Board is satisfied that the level of retained risk is appropriate and commensurate with the financial rewards that should result from achievement of its strategy.

RISKS ASSOCIATED WITH OUR BUSINESS

In common with other pharmaceutical development companies, the Group faces a number of risks and uncertainties. Internal processes are in place to help identify, manage and mitigate these risks.

The main risks have been identified as follows:

- We have a limited operating history, have never generated any product revenue, have incurred significant operating losses since our inception, expect to incur significant operating losses for the foreseeable future and may never achieve or maintain profitability.
- We will need additional funding to complete the development and commercialization of ensifentrine, if approved, and if we are unable to raise capital when needed, we could be forced to delay, reduce, modify or eliminate our product development programs or commercialization efforts.
- We depend heavily on the success of ensifentrine, our only product candidate, and we cannot give any assurance that ensifentrine will receive regulatory approval for any indication, which is necessary before it can be commercialized.
- Ensifentrine is in early-stage clinical development. If clinical trials of ensifentrine are prolonged or delayed, or if ensifentrine in later stage clinical trials fails to show the desired safety and efficacy, we or our collaborators may be unable to obtain required regulatory approvals and be unable to commercialize ensifentrine on a timely basis, or at all.
- We may encounter regulatory issues or changes that increase our costs and delay or impede our development and commercialization efforts.
- Britain's withdrawal from the European Union has created significant uncertainty about the future relationship between the United Kingdom and the EU, including applicability of laws and regulations, as well as potentially negative impacts on economic conditions, trade and financial markets.
- We rely, and expect to continue to rely, on third parties to conduct our clinical trials and pre-clinical testing, and to manufacture our product candidates for pre-clinical and clinical testing, and those third parties may not perform satisfactorily, which could delay our product development activities.
- If we are unable to adequately protect our technology, or to secure and maintain freedom to operate or issued patents protecting our product candidates, others could preclude us from commercializing our technology and products or compete against us more directly.
- We face significant competition from other biotechnology and pharmaceutical companies.
- Our future growth and ability to compete depends on retaining our key personnel and recruiting additional qualified personnel.

On behalf of the Board

Dr. David Zaccardelli
Chief Executive Officer

February 27, 2020

DIRECTORS' REPORT

The Directors present their report together with the audited financial statements for the year ended December 31, 2019.

Results and dividends

The Group results for the year are set out on page 58. There was a loss for the year after taxation amounting to £31.9 million (2018: loss of £19.9 million). This reflects a increase in research and development expenditure. In view of the absence of distributable reserves the Directors cannot recommend the payment of a dividend (2018: £nil). Net cash, cash equivalents and short-term investments at December 31, 2019 decreased to £30.8 million from £64.7 million at December 31, 2018 primarily due to cash spent on research and development activities and general corporate costs.

Research and Development Activities

The Chairman and Chief Executive Officer’s joint statement describes the Group’s research and development strategy and activities.

Directors

The directors of the company who were in office during the year and up to the date of signing of the financial statements were:

Executive Directors
Jan-Anders Karlsson (resigned February 3, 2020)
David Zaccardelli (appointed February 1, 2020)

Non-executive Directors
David Ebsworth
Ken Cunningham
Martin Edwards (appointed April 1, 2019)
Rishi Gupta
Mahendra Shah
Andrew Sinclair
Vikas Sinha
Anders Ullman

To the extent permitted by the U.K. Companies Act 2006, we are empowered to indemnify our directors against any liability they incur by reason of their directorship. We have also entered into a deed of indemnity with each of our directors and executive officers. In addition to such indemnification, we provide our directors and executive officers with directors’ and officers’ liability insurance.

Pensions

Verona Pharma plc operates a defined contribution pension scheme open to all Executive Directors and employees.

Political and charitable contributions

There were no political or charitable contributions made by the Company during the year ended December 31, 2019 (2018: £nil).

Future developments

The Chairman and Chief Executive Officer's joint statement describes the Group's activities, strategy and future prospects.

Significant shareholders

As at December 31, 2019, the following shareholders are recorded as having interests in the Company's ordinary shares of 3% and above:

	Number of Ordinary shares	% of Share Capital
Novo Nordisk Fonden	12,389,985	11.8%
Vivo Capital	11,943,645	11.3%
OrbiMed Advisors	10,003,168	9.5%
New Enterprise Associates	9,757,393	9.3%
Abingworth	7,215,534	6.9%
VenBio Partners	7,000,000	6.7%
Polar Capital	5,300,000	5.0%
Tekla Capital Management	4,412,031	4.2%
Aisling Capital	3,548,768	3.4%
Arthurian Life Sciences	3,400,352	3.2%

Capital Structure

As at December 31, 2019, the Company has 105,326,638 5p ordinary shares, all of which rank pari passu. All shares are admitted to trading on the AIM market of the London Stock Exchange and American Depositary Shares ("ADSs") are traded on Nasdaq following the global offering on April 26, 2017.

As part of the July 2016 placement the Company issued 31,115,927 warrants that give the warrant holder the right to subscribe for 0.4 of an ordinary share at a per share exercise price of 172p (see note 19). As at December 31, 2019, there were 31,003,155 warrants outstanding with rights over 12,401,262 ordinary shares

Corporate Governance

The Corporate Governance report describes the corporate governance of the Group, including the corporate governance code adopted.

Principal Risks and Uncertainties

See the Strategic Report for a discussion of risks facing the Group.

Financial risk management

We are exposed to a variety of financial risks. Our overall risk management program seeks to minimize potential adverse effects of these financial risks on our financial performance.

Credit Risk

We consider all of our material counterparties to be creditworthy. We consider the credit risk for each of our counterparties to be low and do not have a significant concentration of credit risk at any of our counterparties.

Liquidity Risk

We manage our liquidity risk by maintaining adequate cash reserves at banking facilities, and by continuously monitoring our cash forecasts, our actual cash flows and by matching the maturity profiles of financial assets and liabilities.

Market Risk

Foreign currency risk reflects the risk that the value of a financial commitment or recognized asset or liability will fluctuate due to changes in foreign currency rates. Our financial position, as expressed in pounds sterling, are exposed to movements in foreign exchange rates against the U.S. dollar and the euro. Our main trading currencies are pounds sterling, the U.S. dollar and the euro. We are exposed to foreign currency risk as a result of operating transactions and the translation of foreign bank accounts. We monitor our exposure to foreign exchange risk, sensitivity analysis and exposure is described further in note 3.1 in the financial statements. We have not entered into foreign exchange contracts to hedge against gains or losses from foreign exchange fluctuations.

Interest rate risk reflects the risk that the value of a financial instrument will fluctuate as a result of change in market interest rates on classes of financial assets and financial liabilities. We do not hold any derivative instruments to manage interest rate risk.

Branches

The Company’s principal place of business is in London, UK, and operates a subsidiary office in New York, USA.

Hiring policy

The Company's hiring policy with regards to disability, belief, sex and sexual orientation is discussed in the Corporate Governance Report.

Carbon dioxide emissions

The Strategic Report discusses the Company's carbon dioxide emissions.

Post Period Events

There were no post period events to report.

Auditors

PricewaterhouseCoopers LLP have expressed their willingness to continue in office as auditors for another year. In accordance with Section 489 of the Companies Act 2006, a resolution proposing that PricewaterhouseCoopers LLP be re-appointed as auditors of the Company and that the Directors be authorized to fix their remuneration will be proposed at the Annual General Meeting.

Annual General Meeting

A notice of Annual General Meeting of the Company will be sent out in due course, setting out time, date and location of the meeting, together with the resolutions relating to the business which the Company proposes to conduct at such meeting.

Statement of Directors’ responsibilities

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulation.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the group financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and company financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law the

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

- select suitable accounting policies and then apply them consistently;
- state whether applicable IFRSs as adopted by the European Union have been followed for the group financial statements and IFRSs as adopted by the European Union have been followed for the company financial statements, subject to any material departures disclosed and explained in the financial statements;
- make judgments and accounting estimates that are reasonable and prudent; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and Company will continue in business.

The directors are also responsible for safeguarding the assets of the group and company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the group and company's transactions and disclose with reasonable accuracy at any time the financial position of the group and company and enable them to ensure that the financial statements comply with the Companies Act 2006.

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

The Group's website, under "The Corporate Governance Code", discusses how the Group applies the code and leverages its principles to support the long-term success of the Group. The Board notes that there were no key corporate governance issues that were required to be addressed in the period.

The directors consider that the annual report and accounts, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Group and Company's position and performance, bushiness model and strategy.

Directors' confirmations

In the case of each director in office at the date the Directors' Report is approved:

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

On behalf of the Board.

Dr. David Zaccardelli
Chief Executive

February 27, 2020

CORPORATE GOVERNANCE REPORT

It is the Board's belief that good corporate governance is integral to a successful business and the Company complies with and reports against the standards of corporate governance prescribed by the UK Corporate Governance Code for Small and Mid-Size Quoted Companies from The Quoted Companies Alliance (the “QCA Code”). Details of how the Company complies with the code can be found on the Company’s website. The Board believes that this corporate governance framework is appropriate for the Company, having regard to its size and nature.

The Group's website, under "The Corporate Governance Code", discusses how the Group applies the code and leverages its principles to support the long-term success of the Group. The Board notes that there were no key corporate governance issues that were required to be addressed in the period.

THE BOARD OF DIRECTORS

At December 31, 2019, the Board comprised 8 non-Executive Directors, and one Executive Director. The Board, through its Nomination and Governance Committee, regularly reviews its composition to ensure that it has a sufficiently wide range of skills and experience to enable it to pursue its strategic goals and to address anticipated issues in the foreseeable future. As part of this process, the Board is considering broadening the experience on the Board through the appointment of a non-Executive Director with experience in the commercialization and marketing of respiratory drugs. The Board has also considered and concluded that the appointment of a Senior Independent Director is not necessary at this time, but keeps this issue under review.

The Board typically has six scheduled meetings per year (approximately every two months), with additional Board meetings and Board sub-committee meetings convened as circumstances and business needs dictate. The Board is responsible to the shareholders for the proper management of the Company and sets the overall direction and strategy of the Company, reviews scientific, operational and financial performance, and approves management appointments. All key operational and investment decisions are subject to Board approval.

There is a clear separation of the roles of Chief Executive Officer and non-Executive Chairman. The non-Executive Chairman is responsible for overseeing the running of the Board, ensuring that no individual or group dominates the Board’s decision-making and ensuring the non-Executive Directors are properly briefed on matters. The Chief Executive Officer has the responsibility for implementing the strategy of the Board and managing the day to day business activities of the Company.

In accordance with our Articles of Association, one third of our directors retire from office at every annual general meeting of shareholders. However, if the number of directors serving on our Board is not divisible by three, then the number nearest but not exceeding 33.3% shall retire from office at each annual general meeting of shareholders. Retiring directors are eligible for re-election and, if no other director is elected to fill his or her position and the director is willing, shall be re-elected by default.

The Board has considered the guidelines on independence and regards David Ebsworth, Ken Cunningham, Anders Ullman, Martin Edwards and Vikas Sinha as independent directors. Although Dr. Ullman received consultancy fees during the year ended December 31, 2019 for services in the area of scientific and clinical development advice, the quantum of these fees was small and the Board is satisfied that Dr. Ullman continues to demonstrate independence of character and judgement with respect to his non-Executive Directors duties. Although Mr Sinha holds share options under the Company's 2017 Incentive Plan, the Board considers that the grant of share options to US-based directors is aligned with US best practice and the company's dual listing. The Board is also satisfied that Mr Sinha continues to demonstrate independence of character and judgement with respect to his non-Executive Directors duties. Furthermore, although Dr. Edwards is a Senior Partner of Novo Holdings, which has an 11.8% shareholding in the Company, the Board considers Dr, Edwards to be an independent director under UK and US corporate governance rules.

While the Board considers that each of Rishi Gupta, Andrew Sinclair and Mahendra Shah fulfil their duties to the Company in an exemplary way and demonstrate independence of character and judgement with respect to their non-Executive Director duties, since they are each nominated as a Director by a significant shareholder of the Company, the Board does not regard them as independent.

BIOGRAPHIES

David Zaccardelli, Pharma.D. Dr. Zaccardelli has served as our President and Chief Executive Officer and on our board of directors since February 2020. From December 2018 until its acquisition by Swedish Orphan Biovitrum for up to $915 million in November 2019, Dr. Zaccardelli served as President and CEO of Dova Pharmaceuticals, a US company developing therapeutics for rare diseases. Previously, he was Acting CEO of Cempra, from December 2016 until the company's merger with Melinta Therapeutics in November 2017. From 2004 until 2016, Dr Zaccardelli served in several senior management roles at United Therapeutics Corporation, including Chief Operating Officer, Chief Manufacturing Officer and Executive Vice President, Pharmaceutical Development and Operations. Prior to United Therapeutics, he founded and led a start-up company focused on contract research positions and held a variety of clinical research positions at Burroughs Wellcome & Co, Glaxo Wellcome, and Bausch & Lomb Pharmaceutical. Dr. Zaccardelli received a Pharm.D. from the University of Michigan.

David Ebsworth, Ph.D. Dr. Ebsworth has served as the Non-Executive Chairman of our board of directors since December 2014. From October 2009 to August 2014, Dr. Ebsworth served as Chief Executive Officer of Vifor Pharma, based in Zürich, the specialty pharma division of Galenica AG Group, a pharmaceutical wholesaler and retailer, and as a member of Galenica's Executive Committee. In 2012, Dr. Ebsworth was also named as Chief Executive Officer of Galenica and as Chairman of Galenica's Executive Committee, positions he held until August 2014. In his earlier career, Dr. Ebsworth worked with Bayer AG for over 19 years, heading the Canadian, North American and global pharmaceutical business. He also served as Chief Executive Officer of Oxford Glycosciences, a biotech company, listed on the London Stock Exchange and Nasdaq, which was acquired by Celltech plc (now part of UCB) in 2003. Dr. Ebsworth received a Ph.D. in industrial relations from the University of Surrey.

Ken Cunningham, M.D. Dr. Cunningham has served as a Non-Executive Director on our board of directors since September 2015. Dr. Cunningham has over 25 years' experience in the pharmaceutical industry including leadership roles at several companies focused on developing respiratory medicines. Between 2008 and 2010, he was at SkyePharma plc (now part of Vectura Group plc), initially as Chief Operating Officer and subsequently as Chief Executive Officer where he was involved in the late-stage development of flutiform for asthma. Earlier in his career, Dr. Cunningham held a variety of clinical development and commercial strategy roles at GlaxoWellcome plc and Warner-Lambert. Dr. Cunningham serves as the non-executive chairman of the board of directors of Abzena Holdings (US) LLC and of Medherant Ltd. Dr. Cunningham received a degree in medicine from St. Mary's, Imperial College, London University.

Martin Edwards, M.D. Dr. Edwards has served as a Non-Executive Director on our board of directors since April 2019. Since 2003, Dr. Edwards has held various positions at Novo Holdings, a life sciences investment firm, and most recently as part-time Senior Partner. Earlier in his career, he was Corporate VP and Global Head of Drug Development for Novo Nordisk, where he led all aspects of pre-clinical and clinical drug development. Dr. Edwards currently serves on the boards of directors of Kalvista Pharmaceuticals Inc, F2G Ltd, Harmony Biosciences Inc, Karus Therapeutics Ltd, Nuvelution Pharma Inc, and Vantia Therapeutics Ltd. Dr. Edwards trained in physiology and medicine at the University of Manchester. He is a Member of the Royal College of Physicians, a Member with distinction of the Royal College of General Practitioners, a Fellow of the Faculty of Pharmaceutical Medicine and holds a MBA from the University of Warwick.

Rishi Gupta. Mr. Gupta has served as a Non-Executive Director on our board of directors since July 2016. Mr. Gupta was designated for appointment to our board of directors by OrbiMed Private Investments VI, LP, or OrbiMed, pursuant to our relationship agreement with OrbiMed. Since 2002, Mr. Gupta has held various positions at OrbiMed Advisors LLC, a global healthcare investment firm, where he is currently a Partner. Prior to that, he was a healthcare investment banker at Raymond James & Associates, served as manager of corporate development at Veritas Medicine and was a summer associate at Wachtell, Lipton. Mr. Gupta currently is a member of the board of directors of Avitide, Inc., Turnstone Biologics, Inc., Attenua, Inc, EnLiven Therapeutics, Inc, and Pionyr Immunotherapeutics, Inc. Mr. Gupta received an A.B. in biochemical sciences from Harvard College and a J.D. from Yale Law School.

Mahendra Shah, Ph.D. Dr. Shah has served as a Non-Executive Director on our board of directors since July 2016. Dr. Shah was designated for appointment to our board of directors by funds affiliated with Vivo Capital pursuant to our relationship agreement with such funds. Dr. Shah is a successful pharmaceutical entrepreneur and executive and, since March 2010, has served as a Managing Director of Vivo Capital, a healthcare investment firm. Dr. Shah serves as a member of the board of directors of Scilex Pharmaceuticals, Inc., Fortis Inc., Citrine Medicines, Inc., and several private companies in the biopharmaceutical and biotechnology industries. Dr. Shah received his Ph.D. in industrial pharmacy from St. John’s University and a Master’s Degree in Pharmacy from L.M. College of Pharmacy in Gujarat, India.

Andrew Sinclair, Ph.D. Dr. Sinclair has served as a Non-Executive Director on our board of directors since July 2016. Dr. Sinclair was designated for appointment to our board of directors by Abingworth Bioventures VI, LP, or Abingworth, pursuant to our relationship agreement with Abingworth.Since 2008, Dr. Sinclair has held various positions at Abingworth LLP, a life sciences investment group, where he is currently a Partner and Portfolio Manager. Dr. Sinclair is a member of the Institute of Chartered Accountants in England and Wales and received a Ph.D. in chemistry and genetic engineering at the BBSRC Institute of Plant Science, Norwich, and a B.Sc. in microbiology from King's College London.

Vikas Sinha. Mr. Sinha has served as a Non-Executive Director on our board of directors since September 2016. Mr. Sinha has over 20 years’ experience working in executive finance roles in the life sciences industry. Mr. Sinha is co-founder and Chief Financial Officer of ElevateBio, Inc., a holding company focused on building cell and gene therapy companies. He also serves as President and Chief Financial Officer of AlloVir, Inc., an ElevateBio portfolio company. From 2005 to 2016, Mr. Sinha was the Chief Financial Officer of Alexion Pharmaceuticals, Inc., a biotechnology company, where he was responsible for finance, business development, strategy, investor relations and IT. Prior to joining Alexion, Mr. Sinha held various positions with Bayer AG in the United States, Japan, Germany and Canada, including Vice President and Chief Financial Officer of Bayer Pharmaceuticals Corporation in the United States and Vice President and Chief Financial Officer of Bayer Yakuhin Ltd. in Japan. Mr. Sinha holds a master's degree in business administration from the Asian Institute of Management. He is also a qualified Chartered Accountant from the Institute of Chartered Accountants of India and a Certified Public Accountant in the United States.

Anders Ullman, M.D., Ph.D. Dr. Ullman has served as a Non-Executive Director on our board of directors since September 2015. From 2016 to 2018, Dr. Ullman served as Head of the COPD Centre at Sahlgrenska University Hospital, Sweden. From 2013 to 2014, he was Executive Vice President and Head of Research and Development in the BioScience business unit of Baxter International Inc., a healthcare company, which became Baxalta Inc. From 2007 to 2013, Dr. Ullman was Executive Vice President, Head of Research and Development at Nycomed Pharma Private Limited (now part of Takeda Pharmaceuticals Company Limited), where he led the development and approval of Daxas, the PDE4 inhibitor used to prevent COPD exacerbations. Earlier in his career, he held a number of roles in AstraZeneca. Dr. Ullman serves on the board of directors of Pexa AB. Dr. Ullman received a M.D. and a Ph.D. in clinical pharmacology from the University of Gothenburg.

Committees of our Board of Directors

Our Board has three standing committees: an Audit and Risk Committee, a Remuneration Committee and a Nomination and Governance Committee.

The composition and scope of the Audit and Risk Committee of the Board is described further below, within the Audit and Risk Committee Report.

Remuneration Committee of the Board

The Remuneration Committee, which consists of Dr. Ken Cunningham, Dr. David Ebsworth and Rishi Gupta, assists the Board in determining directors' and executive officers' compensation. Dr Cunningham serves as Chairman of the Committee.

The Remuneration Committee's responsibilities include, among other things:

- identifying, reviewing and proposing policies relevant to the compensation of the Company's directors and executive officers;
- evaluating each executive officer's performance in light of such policies and reporting to the Board;
- analyzing the possible outcomes of the variable remuneration components and how they may affect the remuneration of the executive officers;
- recommending any equity long-term incentive component of each executive officer's compensation in line with the remuneration policy and reviewing our executive officer compensation and benefits policies generally;
- appointing and setting the terms of engagement for any remuneration consultants who advise the Committee and obtain benchmarking data with respect to the directors' and executive officers' compensation; and
- reviewing and assessing risks arising from our compensation policies and practices.

The Directors' Remuneration Report is presented on pages 33 to 52.

Nomination and Governance Committee of the Board

The Nomination and Governance Committee, which consists of Dr. David Ebsworth, Dr. Mahendra Shah and Dr. Anders Ullman, assists our Board in identifying individuals qualified to become executive and non-executive directors of our Company consistent with criteria established by our Board and in developing our corporate governance principles. Dr Ebsworth serves as Chairman of the Committee.

The Nomination and Governance Committee's responsibilities include, among other things:

- reviewing and evaluating the structure, size and composition of our Board and making recommendations with regard to any adjustments considered necessary;
- drawing up selection criteria and appointment procedures for Board members;
- identifying and nominating, for the approval of our Board, candidates to fill vacancies on the Board and its corresponding committees;
- keeping under review the leadership needs of the Company, both executive and non-executive, and planning the orderly succession of such appointments; and
- assessing the functioning of our Board and individual members and reporting the results of such assessment to the Board.

AUDIT AND RISK COMMITTEE REPORT

In this Report, we describe the work of the Audit and Risk Committee and the significant issues considered in 2018.

Audit and Risk Committee of the Board

The Audit and Risk Committee, which consists of Vikas Sinha, Dr. David Ebsworth and Dr. Andrew Sinclair, assists the Board in overseeing our accounting and financial reporting processes and the audits of our financial statements and monitoring UK Governance Code compliance and business risk. Mr. Sinha serves as Chairman of the Audit and Risk Committee. The Audit and Risk Committee consists of members of our Board who are financially literate and are also considered to be "audit committee financial experts" as defined by applicable SEC rules and have the requisite financial sophistication as defined under the applicable Nasdaq rules and regulations. Our Board has determined that all of the members of the Audit and Risk Committee satisfy the "independence" requirements set forth in Rule 10A-3 under the Exchange Act. The Audit and Risk Committee is governed by a charter that complies with Nasdaq rules.

The Audit and Risk Committee's responsibilities include, among other things:

- recommending the appointment of the independent auditor to the general meeting of shareholders;
- the appointment, compensation, retention and oversight of the independent auditor;
- pre-approving the audit services and non-audit services to be provided by the independent auditor before the auditor is engaged to render such services;
- evaluating the independent auditor's qualifications, performance and independence, and presenting its conclusions to our Board on at least an annual basis;
- reviewing and discussing with the executive officers, our Board and the independent auditor our financial statements and our financial reporting process;
- considering and recommending to our Board whether the audited financial statements be approved; and
- monitoring our review and mitigation of corporate and operational risk.

The Audit and Risk Committee meets as often as one or more members of the Committee deem necessary, but in any event must meet at least four times per year. The Audit and Risk Committee must meet at least once per year with our independent auditor, without our executive officers being present.

Risk Identification and Management

The Audit and Risk Committee monitors the Company’s approach to risk management. Management review the Company's risks on an ongoing basis and consider both corporate and project risk, which is risk relating the Company's sole product candidate, ensifentrine. Management report their risk assessment to the Committee analyzing risk by severity and probability of occurrence. They also discuss mitigation strategies that have been or are intended to be implemented.

External Auditor

PricewaterhouseCoopers LLP (PwC) has been the Group’s auditor since 2016. PwC operate procedures to safeguard against the possibility of their objectivity and independence being compromised. This includes the use of quality review partners, consultation with internal compliance teams and the carrying out of an annual independence procedure within their firm. PwC report to the Audit Committee on matters including independence and non-audit fees on an annual basis. The audit partner changes every five years. The amount charged by the external auditors for the provision of services during the twelve month period under review is set out in note 7 to the Financial Statements.

The Committee assesses the performance of the auditor and is comfortable that PwC has operated effectively and a resolution to reappoint the firm as auditors will be put to shareholders and the Company's AGM

Internal Control

The Audit and Risk Committee reviews the Group's internal control framework. The Group does not have an internal audit function and so the Committee has engaged an external firm of accountants to test management's systems of internal control. Any significant control deficiencies and mitigation strategies are reported to the Committee for review.

Significant financial reporting issues considered by the Committee in 2019

The Audit and Risk Committee considers risk areas in the financial statements throughout the year and before the audit commences. The Committee considered the following items to be areas of risk:

Warrant financial liability

The fair value of these warrants is determined by applying the Black-Scholes model. Certain assumptions are used to determine the fair value of the Warrants at each quarter end and require estimates to be made. The key estimates and assumptions assessed include volatility and risk free rate. The magnitude of the liability means that miscalculations or incorrect assumptions could have a significant impact on the liability and income statement change. The Committee reviews management's assessment of the liability.

Ligand contingent liability

The Group has a material liability for the future payment of royalties and milestones associated with contractual liabilities on ensifentrine, a development product acquired as part of the acquisition of Rhinopharma. The liability is measured at amortized cost. At each reporting date the liability is re-measured where there are changes in estimated cashflows or probabilities of success. The contingent liability therefore requires quarterly re-assessment for any such triggering event. The committee considered that Management's conclusion that there are no changes in estimated cashflows or probabilities of success in the year is appropriate.

Management believe that the probabilities of success are likely to change after a successful End of Phase 2 meeting with the FDA. The Committee agrees with this assertion.

Up to the year ended December 31, 2018, movements in the liability relating to re-measurements of cash flows or changes in the probabilities of success were taken to the Consolidated Statement of Comprehensive Income. During the year ended December 31, 2019, the Company reviewed the accounting for this item and has determined that these movements in the liability will now be recognized in the cost of the corresponding asset. The corresponding asset is the intangible IP R&D asset.

The Group believes that this change in accounting policy results in the Consolidated Financial Statements providing a more relevant and reliable view of its financial position and performance because without an adjustment to the IP R&D asset on the re-measurement of the liability, the cost of the asset would not be fairly reflected on the Consolidated Statement of Financial Position. The Consolidated Statement of Financial Position more faithfully represents the financial position of the Group if the intangible asset is adjusted by any re-measurement of the liability for changes in estimated cash flows, to give a fairer reflection of the cost of the intangible asset.

The Group has reviewed the International Financial Reporting Interpretations Committee ("IFRIC") discussion of accounting for variable payments made for the purchase of an intangible asset that is not part of a business combination that concluded that it was too broad for it to address within the confines of existing IFRS standards. As a result, practice in this area is mixed and many pharmaceutical companies follow a cost accumulation model. The Group also noted that adjusting the cost of the asset when a liability is remeasured for changes in estimated cash flows is consistent with the guidance in IFRIC 1 for decommissioning liabilities and IFRS 16 for lease liabilities.

The committee agreed with the change in policy as it more accurately reflects a more relevant and reliable view of its financial position.

Going Concern

The Group has incurred recurring losses since inception, including net losses of £31.9 million, £19.9 million and £20.5 million for the years ended December 31, 2019, 2018 and 2017, respectively. In addition, as of December 31, 2019, the Group had an accumulated loss of £101.1 million. The Group expects to continue to generate operating losses for the foreseeable future. As of the issuance date of the annual consolidated financial statements, the Group expects that its cash and cash equivalents would be sufficient to fund its operating expenses and capital expenditure requirements for at least 12 months from the issuance date of these annual consolidated financial statements. Accordingly, the consolidated financial statements have been prepared on a basis that assumes the Group will continue as a going concern and which contemplates the realization of assets and satisfaction of liabilities and commitments in the ordinary course of business.

The Group intends to initiate its Phase 3 program for the maintenance treatment of COPD once it believes it has alignment with the FDA on its planned design for the Phase 3 clinical program. The Group will require significant additional funding to initiate and complete this Phase 3 program and will need to secure the required capital to fund the program. The Group will seek additional funding through public or private financings, debt financing, collaboration or licensing agreements and other arrangements. However, there is no guarantee that the Group will be successful in securing additional finance on acceptable terms, or at all, and should the Group be unable to raise sufficient additional funds it will be required to defer the initiation of Phase 3 clinical trials until such funding can be obtained. This could also force the Group to delay, reduce or eliminate some or all of its research and development programs, product portfolio expansion or commercialization efforts, or pursue alternative development strategies that differ significantly from its current strategy, which could have a material adverse effect on the Group's business, results of operations and financial condition.

RISK MANAGEMENT AND INTERNAL CONTROL

The Board is responsible for the systems of internal control and for reviewing their effectiveness. The internal controls are designed to manage rather than eliminate risk and provide reasonable but not absolute assurance against material misstatement or loss. The Board reviews the effectiveness of these systems annually by considering the risks potentially affecting the Group.

In addition to consideration of financial risk as part of the review of broader internal control, the Group is required to assess and report on the effectiveness of the internal controls over financial reporting under Section 404(a) of the Sarbanes-Oxley Act. As the Group currently qualifies as an 'emerging growth company', as defined in the Jumpstart Our Business Start-Ups Act of 2012, Verona Pharma is currently exempt from the auditor attestation requirements of Section 404(b) of the Sarbanes-Oxley Act. The Group will lose this exemption at the earlier of when it fails to qualify as an emerging growth company or the financial year ended December 31, 2022.

The Group does not consider it necessary to have an internal audit function due to the small size of the administrative function. This need is evaluated on an annual basis.

A comprehensive budgeting process is completed once a year, shortly prior to the start of each new financial year, which is reviewed and approved by the Board; a further reforecasting exercise is prepared mid-year, which is also reviewed and approved by the Board. Detailed management accounts are produced on a monthly basis, with all significant variances investigated promptly. The management accounts are reviewed and commented on by the Board at the meetings every two months and are reviewed on a monthly basis by the management team and budget holders.

The Group maintains appropriate insurance cover, including in respect of actions taken against the Directors because of their roles, as well as against material loss or claims against the Group. The insured values and type of cover are comprehensively reviewed on an annual basis.

ATTENDANCE AT BOARD AND COMMITTEE MEETINGS

Our expectation is that Non-Executive Directors should be prepared to commit, on average, a minimum of two days per month to the Company's business, recognizing that particular events may from time to time require them to devote to the Company more time than this. Non-Executive Directors are expected to be available to serve on one or more Board committees which may require additional time commitment, particularly in the case of the Chairman of the Board and the Chairman of the Board committees.

The Directors attended the following Board and committee meetings during the year:

Director	Board meetings	Audit Committee	Remuneration Committee	Governance and Nomination Committee
Jan-Anders Karlsson	8/8	—	—	—
David Ebsworth	8/8	3/5	3/3	1/1
Ken Cunningham	7/8	—	3/3	—
Martin Edwards	5/5	—	—	—
Anders Ullman	6/8	—	—	1/1
Rishi Gupta	8/8	—	3/3	—
Mahendra Shah	8/8	—	—	1/1
Andrew Sinclair	7/8	5/5	—	—
Vikas Sinha	8/8	5/5	—	—

The Board undertakes an annual performance evaluation process, based on clear and relevant objectives and seeking continuous improvement.

Generally, the performance evaluation is conducted in June each year and done in the form of a structured questionnaire circulated to all Directors, asking them to rate the performance of the Board and its Committees in a number of strategic areas and provide a rationale for any low rating. Results are analyzed by the Chairman and Legal Counsel and any key themes are reported and discussed with the Board. Any recommendations arising from such review which are designed to specifically address any issues identified are implemented by the Board.

The annual performance evaluation conducted in 2019 resulted in a recommendation, which is being implemented by the Board, to expand the Board's risk management oversight of all key business, strategic and operational risks.

Corporate Social Responsibility

The Board of Verona Pharma recognizes the importance of sound corporate governance and complies with and reports against the standards of corporate governance prescribed by the Corporate Governance Code for Small and Mid-Size Quoted Companies from The Quoted Companies Alliance (the "QCA Code"). The Board believes that this corporate governance framework is appropriate for the Company, having regard to its size and nature. The Board periodically reviews the QCA Code and updates the framework if necessary, with the last review undertaken on September 1, 2018.

Whistle-blowing

The company has formal arrangements in place to facilitate 'whistle-blowing' by employees through a contract with a third party service provider. If a complaint is made to this third party, the content is sent anonymously by email to the Company's Compliance Officer, so that appropriate action can be taken.

Employment

The company endeavors to appoint employees with appropriate skills, knowledge and experience for the roles they undertake and thereafter to develop, incentivize and retain staff. The Board recognizes its legal responsibility to ensure the well-being, safety and welfare of the company's employees and maintain a safe and healthy working environment for them and our visitors. If an employee has a concern about unsafe conditions or tasks, they are encouraged to report their concerns immediately to their manager or the Company's legal counsel.

Diversity Policy

The Company is fully committed to the elimination of unlawful and unfair discrimination and values the differences that a diverse workforce brings to the organization. The Company endeavors to not discriminate because of age, disability, gender reassignment, marriage and civil partnership, pregnancy and maternity, race (which includes color, nationality and ethnic or national origins), religion or belief, sex or sexual orientation. The Company will undertake an annual review of its policies and procedures to establish its position with regard to compliance and best practice, and monitor and promote a healthy corporate culture

Relations with shareholders

The Board values good relations with the Company's shareholders and understands the importance of effectively communicating the Company's operational and financial performance as well as its future strategy. The Company's website provides financial information as well as historical news releases and matters relating to corporate governance.

The Chairman of the Board and the CEO maintain ongoing dialogue with shareholders and communicate their views to the Board. The Board recognizes it is accountable to shareholders and ensures that their views are taken into account in agreeing the Company's strategy and other operational matters. The Board also recognizes the importance of treating all shareholders equally.

Annual and interim results are communicated by regulatory news services as are ad hoc operational and regulatory releases. Shareholders may also attend the Annual General Meeting where they can discuss matters with the board.

Letter from the Chair of the Remuneration Committee

Dear Shareholders,

On behalf of the Remuneration Committee, I am pleased to present our Directors' Remuneration Report for the year ended December 31, 2019, which will be subject to an advisory vote under a resolution to be proposed at the 2020 Annual General Meeting ("AGM"). Shareholders approved the Remuneration Policy at the 2018 AGM.

Key decisions and activities in the year ended December 31, 2019

In the year ended December 31, 2019, the Committee has undertaken the following key decisions and activities:

- Considered the annual bonus objectives for the financial year ended December 31, 2019 for the Executive Director. These objectives were approved by the Board in March 2019.
- Assessed performance against the annual bonus objectives for the financial year ended December 31, 2019 for the Executive Director. The Committee recommended to the Board the level of bonuses to be paid to the Executive Director and members of the senior management team, determined according to performance against the bonus objectives. No discretion was exercised in this assessment. The Board accepted this recommendation and such amounts have been included within these 2019 annual report and accounts.
- Considered and approved awards of share options and restricted stock units to employees under the Company's 2017 Incentive Plan.
- Benchmarked and reviewed healthcare and other benefits packages offered to US employees to ensure compensation is competitive in the US market to attract and retain employees.

The Company has made significant progress during 2019 in the clinical development of ensifentrine, with the reporting of data from its three day exploratory pharmacological Phase 2a clinical trial evaluating the effect of nebulized ensifentrine when used on top of inhaled dual and triple bronchodilator and inhaled corticosteroid (ICS) therapy for COPD maintenance treatment, reporting of data from its one week Phase 2 clinical trial to evaluate a dry powder inhaler (DPI) formulation of ensifentrine, initiation (and reporting in January 2020) of data from its four week Phase 2b study evaluating the effect of nebulized ensifentrine when used as add-on to single bronchodilator therapy for COPD maintenance treatment, and initiation of a Phase 2 clinical trial to evaluate an MDI formulation of ensifentrine.

On February 3, 2020, the Company announced changes to its senior management, with the appointment of Dr. David Zaccardelli as President and Chief Executive Officer (CEO) and executive director, as successor to Dr. Jan-Anders Karlsson following his retirement after 8 years of dedicated service to the Company. Dr. Zaccardelli's appointment was the culmination of an extensive executive search process to give effect to the Board's strategy to locate the Company's senior management in the US to lead the late-stage clinical development and commercialization of ensifentrine. Mr. Mark Hahn has also been appointed as Chief Financial Officer of the Company, with effect from March 1, 2020, replacing Mr. Piers Morgan. We believe that Dr. Zaccardelli and Mr. Hahn together bring substantial pharmaceutical leadership, operational and financial expertise and the Committee looks forward to working with them during this important and exciting stage of the Company's development.

I hope that you remain supportive of our remuneration approach and will vote in favor of the Directors' Remuneration Report.

Yours faithfully,

Dr Ken Cunningham
Chair of the Remuneration Committee

February 27, 2020

Annual Report on Remuneration

Single total figure of remuneration of each Director (audited)

The Directors received the following remuneration for the years ended December 31, 2019 and December 31, 2018:

Year Ended December 31, 2019	Base Salary	Bonus	Employer's Pension	Share-based payment [i]	Other [ii]	2019 Total
	£	£	£	£	£	£
Executive						
Jan-Anders Karlsson	330,000	174,240	10,000	151,862	12,849	678,951
Non-Executive						
David Ebsworth	108,000	—	—	—	—	108,000
Ken Cunningham	40,000	—	—	—	—	40,000
Anders Ullman	30,000	—	—	—	26,000	56,000
Rishi Gupta	30,000	—	—	—	—	30,000
Mahendra Shah	30,000	—	—	—	—	30,000
Andrew Sinclair	30,000	—	—	—	—	30,000
Vikas Sinha	42,000	—	—	—	—	42,000
Martin Edwards[1]	22,500	—	—	—	—	22,500
	662,500	**174,240**	**10,000**	**151,862**	**38,849**	**1,037,451**

Year Ended December 31, 2018	Base Salary	Bonus	Employer's Pension	Share-based payment	Other	2018 Total
	£	£	£	£	£	£
Executive						
Jan-Anders Karlsson	300,000	225,000	10,000	293,054	12,491	840,545
Non-Executive						
David Ebsworth	108,000	—	—	—	—	108,000
Ken Cunningham	40,000	—	—	—	—	40,000
Anders Ullman	30,000	—	—	—	26,000	56,000
Rishi Gupta	30,000	—	—	—	—	30,000
Mahendra Shah	30,000	—	—	—	—	30,000
Andrew Sinclair	30,000	—	—	—	—	30,000
Vikas Sinha	42,000	—	—	9,229	—	51,229
	610,000	**225,000**	**10,000**	**302,283**	**38,491**	**1,185,774**

[1] Appointed April 1, 2019.

[i] Share based payments represent the intrinsic value of share options that vested during the years ended December 31, 2018 and December 31, 2019 and the intrinsic value of RSUs granted in the years ended December 31, 2018 and December 31, 2019. The intrinsic value of the share options is the difference between the share price on the date of vesting and the exercise price of the option. In the case of RSUs, the share price on the day of issue. No amount of this award was attributable to share price appreciation.

The face value of the awards is defined as the market value of the shares on the date of grant. This was a weighted average value of £0.53 per share in the year, meaning the total face value of the options and RSUs issued in 2019 was £959,720. The fair value of the options and RSUs issued in the 2019 was £642,267.

[ii)] Other benefits represent healthcare benefits and consultancy fees during the year ended December 31, 2019.

Annual performance bonus

The Company has a discretionary bonus scheme for all employees and the Executive Director. Bonus payments are a percentage of base salary based on performance measured against target objectives and, dependent upon the position of the employee within the Company, also against stretch objectives. For the Executive Director's bonus during the 2019 performance period, the total of the target bonus objectives was 66% and the total of the stretch bonus objectives was an additional 66% of base salary, giving a maximum bonus potential of 132% of base salary. Considering the actual performance achieved and the associated bonus weighting of each objective, the Remuneration Committee considered it appropriate to make a bonus award to the Executive Director equivalent to 53% of base salary. No discretion was exercised in this calculation. The annual bonus award was paid in cash in January 2020.

The performance objectives achieved by the Executive Director included the following:

- complete enrollment in the 4 week 416 patient Phase 2b dose-ranging study of nebulized ensifentrine;
- report data from the Phase 2 study of a dry powder inhaler (DPI) formulation of ensifentrine;
- undertake manufacturing of ensifentrine drug product for planned Phase 3 clinical program;
- prepare for the planned End of Phase 2 meeting with the FDA to provide guidance on the design of the Phase 3 program;
- recruit core clinical team for planned Phase 3 clinical program;
- complete a tender process for the contract research organization (CRO) for the planned Phase 3 clinical program;
- undertake certain activities within an agreed budget;
- publication of ensifentrine clinical data in reputable medical journals; and
- increase US analyst research coverage of the Company.

The performance objectives not achieved by the Executive Director during the 2019 performance period included the following:

- report data from the Phase 2 single dose study of a pressurized metered dose inhaler (pMDI) formulation of ensifentrine for the treatment of COPD; and
- raise funding to advance the development of ensifentrine and supporting business activities.

Long term incentive awards during the financial year

The Executive Director may be granted long term incentive awards at the discretion of the Remuneration Committee. During the 2019 performance period, the Executive Director was awarded options under the Company's 2017 Incentive Plan to subscribe for the Company's ordinary shares split into two different types of awards:

- options to subscribe for ordinary shares ("Options"), whereby each option has an exercise price equivalent to the closing market ordinary share price on the day prior to grant; and
- restricted share units ("RSUs"), whereby each unit represents a right to receive one ordinary share per RSU, or an amount in cash or other consideration.

In accordance with the Remuneration Policy, the vesting of awards was set by the Remuneration Committee with the objective of aligning long-term employee interests with those of shareholders and providing a competitive remuneration structure that attracts, incentivizes and retains all employees in the key markets in which the Company operates. To provide a consistent remuneration structure across these markets and a structure that is competitive in the US in which the Company competes for candidates, during the 2019 performance period, awards granted to the Executive Director and senior management vest 50% in three substantially equal annual instalments following the grant date and 50% in four substantially equal annual instalments following the grant date.

In general, the awards are subject to a service condition and may be exercised at any time between the vesting date and the tenth anniversary of the date of grant. Awards which do not vest at the end of the vesting period will lapse permanently.

Payments to past Directors (audited)

There were no payments to past Directors made during the financial year ending December 31, 2019.

Payments for Loss of Office (audited)

There were no payments made to Directors for Loss of Office during the financial year ending December 31, 2019.

Payments for Loss of Office after the financial year ending December 31, 2019

On February 1, 2020, Dr. Jan-Anders Karlsson retired as CEO and Executive Director of the Company. Between February 1, 2020 and February 28, 2020 ("Separation Date"), Dr. Karlsson will work with the incoming CEO to ensure a smooth transition period, and will continue to receive his salary, pension and other contractual benefits up to that date. Dr. Karlsson will also receive the following payments in connection with his retirement:

salary, pension and other contractual benefits in lieu of his 12 months contractual notice period, payable in monthly instalments from the Separation Date to 28 February 2021;

target bonus entitlement of 66% of base salary for the current financial year from 1 January 2020 to the Separation Date, and stretch bonus entitlement of 132% of base salary for the 12 months contractual notice period from the Separation Date to 28 February 2021, to be paid on the Separation Date;

payment of £100,000 for loss of office; and

contribution of up to £4,000 (plus VAT) towards legal fees incurred in connection with his loss of office.

Additionally, the Board exercised its discretion under the Company's equity incentive plans to treat Dr. Karlsson as a 'good leaver' and for certain outstanding vested equity incentives to remain exercisable for the duration of their term, and for certain outstanding unvested equity incentives to either vest according to the applicable vesting schedule, or to be forfeited as of February 28, 2021, unless an earlier change in control event occurs, Dr. Karlsson dies or the Company breaches the terms of the Separation Agreement or the Settlement Agreement entered into between the Company and Dr. Karlsson.

Statement of Directors' Shareholding and Share Interests (audited)

The table below details the total number of shares owned (including their beneficial interests), the total number of share options held, the number of share options vested but not yet exercised and the total number of restricted share units ("RSUs") held as at December 31, 2019:

		Options and RSUs			
December 31, 2019	**Shares**	**Options - not vested**	**Options Vested, not exercised**	**RSUs not vested**	**Total (Shares and options)**
Executives					
Jan-Anders Karlsson	193,545	2,718,505	2,322,787	648,660	5,883,497
Non Executives					
Vikas Sinha	22,222	40,128	80,256	—	142,606
David Ebsworth	395,387	—	—	—	395,387
	611,154	**2,758,633**	**2,403,043**	**648,660**	**6,421,490**

The interests of the Directors in the Company's share options and RSUs as at December 31, 2019, is as follows:

Director	Date of Grant	Price Per share (£)	Type	January 1, 2019	Granted during the period	Exercised During the period	December 31, 2019	Date from which exercisable	Expiry date
Jan-Anders Karlsson	9/17/2012	2.5	EMI	40,000	—	—	40,000	i)	6/1/2022
	9/17/2012	5	EMI	20,000	—	—	20,000	i)	6/1/2022
	9/17/2012	6	EMI	20,000	—	—	20,000	i)	6/1/2022
	9/17/2012	7.5	EMI	20,000	—	—	20,000	i)	6/1/2022
	7/29/2013	2	Unapproved	100,000	—	—	100,000	ii)	7/29/2023
	5/15/2014	1.75	Unapproved	60,000	—	—	60,000	iii)	5/15/2024
	1/29/2015	1.25	Unapproved	300,000	—	—	300,000	iv)	1/29/2025
	2/9/2016	2	Unapproved	100,000	—	—	100,000	v)	2/9/2026
	2/9/2016	3.3	Unapproved	100,000	—	—	100,000	v)	2/9/2026
	8/3/2016	1.8	Unapproved	500,000	—	—	500,000	vi)	8/3/2026
	4/26/2017	1.32	Unapproved	1,385,598	—	—	1,385,598	vii)	4/26/2027
	4/28/2017	—	RSU	245,250	—	—	245,250	viii)	4/26/2027
	3/8/2018	—	RSU	136,986	—	—	136,986	ix)	3/8/2028
	3/8/2018	1.46	Unapproved	868,758	—	—	868,758	ix)	3/8/2028
	4/1/2019	—	RSU	—	266,424	—	266,424	xi)	3/29/2029
	4/1/2019	0.57	Unapproved	—	1,026,944	—	1,026,944	xi)	3/29/2029
	11/26/2019	0.45	Unapproved	—	500,000	—	500,000	xii)	11/26/2029
Vikas Sinha	4/26/2017	1.32	Unapproved	120,384	—	—	120,384	x)	4/26/2027

All options are subject to service rather than performance conditions.

i) The options vested in 3 tranches, the first third of options vested on June 1, 2013, the second third on June 1, 2014 and the final third on June 1 2015.

ii) The options vested in 3 tranches, the first third of options vested on July 29, 2014, the second third on July 29, 2015 and the final third on July 29, 2016.

iii) The options vested in 3 tranches, the first third of options vested on May 15, 2015, the second third on May 15, 2016, and the final third on May 15, 2017.

iv) Half of these options vested on January 29, 2017 and the final half vested on January 29, 2018.

v) These options vested in two tranches with one half vested on February 9, 2018 and the other half vested on February 9, 2019.

vi) These options vested in two tranches with one half vested on August 3, 2018 and the other half vested on August 3, 2019.

vii) These options will vest 50% in three tranches and 50% in four tranches. For the options vesting in three tranches, one third vested on April 26, 2018, one third vested on April 26, 2019 and the final third will vest on April 26, 2020. For the options vesting in four tranches, one quarter vested on April 26, 2018, one quarter vested on April 26, 2019, one quarter will vest on April 26, 2020 and the final quarter will vest on April 26, 2021.

viii) These RSUs will vest 50% in three tranches and 50% in four tranches. For the RSUs vesting in three tranches, one third will vest on the later of the date that is two UK business days after the Company's first quarter financial results are announced in each of 2018, 2019 and 2020, and the date that the Company comes out of a closed period under its Share Dealing Policy following each anniversary of the date of grant ("Open Period Date"). For the RSUs vesting in four tranches, one quarter will vest on the later of the date that is two UK business days after the Company's first quarter financial results are announced in each of 2018, 2019, 2020 and 2021, and the date that the Company comes out of a closed period under its Share Dealing Policy following each anniversary of the date of grant ("Open Period Date").

ix) These options will vest 50% in three tranches and 50% in four tranches. For the options vesting in three tranches, one third vested on March 8, 2019, one third will vest on March 8, 2020 and the final third will vest on March 8,

2021. For the options vesting in four tranches, one quarter vested on March 8, 2019, one quarter will vest on March 8, 2020, one quarter will vest on March 8, 2021 and the final quarter will vest on March 8, 2022.

x) These options will vest in three tranches; one third vested on April 26, 2018, one third vested on April 26, 2019 and the final third will vest on April 26, 2020.

xi) These options will vest 50% in three tranches and 50% in four tranches. For the options vesting in three tranches, one third will vest on April 1, 2020, one third will vest on April 1, 2021 and the final third will vest on April 1, 2022. For the options vesting in four tranches, one quarter will vest on April 1, 2020, one quarter will vest on April 1, 2021, one quarter will vest on April 1, 2022 and the final quarter will vest on April 1, 2023.

xii) These options will vest 50% in three tranches and 50% in four tranches. For the options vesting in three tranches, one third will vest on November 26, 2020, one third will vest on November 26, 2021 and the final third will vest on November 26, 2022. For the options vesting in four tranches, one quarter will vest on November 26, 2020, one quarter will vest on November 26, 2021, one quarter will vest on November 26, 2022 and the final quarter will vest on November 26, 2023.

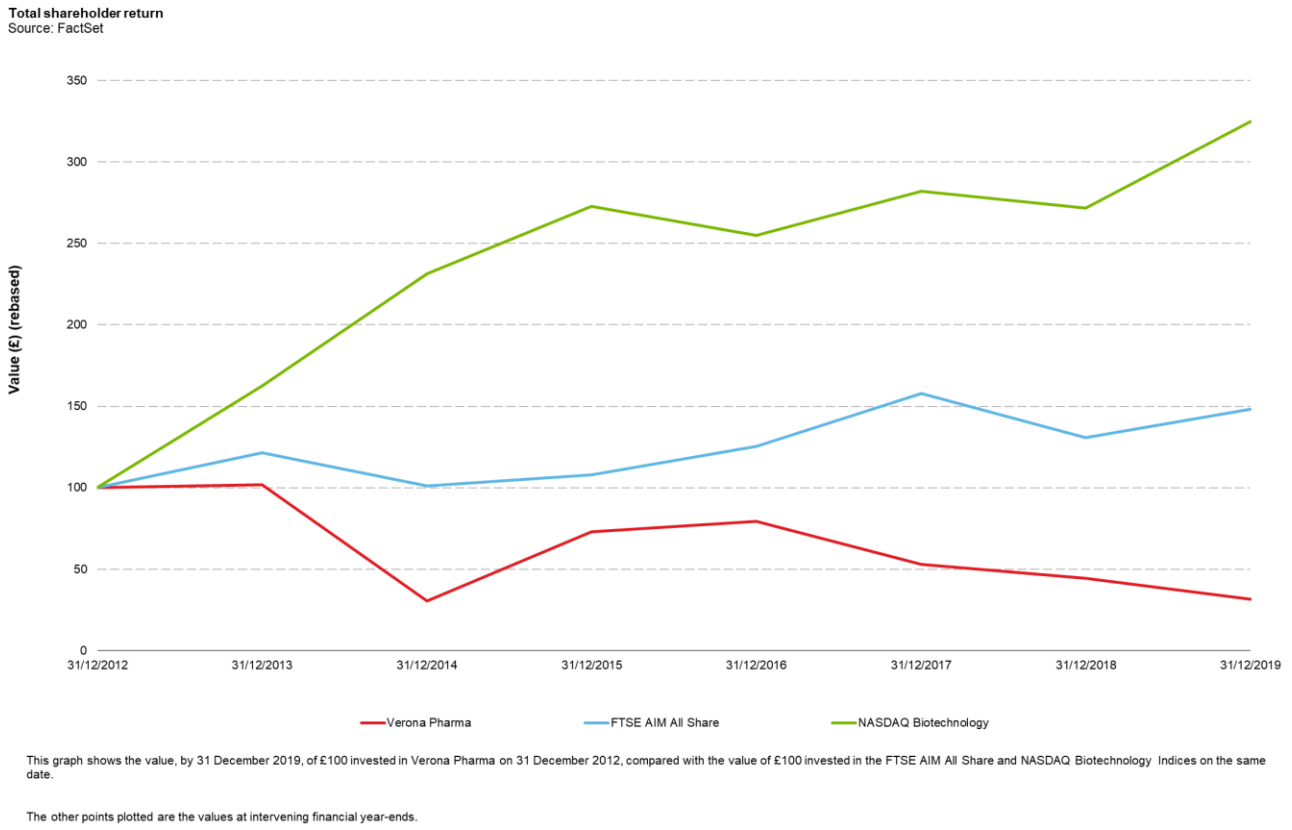
Directors' interests (audited)

The beneficial and non-beneficial interests in the Company's shares of the Directors and their families as at December 31, 2019 were as follows:

Name	Held at December 31, 2019	Held at December 31, 2018
David Ebsworth	395,387	147,787
Jan-Anders Karlsson	193,545	193,545
Vikas Sinha	22,222	22,222
Anders Ullman	Nil	Nil
Rishi Gupta	Nil	Nil
Mahendra Shah	Nil	Nil
Andrew Sinclair	Nil	Nil
Ken Cunningham	Nil	Nil
Martin Edwards	Nil	Nil

Total Shareholder Return

The graph below shows the Company's performance, measured by total shareholder return, for UK ordinary shares listed on AIM against the AIM All Share Index (AIM: VRP). The AIM All Share Index has been selected for this comparison because Verona Pharma has been trading on this exchange for over five years and is considered to be the most suitable comparator index.



CHIEF EXECUTIVE OFFICER TOTAL REMUNERATION HISTORY

2017 was the first year that Verona Pharma prepared a Directors' Remuneration Report and took the exemption not to disclose 5 years of history of remuneration. The Company has chosen to disclose remuneration history from 2017 onwards.

	2019	2018	2017
Total CEO remuneration (£'000s)	679	841	1,075
Annual variable element award rates against maximum opportunity	40%	57%	66%
Long-term incentive vesting rates against maximum opportunity	100%	100%	100%

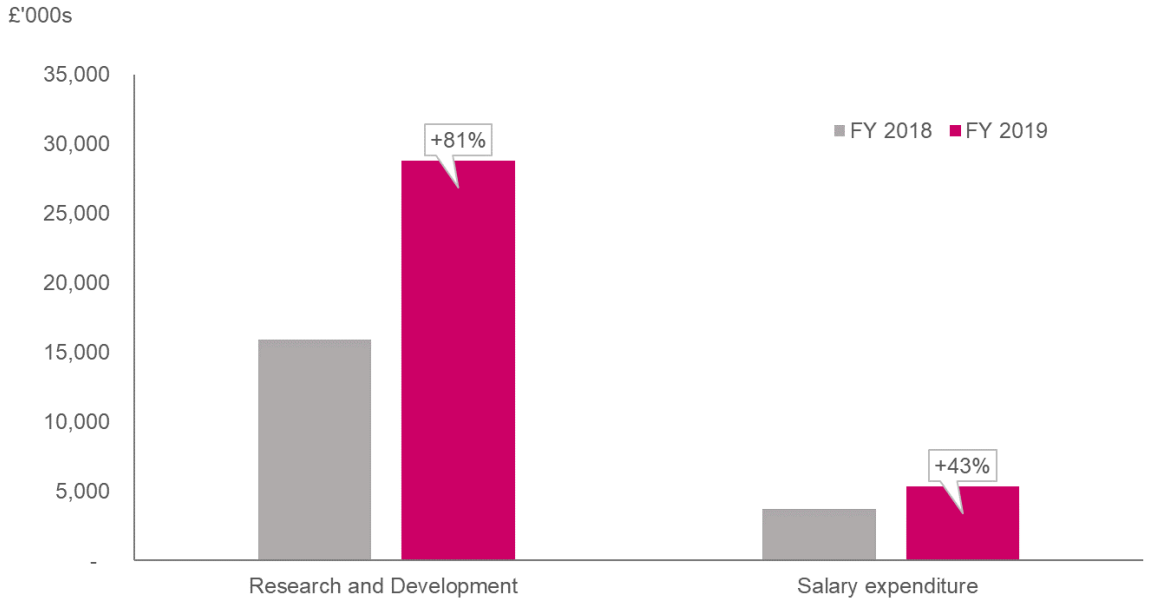
PERCENTAGE CHANGE OF CHIEF EXECTUTIVE OFFICER TOTAL REMUNERATION

The table below shows the percentage change in remuneration of the Chief Executive Officer and the Group's employees as a whole as set out below between the year ended December 31, 2018, and the year ended December 31, 2019:

	Percentage increase for year ended December 31, 2019, compared to year ended December 31, 2018.	
	CEO	Average Employee
Base salary	10%	8%
Short-term incentives	(23)%	20%
Taxable benefits	3%	—%

Relative importance of spend on pay

The Committee considers the Company's research and development expenditure relative to salary expenditure for all employees, to be the most appropriate metric for assessing overall spend on pay due to the nature and stage of the Company's business. Dividend distribution and share buy-back comparators have not been included as the Company has no history of such transactions. The graph below illustrates the gross pay to all employees per year as compared to research and development expenditure and illustrates the year-on-year change. The Committee notes that research and development expenditure increased from 2018 to 2019 due to the timing of clinical trials, specifically the Phase 2b 400 patient trial for which results were reported in January 2020.



Structure and Role of Remuneration Committee and Approach to Remuneration Matters

The Remuneration Committee is comprised of Dr. Ken Cunningham, who chairs the Committee, Dr. David Ebsworth and Mr. Rishi Gupta. The constitution of the Committee is in compliance with the UK Corporate Governance Code for Small and Mid-Size Quoted Companies from The Quoted Companies Alliance (the "QCA Code"), and the members of the Committee are Independent Directors as defined in Rule 10A-3 under the US Securities Exchange Act. It is the Board's belief that good corporate governance is integral to a successful business and the Company complies with and reports against the standards of corporate governance prescribed by the QCA Code. The Board believes that this corporate governance framework is appropriate for the Company, having regard to its size and nature.

The Committee's approach to remuneration matters is to enable the Company to attract and retain talent, incentivize long-term value generation and effectively manage the Company's cash resources. It is the belief of the Committee that this is best achieved through a greater emphasis on variable rather than fixed remuneration,

comprised of a mix of base salary and benefits, along with the flexibility to appropriately reward and incentivize with variable pay and longer term incentives, as described within the Remuneration Policy.

When applying the Policy to Executive Directors, the Committee seeks to comply with the QCA Code so far as it is practical to do so, having regard to the size, nature and business requirements of the Company. Operation of the Policy will largely be compliant with the remuneration elements of the QCA Code, but we are aware that in certain instances we will differ from the QCA Code. These instances reflect differences in US market practice when compared to the UK, and the need to balance our governance obligations against the importance of offering competitive remuneration packages in the markets in which we compete and operate.

The terms of reference of the Committee can be found on our website at www.veronapharma.com.

External advice

During the year, the Company engaged AoN Consulting, Inc. and Mercer (US) Inc. to support management and the Committee with advice on remuneration matters, in particular peer-group benchmarking of Director and senior management remuneration and the grant of long term equity incentives under the 2017 Incentive Plan that was approved at the Annual General Meeting of shareholders in April 2017. The Company also engaged Aon Consulting Ltd to support management in the valuation of option awards granted under the 2017 Incentive Plan. The Committee is satisfied that AoN Consulting, Inc. and Aon Consulting Ltd provide independent and objective advice. During 2019 fees of £27,200 were paid to Aon Consulting Inc and £3,488 were paid to Aon Hewitt Ltd.

Proposed Application of the Remuneration Policy for the Year Ended December 31, 2020

i) Fixed elements of remuneration

With effect from January 1, 2020, the base salary of Dr. Jan-Anders Karlsson in his role as Chief Executive Officer (CEO) and Executive Director of the Company is £363,000 per annum.

On February 1, 2020, Dr. Jan-Anders Karlsson resigned as CEO and Executive Director of the Company, and Dr. David Zaccardelli was appointed as President and CEO and Executive Director of the Company. In accordance with the Remuneration Policy, the Remuneration Committee has considered Dr. Zaccardelli's base salary in the context of a number of factors, including the market benchmarking exercise carried out by AoN Consulting, Inc., the skills and experience of Dr. Zaccardelli, and the location, responsibilities and scale and complexity of the role. The base salary of Dr. Zaccardelli in his role as CEO and Executive Director is $750,000 per annum, $250,000 of which is paid in cash, and $500,000 of which is paid in restricted stock units (RSUs) in the Company.

ii) Variable elements of remuneration

Short-term incentives

The target bonus for Dr. Zaccardelli for the 2020 performance period will be 50% of base salary. The performance objectives for Dr. Zaccardelli against which the Committee will determine the annual bonus were approved by the Board in February 2020. The detail behind the performance objectives is currently considered to be commercially sensitive as they relate to the strategy that the Company intends to take with respect to the advancement of the ensifentrine clinical development program and the Company's financial and commercial goals. To the extent that the objectives do not comprise commercially sensitive information, the Company expects to disclose both the objectives and performance against those objectives in next year's Directors' Remuneration Report.

Long-term incentive awards

The Company anticipates that long term incentives for 2020 will be awarded at the earliest practicable opportunity. The Company has historically awarded share options to all employees in order to align long-term employee interests with those of shareholders. Details of the awards to the Executive Director will be disclosed

in the necessary Regulatory Information Service announcement, and in the Annual Report on Remuneration for the year ended December 31, 2020.

iii) Chairman and Non-Executive Director fees (audited)

Chairman fees

The Chairman is paid a flat fee to include attendance at meetings, committee memberships, and all other related activities. The current chairman fee was reviewed in 2017 as part of the benchmarking exercise undertaken by the Company's external remuneration advisers at that time.

Non-Executive Director cash fees

Non-Executive Directors are paid a basic fee. In addition to the basic fee, committee fees may be paid for chairmanship or membership of a Board committee. Non-Executive Director fees were reviewed in 2017 as part of the benchmarking exercise undertaken by the Company's external remuneration advisers at that time.

The table below shows the annual fees currently payable to our Chairman and non-Executive Directors. The Company plans to undertake a peer-group benchmarking exercise during 2020 of the Chairman and Non-Executive compensation, and may agree to adjust the compensation as appropriate to be in line with such benchmarking.

Name	Annual Fees (£)
David Ebsworth	108,000
Ken Cunningham	40,000
Anders Ullman	30,000
Rishi Gupta	30,000
Mahendra Shah	30,000
Andrew Sinclair	30,000
Vikas Sinha	42,000
Martin Edwards	22,500

The Remuneration Policy provides that Executive Directors may have contracts with an indefinite term provided the contracts have a notice period which does not exceed 12 months.

Dr. Ken Cunningham, Dr. Anders Ullman and Mr. Vikas Sinha have letters of appointment which are subject to a three-month notice period. Dr. Mahendra Shah, Dr. Andrew Sinclair and Mr. Rishi Gupta have been designated as non-Executive Directors of our Board under relationship agreements we entered into in June 2016 with entities affiliated with each of Vivo Capital, Abingworth and OrbiMed, respectively. The appointment rights under these relationship agreements will automatically terminate upon the respective entity ceasing to beneficially hold 6.5% of our issued ordinary shares, or our ordinary shares ceasing to be admitted to AIM.

The non-Executive Directors' remuneration is reviewed by the Board annually. In accordance with the Company's Articles of Association, one third of Directors are subject to retirement by rotation at each AGM. Mr. Rishi Gupta, Dr. Mahendra Shah and Mr. Vikas Sinha will be retiring by rotation at the next AGM and, being eligible, will seek re-election. Pursuant to our Articles of Association, if no other director is elected to fill their respective positions and the directors are willing, they shall be re-elected by default. Dr. David Zaccardelli, having been appointed as a director since the last AGM, will also seek re-election at the next AGM.

Details of Directors' service contracts or letters of appointment for the year ended December 31, 2019 are as follows:

Director	Date of Contract
Executive	
Jan-Anders Karlsson	June 1, 2012
Non-Executive	
David Ebsworth	December 1, 2014
Ken Cunningham	September 10, 2015
Anders Ullman	September 10, 2015
Rishi Gupta	July 29, 2016
Mahendra Shah	July 29, 2016
Andrew Sinclair	July 29, 2016
Vikas Sinha	September 12, 2016
Martin Edwards	April 1, 2019

The information in this part of the Directors' Remuneration Report ('DRR') is not subject to audit.

Directors' Remuneration Policy

The Policy was approved by the Company's shareholders at the 2018 AGM and will remain in force for three years from that date (until the AGM in 2021), or until a revised Remuneration Policy is approved by shareholders.

Statement of voting on the Remuneration Policy at the 2018 Annual General Meeting

At the Annual General Meeting held on May 2, 2018, votes cast by proxy at the meeting in respect of the Directors' Remuneration Policy were as follows:

	In favor votes	Against votes	Total votes cast	Votes withheld
To approve the Remuneration Policy	79,085,704	4,810,731	83,896,435	4,000
% of votes cast	94.27%	5.73%	100%	—

Statement of voting on the Remuneration Report at the 2019 Annual General Meeting

At the Annual General Meeting held on May 7, 2019, votes cast by proxy at the meeting in respect of the Directors' Remuneration Report were as follows:

	In favor votes	Against votes	Total votes cast	Votes withheld
To approve the Remuneration Report	75,858,401	8,075,434	83,933,835	5,600
% of votes cast	90.38%	9.62%	100%	—

Remuneration philosophy

The aim of the Policy is to enable the Group to offer remuneration packages that are designed to promote the long-term success of the Group by:

- being sufficiently competitive to enable the Group to attract, incentivize and retain the Executive Directors and management it needs to operate its business;

- supporting and rewarding the delivery of the Group's strategy and corporate objectives and ultimately creating value for shareholders;
- aligning Executive Directors and management with the long-term interests of shareholders and helping to retain them by delivering a significant element of remuneration in shares;
- effectively managing the Group's cash resources; and
- being flexible enough to cope with the Group's changing needs as it grows and the strategy evolves.

Currently the Group has only one Executive Director, but the Policy will apply equally to any additional Executive Directors who may be appointed in the future.

The Committee annually reviews the operation of the remuneration packages to ensure they are operating within an acceptable risk profile and that they do not inadvertently encourage any economic, social or governance issues.

Remuneration Policy

Remuneration Policy for Executive Directors

The total remuneration for the Executive Director is made up of the following elements:

- Salary;
- Benefits;
- Annual bonus;
- Long-term incentive awards; and
- Pension.

The Company adopted the 2017 Incentive Plan on completion of the Nasdaq IPO in April 2017, and since January 1, 2017 the Company has only granted equity incentives under the 2017 Incentive Plan.

Salary	Benefits	Annual bonus
Purpose and link to strategy Provides market competitive fixed remuneration that reflects the responsibilities of the role undertaken, the experience of the individual and performance in the role over time.	*Purpose and link to strategy* Provides market competitive, yet cost-effective employment benefits.	*Purpose and link to strategy* To incentivize and award delivery of the Company's strategy and corporate objectives on an annual basis.
Operation Reviewed annually taking into account individual responsibilities, experience, performance, inflation and market rates. The Committee will also consider the pay and employment conditions in the wider workforce when determining Executive Directors' salaries. Salary increases are normally effective from 1 January each year. Salaries are periodically benchmarked against a relevant peer group of life sciences companies, many of which are dual-listed on Nasdaq and AIM, or other European stock exchange, with a similar stage of clinical development, and similar market capitalization or net assets.Salaries are typically aligned with the 50th percentile of peer group comparator data but the Committee may vary from this general rule where it considers that special circumstances apply or where recruitment or retention of a particular role is required.	*Operation* For Executive Directors this includes private medical insurance and life insurance. Other employment benefits may be provided from time to time on similar terms as those of other employees. If an Executive Director is based outside the UK additional benefits and assistance with relocation may be provided which reflect local market norms or legislation.	*Operation* Annual bonus performance targets are set at the start of the year by the Board and performance against objectives is assessed by the Remuneration Committee after the end of the relevant financial year. Bonuses will be paid in cash.
Maximum potential value The current base salary of the Executive Director is set out in the application of policy section of the Directors' Remuneration Report. There is no formal maximum limit. Larger increases may be permitted to reflect a change in responsibilities or a significant increase in the scale or complexity of the role, or increases in line with the remuneration of the Group's wider workforce.	*Maximum potential value* There is no formal maximum limit as the value of insured benefits will vary from year to year based on the cost from third-party providers.	*Maximum potential value* The maximum payable to an Executive Director is 150% of base salary. In exceptional circumstances, the Committee may determine that the maximum bonus opportunity will be 200% of base salary.
Performance metrics The overall performance of the individual and Group is a key determinant for salary increases.	*Performance metrics* None.	*Performance metrics* Research and development, business development, financial and commercial targets are weighted and set at the start of the year by the Board. Details of the performance measures for the current year are provided in the Directors' Remuneration Report, subject to any non-disclosure on the basis of commercially-sensitive information.

Equity Incentives	**Pension**
Purpose and link to strategy To align the interests of Executive Directors and management with long-term shareholder interests and to attract, incentivize and retain staff. To incentivize and recognize achievement of longer-term corporate objectives and sustained shareholder value creation. To effectively manage the Group's cash resources.	*Purpose and link to strategy* To provide a competitive and tax-efficient pension savings plan which complies with at least the minimum contributions requirements of the applicable jurisdiction.
Operation Conditional awards are granted annually under the 2017 Incentive Plan. The awards vest over a period of at least three years and may include a mix of share options, restricted share units, performance shares and other awards available for issuance under the 2017 Incentive Plan.	*Operation* Executive Directors are eligible to join a defined contribution pension scheme.
Maximum potential value The total number of awards made under the 2017 Incentive Plan is subject to the overall limits set out in the 2017 Incentive Plan.	*Maximum potential value* The maximum contribution, cash supplement (or combination thereof) payable by the Company is 6% of salary.
Performance metrics Vesting may be on a time-phased basis or subject to performance conditions, as determined in the discretion of the Committee.	*Performance metrics* None.

The Committee operates the annual bonus and 2017 Incentive Plan, in accordance with their rules, and where relevant, the AIM and SEC Rules. To maintain an efficient administrative process, the Committee retains the following discretion relating to remuneration:

a. the eligibility to participate in the plans;

b. the timing of grant of awards and any payments;

c. the size of awards and payments (subject to the maximum limits set out in the Policy table above and the respective plan rules);

d. the determination of whether any performance conditions have been met;

e. determining a good or bad leaver under the terms of the plans;

g. adjustments required in certain capital events such as rights issues, corporate restructuring, events and special dividends; and

h. the annual review of performance objectives for the annual bonus plan and, if applicable, the 2017 Incentive Plan.

In certain exceptional circumstances, such as a material acquisition/divestment of a Group business or a change in the broader business environment, which mean the original performance conditions are no longer appropriate, the Committee may adjust the objectives, alter weightings or set different measures as necessary, to ensure the conditions achieve their original purpose and are not materially less difficult to satisfy.

Historical equity incentive awards

Awards which were granted prior to January 1, 2017 are disclosed separately in this Remuneration Report. These awards remain eligible to vest, based on their original terms which are described separately in the Directors' Report on Remuneration.

Annual bonus

The annual bonus is designed to drive the achievement of the Company's strategic and corporate objectives. These targets are agreed by the Board and selected because of their importance in value creation for shareholders. Objectives are weighted for Executive Directors in proportion to the degree of importance of that objective for the Company. The weightings are agreed by the Remuneration Committee.

Remuneration on recruitment

The remuneration package for any new Executive Director will be determined by the Remuneration Committee in accordance with the terms of the Policy at the time of appointment (including salary, benefits, annual bonus, long-term incentive awards and pension). It is recognised that in order to attract and recruit talented individuals the Policy needs to allow sufficient flexibility with respect to remuneration on recruitment. The following policies apply to the remuneration on recruitment of new Executive Directors:

Salary: Base salary will be determined based on the responsibilities of the role, experience of the individual and current market rates. It may be considered necessary to appoint a new Executive Director on or below market rates (e.g. to reflect limited board experience). In such circumstances, phased increases above those of the wider workforce may be required over an appropriate time period, to bring the salary to the desired market level, subject to the continued development in the role.

Annual bonus: The ongoing annual bonus maximum will be in line with that outlined in the Policy table for existing Executive Directors, pro-rated to reflect the period of service. Depending on the timing or nature of an appointment it may be necessary to set different initial performance measures and targets for the first year of appointment.

Long-term incentive awards: 2017 Incentive Plan awards are granted in line with the policy outlined for existing Executive Directors. An award may be made shortly following an appointment (provided the Company is not in a closed period under its Share Dealing Policy). For internal appointments, existing awards will continue on their original terms.

Benefits: Benefits provided should be in line with those of existing Executive Directors. For external and internal appointments, where required to meet business needs, reasonable relocation support will be provided. In addition, if it becomes necessary to appoint a new Executive Director from outside the UK, additional benefits may be provided to reflect local market norms or legislation.

Pension: A company contribution or cash supplement up to the maximum as outlined for existing Executive Directors.

Sign-on payments and buy-out awards: To enable the recruitment of exceptional talent, the Committee may offer additional cash and/or share-based remuneration to take account of and compensate for remuneration that the Director is required to relinquish when leaving a former employer. The Committee will seek to structure any such replacement awards to be no more generous overall in terms of quantum or vesting than the award to be forfeited from the previous employer and will take into account the timing, form and performance requirements of

the awards forgone. Where appropriate, any long-term incentive awards will be granted under the 2017 Incentive Plan, however, the Remuneration Committee will have discretion to make use of the flexibility to make awards under any relevant exemptions in the AIM and SEC Rules.

For an internal Executive Director appointment, any variable pay element awarded in respect of the prior role will be allowed to pay out according to its terms. In addition, any other contractual remuneration obligations existing prior to appointment may continue.

The fees for any new Chairman and non-Executive Director appointments will be set in accordance with the prevailing policy and at a level that is consistent with those of the existing Chairman and non-Executive Directors.

Policy for payments on loss of office

The company does not have a policy of fixed term employment contracts, however, all Directors put themselves forward for re-election at the Annual General Meeting. The notice period for the existing Executive Director's employment contract is twelve months and three months for the existing Chairman's and non-Executive Directors' letters of appointment from either party.

The Committee's approach to payments in the event that an Executive Director's employment is terminated is to take account of the individual circumstances including the reason for termination, individual performance, contractual obligations and the terms of the equity incentive plans in which the Executive Director participates.

Termination by notice from the Company: up to 12 months' notice, with the discretion for the Remuneration Committee to make a payment in lieu of notice for base salary, pro-rated maximum bonus, pension and other benefits that would otherwise have been paid during the notice period.

Annual bonus: There is no automatic contractual entitlement to bonus on termination, although this may be considered in the discretion of the Remuneration Committee.

Long-term incentives: whether any long-term incentive awards would vest and be exercisable upon loss of office would be subject to the relevant plan rules under which such award was granted, which allow vesting and exercise of awards in the event of death, retirement, ill-health, injury, redundancy and any other reason at the discretion of the Remuneration Committee. The Committee retains discretion to determine the extent to which the award will vest, taking into consideration the circumstances. Unvested awards normally lapse, although the Committee retains the power to determine, in accordance with the "good leaver" provisions of the relevant plan rules, what proportion of unvested awards will be retained and what proportion will lapse. In determining this, the Committee will give consideration to the reason for leaving, the extent of achievement of performance objectives at the date of leaving and may decide to time pro-rate awards. On a change of control, all unvested awards vest on the date of change of control.

Additional payments: The Committee reserves the right to make payments it considers reasonable under a compromise or settlement agreement, including payment or reimbursement of reasonable legal and professional fees, untaken holiday and any payment in respect of statutory rights under employment law in the UK or other jurisdictions. Payment or reimbursement of reasonable outplacement fees may also be provided.

Remuneration Policy for Non-Executive Directors

The Remuneration Committee is responsible for evaluating and making recommendations to the Board on fees payable to the Chairman. The Chairman does not participate in discussions in respect of fees. The Chairman and Chief Executive Officer are responsible for evaluating and making recommendations to the Board on the fees payable to the Company's non-Executive Directors.

Remuneration Element	Purpose and link to strategy	Operation and Maximum
Chairman's fee	To attract and retain a high calibre individual with the requisite experience and knowledge.	The current fee is set out in the implementation of policy section of the Directors' Remuneration Report. There is no formal maximum. Fees are reviewed on a periodic basis against those in similar sized companies to ensure they remain competitive and adequately reflect the time commitments and scope of the role. Any increase in fee levels may be above that of the wider workforce in a particular year to reflect the periodic nature of any review and/or any change in responsibilities/time commitments. The Chairman may also receive limited travel and/or hospitality related benefits in connection with the role. The Chairman may not receive any consultancy or other payments outside his fee.
Non-Executive Director fee	To attract and retain high calibre individuals with the requisite experience and knowledge.	The current fee levels are set out in the implementation of policy section of the Directors' Remuneration Report. There is no formal maximum. Fees are reviewed on a periodic basis against those in similar sized companies to ensure they remain competitive and adequately reflect the time commitments and scope of the role. A Board fee is paid to each non-Executive Director. Supplemental fees may be paid to the Senior Independent Director and for chairmanship and membership of Committees to recognize the additional time commitments and responsibilities of these roles. Any increase in fee levels may be above that of the wider workforce in a particular year to reflect the periodic nature of any review and/or any change in responsibilities/time commitments. If business needs arise, non-Executive Directors may also be engaged to provide limited consulting services outside their director responsibilities and receive fees for those services. Non-Executive Directors may also receive limited travel and/or hospitality related benefits in connection with the role.

Illustrations of Minimum, Expected, and Maximum remuneration for the Executive Director

Scenarios

The charts set out for illustrative purposes only, what annual remuneration the Company expects the Executive Director, Dr. David Zaccardelli, to obtain at minimum, expected and maximum achievement of performance targets with respect to the eleven-month period of his employment, commencing on February 1, 2020.

The assumptions used in the calculations are set out below:

Fixed base salary includes:

- base salary of $750,000 per annum, payable as $250,000 cash and $500,000 worth of restricted stock units (RSUs) issued, subject to the Company's Share Dealing Policy, under the Company's 2017 Incentive Plan based on the Fair Market Value of the RSUs (as defined in the Plan) on the date of issue; and
- benefits;

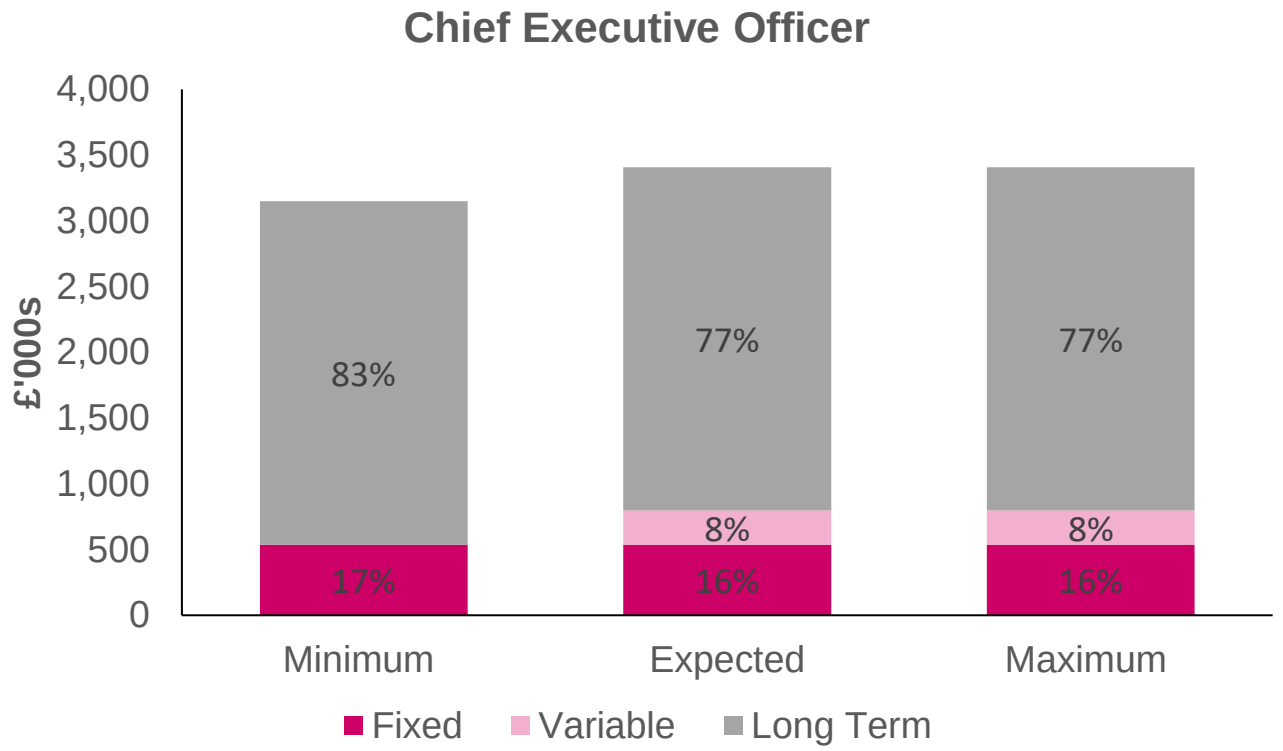
Minimum: this illustration assumes, pro-rated for the eleven month period, fixed base salary, as set out above, plus the contractual entitlement to receive, subject to shareholder approval at the Company's next Annual General

Meeting, such number of restricted stock units (RSUs) equivalent to 4% of the Company's issued share capital as a sign-on grant under the 2017 Incentive Plan. The value of the RSUs for this illustration is calculated according to the black-scholes valuation model. This illustration assumes no annual bonus;

Expected: this illustration assumes the Minimum remuneration set out above, plus an annual bonus, pro-rated for the eleven-month period. As there is no prior period to make an estimate of the Executive Director's annual bonus, we make the assumption that the Executive Director will receive the maximum annual bonus of 50% of base salary, being $343,750 for the eleven month period.

Maximum: this illustration assumes the Minimum remuneration set out above, plus the maximum annual bonus of 50% of base salary, being $343,750 for the eleven month period. This illustration assumes no additional grant is made under the 2017 Incentive Plan.

The Group has used the exchange rate 1.326752 the year end rate.



Statement of consideration of employees' pay and remuneration conditions elsewhere in the Group

The Company does not formally consult with employees when drawing up the Remuneration Policy. However, the Remuneration Committee is made aware of employment conditions in the wider Group. The same broad principles apply to the remuneration policy for both the Executive Director and the wider employee population. However, the remuneration for the Executive Director has a stronger emphasis on variable pay than for other employees. In particular, the following approach is used for the wider employee population in the Group:

- Salaries, benefits and pensions are compared to appropriate market rates and set at approximately mid-market level with allowance for role, responsibilities and experience.

- When setting salary levels for the Executive Director, the Committee considers the salary increases provided to other employees.

- An annual bonus plan is available to all employees and is based on business and individual performance.

Statement of consideration of Shareholders' views

The Remuneration Committee will consider any shareholder feedback received at the AGM and ongoing shareholder feedback throughout the year, when reviewing and applying the Remuneration Policy each year. The guidance from shareholder representative bodies is also considered on an ongoing basis. More specifically, the Committee will consult with major shareholders when proposing any significant changes to the Policy in the future.

Independent auditors' report to the members of Verona Pharma plc

Report on the audit of the financial statements

Opinion

In our opinion, Verona Pharma plc's group financial statements and parent company financial statements (the "financial statements"):

- give a true and fair view of the state of the group's and of the parent company's affairs as at 31 December 2019 and of the group's loss and the group's and the parent company's cash flows for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and, as regards the parent company's financial statements, as applied in accordance with the provisions of the Companies Act 2006; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements, included within the Annual Report and Accounts (the "Annual Report"), which comprise: the consolidated and company only statements of financial position as of December 31, 2019; the consolidated statement of comprehensive income, the consolidated and company only statements of cash flows and the consolidated and company only statements of changes in equity for the year then ended; and the notes to the financial statements, which include a description of the significant accounting policies.

Basis for opinion

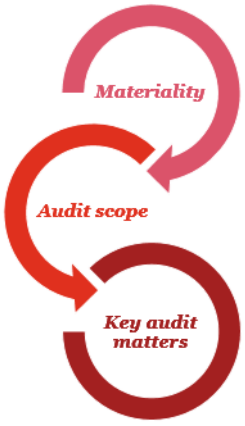
We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We remained independent of the group in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the FRC's Ethical Standard, as applicable to listed entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

Our audit approach

Overview



- Overall group materiality: £2.04 million (2018: £1.15 million), based on 5% of loss before tax less the impact of the annual revaluation of warrants.
- Overall parent company materiality: £1.94 million (2018: £1.09 million), based on 5% of loss before tax less the impact of the annual revaluation of warrants.

- We identified one significant component, Verona Pharma Plc, which in our view required a full scope audit based on its size.
- No component auditors supported the group audit team which conducted all necessary audit procedures.
- Verona Pharma plc represents 93% of group loss before tax and 98% of group total assets.

- Valuation of warrant liability (Group and Parent).
- Accounting for research and development expenditure (Group and Parent).
- Valuation of the assumed contingent liability (Group and Parent).

The scope of our audit

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements. In particular, we looked at where the directors made subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits we also addressed the risk of management override of internal controls, including evaluating whether there was evidence of bias by the directors that represented a risk of material misstatement due to fraud.

Key audit matters

Key audit matters are those matters that, in the auditors' professional judgement, were of most significance in the audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by the auditors, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. These matters, and any comments we make on the results of our procedures thereon, were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. This is not a complete list of all risks identified by our audit.

Key audit matter	***How our audit addressed the key audit matter***
Valuation of warrant liability (Group and Company) On 29 July 2016 Verona Pharma plc issued 12,401,262 units to new and existing shareholders. Each unit comprised of one Placing Share and one Warrant with an entitlement to subscribe for 0.4 of an Ordinary Share at a later date and the option to take a non-cash alternative which could result in a variable number of shares being issued. A financial liability of £895k is recorded in the financial statements reflecting the fair value of unexercised warrants as at 31 December 2019. Certain assumptions are used to determine the fair value of the Warrants at each financial year end. The key inputs to the calculation include: Volatility Expected term to exercise Current share price Our audit focussed on the risk that the fair value of the warrants could be misstated.	We used our internal specialists to make an independent assessment of the volatility and risk-free rate using externally derived data and observed these to be within a reasonable range. We agreed the term to exercise to the signed contract and verified the share price at 31 December 2019 to an external source. Using the Black-Scholes option pricing model we recalculated the value of each warrant using management's inputs with no difference identified.
Accounting for research and development expenditure (Group and Company) The majority of the £33.5m research and development expenditure arises through the Company outsourcing research to third-parties contract research organisations ("CROs"). At the year-end management are required to calculate the costs recognised based on the progress of the CRO contract versus the amounts billed to date. Due to the nature of the clinical trials and general research it is often difficult to estimate the length of time a particular trial is going to take. Outsourcing to CROs restricts visibility and the ability to monitor the progression of a piece of research, or a trial's stage of completion. As a result it can be difficult for Verona Pharma plc to measure what costs have been incurred in relation to a trial at a particular point in time and as such, based on billings received, whether project accruals and prepayments recorded are reasonably estimated. Our audit risk is focussed on whether the relevant expenditure has been appropriately included in the income statement and whether prepayments and accruals are appropriately calculated and recognised.	For a sample of project costs we obtained management's calculations of how the costs had been recognised as at 31 December 2019 verifying the mathematical calculation used. For the selected sample of project costs we obtained the underlying contracts and understood the basis on which management had recognised costs, assessing assumptions used. We obtained management's calculation of the accrual and prepayment position and verified the mathematical calculation. We sampled invoices detailed in management's calculation and tested back to the invoice and verified that the cost description in the invoice matched costs included in management's schedule. We verified the status of sampled projects with the relevant R&D project manager. For a sample of projects we contacted the relevant CRO to confirm the status of a specific item of the project to determine the stage of completion and verify that the charge recognised in the income statement and the prepayment or accrual amounts calculated are appropriate. We verified completeness of management's calculation of the accruals and prepayments position by testing a sample of invoices received pre year end to ensure that these had been included in management's calculations.
Valuation of the assumed contingent liability (Group and Company) On 19 September 2006 Verona Pharma plc acquired RhinoPharma Ltd which held contingent liabilities relating to future potential milestone and royalty payments due to Vernalis Pharmaceuticals Limited (now Ligand	Management have concluded that there is no triggering event in the year. We have independently evaluated this conclusion through consideration of the success of trials of Ensifentrine and whether these suggested a significant change in the expected development timeline or change in the overall probability of success as at 31 December 2019.

Key audit matter	*How our audit addressed the key audit matter*
Pharmaceuticals, Inc). Per IFRS 3 the existing contingent payments of the acquiree are an assumed liability of the buyer. Consequently, Verona Pharma plc fair valued the contingent liability on the date of acquisition and recorded it on the balance sheet. At each subsequent period end the liability is required to be re-measured when there is a change in success factors that would change the estimated future payments, such as an improved probability of success due to positive trial results. The contingent liability therefore requires annual re-assessment for any such triggering event. Our audit focussed on the risk that there has been a triggering event which would mean the estimated future payments should be reassessed. Re-measurements of this nature are complex and subject to significant management judgement. The carrying value of the contingent consideration was £1.1million at 31 December 2019.	We did not identify any changes in success factors as the company had not moved in to the next phase of clinical trials at year end and therefore agree with management's conclusion that no triggering event occurred during the year. During the year management elected to voluntarily change their accounting policy as regards how any subsequent remeasurements of the liability are treated. Previously the accounting policy was to expense this to the statement of comprehensive income. As a result of the change in policy remeasurements relating to changes in estimated cash flows and probabilities of success will now be recorded as movements in the associated IP R&D asset. We have verified that this accounting treatment is acceptable under IFRS and that the provisions of IAS 8 have been applied, including the restatement of comparative information to reflect the change in accounting policy.

How we tailored the audit scope

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the structure of the group and the parent company, the accounting processes and controls, and the industry in which they operate.

For each component in the scope of our group audit, we allocated a materiality that is less than our overall group materiality. For the one component in the scope of our group audit, Verona Pharma plc, we allocated a materiality of £1.94 million which is less than our overall group materiality.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £0.09 million (group audit) (2018: £0.06 million) and £0.09 million (parent company audit) (2018: £0.05 million) as well as misstatements below those amounts that, in our view, warranted reporting for qualitative reasons.

Materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

	Group financial statements	*Parent company financial statements*
Overall materiality	£2.04 million (2018: £1.15 million).	£1.94 million (2018: £1.09 million).
How we determined it	5% of loss before tax less the impact of the annual revaluation of warrants.	5% of loss before tax less the impact of the annual revaluation of warrants.
Rationale for benchmark applied	Based on the benchmarks used in the annual report, loss before tax is the primary measure used by the shareholders in assessing the financial performance of the group and is a generally accepted auditing benchmark. We have adjusted this to remove the impact of the annual revaluation of the fair value of warrants as this varies considerably each period being impacted by share price and volatility. As a result of this it can cause significant movements in the loss before tax. Although large in size this is a non-cash item which we assess would have limited impact on a user of the financial statements.	Based on the benchmarks used in the annual report, loss before tax is the primary measure used by the shareholders in assessing the financial performance of the parent company and is a generally accepted auditing benchmark. We have adjusted this to remove the impact of the annual revaluation of the fair value of warrants as this varies considerably each period being impacted by share price and volatility. As a result of this it can cause significant movements in the loss before tax. Although large in size this is a non-cash item which we assess would have limited impact on a user of the financial statements.

For each component in the scope of our group audit, we allocated a materiality that is less than our overall group materiality. For the one component in the scope of our group audit, Verona Pharma plc, we allocated a materiality of £1.94 million which is less than our overall group materiality.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £0.09 million (group audit) (2018: £0.06 million) and £0.09 million (parent company audit) (2018: £0.05 million) as well as misstatements below those amounts that, in our view, warranted reporting for qualitative reasons.

Conclusions relating to going concern

ISAs (UK) require us to report to you when:

- the directors' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the group's and parent company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

We have nothing to report in respect of the above matters.

However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the group's and parent company's ability to continue as a going concern. For example, the terms of the United Kingdom's withdrawal from the European Union are not clear, and it is difficult to evaluate all of the potential implications on the group's trade, customers, suppliers and the wider economy.

Reporting on other information

The other information comprises all of the information in the Annual Report other than the financial statements and our auditors' report thereon. The directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except to the extent otherwise explicitly stated in this report, any form of assurance thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

With respect to the Strategic Report and Directors' report, we also considered whether the disclosures required by the UK Companies Act 2006 have been included.

Based on the responsibilities described above and our work undertaken in the course of the audit, the Companies Act 2006 and ISAs (UK) require us also to report certain opinions and matters as described below.

Strategic Report and Directors' report

In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic Report and Directors' report for the year ended 31 December 2019 is consistent with the financial statements and has been prepared in accordance with applicable legal requirements.

In light of the knowledge and understanding of the group and parent company and their environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic Report and Directors' report.

Directors' Remuneration

In our opinion, the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006.

Responsibilities for the financial statements and the audit

Responsibilities of the directors for the financial statements

As explained more fully in the Statement of Directors' responsibilities set out on pages 22 to 23 , the directors are responsible for the preparation of the financial statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The directors are also responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the group's and the parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so.

Auditors' responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditors' report.

Use of this report

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

Other required reporting

Companies Act 2006 exception reporting

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

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- certain disclosures of directors' remuneration specified by law are not made; or
- the parent company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

Sam Taylor (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Reading
27 February 2020

VERONA PHARMA PLC
CONSOLIDATED STATEMENT OF COMPREHESIVE INCOME
FOR THE YEAR ENDED DECEMBER 31, 2019

	Notes	Year ended December 31, 2019	Year ended December 31, 2018
		£'000s	£'000s
Research and development costs		(33,476)	(19,294)
General and administrative costs		(7,607)	(6,297)
Operating loss	7	(41,083)	(25,591)
Finance income	9	2,351	2,783
Finance expense	9	(474)	(1,325)
Loss before taxation		(39,206)	(24,133)
Taxation — credit	10	7,265	4,232
Loss for the year		(31,941)	(19,901)
Other comprehensive income / (loss):			
Items that might be subsequently reclassified to profit or loss			
Exchange differences on translating foreign operations		(33)	38
Total comprehensive loss attributable to owners of the Company		(31,974)	(19,863)
Loss per ordinary share — basic and diluted (pence)	5	(30.3)	(18.9)

The accompanying notes form an integral part of these consolidated financial statements.

VERONA PHARMA PLC
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
AS OF DECEMBER 31, 2019

	Notes	As of December 31, 2019	Restated As of December 31, 2018
		£'000s	£'000s
ASSETS			
Non-current assets:			
Goodwill	11	441	441
Intangible assets	12	2,757	2,618
Property, plant and equipment	13	43	21
Right-of-use assets	14	971	—
Total non-current assets		4,212	3,080
Current assets:			
Prepayments and other receivables	15	2,770	2,463
Current tax receivable		7,396	4,499
Short term investments		7,823	44,919
Cash and cash equivalents		22,934	19,784
Total current assets		40,923	71,665
Total assets		45,135	74,745
EQUITY AND LIABILITIES			
Capital and reserves attributable to equity holders:			
Share capital	17	5,266	5,266
Share premium		118,862	118,862
Share-based payment reserve		10,364	7,923
Accumulated loss		(100,627)	(68,633)
Total equity		33,865	63,418
Current liabilities:			
Derivative financial instrument	19	895	2,492
Lease liability	14	460	—
Trade and other payables	20	8,261	7,733
Total current liabilities		9,616	10,225
Non-current liabilities:			
Assumed contingent obligation	21	1,103	996
Non-current lease liability	14	491	—
Deferred income		60	106
Total non-current liabilities		1,654	1,102
Total equity and liabilities		45,135	74,745

The accompanying notes form an integral part of these consolidated financial statements.

VERONA PHARMA PLC
COMPANY ONLY STATEMENT OF FINANCIAL POSITION
AS OF DECEMBER 31, 2019

	Notes	As of December 31, 2019	Restated As of December 31, 2018
		£'000s	£'000s
ASSETS			
Non-current assets:			
Goodwill	11	441	441
Intangible assets	12	2,757	2,618
Property, plant and equipment	13	43	21
Right-of-use asset	14	731	—
Investments	16	1,342	913
Total non-current assets		5,314	3,993
Current assets:			
Prepayments and other receivables	15	3,093	2,602
Current tax receivable		7,249	4,290
Short term investments		7,823	44,919
Cash and cash equivalents		22,823	19,596
Total current assets		40,988	71,407
Total assets		46,302	75,400
EQUITY AND LIABILITIES			
Capital and reserves attributable to equity holders:			
Share capital	17	5,266	5,266
Share premium		118,862	118,862
Share-based payment reserve		10,364	7,923
Accumulated loss		(100,259)	(68,514)
Total equity		34,233	63,537
Current liabilities:			
Derivative financial instrument	19	895	2,492
Lease Liability	14	335	—
Trade and other payables	20	9,256	8,269
Total current liabilities		10,486	10,761
Non-current liabilities:			
Assumed contingent liability	21	1,103	996
Non-current lease liability	14	419	—
Deferred income		61	106
Total non-current liabilities		1,583	1,102
Total equity and liabilities		46,302	75,400

The accompanying notes form an integral part of these consolidated financial statements.

The Parent has taken advantage of the exemption permitted by Section 408 of the Companies Act 2006 not to present an income statement for the year. The Parent Company's loss for the year was £31.7 million (2018: loss of £19.9 million), which has been included in the Group’s income statement.

The financial statements on pages 58 to 101 were approved by the Company's board of directors on February 27, 2020 and signed on its behalf by Dr. David Zaccardelli, Chief Executive Officer of the Company.

Dr. David Zaccardelli
Chief Executive Officer of the Company.
Company number: 05375156

VERONA PHARMA PLC
CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED DECEMBER 31, 2019

	Share Capital	Share Premium	Share-based Payment Reserve	Total Accumulated Losses	Total Equity
	£'000s	£'000s	£'000s	£'000s	£'000s
Balance at January 1, 2018, as previously reported	5,251	118,862	5,022	(49,254)	79,881
Impact of change in accounting policy	—	—	—	484	484
Balance at January 1, 2018 (Restated)	5,251	118,862	5,022	(48,770)	80,365
Loss for the year	—	—	—	(19,901)	(19,901)
Other comprehensive income for the year:					
Exchange differences on translating foreign operations	—	—	—	38	38
Total comprehensive loss for the year	—	—	—	(19,863)	(19,863)
New share capital issued	15	—	—	—	15
Share-based payments	—	—	2,901	—	2,901
Balance at December 31, 2018 (Restated)	5,266	118,862	7,923	(68,633)	63,418
Balance at January 1, 2019	5,266	118,862	7,923	(68,633)	63,418
Impact of change in accounting policy	—	—	—	(20)	(20)
Adjusted Balance at January 1, 2019	5,266	118,862	7,923	(68,653)	63,398
Loss for the year	—	—	—	(31,941)	(31,941)
Other comprehensive loss for the year:					
Exchange differences on translating foreign operations	—	—	—	(33)	(33)
Total comprehensive loss for the year	—	—	—	(31,974)	(31,974)
Share-based payments	—	—	2,441	—	2,441
Balance at December 31, 2019	5,266	118,862	10,364	(100,627)	33,865

The currency translation reserve for 2018 and 2019 is not considered material and as such is not presented in a separate reserve but is included in the total accumulated losses reserve.

VERONA PHARMA PLC
COMPANY ONLY STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED DECEMBER 31, 2019

	Share Capital	Share Premium	Share-based Payment Reserve	Total Accumulated Losses	Total Equity
	£'000s	£'000s	£'000s	£'000s	£'000s
Balance at January 1, 2018, as previously reported	5,251	118,862	5,022	(49,084)	80,051
Impact of change in accounting policy	—	—	—	484	484
Balance at January 1, 2018 (Restated)	5,251	118,862	5,022	(48,600)	80,535
Loss for the year	—	—	—	(19,914)	(19,914)
Other comprehensive income for the year:					
Total comprehensive loss for the year	—	—	—	(19,914)	(19,914)
New share capital issued	15	—	—	—	15
Share-based payments recognized as an expense	—	—	2,865	—	2,865
Share-based payments recognized as an investment	—	—	36	—	36
Balance at December 31, 2018 (Restated)	5,266	118,862	7,923	(68,514)	63,537
Balance at January 1, 2019	5,266	118,862	7,923	(68,514)	63,537
Impact of change in accounting policy	—	—	—	(20)	(20)
Adjusted Balance at January 1, 2019	5,266	118,862	7,923	(68,534)	63,517
Loss for the year	—	—	—	(31,725)	(31,725)
Other comprehensive income for the year:					
Total comprehensive loss for the year	—	—	—	(31,725)	(31,725)
Share-based payments recognized as an expense	—	—	2,012	—	2,012
Share-based payments recognized as an investment	—	—	429	—	429
Balance at December 31, 2019	5,266	118,862	10,364	(100,259)	34,233

VERONA PHARMA PLC
CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2019

	Year ended December 31, 2019	Year ended December 31, 2018
	£'000s	£'000s
Cash used in operating activities:		
Loss before taxation	(39,206)	(24,133)
Finance income	(2,351)	(2,783)
Finance expense	474	1,325
Share-based payment charge	2,441	2,901
Increase in prepayments and other receivables	(484)	(640)
Increase in trade and other payables	449	531
Depreciation of property, plant, equipment and right of use asset	398	8
Unrealised FX gains / losses	(8)	—
Amortization of intangible assets	106	90
Cash used in operating activities	(38,181)	(22,701)
Cash inflow from taxation	4,361	4,590
Net cash used in operating activities	(33,820)	(18,111)
Cash flow from investing activities:		
Interest received	887	883
Purchase of plant and equipment	(38)	(13)
Payment for patents and computer software	(244)	(255)
Purchase of short term investments	(7,940)	(59,700)
Maturity of short term investments	45,134	64,366
Net cash generated from investing activities	37,799	5,281
Cash flow used in financing activities:		
Repayment of finance lease liabilities	(426)	—
Net cash used in financing activities	(426)	—
Net increase / (decrease) in cash and cash equivalents	3,553	(12,830)
Cash and cash equivalents at the beginning of the year	19,784	31,443
Effect of exchange rates on cash and cash equivalents	(403)	1,171
Cash and cash equivalents at the end of the year	22,934	19,784

VERONA PHARMA PLC
COMPANY ONLY STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2019

	Year ended December 31, 2019	Year ended December 31, 2018
	£'000s	£'000s
Cash used in operating activities:		
Loss before taxation	(39,046)	(24,191)
Finance income	(2,351)	(2,783)
Finance expense	463	1,325
Share-based payment charge	2,012	2,865
Increase in prepayments and other receivables	(624)	(654)
Increase in trade and other payables	935	164
Depreciation of property, plant, equipment and right of use asset	329	8
Unrealised FX gains/ losses	(5)	—
Amortization of intangible assets	105	90
Cash used in operating activities	(38,182)	(23,176)
Cash inflow from taxation	4,361	4,992
Net cash used in operating activities	(33,821)	(18,184)
Cash flow from investing activities:		
Interest received	887	883
Purchase of plant and equipment	(38)	(13)
Payment for patents and computer software	(244)	(255)
Purchase of short term investments	(7,940)	(59,700)
Maturity of short term investments	45,134	64,366
Net cash generated from investing activities	37,799	5,281
Cash flow used in financing activities:		
Gross proceeds from issue of shares and warrants	—	15
Repayment of finance lease liabilities	(348)	—
Net cash (used in) / generated from financing activities	(348)	15
Net increase / (decrease) in cash and cash equivalents	3,630	(12,888)
Cash and cash equivalents at the beginning of the year	19,596	31,313
Effect of exchange rates on cash and cash equivalents	(403)	1,171
Cash and cash equivalents at the end of the year	22,823	19,596

1. General information

Verona Pharma plc (the Company") and its subsidiaries (together the "Group") are a clinical-stage biopharmaceutical group focused on developing and commercializing innovative therapeutics for the treatment of respiratory diseases with significant unmet medical needs.

The Company is a public limited company, which is dual listed on the AIM, a market of the London Stock Exchange, and The Nasdaq Global Market ("Nasdaq"). The company is incorporated and domiciled in the United Kingdom. The address of the registered office is 1 Central Square, Cardiff, CF10 1FS, United Kingdom.

The Company has two subsidiaries, Verona Pharma Inc. and Rhinopharma Limited ("Rhinopharma"), both of which are wholly owned.

The Company listed its American Depositary Shares ("ADS") on Nasdaq in April 2017 ("the 2017 Global Offering").

The ADSs trade on The Nasdaq the symbol “VRNA” and Verona Pharma’s ordinary shares trade on AIM under the symbol “VRP”.

2. Accounting policies

A summary of the principal accounting policies, all of which have been applied consistently throughout the year, is set out below.

2.1 Basis of preparation

The consolidated financial statements of the Group and the financial statements of the Company have been prepared in accordance with International Financial Reporting Standards ("IFRSs") as issued by the International Accounting Standards Board and IFRS Interpretations Committee applicable to companies reporting under IFRS.

The consolidated financial statements of the Group and the financial statements of the Company have been prepared under the historical cost convention, with the exception of derivative financial instruments which have been measured at fair value.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Group’s and Company's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in note 4.

Going concern

The Group has incurred recurring losses since inception, including net losses of £31.9 million, £19.9 million and £20.5 million for the years ended December 31, 2019, 2018 and 2017, respectively. In addition, as of December 31, 2019, the Group had an accumulated loss of £100.6 million. The Group expects to continue to generate operating losses for the foreseeable future. As of the issuance date of the annual consolidated financial statements, the Group expects that its cash and cash equivalents, would be sufficient to fund its operating expenses and capital expenditure requirements for at least 12 months from the issuance date of these annual consolidated financial statements. Accordingly, the consolidated financial statements have been prepared on a basis that assumes the Group will continue as a going concern and which contemplates the realization of assets and satisfaction of liabilities and commitments in the ordinary course of business.

2.1 Basis of preparation (continued)

The Group intends to initiate its Phase 3 program for the maintenance treatment of COPD once it believes it has alignment with the FDA on its planned design for the Phase 3 clinical program. The Group will require significant additional funding to initiate and complete this Phase 3 program and will need to secure the required capital to fund the program. The Group will seek additional funding through public or private financings, debt financing, collaboration or licensing agreements and other arrangements. However, there is no guarantee that the Group will be successful in securing additional finance on acceptable terms, or at all, and should the Group be unable to raise sufficient additional funds it will be required to defer the initiation of Phase 3 clinical trials, until such funding can be obtained. This could also force the Group to delay, reduce or eliminate some or all of its research and development programs, product portfolio expansion or commercialization efforts, or pursue alternative development strategies that differ significantly from its current strategy, which could have a material adverse effect on the Group's business, results of operations and financial condition.

Business combination

The Group applies the acquisition method to account for business combinations. The consideration transferred for the acquisition of a subsidiary is the fair value of the assets transferred, the liabilities incurred to the former owners of the acquiree and the equity interests issued by the Group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. Goodwill arising on acquisitions is capitalized and is subject to an impairment review, both annually and when there are indications that the carrying value may not be recoverable.

Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. Acquisition-related costs are expensed as incurred and included in administrative expenses.

Basis of consolidation

These consolidated financial statements include the financial statements of Verona Pharma plc and its wholly owned subsidiaries Verona Pharma, Inc. and Rhinopharma. The acquisition method of accounting was used to account for the acquisition of Rhinopharma.

Inter-company transactions, balances and unrealized gains on transactions between group companies are eliminated.

Verona Pharma Inc. and Rhinopharma adopt the same accounting policies as the Group.

2.2 Foreign currency translation

Items included in the Group's consolidated financial statements are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The consolidated financial statements are presented in pounds sterling ("£"), which is the functional and presentational currency of the Group.

Transactions in foreign currencies are recorded using the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated using the rate of exchange ruling at the balance sheet date and the gains or losses on translation are included in the Consolidated Statement of Comprehensive Income. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the original transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

The assets and liabilities of foreign operations are translated into pounds sterling at the rate of exchange ruling at the balance sheet date. Income and expenses are translated at weighted average exchange rates for the period. The exchange differences arising on translation for consolidation are recognized in Other Comprehensive Income.

2.3 Cash and cash equivalents

Cash and cash equivalents includes cash in hand, deposits held at call with banks and other short-term highly liquid investments with original maturities of three months or less.

2.4 Deferred taxation

Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred tax is determined using tax rates and laws that have been enacted or substantially enacted by the balance sheet date and expected to apply when the related deferred tax is realized or the deferred liability is settled.

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

2.5 Research and development costs

Capitalization of expenditure on product development commences from the point at which technical feasibility and commercial viability of the product can be demonstrated and the Group is satisfied that it is probable that future economic benefits will result from the product once completed. No such costs have been capitalized to date.

Expenditure on research and development activities that do not meet the above criteria is charged to the Consolidated Statement of Comprehensive Income as incurred.

2.6 Property, plant and equipment

Property, plant and equipment are stated at cost, net of depreciation and any provision for impairment. Cost includes the original purchase price of the asset and the costs attributable to bringing the asset to its working condition for its intended use. Depreciation is calculated to write off the cost less their estimated residual values, on a straight-line basis over the expected useful economic lives of the assets concerned. The principal annual periods used for this purpose are:

Computer hardware	3 years

2.7 Intangible assets and goodwill

(a) Goodwill

Goodwill arises on the acquisition of subsidiaries and represents the excess of the consideration transferred over the fair value of the identifiable net assets acquired.

(b) Patents

Patent costs associated with the preparation, filing, and obtaining of patents are capitalized and amortized on a straight-line basis over the estimated useful lives of ten years.

(c) Computer software

Amortization is calculated so as to write off the cost less estimated residual values, on a straight-line basis over the expected useful economic life of two years.

(d) In-process research & development ("IP R&D")

The IP R&D asset acquired through a business combination, that had not reached technical feasibility, was initially recognized at fair value. Subsequent movements in the assumed contingent liability (see 2.12) that relate to changes in estimated cashflows or probabilities of success are recognized as additions to the IP R&D asset that it relates to. There were no changes in estimated cashflows or probabilities of success in the years ended 31 December, 2019, or 2018.

This is a change in accounting policy as prior to January 1, 2019 movements in the assumed contingent liability were taken to the Statement of Comprehensive Income (see note 2.18). As a result of the change in accounting policy £484 thousand was restated from Accumulated Loss to the IP R&D asset.

The asset is subject to impairment testing until completion, abandonment of the project or when the research findings are commercialized through a revenue generating project. The Group determines whether intangible assets are impaired on an annual basis or when there is an indication of impairment.

2.8 Impairment of intangible assets, goodwill and non-financial assets

The Group holds intangible assets relating to acquired IP R&D, patent costs and goodwill. Goodwill and intangible assets are tested annually for impairment or if there is an indication of impairment. The Group is a single cash generating unit ("CGU") so all intangibles are allocated to the Group as one CGU.

As at 31 December, 2019, and 2018 the Group carried out impairment reviews with reference to its market capitalization. At points during the year ended 31 December 2019, the Group's market capitalization was less than its net assets. As a result, the Group carried out an impairment review by forecasting expected sales of ensifentrine, delivered by nebulizer for the maintenance treatment of chronic COPD, and associated costs. This cashflow forecast was then discounted to its net present value to demonstrate that the value in use of the ensifentrine was greater than the Group's net assets. The Group was required to make various estimates and assumptions as inputs for this model including, but not limited to:

- market size and product acceptance by clinicians, patients and reimbursement bodies;
- gross and net selling price;
- costs of manufacturing, product distribution and marketing support;
- costs of the Group's overhead;
- size and make up of a sales force;
- probabilities of success; and
- discount rate.

2.9 Employee Benefits

(a) Pension

The Group operates defined contribution pension schemes for its employees. Contributions payable for the year are charged to the Consolidated Statement of Comprehensive Income. The Group has no further liability once the contributions have been paid.

(b) Bonus plans

The Group recognizes a liability and an expense for bonus plans if contractually obligated or if there is a past practice that has created a constructive liability.

2.10 Share-based payments

The Group operates a number of equity-settled, share-based compensation schemes. The fair value of share based payments is determined using the Black-Scholes model and requires several assumptions and estimates as disclosed in note 18.

The fair value of share-based payments under these schemes is expensed on a straight-line basis over the share based payments' vesting periods, based on the Group's estimate of shares that will eventually vest.

2.11 Provisions

Provisions are recognized when the Group has a present legal or constructive liability as a result of past events, it is probable that an outflow of resources will be required to settle the liability, and the amount can be reliably estimated. Provisions are measured at the present value of the expenditures expected to be required to settle the liability using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability.

2.12 Assumed contingent liability related to the business combination

In 2006 the Group acquired Rhinopharma and assumed contingent liabilities owed to Vernalis Pharmaceuticals Limited which was subsequently acquired by Ligand Pharmaceuticals, Inc. (“Ligand”). The Group refers to the assignment and license agreement as the Ligand Agreement.

Ligand assigned to the Group all of its rights to certain patents and patent applications relating to ensifentrine and related compounds (the "Ligand Patents") and an exclusive, worldwide, royalty-bearing license under certain Ligand know-how to develop, manufacture and commercialize products (the "Licensed Products") developed using Ligand Patents, Ligand know-how and the physical stock of certain compounds.

The assumed contingent liability comprises a milestone payment on obtaining the first approval of any regulatory authority for the commercialization of a Licensed Product, low to mid-single digit royalties based on the future sales performance of all Licensed Products and a portion equal to a mid-twenty percent of any consideration received from any sub-licensees for the Ligand Patents and for Ligand know-how.

The liability was initially recognized at fair value and subsequently measured at amortized cost. The assumed contingent liability is estimated as the expected value of the milestone payment and royalty payments. This expected value is based on estimated future royalties payable, derived from sales forecasts, and an assessment of the probability of success using standard market probabilities for respiratory drug development. The risk-weighted value of the assumed contingent arrangement is discounted back to its net present value applying an effective interest rate of 12%.

Royalties payable are based on the future sales performance so the amount payable is unlimited. Sales that may be achieved are difficult to predict and subject to estimate, which is inherently uncertain.

2.12 Assumed contingent liability related to the business combination (continued)

The assumed contingent liability is accounted for as a liability and its value is measured at amortized cost using the effective interest rate method, and is re-measured for changes in estimated cash flows or when the probability of success changes.

Remeasurements relating to changes in estimated cash flows and probabilities of success are recognized in the IP R&D asset it relates to ("see 2.7"). This is a change in accounting policy for the year ended December 1, 2019 (see 2.18). The unwind of the discount is recognized in finance expense.

2.13 Financial instruments — initial recognition and subsequent measurement

The Group classifies a financial instrument, or its component parts, as a financial liability, a financial asset or an equity instrument in accordance with the substance of the contractual arrangement and the definitions of a financial liability, a financial asset and an equity instrument.

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

(a) Financial assets, initial recognition and measurement and subsequent measurement

The Group has no financial assets recorded at fair value through profit or loss ("FVPTL"). All assets are initially recognized initially at fair value plus transaction costs and subsequently measured at amortized cost using the effective interest method.

(b) Financial liabilities, initial recognition and measurement and subsequent measurement

Financial liabilities are classified as measured at amortized cost or FVTPL.

The Group's warrants are classified as FVTPL and fair value gains and losses are recognized in profit or loss.

Other financial liabilities are initially recognized at fair value and subsequently measured at amortized cost using the effective interest method. Interest expense and foreign exchange gains and losses are recognized in profit or loss. Any gain or loss on derecognition is also recognized in profit or loss.

The Group's financial liabilities include trade and other payables, the Group’s warrants and the assumed contingent liability.

(c) Derivative financial instruments

Derivatives are initially recognized at fair value on the date a derivative contract is entered into and are subsequently re-measured at fair value at the end of each reporting date. The Group holds one type of derivative financial instrument, the warrants, as explained in Note 2.14.

The full fair value of the derivative is classified as a non-current liability when the warrants are exercisable in more than 12 months and as a current liability when the warrants are exercisable in less than 12 months.

Changes in fair value of a derivative financial liability when related to a financing arrangement are recognized in the Consolidated Statement of Comprehensive Income within Finance Income or Finance Expense.

2.14 Derivative financial instrument - warrants

Warrants issued by the Group to investors as part of a share subscription are compound financial instruments where the warrant meets the definition of a financial liability.

The financial liability component is initially measured at fair value in the Consolidated Statement of Financial Position. Equity is measured at the residual between the subscription price for the entire instrument and the liability component. The financial liability component is remeasured. Equity is not remeasured.

2.15 Short Term Investments

Short term investments include fixed term deposits held at banks with original maturities between three months and a year. They are classified as loans and receivables and are measured at amortized cost using the effective interest method.

2.16 Transaction costs

Qualifying transaction costs might be incurred in anticipation of an issuance of equity instruments and may cross reporting periods. The entity defers these costs on the balance sheet until the equity instrument is recognized. Deferred costs are subsequently reclassified as a deduction from equity when the equity instruments are recognized, as the costs are directly attributable to the equity transaction. If the equity instruments are not subsequently issued, the transaction costs are expensed. Any costs not directly attributable to the equity transaction are expensed.

Transaction costs that relate to the issue of a compound financial instrument are allocated to the liability and equity components of the instrument in proportion to the allocation of proceeds. Where the liability component is held at fair value through profit or loss, the transaction costs are expensed to the Consolidated Statement of Comprehensive Income. For liabilities held at amortized cost, transaction costs are deducted from the liability and subsequently amortized. The amount of transaction costs accounted for as a deduction from equity in the period is disclosed separately in accordance with International Accounting Standard (“IAS 1”).

2.17 Investments in subsidiaries

Investments in subsidiaries are shown at cost less any provision for impairment.

2.18 Changes in accounting policy

Accounting for the assumed contingent liability

As discussed in note 2.12, in 2006 the Group acquired Rhinopharma and assumed contingent liabilities owed to Vernalis Pharmaceuticals Limited which was subsequently acquired by Ligand Pharmaceuticals, Inc. ("Ligand").

Ligand assigned to the Group all of its rights to certain patents and patent applications relating to ensifentrine and related compounds and an exclusive, worldwide, royalty-bearing license to develop, manufacture and commercialize products. The assumed contingent liability comprises a milestone payment on obtaining the first approval of any regulatory authority and royalties based on the future sales of ensifentrine.

The initial fair value of the assumed contingent liability was estimated as the expected value of the milestone payment and royalty payments. This expected value is based on estimated future royalties payable, derived from sales forecasts, an assessment of the probability of success using standard market probabilities for respiratory drug development discounted to net present value applying an effective interest rate of 12%.

The assumed contingent liability is accounted for as a liability and its value is measured at amortized cost using the effective interest rate method, and is re-measured for changes in estimated cash flows or when the probability of success changes.

2.18 Changes in accounting policy (continued)

Up to the year ended December 31, 2018, movements in the liability relating to re-measurements of cash flows or changes in the probabilities of success were taken to the Consolidated Statement of Comprehensive Income. During the year ended December 31, 2019, the Company reviewed the accounting for this item and has determined that these movements in the liability will now be recognized in the cost of the corresponding asset. The corresponding asset is the intangible IP R&D asset.

The Group believes that this change in accounting policy results in the Consolidated Financial Statements providing a more relevant and reliable view of its financial position and performance because without an adjustment to the IP R&D asset on the re-measurement of the liability, the cost of the asset would not be fairly reflected on the Consolidated Statement of Financial Position. The Consolidated Statement of Financial Position more faithfully represents the financial position of the Group if the intangible asset is adjusted by any re-measurement of the liability for changes in estimated cash flows, to give a fairer reflection of the cost of the intangible asset.

The Group has reviewed the International Financial Reporting Interpretations Committee ("IFRIC") discussion of accounting for variable payments made for the purchase of an intangible asset that is not part of a business combination that concluded that it was too broad for it to address within the confines of existing IFRS standards. As a result, practice in this area is mixed and many pharmaceutical companies follow a cost accumulation model. The Group also noted that adjusting the cost of the asset when a liability is remeasured for changes in estimated cash flows is consistent with the guidance in IFRIC 1 for decommissioning liabilities and IFRS 16 for lease liabilities.

There were no such re-measurements of the liability in the years ended December 31, 2019, 2018 and 2017. Movements in the liability in these periods related to the unwinding of the discount and movements in exchange rates.

IAS 8 requires the opening balance of each affected component of equity to be adjusted for the earliest prior period presented and the other comparative amounts disclosed for each prior period presented as if the new accounting policy had always been applied.

The impact to the Group, therefore, is the restatement of £484 thousand from Accumulated Loss to the IP R&D asset, which relates to re-measurements recorded prior to January 1, 2017. As there were no re-measurements in the years ended December 31, 2019, 2018 and 2017 the £484 thousand adjustment is the same at each reporting period.

The following table is a summary of the restatement:

Financial statement line item	As reported	Adjustment for the change in accounting	As adjusted
January 1, 2017	**£'000s**	**£'000s**	**£'000s**
Accumulated loss	28,728	(484)	28,244
Intangible assets - IP R&D	1,469	484	1,953

This adjustment also increases non-current assets, total assets and total equity by £484 thousand in each of the years presented.

2.18 Changes in accounting policy (continued)

Adoption of IFRS 16

IFRS 16 'Leases' is effective for accounting periods beginning on or after January 1, 2019 and replaces IAS 17 'Leases'. It eliminates the classification of leases as either operating leases or finance leases and, instead, introduces a single lessee accounting model. The adoption of IFRS 16 resulted in the Group recognizing lease liabilities within current liabilities, and corresponding right-of-use assets.

The Group's principal lease arrangements are for office space. The Group has adopted IFRS 16 retrospectively with the cumulative effect of initially applying the standard as an adjustment to the opening balance of retained earnings at January 1, 2019. The standard permits a choice on initial adoption, on a lease-by-lease basis, to measure the right-of-use asset at either its carrying amount as if IFRS 16 had been applied since the commencement of the lease, or an amount equal to the lease liability, adjusted for any accrued or prepaid lease payments as at the time of adoption. The Group has elected to measure the right-of-use asset at its carrying value as if IFRS 16 had been applied since the commencement of the lease, with the result of a £20 thousand reduction in opening total accumulated losses.

Initial adoption resulted in the recognition of right-of-use assets of £326 thousand and lease liabilities of £316 thousand.

	£'000s
Lease commitments (including prepayments) disclosed as at December 31, 2018	600
Less: adjustments relating to prepaid lease payments	(28)
Lease commitments as at December 31, 2018	572
Discounted using the group's incremental borrowing rate	526
Less: short-term leases recognized on a straight-line basis as expense	(210)
Lease liability recognized as at January 1, 2019	316

In applying IFRS 16 for the first time, the group has used the following practical expedients permitted by the standard:

- the use of a single discount rate of 8% to a portfolio of leases with reasonably similar characteristics;
- accounting for leases with a remaining lease term of less than 12 months as at January 1, 2019, as short-term leases; and
- the use of hindsight in determining the lease term where the contract contains options to extend or terminate the lease.

The Group is applying IFRS 16's low-value and short-term exemptions. The adoption of IFRS 16 has had no impact on the Group's net cash flows, although a presentation change has been reflected in 2019 whereby cash outflows of £426 thousand are now presented as financing, instead of operating. General and administrative costs are £123 thousand lower than if IFRS 16 not been adopted, as depreciation of the right of use asset is less than the lease costs. There is a £50 thousand increase in finance expense from the presentation of a portion of lease costs as interest costs. There is no significant impact on overall loss before tax and loss per share.

At the time of adoption it was not reasonably certain that the Group would extend the leases. However, in the period the Group determined that this was the case and agreed extensions. As a result it recognized an additional liability and right-of-use asset of £1,047 thousand.

2.19 New standards, amendments and interpretations adopted by the Group

The following standard has been adopted by the Group for the first time for the financial year beginning on or after January 1, 2019:

- IFRS 16 "Leases"

The Group adopted IFRS 16 on January 1, 2019, and, as a consequence, changed its accounting policies. See note 2.18.

2.20 New standards, amendments and interpretations issued but not effective for the financial year beginning January 1, 2019 and not early adopted

There are no IFRS standards or interpretations not yet effective that would be expected to have a material impact on the Group.

3. Financial Instruments

3.1 Financial Risk Factors

The Group's activities have exposed it to a variety of financial risks: market risk (including currency risk and interest rate risk), credit risk, and liquidity risk. The Group's overall risk management program is focused on preservation of capital and the unpredictability of financial markets and has sought to minimize potential adverse effects on the Group's financial performance and position.

(a) Currency risk

Foreign currency risk reflects the risk that the Group's net assets will be negatively impacted due to fluctuations in exchange rates. The Group has not entered into foreign exchange contracts to hedge against gains or losses from foreign exchange fluctuations.

The summary data about the Group's exposure to currency risk is as follows. Figures are the pound sterling values of balances in each currency:

	December 31, 2019			December 31, 2018		
	GBP	USD	EUR	GBP	USD	EUR
	£'000s	£'000s	£'000s	£'000s	£'000s	£'000s
Cash and cash equivalents	18,517	4,399	18	11,293	8,470	21
Short term Investments	6,316	1,507	—	19,850	25,069	—
Trade and other payables	3,226	4,306	728	2,872	4,329	532

Sensitivity Analysis

A reasonably possible strengthening or weakening of the Euro or U.S. dollar against pounds sterling as of December 31, 2019 and 2018 would have affected the measurement of the financial instruments denominated in a foreign currency (excluding the assumed contingent liability).

The following table shows how a movement in a currency would give rise to a profit or (loss) and a corresponding entry in equity.

3.1 Financial Risk Factors (continued)

	Profit or loss and equity	
	Strengthening	Weakening
December 31, 2019	**£'000s**	**£'000s**
EUR (5% movement)	(36)	36
USD (5% Movement)	80	(80)
December 31, 2018	**£'000s**	**£'000s**
EUR (5% movement)	(26)	26
USD (5% Movement)	1,461	(1,461)

Foreign currency denominated trade payables are short term in nature (generally 30 to 45 days). The Group has a U.S. operation, the net assets of which are exposed to foreign currency translation risk.

Estimated cashflows relating to the assumed contingent liability are predominantly denominated in US dollars. In the years ended December 31, 2019, and 2018, movements in foreign exchange rates were not material and no sensitivity analysis is therefore provided.

(b) Credit risk

Credit risk reflects the risk that the Group may be unable to recover contractual receivables. As the Group is still in the development stage no policies are currently required to mitigate this risk.

For banks and financial institutions, only independently rated parties with a minimum rating of "B+" are accepted. The Directors recognize that this is an area in which they may need to develop specific policies should the Group become exposed to further financial risks as the business develops.

As of December 31, 2019, and December 31, 2018, cash and cash equivalents and short term investments were placed at the following banks:

Cash and Cash Equivalents	**Year ended December 31, 2019**	**Credit rating**	**Year ended December 31, 2018**	**Credit rating**
	£'000		**£'000**	
Banks				
Royal Bank of Scotland	1	A1	150	A1
Lloyds Bank	8,355	Aa3	15,862	Aa3
Citibank	6,529	Aa3	3,135	A1
Barclays	1,968	A1	449	A2
Wells Fargo	111	Aa1	188	Aa1
Close Brothers	5,970	Aa3	—	—
Total	22,934		19,784	

3.1 Financial Risk Factors (continued)

Short Term Investments	Year ended December 31, 2019	Credit rating	Year ended December 31, 2018	Credit rating
	£'000		£'000	
Banks				
Royal Bank of Scotland	5,616	A1	9,186	A1
Lloyds Bank	—	Aa3	1,567	Aa3
Standard Chartered	—	A1	15,450	A1
Citibank	—	Aa3	7,053	A1
Barclays	2,207	A1	11,663	A2
Total	7,823		44,919	

(c) Management of capital

The Group considers capital to be its equity reserves. At the current stage of the Group's life cycle, the Group's objective in managing its capital is to ensure funds raised meet the research and operating requirements until the next development stage of the Group 's suite of projects.

The Group ensures it is meeting its objectives by reviewing its Key Performance Indicators to ensure the research activities are progressing in line with expectations, costs are controlled and unused funds are placed on deposit to conserve resources and increase returns on surplus cash held.

(d) Interest rate risk

As of December 31, 2019, the Group had cash deposits of £22.9 million (2018: £19.8 million) and short term investments of £7.8 million (2018: £44.9 million). The rates of interest received during 2019 ranged between 0.0% and 2.87%. A 0.25% increase in interest rates would not have a material impact on finance income. The Group's exposure to interest rate risk, which is the risk that the interest received will fluctuate as a result of changes in market interest rates on classes of financial assets and financial liabilities, was as follows:

	December 31, 2019		December 31, 2018	
	Floating interest rate	Fixed interest rate	Floating interest rate	Fixed interest rate
	£'000s	£'000s	£'000s	£'000s
Financial asset				
Cash deposits	10,006	12,928	15,082	4,702
Short Term Investments	—	7,823	—	44,919
Total	10,006	20,751	15,082	49,621

(e) Liquidity risk

The Group periodically prepares working capital forecasts for the foreseeable future, allowing an assessment of the cash requirements of the Group, to manage liquidity risk. The following table provides an analysis of the Com Group's financial liabilities. The carrying value of all balances approximates to their fair value. The Group's maturity analysis for the derivative financial instrument from the issue of warrants is given in note 19.

3.1 Financial Risk Factors (continued)

	LESS THAN 1 YEAR	BETWEEN 1 AND 2 YEARS	BETWEEN 2 AND 5 YEARS	OVER 5 YEARS
	£'000s	£'000s	£'000s	£'000s
At December 31, 2019				
Trade payables	1,455	—	—	—
Accruals	6,806	—	—	—
Lease liability[2]	476	557	—	—
Assumed contingent liability[1]	—	—	—	1,807
Total	8,737	557	—	1,807

(1) This table includes the undiscounted amount of the assumed contingent liability. See note 21.

(2) This table includes the undiscounted amount of the finance lease liability. See note 2.18.

	LESS THAN 1 YEAR	BETWEEN 1 AND 2 YEARS	BETWEEN 2 AND 5 YEARS	OVER 5 YEARS
	£'000s	£'000s	£'000s	£'000s
At December 31, 2018				
Trade payables	2,839	—	—	—
Other payables	12	—	—	—
Accruals	4,882	—	—	—
Assumed contingent liability[1]	—	—	—	1,807
Total	7,733	—	—	1,807

(1) This table includes the undiscounted amount of the assumed contingent liability. See note 21.

3.2 Fair value estimation

The carrying amounts of cash and cash equivalents, receivables, accounts payable and accrued liabilities approximate to fair value due to their short-term nature. The carrying amount of the assumed contingent liability approximates to fair value as the underlying assumptions are currently similar.

For financial instruments that are measured in the Consolidated Statement of Financial Position at fair value, IFRS 7 requires disclosure of fair value measurements by level of the following fair value measurement hierarchy:

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1);
- Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly or indirectly (level 2); and
- Inputs for the asset or liability that are not based on observable market data (level 3).

For the year ended December 31, 2019, and 2018, fair value adjustments to financial instruments measured at fair value through profit and loss resulted in the recognition of finance income of £1.6 million in 2019 and a finance loss of £1.2 million in 2018.

3.2 Fair value estimation (Continued)

The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques. These valuation techniques maximize the use of observable market data where it is available and rely as little as possible on entity specific estimates. If all significant inputs required to ascertain the fair value of an instrument are observable, the instrument is included in level 2. If one or more of the significant inputs are not based on observable market data, the instrument is included in level 3.

	Level 3	Total
	£'000s	£'000s
At December 31, 2019		
Derivative financial instrument	895	895
Total	895	895

Movements in Level 3 items during the years ended December 31, 2019, and 2018 are as follows:

Derivative financial instrument	2019	2018
	£'000s	£'000s
At January 1	2,492	1,273
Fair value adjustments recognized in profit and loss	(1,597)	1,219
At December 31	895	2,492

Further details relating to the derivative financial instrument are set out in notes 4 and 19 of these financial statements.

In determining the fair value of the derivative financial instrument, the Group applied the Black Scholes model; key inputs include the share price at reporting date, estimations on timelines, volatility and risk-free rates. These assumptions and the impact of changes in these assumptions, where material, are disclosed in note 19.

3.3 Change in liabilities arising from financing activities

The Group has provided a reconciliation so that changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes can be evaluated.

	2019
	Derivative financial instrument
	£'000s
At January 1	2,492
Fair value adjustments - non cash	(1,597)
At December 31	895

See note 19 for information relating to the derivative financial instrument.

3.3 Change in liabilities arising from financing activities (continued)

	2019
	Lease liability
	£'000s
At January 1	316
Capitalization of rental leases - non cash	1,061
Payment of lease liability - cash	(426)
At December 31	951

See note 14 and note 2.18 for information relating to capitalized leases.

4. Critical accounting estimates and judgments

The preparation of financial statements in conformity with IFRS requires the use of accounting estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reporting period. Although these estimates are based on management's best knowledge of current events and actions, actual results ultimately may differ from those estimates. IFRS also requires management to exercise its judgment in the process of applying the Group's accounting policies.

The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are as follows:

(a) Assumed contingent liability

The Group has a material liability for the future payment of royalties and milestones associated with contractual liabilities on ensifentrine, acquired as part of the acquisition of Rhinopharma. The estimation of the amounts and timing of future cashflows requires the forecast of royalties payable and the estimation of the likelihood that the regulatory approval milestone will be achieved (see notes 2.12 and 21). The estimates for the assumed contingent liability are based on a discounted cash flow model. Key estimates included the calculation of deferred consideration are:

- development, regulatory and marketing risks associated with progressing the product to market approval in key target territories;
- market size and product acceptance by clinicians, patients and reimbursement bodies;
- gross and net selling price;
- launch of competitive products;
- probabilities of success; and
- time to crystallization of contingent consideration.

4. Critical accounting estimates and judgments (continued)

When there is a change in the expected cash flows or probabilities of success, the assumed contingent liability is re-measured with the change in value recognized in the IP R&D asset it relates to. This is a change in accounting policy for the year ended December 1, 2019, (see 2.18). The assumed contingent liability is measured at amortized cost with the discount unwinding in finance expense throughout the year. Actual outcomes could differ significantly from the estimates made.

The Group has judged that the probabilities of success will change when it moves from one stage of clinical development to another. Management have determined that, for the purposes of assessing probabilities of success, the Group will move from Phase 2 to Phase 3 after an End of Phase 2 Meeting with the Food and Drug Administration ("FDA") in the US that provides confidence over ensifentrine's historical development program and planned Phase 3 program. A remeasurement of the liability at this time is likely to result in a significant increase in both the liability and the corresponding IPR&D asset. The Group has previously announced that it expects to meet with the FDA in the first half of 2020. The Group notes that there is no guarantee that the meeting will take place in the timeframe anticipated or that there will be a successful outcome.

Should the probabilities of success and estimates of cash flows change there will be a material increase in the assumed contingent liability and corresponding IP R&D asset. The amount will be dependent on feedback from the FDA and the probabilities of success applied. Should the Company determine that it has moved from Phase 2 to Phase 3 then the value of the liability could increase by between £15 million and £30 million; the increase in the value of the liability will give rise to an approximately equivalent increase in the value of the IP R&D asset, as described further in Note 2.7.

The value of the assumed contingent liability as of December 31, 2019 amounted to £1.1 million. (2018: £1.0 million).

(b) Valuation of the Derivative Financial Liability

In July 2016, the Company issued 31,115,926 units to new and existing investors at the placing price of £1.4365 per unit. Each unit comprises one ordinary share and one warrant. The warrants entitle the investors to subscribe for in aggregate a maximum of 12,401,262 ordinary shares.

In accordance with IAS 32 and the Group’s accounting policy, as disclosed in note 2.14, the Group classified the warrants as a derivative financial liability to be presented on the Group's Consolidated Statement of Financial Position.

The fair value of these warrants is determined by applying the Black-Scholes model. Assumptions are made on inputs such as term, volatility and risk free rate in order to determine the fair value per warrant. For further details see note 19.

5. Earnings per share

Basic loss per ordinary share of 30.3p (2018: 18.9p) for the Group is calculated by dividing the loss for the year ended December 31, 2019 by the weighted average number of ordinary shares in issue of 105,326,638 as of December 31, 2019 (2018: 105,110,504). Potential ordinary shares are not treated as dilutive as the entity is loss making and such shares would be anti-dilutive.

6. Segmental reporting

The Group’s activities are covered by one operating and reporting segment: Drug Development. There have been no changes to management’s assessment of the operating and reporting segment of the Group during the year.

All non-current assets are based in the United Kingdom.

7. Operating loss

Group

	Year ended December 31, 2019	Year ended December 31, 2018
	£'000s	£'000s
Operating Loss is stated after charging / (crediting):		
Research and development costs:		
Employee benefits (note 8)	4,688	3,360
Amortization of patents (note 12)	102	85
Legal, professional consulting and listing fees	537	161
Other research and development expenses	28,149	15,688
Total research and development costs	33,476	19,294
General and administrative costs:		
Employee benefits (note 8)	3,093	3,240
Legal, professional consulting and listing fees	2,155	1,296
Amortization of computer software (note 12)	4	5
Depreciation of property, plant and equipment (note 13)	16	8
Depreciation of right-of-use assets (note 14)	382	-
Operating lease charge — land and buildings	-	384
Loss / (gain) on variations in foreign exchange rate	345	(9)
Other general and administrative expenses	1,612	1,373
Total general and administrative costs	7,607	6,297
Operating loss	41,083	25,591

During the periods indicated, the Group obtained the services from and paid the fees of the Group's auditors and their associates as detailed below:

	Year ended December 31, 2019	Year ended December 31, 2018
	£'000s	£'000s
Audit of Verona Pharma plc and consolidated financial statements	148	114
Audit related services	52	68
Other services	67	86
Total	267	268

7. Operating loss (continued)

Audit-Related Services

For the year ended December 31, 2019, audit related services include fees for quarterly interim reviews.

For the year ended December 31, 2018, audit related services include fees for quarterly interim reviews.

Other Services

For the year ended December 31, 2019, other services related to advice relating to fund raising.

For the year ended December 31, 2018, other services related to a review of the Company's F-3 shelf registration statement.

8. Directors' emoluments and staff costs

Group

	Year ended December 31, 2019	Year ended December 31, 2018
The average number of employees (excluding directors) of the Group during the year:		
Research and development	13	7
General and administrative	9	7
Total	22	14

	Year ended December 31, 2019	Year ended December 31, 2018
	£'000s	£'000s
Aggregate emoluments of directors:		
Salaries and other short-term employee benefits	850	830
Social security costs	112	94
Incremental payment for additional services	26	26
Other pension costs	10	10
Total directors' emoluments	998	960
Share-based payment charge	925	1,337
Directors' emoluments including share-based payment charge	1,923	2,297

	Year ended December 31, 2019	Year ended December 31, 2018
	£'000s	£'000s
Aggregate executive officers costs:		
Wages and salaries	1,150	857
Social security costs	98	83
Share-based payment charge	751	769
Other pension costs	21	19
Total executive officers costs	2,020	1,728

8. Directors' emoluments and staff costs (continued)

	Year ended December 31, 2019	Year ended December 31, 2018
	£'000s	£'000s
Aggregate other staff costs:		
Wages and salaries	2,788	1,622
Social security costs	265	150
Share-based payment charge	765	795
Other pension costs	46	34
Total other staff costs	3,864	2,601

The Group considers key management personnel to comprise directors and executive officers.

The Group operates defined contribution pension schemes for its employees and executive director. The total pension cost during the year ended December 31, 2019 was £77 thousand (2018: £63 thousand). There were no prepaid or accrued contributions to the scheme at December 31, 2019 (2018 £nil)

Company

	Year ended December 31, 2019	Year ended December 31, 2018
The average number of employees (excluding directors) of the Company during the year:		
Research and Development	5	4
General and Administrative	8	4
Total	13	8

	Year ended December 31, 2019	Year ended December 31, 2018
	£'000s	£'000s
Aggregate emoluments of directors:		
Salaries and other short-term employee benefits	850	830
Social security costs	112	94
Incremental payment for additional services	26	26
Other pension costs	10	10
Total directors' emoluments	998	960
Share-based payment charge	925	1,337
Directors' emoluments including share-based payment charge	1,923	2,297

8. Directors' emoluments and staff costs (continued)

	Year ended December 31, 2019	Year ended December 31, 2018
	£'000s	£'000s
Aggregate executive officers costs:		
Wages and salaries	592	532
Social security costs	75	73
Share-based payment charge	639	957
Other pension costs	21	19
Total executive officers costs	1,327	1,581

	Year ended December 31, 2019	Year ended December 31, 2018
	£'000s	£'000s
Aggregate other staff costs:		
Wages and salaries	1,241	984
Social security costs	172	118
Share-based payment charge	447	571
Other pension costs	46	34
Total other staff costs	1,906	1,707

The Group considers key management personnel to be the aggregate of directors and executive officers.

The Company operates a defined contribution pension schemes for its. employees and executive director. The total pension cost during the year ended December 31, 2019 was £77 thousand (2018: £63 thousand). There were no prepaid or accrued contributions to the scheme at December 31, 2019 (2018: £nil).

In respect of Directors' remuneration, the Company has taken advantage of the permission in Paragraph 6(2) of Statutory Instrument 2008/410 to omit aggregate information that is capable of being ascertained from the detailed disclosures in the audited section of the Directors' Remuneration Report on pages 33 to 52 which form part of these Consolidated Financial Statements.

9. Finance income and expense

Group	Year ended December 31, 2019	Year ended December 31, 2018
	£'000s	£'000s
Finance income:		
Interest received on cash balances	754	861
Foreign exchange gain on translating foreign currency denominated balances	—	1,922
Fair value adjustment on derivative financial instruments (note 19)	1,597	—
Total finance income	2,351	2,783

9. Finance income and expense (continued)

	Year ended December 31, 2019	Year ended December 31, 2018
	£'000s	£'000s
Finance expense:		
Fair value adjustment on derivative financial instruments (note 19)	—	1,219
Interest on discounted lease liability	50	—
Foreign exchange loss on translating foreign currency denominated balances	305	—
Unwinding of discount factor related to the assumed contingent arrangement (note 21)	119	106
Total finance expense	474	1,325

Company

	Year ended December 31, 2019	Year ended December 31, 2018
	£'000s	£'000s
Finance income:		
Interest received on cash balances	754	861
Foreign exchange gain on translating foreign currency denominated balances	—	1,922
Fair value adjustment on derivative financial instruments (note 19)	1,597	—
Total finance income	2,351	2,783

	Year ended December 31, 2019	Year ended December 31, 2018
	£'000s	£'000s
Finance expense:		
Fair value adjustment on derivative financial instruments (note 19)	—	1,219
Interest on discounted lease liability	39	—
Foreign exchange loss on translating foreign currency denominated balances	305	—
Unwinding of discount factor related to the assumed contingent arrangement (note 21)	119	106
Total finance expense	463	1,325

10. Taxation

	Year ended December 31, 2019	Year ended December 31, 2018
	£'000s	£'000s
Analysis of tax credit for the year		
Current tax:		
U.K. tax credit	(7,250)	(4,290)
U.S. tax charge	56	30
Adjustment in respect of prior periods	(71)	28
Total tax credit	(7,265)	(4,232)
Factors affecting the tax credit for the year		
Loss on ordinary activities before taxation	(39,206)	(24,133)
Multiplied by standard rate of corporation tax of 19% (2018: 19%)	(7,449)	(4,585)
Effects of:		
Non-deductible expenses	515	540
Fair value adjustment on derivative financial instruments	(303)	232
Research and development incentive	(3,119)	(1,846)
Temporary differences not recognized	(6)	(3)
Difference in overseas tax rates	16	8
Tax losses carried forward not recognized	3,152	1,394
Adjustment in respect of prior periods	(71)	28
Total tax credit	(7,265)	(4,232)

U.K. corporation tax is charged at 19% (2018: 19.00%) and U.S. federal and state tax at 27.6% (2018: 27.6%).

The following tables represent deferred tax balances recognized in the Consolidated Statement of Financial Position. There were no movements in either the deferred tax asset or the deferred tax liability.

	As at December 31, 2019	As at December 31, 2018
	£'000s	£'000s
Deferred tax assets	332	250
Deferred tax liabilities	(332)	(250)
Net balances	—	—

The deferred tax liability relates to the difference between the accounting and tax bases of the IP R&D intangible asset. A deferred tax asset relating to UK tax losses has been recognized and offset against the liability.

Factors that may affect future tax charges

The Group has U.K. tax losses available for offset against future profits in the United Kingdom. However an additional deferred tax asset has not been recognized in respect of such items due to uncertainty of future profit streams. As of December 31, 2019, the unrecognized deferred tax asset at 17% is estimated to be £9.27 million (2018: £6.65 million at 17%).

11. Goodwill

Group and Company

	As of December 31, 2019	As of December 31, 2018
	£'000s	£'000s
Goodwill at January 1 and December 31	441	441

Goodwill represents the excess of the purchase price over the fair value of the net assets acquired in connection with the acquisition of Rhinopharma in September 2006. Goodwill is not amortized, but is tested annually for impairment.

The Group has one CGU so goodwill is tested for impairment together with its intangible assets. It was tested with reference to the Group's market capitalization as of December 31, 2019, the date of testing of IP R&D and goodwill impairment. The market capitalization of the Group was approximately £65.3 million as of December 31, 2019, (2018: 92.2 million) compared to the Group's net assets of £33.9 million (2018: £63.4 million). Therefore, no impairment was required.

The Group notes that after the reduction in its share price since December 31, 2018, and before the increase by December 31, 2019, at various points in the three months to March 31, 2019, the market value of the Group was less than its net book value. The Group therefore carried out an impairment review as at March 31, 2019. From market research the Group assessed, among other inputs, potential patient numbers from likely physician prescribing patterns, price points, the time from possible launch to peak sales, script rejection, attrition rates and probability of success. The Group also carried out a sensitivity analysis on key assumptions and assessed that a reasonable change in these assumptions would not lead to the value in use falling below net book value. Consequently, management determined that the Group's value in use exceeded the carrying value of the Group's assets and that no impairment was required.

At various other points in the year ended December 31, 2019, the market value of the Group was less than its net book value. Consequently, management re-performed the impairment review quarterly, and identified no changes to market conditions, the competitive landscape, market research insights or other factors that would change its conclusions. As a result, management determined that the Group's value in use exceeded the carrying value of the Group's assets and that no impairment was required at those dates.

12. Intangible assets

Group and Company

	IP R&D	Computer software	Patents	Total
	£'000s	£'000s	£'000s	£'000s
Cost				
At January 1, 2018 (Restated)	1,953	11	727	2,691
Additions	—	4	251	255
Disposals	—	—	(6)	(6)
At December 31, 2018 (Restated)	1,953	15	972	2,940
Accumulated amortization				
At January 1, 2018	—	6	232	238
Charge for year	—	5	85	90
Disposals	—	—	(6)	(6)
At December 31, 2018	—	11	311	322
Net book value				
At December 31, 2018 (Restated)	1,953	4	661	2,618

	IP R&D	Computer software	Patents	Total
	£'000s	£'000s	£'000s	£'000s
Cost				
At January 1, 2019	1,953	15	972	2,940
Additions	—	3	242	245
At December 31, 2019	1,953	18	1,214	3,185
Accumulated amortization				
At January 1, 2019	—	11	311	322
Charge for year	—	4	102	106
At December 31, 2019	—	15	413	428
Net book value				
At December 31, 2019	1,953	3	801	2,757

Intangible assets comprise patents, computer software and an IP R&D asset that arose on the acquisition of Rhinopharma and investment in patents to protect ensifentrine.

The IP R&D asset acquired through the business combination was initially recognized at fair value. Subsequent movements in the assumed contingent liability that relate to changes in estimated cash flows or probabilities of success are recognized as additions to the IP R&D asset that it relates to. This is a change in accounting policy (see note 2.18). The asset is not amortized and is tested annually for impairment.

Patents are amortized over a period of ten years and are tested annually for impairment.

Intangible assets are tested for impairment with goodwill, as the Group has only one CGU. See note 11 for information about the impairment review.

13. Property, plant and equipment

Group and Company

	Computer hardware	Total
	£'000s	£'000s
Cost		
At January 1, 2018	26	26
Additions	13	13
At December 31, 2018	39	39
Accumulated depreciation		
At January 1, 2018	10	10
Charge for the year	8	8
At December 31, 2018	18	18
Net book value		
At December 31, 2018	21	21

	Computer hardware	Total
	£'000s	£'000s
Cost		
At January 1, 2019	39	39
Additions	38	38
At December 31, 2019	77	77
Accumulated depreciation		
At January 1, 2019	18	18
Charge for the year	16	16
At December 31, 2019	34	34
Net book value		
At December 31, 2019	43	43

14. Right-of-use assets - property leases

The right-of-use asset relates to rented office space in London and New York where the Group generally enters in to leases for terms of less than three years. Before the adoption of IFRS 16 these leases were classified as operating leases.

Group

The Consolidated Statement of Financial Position shows the following amounts relating to leases:

	Year ended December 31, 2019	As of January 1, 2019*
	£'000s	£'000s
Right-of-use assets		
Right-of-use assets	971	326
	971	326
Lease liabilities		
Current	(460)	(316)
Non Current	(491)	—
	(951)	(316)

Additions to the right-of-use assets were £1,047,000 and were recognized when the Group was reasonably certain to extend the leases. The additions related to both of the Group's office locations, both of which agreements have similar terms and conditions.

To calculate the value of the lease liabilities the Group applied a discount rate of 8%.

The leases end in 2021 and 2022 and include options to extend them. The Group has determined it is not yet reasonably certain to operate the option to extend the leases and so has recognized lease payments only to these points in its calculation of the lease liabilities.

The right-of-use lease assets are depreciated over the term of the leases.

The Consolidated Statement of Comprehensive Income includes the following amounts relating to leases:

	Year ended December 31, 2019	Year ended December 31, 2018
	£'000s	£'000s
Depreciation charge of right-of-use assets		
Right-of-use assets	(382)	—
	(382)	—
Interest expense (including finance cost)	50	—
Expense relating to short-term leases (included in general and administrative expenses)	78	—

The total cash outflow for leases in 2019 was £492,000.

14. Right-of-use assets - property leases (continued)

Company

The right-of-use asset relates to rented office space in London where the Company generally enters in to leases for terms of less than three years. Before the adoption of IFRS 16 these leases were classified as operating leases.

The Company's Statement of Financial Position shows the following amounts relating to leases:

	Year ended December 31, 2019	As of January 1, 2019*
	£'000s	£'000s
Right-of-use assets		
Right-of-use assets	731	326
	731	326
Lease liabilities		
Current	(335)	(316)
Non Current	(419)	—
	(754)	(316)

Additions to the right-of-use assets were £718,000 and were recognized when the Company was reasonably certain to extend the leases. The additions related to the Company's office location.

To calculate the value of the lease liabilities the Company applied a discount rate of 8%.

The leases end in 2022. The Company has determined it is not yet reasonably certain to operate the option to extend the leases and so has recognized lease payments only to these points in its calculation of the lease liabilities.

The right-of-use lease assets are depreciated over the term of the leases.

The Consolidated Statement of Comprehensive Income includes the following amounts relating to leases:

	Year ended December 31, 2019	Year ended December 31, 2018
	£'000s	£'000s
Depreciation charge of right-of-use assets		
Right-of-use assets	(313)	—
	(313)	—
Interest expense (including finance cost)	39	—

The total cash outflow for leases in 2019 was £348,000.

15. Prepayments and other receivables

Group

	As of December 31, 2019	As of December 31, 2018
	£'000s	£'000s
Prepayments	1,309	1,362
Other receivables	1,461	1,101
Total prepayments and other receivables	2,770	2,463

The prepayments balance includes prepayments for insurance and clinical activities.

Company

	As of December 31, 2019	As of December 31, 2018
	£'000s	£'000s
Prepayments	1,331	1,346
Other receivables	1,437	1,069
Amounts due from group undertakings	325	187
Total prepayments and other receivables	3,093	2,602

Amounts due from group undertakings are unsecured, interest free and repayable on demand.

The prepayments balance includes prepayments for insurance and clinical activities.

16. Investment in subsidiaries

The Company has two wholly owned subsidiaries, Rhinopharma Limited and Verona Pharma Inc.

	As of December 31, 2019	As of December 31, 2018
	£'000s	£'000s
Net book value:		
At the start of the year	913	877
Capital contribution arising from share-based payments	429	36
Net book amount at the end of year	1,342	913

A capital contribution arises where share-based payments are provided to employees of the subsidiary undertaking, Verona Pharma Inc, settled with equity to be issued by the Company.

16. Investment in subsidiaries (continued)

The Company's investments comprise interests in Group undertakings, details of which are shown below:

Name of undertaking	Verona Pharma Inc.	Rhinopharma Limited
Country of incorporation	Delaware USA	British Columbia Canada
Description of shares held	$0.001 Common stock	Without Par Value Common shares
Proportion of shares held by the Company	100%	100%

Verona Pharma Inc. was incorporated on the 12 December 2014 under the laws of the State of Delaware, USA and has its registered office at 2711 Centerville Road, Suite 400, City of Wilmington 19808, County of New Castle, Delaware, United States of America.

Rhinopharma Limited is incorporated under the laws of the Province of British Columbia, Canada and has its registered office at Suite 700, 625 Howe Street, Vancouver, British Columbia, Canada V6C 2T6. Rhinopharma Limited was a drug discovery and development company focused on developing proprietary drugs to treat allergic rhinitis and other respiratory diseases prior to its acquisition by the Company on September 18, 2006.

17. Share Capital

Group and Company

The movements in the Company's share capital are summarized below:

Date	Description	Number of shares	Share Capital amounts in £'000s
January 1, 2018		**105,017,401**	**5,251**
August 9, 2018	Vesting of RSUs	58,112	3
September 20, 2018	Vesting of RSUs	251,125	12
As at December 31, 2018		**105,326,638**	**5,266**
As at December 31, 2019		**105,326,638**	**5,266**

The total number of authorized ordinary shares, with a nominal value of £0.05 each, is 200,000,000 (share capital of £10,000,000). All 105,326,638 ordinary shares at December 31, 2019 are allotted, unrestricted, called up and fully paid. All issued shares rank pari passu.

During 2018, the Company issued 309,237 ordinary shares upon vesting of employee restricted share units.

18. Share-based payments charge

Group and Company

The Group operates various share based payment incentive schemes for its staff.

In accordance with IFRS 2 "Share Based Payments," the cost of equity-settled transactions is measured by reference to their fair value at the date at which they are granted. Where equity-settled transactions were entered into with third party service providers, fair value is determined by reference to the value of the services provided. For other equity-settled transactions fair value is determined using the Black-Scholes model. The cost of equity-settled transactions is recognized over the period until the award vests. No expense is recognized for awards that do not ultimately vest. At each reporting date, the cumulative expense recognized for equity-based transactions reflects the extent to which the vesting period has expired and the number of awards that, in the opinion of the Directors at that date, will ultimately vest.

The costs of equity-settled share-based payments to employees are recognized in the Statement of Comprehensive Income, together with a corresponding increase in equity during the vesting period. During the twelve months ended December 31, 2019, the Group recognized a share-based payment expense of £2.44 million (2018: £2.90 million). The charge is included within both general and administrative costs as well as in research and development costs and represents the current year's allocation of the expense for relevant share options.

The Group operates an Unapproved Share Option Scheme under which options were issued before 31 December 2016. The Group also operates a tax efficient EMI Option Scheme under which options were issued before 31 December 2016. In 2017 the Group commenced the 2017 Incentive Award Plan under which the Group grants share options and Restricted Stock Units ("RSUs") to employees and directors.

Since 2017 options are issued with an exercise price at the share price the evening before the date of issue. They vest over terms of one to four years.

RSUs also vest over terms of one to four years. In the year ended December 31, 2019, the Company modified the terms of all the RSUs issued prior January 1, 2019, to include a market based performance condition. The Company's share price must be maintained above £2 for thirty days for the RSUs to vest, in addition to the existing service condition. The RSUs vest after a five year term irrespective of whether the £2 market condition was met. This modification did not result in an increase in the fair value of the RSUs. The RSUs issued in the year ended December 31, 2019, also include the same market condition and five year term.

In the year ended December 31, 2019, under the 2017 Incentive Award Plan, the Group granted 5,569,050 (2018: 2,090,847) share options and 740,496 RSUs (2018: 273,390). The total fair values of the options and RSUs were estimated using the Black-Scholes option-pricing model for equity-settled transactions and amounted to £2.25 million (2018: £2.32 million). The cost is amortized over the vesting period of the options and RSUs on a straight-line basis.

The following assumptions were used for the Black-Scholes valuation of share options and RSUs granted in 2018 and 2019. For the options granted under the Unapproved Scheme the table indicates the ranges used in determining the fair-market values, aligning with the various dates of the underlying grants. The volatility is calculated using historical weekly averages of the Group's share price over a period that is in line with the expected life of the options and RSUs.

18. Share-based payments charge (continued)

Issued in 2018	Unapproved Scheme	Restricted Stock Units
Options granted	2,090,847	273,390
Risk-free interest rate	1.08% - 1.22%	1.08% - 1.22%
Expected life of options	5.5 - 7 years	5.5 - 7 years
Annualized volatility	69.88% -71.35%	69.88% -71.35%
Dividend rate	0.00%	0.00%
Vesting period	1 to 4 years	1 to 4 years

Issued in 2019	Unapproved Scheme	Restricted Stock Units
Options granted	5,569,050	740,496
Risk-free interest rate	0.39% - 0.82%	0.76% - 0.82%
Expected life of options	5.5 - 7 years	5.5 - 7 years
Annualized volatility	67.98% - 69.71%	63.82% - 69.71%
Dividend rate	0.00%	0.00%
Vesting period	1 to 4 years	1 to 4 years

The Group had the following share options movements in the year ended December 31, 2019:

Year of issue	Exercise price (£)	At January 1, 2019	Options granted	Options forfeited	Options expired	At December 31, 2019	Expiry date	
2012	2.50 - 7.50	99,993	—	—	—	99,993	June 1, 2022	
2013	2	99,990	—	—	(19,998)	79,992	April 15, 2023	
2013	2.00	159,999	—	—	—	159,999	July 29, 2023	
2014	1.75	109,998	—	—	—	109,998	May 15, 2024	
2014	1.75	49,998	—	—	—	49,998	May 15, 2024	*
2015	1.25	41,997	—	—	—	41,997	January 29, 2025	*
2015	1.25	549,999	—	—	—	549,999	January 29, 2025	
2016	2	240,000	—	—	—	240,000	February 2, 2026	
2016	2.00	21,996	—	—	—	21,996	February 2, 2026	*
2016	1.80	676,664	—	—	—	676,664	August 3, 2026	
2016	1.89	299,997	—	—	—	299,997	September 13, 2026	
2016	2.04	300,000	—	—	—	300,000	September 16, 2026	
2017	1.32 - 1.525	4,093,164	—	—	—	4,093,164	April 26, 2027	
2018	1.46	2,008,319	—	(34,614)	—	1,973,705	March 8, 2028	
2019	570.00	—	3,903,050	(87,356)	—	3,815,694	March 29, 2029	
2019	595.00	—	346,000	—	—	346,000	June 11, 2029	
2019	457.00	—	100,000	—	—	100,000	August 22, 2029	
2019	0.436	—	720,000	—	—	720,000	November 6, 2029	
2019	445.00	—	500,000	—	—	500,000	November 26, 2029	
Total		8,752,114	5,569,050	(121,970)	(19,998)	14,179,196		

* Options granted under the EMI Scheme.

18. Share-based payments charge (continued)

The Company had the following RSU movements in the year ended December 31, 2019:

Year of issue	Exercise price (£)	At January 1, 2019	Units granted	Units vested	Units forfeited	At December 31, 2019	Expiry date
2017		729,987	—	—	—	729,987	April 26, 2027
2018		132,486	—	—	—	132,486	March 8, 2028
2019			740,496	—	—	740,496	March 29, 2027
Total		862,473	740,496	—	—	1,602,969	

Outstanding and exercisable share options by scheme as of December 31, 2019:

Plan	Outstanding	Exercisable	Weighted average exercise price in £ for Outstanding	Weighted average exercise price in £ for Exercisable
Unapproved	13,965,212	5,552,293	1.12	1.55
EMI	213,984	213,984	3.06	3.06
Total	14,179,196	5,766,277	1.15	1.61

As of December 31, 2019 there were no restricted share options exercisable (2018: nil) and there is no exercise price for restricted share options.

The options outstanding at December 31, 2019 had a weighted average remaining contractual life of 7.7 years (2018: 8.0 years). For 2018 and 2019, the number of options granted and expired and the weighted average exercise price of options were as follows:

	Number of options	Weighted average exercise price (£)
At January 1, 2018	7,527,458	1.53
Options granted in 2018:		
Employees	1,222,089	1.46
Directors	868,758	1.46
Options forfeited in the year	(799,524)	1.43
Options expired in the year	(66,667)	1.75
At December 31, 2018	8,752,114	1.53
Exercisable at December 31, 2018	3,542,884	1.66

18. Share-based payments charge (continued)

	Number of options	Weighted average exercise price (£)
At January 1, 2019	8,752,114	1.53
Options granted in 2019:		
Employees	4,042,106	0.55
Directors	1,526,944	0.53
Options forfeited in the year	(121,970)	0.82
Options expired in the year	(19,998)	2.00
At December 31, 2019	14,179,196	1.15
Exercisable at December 31, 2019	5,766,277	1.60

The following table shows the number of RSUs issued, exercised and forfeited in 2018. The fair value of each unvested RSU at grant date was £1.46.

	Number of RSUs
At January 1, 2018	1,052,236
Granted:	
Employees	136,404
Directors	136,986
RSUs vested in the year	(309,237)
RSUs forfeited in the year	(153,916)
At December 31, 2018	862,473

The following table shows the number of RSUs issued in 2019. There were no RSUs forfeited, canceled or vested in 2019. The fair value of each unvested RSU granted in 2019 was £0.57.

	Number of RSUs
At January 1, 2019	862,473
Granted:	
Employees	474,072
Directors	266,424
RSUs vested in the year	—
RSUs forfeited in the year	—
At December 31, 2019	1,602,969

The cost is amortized over the vesting period of the options on a straight-line basis. The expense for the Group during 2019 amounted to £2.9m and £0.04m in relation to Verona Pharma Inc is held as an investment.

19. Derivative financial instrument

Group and Company

On July 29, 2016, the Group issued 31,115,926 units to new and existing investors at the placing price of £1.4365 per unit. Each unit comprises one ordinary share and one warrant.

The warrant holders can subscribe for 0.4 of an ordinary share at a per share exercise price of £1.7238. The warrant holders can opt for a cashless exercise of their warrants, whereby the warrant holders can choose to exchange the warrants held for reduced number of warrants exercisable at nil consideration. The reduced number of warrants is calculated based on a formula considering the share price and the exercise price of the warrants. The warrants are therefore classified as a derivative financial liability, since their exercise could result in a variable number of shares to be issued.

The warrants entitled the investors to subscribe for, in aggregate, a maximum of 12,401,262 shares. The warrants can be exercised until May 2, 2022.

In the year ended December 31, 2019, no warrants were forfeited (2018: nil).

The table below presents the assumptions in applying the Black-Scholes model to determine the fair value of the warrants.

	As of December 31, 2019	As of December 31, 2018
Shares available to be issued under warrants	12,401,262	12,401,262
Exercise price	£ 1.7238	£ 1.7238
Risk-free interest rate	0.540%	0.760%
Expected term to exercise	2.34 years	3.34 years
Annualized volatility	65.56%	60.72%
Dividend rate	0.00%	0.00%

As per the reporting date, the Group updated the underlying assumptions and calculated a fair value of these warrants amounting to £0.9 million. The variance of £(1.6) million is recorded as finance income in the Consolidated Statement of Comprehensive Income.

	Derivative financial instrument	Derivative financial instrument
	2019	2018
	£'000s	£'000s
At January 1	2,492	1,273
Fair value adjustments recognized in profit or loss	(1,597)	1,219
At December 31	895	2,492

For the amount recognized at December 31, 2019, the effect when the following parameter deviates up or down is presented in the below table.

	Volatility (up / down 10% pts)
	£'000s
Variable up	1,306
Base case, reported fair value	**895**
Variable down	535

20. Trade and other payables

Group

	As of December 31, 2019	As of December 31, 2018
	£'000s	£'000s
Trade payables	1,455	2,839
Other payables	—	12
Accruals	6,806	4,882
Total trade and other payables	8,261	7,733

Company

	As of December 31, 2019	As of December 31, 2018
	£'000s	£'000s
Trade payables	1,455	2,839
Other payables	—	12
Amount due to group undertakings	1,474	722
Accruals	6,327	4,696
Total trade and other payables	9,256	8,269

Amounts due to group undertakings are unsecured, interest free and repayable on demand.

21. Assumed contingent liability related to the business combination

Group and Company

The value of the assumed contingent liability as of December 31, 2019 is £1.1 million (2018: £1.0 million). The increase in value of the assumed contingent liability during 2019 amounted to £0.1 million (2018: £0.1 million).

The assumed contingent liability relates to the acquisition, in 2006, of rights to certain patents and patent applications relating to ensifentrine and related compounds under which the Group is obliged to pay royalties to Ligand (see 2.12).

The assumed contingent liability is measure at the expected value of the milestone payment and royalty payments. This expected value is based on estimated future royalties payable, derived from sales forecasts, and an assessment of the probability of success using standard market probabilities for respiratory drug development. The risk-weighted value of the assumed contingent arrangement is discounted back to its net present value applying an effective interest rate of 12%.

The assumed contingent liability is accounted for as a liability and its value is measured at amortized cost using the effective interest rate method, and is re-measured for changes in estimated cash flows or when the probability of success changes.

Re-measurements relating to changes in estimated cash flows and probabilities of success are recognized in the IP R&D asset it relates to ("see 2.7"). This is a change in accounting policy for the year ended December 1, 2019 (see 2.18). The unwind of the discount is recognized in finance expense.

21. Assumed contingent liability related to the business combination (continued)

The Group considers that probabilities of success will change when it moves from one stage of clinical development to another. See note 4 for a further discussion of this.

	2019	2018
	£'000s	£'000s
January 1	996	875
Impact of changes in foreign exchange rates	(12)	15
Unwinding of discount factor	119	106
December 31	1,103	996

There is no material difference between the fair value and carrying value of the financial liability.

For the amount recognized as at December 31, 2019, of £1,103 thousand, the effect if underlying assumptions were to deviate up or down is presented in the following table (assuming the probability of success does not change):

	Discount rate (up / down 1 % pt)	Revenue (up / down 10 % pts)
	£'000s	£'000s
Variable up	1,067	1,135
Base case, reported fair value	**1,103**	**1,103**
Variable down	1,141	1,071

22. Related parties transactions and other shareholder matters

(i) Related party transactions

The Directors have authority and responsibility for planning, directing and controlling the activities of the Group and they therefore comprise key management personnel as defined by IAS 24, ("Related Party Disclosures").

Directors and key management personnel remuneration is disclosed in note 8.

(ii) Other shareholder matters

The Group has entered into the following arrangements with parties who are significant shareholders of the Group, though they are not classed as related parties.

The Group entered into relationship agreements with Vivo Ventures Fund VII, L.P., Vivo Ventures VII Affiliates Fund, L.P., Vivo Ventures Fund VI, L.P., Vivo Ventures VI Affiliates Fund, L.P. (collectively, "Vivo Capital"), Orbimed Private Investments VI L.P. ("Orbimed") and Abingworth Bioventures VI L.P. ("Abingworth"). As agreed in these relationship agreements, the above parties invested in the Group as part of the July 2016 Placement, and the Group agreed to appoint representatives designated by Vivo Capital, OrbiMed and Abingworth to the board of directors, who are Dr. Mahendra Shah, Mr. Rishi Gupta, and Dr. Andrew Sinclair.

The appointment rights within the relationship agreement with Arix and Arthurian terminated on closing of the Global Offering on April 26, 2017. Dr Cunningham agreed to continue to serve on the Group's board of directors as an independent director. The respective appointment rights under the remaining relationship agreements will automatically terminate upon (i) Vivo Capital, OrbiMed or Abingworth (or any of their associates), as applicable, ceasing to beneficially hold 6.5% of the issued ordinary shares, or (ii) the ordinary shares ceasing to be admitted to AIM.

Piers Morgan, Chief Financial Officer of the Group, and his spouse purchased 88,415 ordinary shares in total for £53 thousand from the market in the year ended December 31, 2019 (2018: £nil).

Dr. Jan-Anders Karlsson, Chief Executive Officer of the Group, purchased 3,250 ordinary shares for £5 thousand from the market in the year ended December 31, 2018. There was no similar transaction as at December 31, 2019.

Dr. David Ebsworth, Chairman of the Group, purchased 247,600 ordinary shares for £124 thousand from the market in the year ended December 31, 2019 (2018: £14 thousand).

At December 31, 2018, there was a receivable of £126 thousand due from one director and two key management personnel relating to tax due on RSUs that vested in the year ended December 31, 2018. This receivable was repaid, together with interest at a rate of 3.9% per annum, by March 6, 2019. There was no such balance as at December 31, 2019.

In the year ended December 31, 2019, a director provided consultancy services for £26 thousand (2018: £26 thousand).

23. Events after the reporting date

On February 3, 2020, the Group announced the appointment of David Zaccardelli as chief executive officer with effect from February 1, 2020, following the retirement of Jan-Anders Karlsson, PhD. The Group also announced the appointment of Mark Hahn as chief financial officer with effect from March 1, 2020, as successor to Piers Morgan.