Velocys plc
Annual report and accounts 2014

VELOCYS

Velocys is the company at the forefront of smaller scale gas-to-liquids (GTL) that turns natural gas or biomass into premium liquid products such as diesel and jet fuel. Smaller scale GTL adds value to shale gas and bio-waste, and makes stranded or flared gas economic – an untapped market of up to 25 million barrels per day.

Velocys technology, protected by over 900 patents, is specifically designed for smaller scales, combining super-active catalysts with intensified reactor systems. The Company's standardised modular plants are easier to ship and faster to install, at lower risk, even in the most remote or challenging locations. Together with world-class partners, Velocys works flexibly to unlock gas resources of 15,000 to 150,000 mmbtu per day, allowing more companies to take advantage of more opportunities.

Velocys plc is listed on the AIM market of the London Stock Exchange (LSE: VLS). The Company is well capitalised and has a multi-disciplinary staff of over 100 operating from its commercial centre in Houston, Texas, USA and technical facilities near Oxford, UK and Columbus, Ohio, USA. Its first commercial plant, funded by Waste Management (NYSE: WM), NRG Energy (NYSE: NRG) and Ventech Engineers, is on track to enter commercial production in H1 2016.

Contents Page

Highlights

- Formation of GTL joint venture with Waste Management, NRG Energy and Ventech
- First commercial plant under construction in Oklahoma, USA on schedule for commissioning in H1 2016
- Acquisition of Pinto Energy and its 4,800 bpd Ashtabula GTL plant development targeting FID at end 2015
- Sale of commercial reactor to CIS customer with delivery in progress
- Cemented manufacturing partnership with Shiloh Industries
- UK High Court ruled in favour of Velocys IP in litigation against CompactGTL
- Revenue* of £1.7 million (FY 2013: £4.8 million) - first year with 100% commercial revenue
- £52 million raised before expenses in oversubscribed equity placing at £2.25 per share
- Cash** at period end of £59.8 million (FY 2013: £26.4 million)

Roy Lipski, CEO of Velocys, said:

"2014 was one of the most successful years in the history of Velocys. With over $85 million of cash on the balance sheet, the unwavering support of major partners and our first commercial plant under construction, Velocys is poised to take advantage of the significant opportunities which typically surface during times of market volatility such as these, and notwithstanding some potential near term headwinds in the oil and gas industry, to establish an even stronger business and market position. Interest in smaller scale GTL remains high and I look forward to achieving the significant milestones ahead of us."

* Before exceptional items.
** Defined as cash, cash equivalents and short term investments (see note 23).

Chairman's statement

The era of smaller scale GTL is now here. The first commercial plant incorporating our technology is under construction.

At a time when lower oil prices have created uncertainty in the fuels industry, smaller scale GTL continues to have a valuable role to play, driven by local needs to bring stranded or wasted gas to market and by demand for its clean premium products. Current market conditions highlight the benefit of a technology that is designed for smaller scales and can therefore access the specific niches of value, typically sites with low- or negative-cost feed stocks or high-value product opportunities where the GTL arbitrage remains strong.

Velocys is well positioned to move forward as a leader in the market for smaller scale GTL. Its position has been firmly established with the decision to proceed with construction of the GTL JV's plant in Oklahoma, USA.

This facility will be our first commercial reference plant, and I am delighted to report that it is advancing well and remains on target for commissioning in H1 2016. In addition to progressing the build on this plant, the GTL JV, now renamed ENVIA Energy, has identified and is evaluating candidate sites for possible next plants.

During 2014, Velocys took another step forward to accelerate the market for smaller scale GTL by acquiring a leading project development company, Pinto Energy, now called Velocys Project Solutions (VPS). This new capability enables Velocys to develop the market faster, and to improve both the breadth and quality of its offering to customers. The team is currently developing the Ashtabula GTL plant and has a further pipeline of projects.

Another major success in 2014 was the outcome of our IP litigation case against CompactGTL. Defending IP is a long and expensive process and not to be undertaken lightly. The overwhelming success of our case, which concluded with the judge ruling in our favour on all items examined, strongly vindicates our position of having a unique technology robustly protected by patents. At a time when others may be looking to enter this attractive new market, our strong IP position is clearly an important competitive advantage.

Key priorities for Velocys going forward are the successful delivery of its first GTL plant, the development of future projects and the building up of resources to support them. We have made substantial progress throughout the year on these objectives, including work with our supply chain partners to ensure all the relevant capabilities are in place. As announced in March last year, Velocys cemented an important collaboration agreement with Shiloh Industries (Shiloh), our reactor manufacturing partner. At that time, Shiloh made a $2 million investment in shares of Velocys.

As further support for these efforts, we have continued to grow the Velocys team. At the end of 2014, the Company had some 115 employees comprising a world class group of technical, engineering and commercial talent. Velocys announced in 2013 the establishment of its new Houston base; we now have the full complement of staff there to support commercial, engineering and project development activities.

In September 2014, Velocys completed a significant equity placing, raising £52 million before expenses. It was oversubscribed and attracted strong support from shareholders. As a result, the Company moves into 2015 well capitalised, with the resources to succeed in its next stage of commercialisation.

Total revenues for the period before exceptional items were £1.7 million (2013: £4.8 million) and were all derived from commercial activities. Cash* at period end stood at £59.8 million (2013: £26.4 million), while cash outflow** was £18.1 million (2013: £12.5 million).

Outlook

Velocys enters 2015 with a very strong balance sheet and in the exciting position of having its first commercial reference plant under construction, which promises to be a significant catalyst for business when complete. Although volatility in the markets may cause a degree of hesitancy in the short term, companies with longer term outlook are already planning for higher oil prices or restored margins. The market for smaller scale GTL remains compelling and there are exciting opportunities ahead for Velocys. I look forward with confidence to seeing our first commercial plant in operation.

Pierre Jungels, CBE
27 March 2015

* Defined as cash, cash equivalents and short term investments.
** Defined as cash movement excluding monies from fund raising and issuance of shares.

Chief executive's report

Velocys is the company at the forefront of smaller scale GTL.

Introduction

In 2014, Velocys reached a momentous milestone event: the first commercial plant using our technology was committed and is now under construction. This achievement is the culmination of many years of effort and preparation, and the Company is focussed on ensuring this plant is successfully brought into operation.

Market conditions

After a sustained period of high oil prices, the second half of 2014 saw a dramatic and unexpected fall. As a result, large scale GTL projects whose rationale is simply to take advantage of the mass-market price arbitrage between natural gas and crude oil will be difficult to progress at this time, as they cannot be placed in the most advantaged locations and since their capital costs are too high for an industry currently struggling with cash flow.

Whilst some investment decisions are under greater scrutiny, good opportunities remain for smaller scale GTL; many local situations are likely to retain their attractiveness, even with lower gas-oil differentials at the major hubs. These projects either utilise economically-priced gas or other low- or negative-cost feed stocks, or serve a market where a premium can be realised, for example by producing high-value speciality products such as base oils or waxes, or by serving isolated areas where liquid fuel import costs are high.

In this tougher market, quality counts; projects need to use the most competitive technology in order to achieve the best economic returns. Those companies, like Velocys, that possess vital elements – a strong balance sheet, supportive partners, and plants that are already committed – are well positioned to benefit from this challenging period whilst others may struggle.

Commercialisation

Sales and prospects

Against this backdrop, we saw a number of the prospects in the Velocys sales pipeline moving forward in 2014, most notably the Oklahoma plant funded by ENVIA Energy, a joint venture partnership between Waste Management, NRG Energy, Ventech Engineers International and Velocys. Not only is this project the first commercial reference plant for smaller scale GTL using Velocys technology, it is the first to be funded by the joint venture that was formed to develop a series of such plants utilising biogas from Waste Management landfill sites supplemented by pipeline gas.

The Oklahoma GTL plant is now under construction with the reactors in build at Shiloh, the modules being fabricated at Ventech's workshop and the groundwork having commenced at the site. This work is on schedule, with commissioning anticipated during the first half of 2016.

As well as being a technology supplier to the Oklahoma project, Velocys is also a minority investor in the plant through the JV. This closer involvement in the project is paying dividends through improved visibility of the key factors required to make such projects successful.

Also in 2014, Velocys received an order for a reactor for a demonstration facility at a customer site in the Commonwealth of Independent States (CIS). This reactor is also in fabrication for delivery during 2015.

Another project that has made significant headway in 2014 is the Red Rock Biofuels project. In September 2014, it was announced that this customer was awarded a $70 million grant from the US Department of Defense to construct a biomass-to-liquids (BTL) plant incorporating Velocys technology. Red Rock Biofuels, a subsidiary of IR1 Group LLC, has experience constructing and operating commercial-scale biofuels facilities. The new BTL plant in Oregon will convert some 170,000 tons per year of forestry and sawmill waste into approximately 1,100 barrels per day of ultra clean transportation fuels. As well as securing the grant, the project owners also announced in 2014 that they had secured an offtake agreement for jet fuel from Southwest Airlines.

Project development

During 2014, in order to accelerate market adoption of its technology, Velocys took steps towards developing "shovel ready" projects which can be independently financed. This was the driver behind the acquisition of Pinto Energy (now renamed Velocys Project Solutions) in June 2014, which gave Velocys an initial team of people skilled in project development and a pipeline of project opportunities. Since then, the new team has been expanded and includes 9 full time staff, with an initial focus on bringing the Ashtabula project, which is now planned to be a 4,800 bpd plant producing speciality waxes and chemicals, to final investment decision (FID) towards the end of 2015.

Pilot plant and demonstration activities

The Velocys pilot plant located in Columbus, Ohio continues to support our sales effort. In addition to providing product samples for potential customers, the plant has been used to demonstrate specific operating conditions for various customers, including a successful run at the conditions for the Oklahoma plant. In preparation for the operation of the Oklahoma plant we established an operational support team and developed

Chief executive's report (continued)

protocols, manuals and training capabilities for commercial operation, as well as the relevant techniques and equipment for catalyst handling on a commercial scale.

At the end of 2013, we announced that the Velocys plant in Fortaleza, Brazil, at a site owned by the Brazilian national oil company, Petrobras, had completed its demonstration. This was the culmination of the joint development agreement ("JDA") between Velocys and its partners for offshore applications of GTL, MODEC and Toyo Engineering, and as a result the JDA was concluded in 2014. Whilst off-shore GTL remains a promising prospect in the long term, we believe that this market will only develop after on-shore plants have been established.

Manufacturing and supply chain

At the start of 2014, Velocys stepped up its partnership with Shiloh, the manufacturer of the Company's reactor cores. Shiloh is one of North America's leading suppliers of engineered metal products and light weighting solutions to the automotive industry. Together we created a supply chain infrastructure that is capable of supporting annual sales of up to 10,000 bpd based on state-of-the-art manufacturing technology and quality systems from the automotive industry, and have plans that allow us to ramp up to 40,000 bpd in line with demand. This partnership involved investment in a multimillion dollar facility at Shiloh's Ohio site where construction of the first reactors is now in progress.

As part of the partnership arrangement, Shiloh purchased 601,326 shares of Velocys at 200p per share, representing a 32% premium to market price at the time.

During 2014, Velocys also launched production of its commercial catalyst which is being manufactured by one of the Company's catalyst manufacturing partners.

Intellectual property

Velocys' IP position was considerably strengthened during 2014 by the very favourable judgement in the litigation case against CompactGTL. Not only did the judge rule that CompactGTL was infringing both the Velocys patents in question, but also the Velocys patents were upheld. We have been awarded costs for which CompactGTL has made an interim payment of £850,000 pending final settlement, and the court ordered an immediate injunction restraining them from carrying out infringing activities. The case is continuing, with determination of damages to Velocys expected to follow after additional disclosures from CompactGTL have been received.

The key significance of this outcome is that it demonstrates the robustness of our IP and our ability to defend it rigorously where we see infringement. Equivalents of the two patents in this case have also been approved in numerous other jurisdictions around the world, including places where smaller scale GTL might be deployed, such as the United States and Canada, and countries where FT reactors and other associated equipment might be manufactured, such as Japan and South Korea.

Velocys has a very substantial patent portfolio comprising more than 900 patents, covering a broad range of countries, which protects key inventions relevant to smaller scale GTL. The Company also holds a significant inventory of trade secrets which it has gained through years of development and practice.

Equity funding

On 29 September 2014, Velocys announced an equity placing of £52 million comprising 23.1 million shares at £2.25 per share, underscoring the commitment and confidence of investors in the Velocys business. These funds will be used to strengthen the Company's balance sheet in support of sales, help the development of selected projects to funding readiness, and support the general working capital needs of the business.

Resources

The Velocys team has expanded to meet the increasing demands and opportunities ahead, particularly in staff with skills in engineering, manufacturing, operations, plant commissioning and project development. Velocys employees are located across three main sites in Oxford, UK and Ohio and Houston, USA. We have a team that is world-class in the very areas needed to successfully deliver our leading technology – drawn from some of the leading players in our industry – as well as an established base at the heart of the oil and gas industry, Houston. From a financial perspective, the fund raise in September 2014 leaves Velocys well capitalised to deliver on its goals and ambitions.

Roy Lipski
Chief executive
27 April 2015

Strategic report

The Directors present their review of the Company's performance during the year to 31 December 2014 and their assessment of the risks faced by Velocys

Principal activities

Velocys is at the forefront of the design and development of technology for the production of premium liquid products such as clean synthetic diesel and jet fuel from both conventional fossil fuels and renewable sources such as bio-waste.

The primary focus of the business is on the emerging market need for modular gas-to-liquids (GTL) plants in the range of 15,000 to 150,000 mmbtu (million British thermal units) per day. It is estimated that this is a market that has the potential of producing as much as 25 million barrels of fuel a day. As this market becomes better recognised a number of competitors have entered it. The Directors consider that, given the size of the potential market opportunity, competition represents a positive factor that will help to stimulate market growth. Velocys is one of the most well established companies in the market and is recognised as a world leader in the development of smaller scale GTL technology.

The Company's core business model incorporates the sale of reactors, licences for use of the reactor and catalyst technology, regular revenue from the catalyst which will be periodically renewed, and fees for engineering and support services.

In addition, Velocys Project Solutions, a subsidiary acquired during 2014 (see note 30), works to bring potential GTL projects to the point of development. Foremost of these is its Ashtabula site in Northeast Ohio. The Company also holds a small stake in the joint venture company formed to run the plant at the first commercial site in Oklahoma using the Company's technology.

The principal activity of Velocys plc is a holding company. The three operating subsidiaries are Velocys, Inc., Velocys Technologies Limited and Velocys Project Solutions, LLC. In the Report and Accounts the entities are referred to collectively as the "Company", while Velocys plc is referred to as the "parent company".

Business review

A review of the Company's activities during the year and future outlook is dealt with in the Chairman's statement on page 2 and the Chief executive's report on pages 3-4.

Financial review

2014 was the first year where all the Company's revenues were from commercial sources as opposed to development payments and milestones. Revenue before exceptional items for 2014 was £1.7 million (2013: £4.8 million)(see note 5), which included the first revenue from a commercial plant plus some revenue from engineering services and studies for potential clients. As explained in the revenue recognition section of note 2, the Company adopted a change in accounting policy relating to recognition of revenue from reactor sales. Under this new policy, the company will recognise revenue on reactors when delivered.

As a result, previously recognised revenue from reactors in build in 2013 was reversed. The net effect of this was a negative exceptional item in revenue of £1.7 million.

Unfunded research and development costs and other administrative expenses increased to £21.0 million before exceptional items (2013: £16.8 million) as the Company continues to grow. Costs after exceptional items of £1.3 million (see note 4) are £22.3 million. The exceptional item, which is a non-cash item, represents an impairment of intangible assets (see note 2). Adjusted losses for the period* were £18.7 million (2013: £14.1 million). Cash outflow ** in the period was £18.1 million (2013: £12.5 million).

Velocys is well capitalised having successfully completed an equity funding on 20 October 2014 which raised £50.3 million (after expenses), and with a $2.0 million investment by the Company's manufacturing partner Shiloh Industries, Inc. in February 2014. At period end, the Company had £59.8 million of cash*** (FY 2013: £26.4 million).

Costs

The breakdown of costs in 2014 was £11.2 million of R&D costs (2013: £10.5m) and £9.9 million of administrative expenses (£6.3 million). The main areas of cost increase have been in areas required to reach full commercialisation: process engineering, value engineering and process control; and the pursuit of in-house project opportunities, such as the Ashtabula project. 2014 also saw significant costs for the operation of the Company's pilot plant, which completed important customer-supporting test runs during the year.

* Adjusted losses exclude the impact of foreign exchange losses, (2014: £1.1 million gain; 2013: £0.3 million loss) non-cash items (depreciation, amortisation and share-based payments: £4.3 million, 2013: £3.7 million) and exceptional non-cash items (2014: £1.3m; 2013: nil).

** Defined as cash movement excluding monies from fund raising and issuing shares.

*** Defined as cash, cash equivalents and short term investments (see note 23).

Strategic report (continued)

Substantial costs were also incurred in defending the Company's IP portfolio, some of which have been recouped as a result of a court judgement.

Key performance indicators

At the current stage of the business, the Directors consider that performance is most appropriately measured by achievement against technical and business development goals, which are outlined in the Chief executive's report. These goals include demonstrations of technical progress, milestones in commercial readiness and manufacturing capability, and indicators of the Company's ability and resources to support new projects and the development of sales prospects.

Employees

Velocys is committed to being a good employer and endeavours to train staff well, to pay them fairly and to maintain a safe environment in which they can work. Velocys is committed to equal opportunity for all its employees.

Velocys keeps detailed environmental health and safety records and takes the safety and well-being of its employees very seriously. During 2014 there were no Lost-Time Accidents across the Company's sites, which meant that the total number of operating hours without such an accident is over two million.

The Company began recording data in 2013 concerning the number of women employees in each area of the business. Of the 115 employees working for Velocys at 31 December 2014 25% were women (2013: 25% of 95 employees). The percentage of female employees broken down by areas of the business was as follows.

	2014	2013
Scientific & engineering	14%	14%
Sales, finance, HR & admin	53%	71%
Senior managers	29%	29%

Two of the eight members of the Board are women (2013: two of eight members).

Given the small size of the Company and the need for highly specialised and scarce talent, it is difficult to plan a goal based around a gender diversity metric. However, this will not deter the Company from ensuring that diversity is considered for placing talent and that gender diversity, as one element of the overall diversity of the Company's staff, will continue to be closely monitored.

Environment

Velocys is concerned to manage the environmental impact of its operations and understands that the first step in doing this is to analyse the key components, and to build up a data picture year on year. Air travel and building operations have been identified as two of the major contributors of CO_2 emissions by the Company.

In 2014 air travel on the Company's behalf contributed 533.6 tonnes of CO_2 (2013: 597.7 tonnes). The 2014 figure captures air travel booked by employees as well as through travel agencies and, referring to the average staff headcount in note 12, equates to 5.0 tonnes per employee (2013: 6.6 tonnes). For 2014 the proportion of air travel that was between the Company's offices in Oxfordshire, Ohio and Texas was 55%; there is no comparable figure for 2013.

During 2014 Velocys maintained records of kilowatt-hours (kWh) billed to the Company in respect of consumption of electricity and domestic gas, to determine its CO_2 emissions attributable to building operations. Emissions from consumption of electricity during the year were 905 tonnes, and from consumption of gas were 746 tonnes; there are no comparable figures for 2013.

Operating risks

The key operating risks of the Company and the measures taken to manage these are summarised below.

Technology

The Company continues to pursue development of the various aspects of its cutting-edge technology through a number of programmes. Each programme has a specific set of milestones, measurable goals, a timeline and budget. Performance against these criteria is monitored every month. Through this process the Company is able to identify any issues at an early stage and to take appropriate mitigating action.

Performance

With the prospect of the start up of its first commercial plant just months away, Velocys is committed to ensuring that its products will be able to meet their respective performance requirements. The measures put in place to achieve this include:

- Reserving the first of the commercial batch of reactors purely for testing
- Working with vendors who fabricate the Company's proprietary catalysts and reactors to secure petrochemical industry-standard warranties for these materials

- In conjunction with third parties, building a set of robust quality assurance/control programmes, and then reviewing and validating the implementation of these programmes
- Modelling client-specific standard and upset conditions using the Company's own testing and pilot facilities, and then developing mitigation or remediation strategies where testing identifies areas of risk
- Expanding the staff base and in particular bringing in personnel with relevant commercial experience
- Working with world-class partners to ensure delivery of products to customers, and combining with existing, well-proven technologies
- Developing commercial terms that do not unduly commit Velocys to performance beyond its capability, especially during the initial period of plant delivery and operation
- Commissioning an independent engineer's report, which has qualified the Company's technology as "sound"
- As the operation of customer plants is outside its control the Company's agreements with its customers state that it shall not be liable to licensees for environmental, toxic waste, hazardous waste or pollution liability.

Scale up

Velocys has engaged in a series of programmes to demonstrate the scale up of its reactor technology from laboratory to commercial scale allowing the technology to be assessed at relevant scale. In 2013 Velocys installed a pilot plant at its facility in Ohio and during 2014 this plant was run to test the target conditions for the ENVIA Energy Oklahoma commercial project.

Prior to that, the Company had successfully demonstrated its FT reactor in 2010, followed by the demonstration of a full-scale (nominal 25 barrel per day) reactor at a customer site in 2012, and progressed to a demonstration programme for a fully integrated GTL unit, which ran for much of 2013.

In the case of catalyst scale up, the Company works with established, reputable catalyst manufacturers in developing the capability to make available commercial quantities of catalyst. Catalyst produced at each stage of the scale up process is tested to ensure it meets the relevant specification. The Company's FT catalyst, supplied with the full-scale FT reactors, is now capable of being produced in commercial quantities.

Market adoption

Velocys is the proponent of a ground-breaking technology, and seeks to maximise the reassurance it can provide to its potential customers by working extensively with partners who are substantial players in their fields, and who have significant interest, through the prospects for competitive advantage, in developing the Company's technology commercially. The Company continually monitors publicly available information on the activities of competitors and on related technologies to ensure that it remains at the forefront of smaller scale GTL development.

The Company has developed a substantial pipeline of opportunities, which are being progressed through its own project development and business development teams as well as through its engineering partners. This pipeline has been boosted markedly by the addition of Velocys Project Solutions. The Company continually monitors and assesses the strength of this pipeline.

Funding

The Directors believe that the cash balance at the end of 2014 provides the Company with adequate funds to continue its operations and to be able to pursue selective opportunities as they arise. Notwithstanding the healthy cash balance at the end of 2014, the Directors continue to review, frequently and carefully, the appropriateness of the Company's ongoing spending commitments, as well as giving due consideration to the costs and benefits of strategic plans.

Manufacturing

Velocys partners with leading equipment and catalyst manufacturers to develop the capability and capacity to deliver commercial sales of its products. By preferring to work with manufacturing partners, with proven track-records in their respective fields, rather than developing in-house capability, the Directors believe that manufacturing risk is considerably reduced.

IP protection

The Company places great emphasis on enhancing and protecting its IP, both patented and non-patented. In 2014, Velocys was successful in its patent infringement and validity case against CompactGTL. This success has provided the opportunity for the Company to demonstrate the strength of its IP and its ability to defend it strongly.

Personnel retention

In a competitive marketplace and as a small, and relatively young company, Velocys is well aware that it needs to work hard to attract and retain high quality personnel, and it uses a range of advisers and has put in

Strategic report (continued)

place a package of benefits as well as a number of key policies in order to be able to do this. The Company has rolled out across its UK and US sites a range of schemes covering incentivisation, share options, training and performance evaluation.

External risks

The performance of Velocys is subject to macroeconomic conditions and changes in external factors such as oil and natural gas prices, interest and exchange rates, and inflation.

These risks are managed through monitoring and analysis of the economic climate and the operating environment, and by ensuring that Velocys has sufficient information to develop a thorough understanding of potential impacts, through which it can develop mitigating policies and contingencies. Additionally, where possible Velocys looks to ensure its contracts provide protection against adverse external factors.

It has been impossible to ignore the change in the oil price over recent months, and for Velocys these parameters have a particular relevance to future demand for those of the business's products that will provide solutions for the production of oil substitutes using natural gas as a feedstock. It is reasonable to expect that variations in the oil and gas prices will affect the economics of such projects.

However the Company holds firm to its belief that there are numerous other drivers for future demand which protect the Company against unpropitious moves in the commodity markets. Specific customer or geographical conditions or requirements will be significant factors for future demand, and may include an array of factors such as local regulatory requirements, security of supply, need for energy diversification, and particular local economics, taxes and subsidies.

Financial risks

The activities of Velocys expose it to a number of financial risks which are dealt with specifically below.

The use of financial derivatives is governed by Company policies, which are approved by the Board of Directors, and which provide a set of written principles for the management of these risks. At present Velocys makes use of financial derivatives only in the management of the foreign exchange exposure arising from funding its US operations.

The financial instruments of the Company, including the parent company, comprise cash and cash equivalents, and short term investments, as well as trade and other receivables, and trade and other payables. The main purpose of these financial instruments is to support the funding of business activities.

Credit risk

The Company's principal financial assets are cash, cash equivalents and short term investments, as well as trade and other receivables.

The Company's credit risk is primarily attributable to its trade receivables, which are concentrated in a small number of high value customer accounts. The Company has policies to manage this risk, including where applicable, carrying out relevant financial checks on customers, requiring letters of credit or advance payments.

The credit risk of liquid funds is limited to counterparties (banks) with high credit ratings assigned by international credit rating agencies. Velocys adheres to a treasury policy which ensures that liquid assets are only placed with high credit rated institutions and that the spread of such assets restricts the Company's exposure to any one institution.

Interest rates

Movements in interest rates affect Velocys through its holdings of cash balances and borrowings. As much certainty of interest income as can be garnered is generated by placing funds on fixed rate deposits as cash flows allow. All of the business's borrowings incur interest charges at a fixed rate.

Liquidity

Company policy is to maintain sufficient cash balances to meet anticipated requirements to a medium term horizon. Cash flow forecasts are regularly reviewed, resulting in cash balances being held for immediate withdrawal as necessary, with other funds being placed on time deposits of varying duration.

Exchange rates

A significant proportion of the Company's activities is undertaken in the US, resulting in a funding requirement for US dollars. Where possible, revenue is receipted in US dollars, which acts as a natural hedge against this exposure. To manage the remaining exposure a proportion of the Company's liquid assets is held in US dollars, and uncertainty over the impact of future exchange rate movements is managed through the use of forward contracts at fixed rates of exchange.

In the Company's consolidated accounts, there are significant US dollar denominated goodwill and purchased intangible assets relating to the acquisition of Velocys, Inc. These balances are subject to exchange rate fluctuations which result in movements in reserves. However, the Directors do not consider it necessary to hedge such exchange rate movements as they do not have any impact on the Company's cash position.

Capital management

The Company believes that at this stage of its development, equity is the most suitable form of funding for its activities and this forms the basis of the capital that it manages.

The Company's objectives when managing this capital are:

- to secure its ability to continue as a going concern
- to maintain an optimal capital structure to reduce the cost of capital
- to preserve sufficient funds to protect it against unforeseen events and risks
- to enable the Company to make funds available to take advantage of opportunities that can deliver positive benefits to the Company's shareholders and provide them with a return which rewards the risks undertaken.

These objectives are met through a robust planning process that includes an annual strategy and risk review, annual budgeting and regular re-forecasting.

The Company believes that it has sufficient cash and cash equivalents to meet its capital management objectives.

Company development activities

The Company continues to invest in development. The catalyst and microchannel technologies currently being developed are expected to make significant contributions to the growth of the business. The Directors regard investment in development as essential for success in the medium to long term.

Approved by the Board and signed on its behalf by:

Roy Lipski
Chief executive
27 April 2015

Directors' report

Business risks
A full explanation of the Company's risks and its risk management policies is made in the strategic report.

Substantial shareholdings
On 10 April 2015, the Company was notified of the following holdings of 3% or more of the issued share capital of Velocys plc.

	Number of shares held	Percentage of issued share capital
Lansdowne Partners	26,631,808	18.77%
Ervington Investments Limited	20,985,412	14.79%
Henderson Global Investors	17,189,515	12.11%
Invesco Asset Management	14,600,000	10.29%
Woodford Investment Management	11,478,922	8.09%
Ruffer LLP	8,400,000	5.92%

Fund raising
On 29 September 2014, the Company announced the successful conditional placing of shares to raise £50.3m net of expenses. This placing was approved at a general meeting of its shareholders on 17 October and the shares were admitted to trading on AIM on 20 October.

On 11 March 2014 the Company announced the purchase of shares by Shiloh Industries Inc ("Shiloh") as part of a commercial partnership to manufacture the Velocys FT reactor. Shiloh subscribed for 601,326 new ordinary shares of 1 pence each at a price of 200p per share.

Dividends
The Directors do not recommend any dividend for the year ended 31 December 2014 (2013: nil).

Directors
The Directors of Velocys plc as at 31 December 2014, who served throughout the year and up to the date of approval of the financial statements, were as follows:

Dr Pierre Jungels (Non-executive Chairman)
Roy Lipski (Chief executive)
Susan Robertson (Chief financial officer)
Dr Paul Schubert (Chief operating officer)
Dr Andrew Jamieson (Non-executive Director)
Dr Jan Verloop (Non-executive Director)
Sandy Shaw (Non-executive Director)
Julian West (Non-executive Director and from January 2015 Senior independent Director)

All Directors are subject to election by shareholders at the first opportunity after their appointment, and to re-election thereafter at intervals of not more than three years. At the 2015 annual general meeting the following Directors will retire and offer themselves for re-election.

- Andrew Jamieson
- Roy Lipski

Directors' qualifying third party indemnity provision
The Company maintains directors' qualifying third party indemnity insurance to provide cover for legal action against its Directors. This has been in place throughout the year and remains in place at the date of this report.

Directors' interests
The Directors who held office at 31 December 2014 had the following interests in the shares of parent company undertakings (as recorded in the Register of Directors' Interests and including those of the spouse or civil partner and children under 18).

	Velocys plc Ordinary £0.01 shares	
Name of Director	**31 December 2014**	31 December 2013
Pierre Jungels	223,031	223,031
Roy Lipski	2,417,098	2,417,098
Susan Robertson	304,874	304,874
Paul Schubert	–	–
Andrew Jamieson	25,000	25,000
Jan Verloop	150,837	150,837
Sandy Shaw	17,758	17,758
Julian West	75,000	75,000

Details of Directors' share options and service contracts are shown in the Directors' remuneration report.

Future developments
The Board aims to continue its corporate strategies as set out in the Chairman's statement and Chief executive's report.

Annual general meeting
The annual general meeting of the Company will be held at Milton Park Innovation Centre, 99 Park Drive, Milton Park, Oxfordshire, OX14 4RY at 10.45am on Tuesday 23 June 2015.

Auditors and disclosure of information to auditors

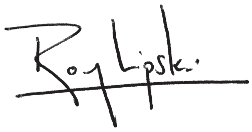
Each of the persons who is a Director at the date of approval of this report confirms that:

- so far as the Director is aware, there is no relevant audit information of which the Company's auditors are unaware, and
- the Director has taken all the steps that he/she ought to have taken as a Director in order to make himself/herself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of s418 of the Companies Act 2006.

PricewaterhouseCoopers LLP have expressed their willingness to continue in office as auditors and a resolution to reappoint them will be proposed at the forthcoming annual general meeting.

Approved by the Board and signed on its behalf by:



Roy Lipski
Chief executive
27 April 2015

Corporate governance report

Corporate governance

Companies who have their securities traded on AIM are not required to comply with the principles and provisions of the UK Corporate Governance Code (2010) and the amendments incorporated in the Corporate Governance Code (2012). The Board, however, has determined that the Company should maintain high standards of corporate governance and whilst not fully complying within this report with the UK Corporate Governance Code, including the full disclosure requirements, has adopted procedures and has taken steps to adopt the underlying principles, in so far as appropriate given the size of the Company and the nature of its operations.

Board of Directors

The Company is controlled by the Board of Directors which comprises three Executives, one of whom is the Chief executive, a Chairman and four Non-executive Directors. All of the Non-executive Directors are considered to be independent. The roles of Chief executive and Chairman are separate. All Directors are able to take independent advice to assist them in their duties if necessary. In January 2015, the Company announced that it had appointed one of the Non-executive Directors, Julian West as Senior independent Director. The detailed biographies of all Directors are provided on the Company's website.

The Board is responsible to shareholders for the proper management of Velocys and meets formally at least six times a year to set the overall direction and strategy of the Company, to review operating and financial performance and to consider and advise on senior management appointments. The Board also monitors and approves financial policy and budgets, including capital expenditure. All key operational decisions are subject to Board approval. The Company Secretary is responsible for ensuring that Board procedures are followed and that any and all applicable rules and regulations are complied with.

Directors are subject to election by shareholders at the first opportunity after their appointment. In addition, one third of Directors are subject to retirement by rotation at each annual general meeting. The Board has a process for evaluating the effectiveness of the Board and its committees by means of a questionnaire survey of all Board members. In addition, the Board has recently introduced a process for the evaluation of performance of and provision of feedback to each individual Board member, including the Chairman.

Committees of the Board

Remuneration committee

The remuneration committee comprises the Non-executive Directors chaired by Sandy Shaw. This committee reviews, inter-alia, the performance of the Executive Directors and sets the scale and structure of their remuneration and basis of their service agreements, having due regard to the interests of shareholders. The remuneration committee also determines the allocation of share options to Executive Directors. No Director has a service agreement exceeding one year. One of the policies of the Remuneration committee is that no individual participates in discussions or decisions concerning his or her own remuneration. The Directors' remuneration report is set out on pages 15 to 18.

Audit committee

The audit committee comprises the Non-executive Directors and is chaired by Dr Jan Verloop. Under its terms of reference it meets at least twice a year, and amongst other duties it reviews the Company's internal controls, accounting policies and financial reporting, and provides a forum through which the external auditors report. It meets at least once a year with the external auditors without Executive Directors present.

Under its current form, the audit committee does not have a member with recent and relevant financial experience with competence in accounting and/or auditing. The Board believes that this departure from the Corporate Governance code is currently acceptable given the stage of development of the Company and the otherwise strong level of financial literacy of its Non-executive members. The Board expects that this will not continue in the medium term and plans to give a high priority to financial experience in future Non-executive Board appointments.

Nominations committee

The nominations committee consists of the Non-executive Directors, under the chairmanship of Dr Pierre Jungels. It meets on average once a year, and amongst its other duties it reviews the composition of the Board and its succession planning, and keeps under review the leadership needs of the Company with a view to ensuring the continued ability of the Company to compete effectively in the marketplace.

Senior management team

The day-to-day management of the Company is overseen by the Senior management team, consisting of the Executive Directors and other senior managers, under the leadership of the Chief executive.

Board and committee attendance at scheduled Board and committee meetings

	Board	Audit committee	Remuneration committee	Nominations committee
Number of meetings held in 2014	7	2	6	2
Attendance* by:				
– Pierre Jungels	100%	100%	100%	100%
– Roy Lipski	100%	n/a	n/a	n/a
– Susan Robertson	100%	n/a	n/a	n/a
– Paul Schubert	100%	n/a	n/a	n/a
– Andrew Jamieson	100%	100%	100%	100%
– Jan Verloop	100%	100%	100%	100%
– Sandy Shaw	100%	100%	100%	100%
– Julian West	100%	100%	100%	100%

* The attendance percentage relates only to applicable meetings. During 2014, all Directors were eligible for Board meetings.

Relations with shareholders
The Board considers effective communication with shareholders to be very important, and encourages regular dialogue with investors. The Board responds promptly to questions received verbally or in writing. Directors regularly attend meetings with shareholders and analysts throughout the year. Shareholders will be given at least 21 days' notice of the annual general meeting, at which they will have the opportunity to discuss the Company's developments and performance.

The Company's web site www.velocys.com contains full details of the Company's activities, press releases and other details, as well as a link to the relevant web page of the London Stock Exchange web site for share price details, share trading activities and graphs, as well as Regulatory News Service ("RNS") announcements.

Maintenance of a sound system of internal control
The Directors have overall responsibility for ensuring that the Company maintains a system of internal control to provide them with reasonable assurance that the assets of the Company are safeguarded and that shareholders' investments are protected. The system includes internal controls appropriate for a Company of the size of Velocys, and covers financial, operational, compliance (including health and safety) and risk management. Such systems are designed to manage, rather than eliminate, the risk of failure to achieve business objectives; any system can provide only reasonable, and not absolute, assurance against material misstatement or loss. The process in place for reviewing Velocys' systems of internal control includes procedures designed to identify and evaluate failings and weaknesses, and, in the case of any categorised as significant, procedures exist to ensure that necessary action is taken to remedy the failings.

The Board has considered its policies with regard to internal controls as set out in the UK Corporate Governance Code and undertakes assessments of the major areas of the business and methods used to monitor and control them. In addition to financial risk, the review covers operational, commercial, regulatory and health and safety risks. The risk review is an ongoing process with reviews being undertaken on a regular basis.

The key procedures designed to provide an effective system of internal controls that are operating up to the date of sign-off of this report are set out below.

Control environment
There is an organisational structure with clearly defined lines of responsibility and delegation of accountability and authority.

Risk management
The Company employs Directors and senior personnel with the appropriate knowledge and experience for a business engaged in activities in its field of operations, and undertakes regular risk assessments and reviews of its activities.

Financial information
The Company prepares detailed budget and working capital projections which are approved annually by the Board and are maintained and updated regularly throughout the year. Detailed management accounts and working capital cash flows are prepared on a monthly basis and compared to budgets and projections to identify any significant variances.

Corporate governance report (continued)

Management of liquid resources
The Board is risk averse when investing the Company's surplus cash. The Company's treasury management policy is reviewed periodically, and sets out strict procedures and limits on how surplus funds are invested.

The Board has considered it inappropriate to establish an internal audit function, given the size of the Company. However, this decision will be reviewed as the operations of the Company develop.

Review of corporate governance disclosures
The Board has voluntarily complied with those key principles of the UK Corporate Governance Code in so far as appropriate given the size of the Company and the nature of its operations. These have not been formally reviewed by the Company's auditors. The auditors' responsibility extends only to reading this report as a part of the Annual report and accounts and considering whether it is consistent with the audited financial statements.

Directors' remuneration report

Introduction
The remuneration committee is committed to maintaining high standards of corporate governance and has taken steps to comply with the principles of best practice in so far as it can be applied practically given the size of the Company and the nature of its operations. Since it is not a requirement for companies that have securities listed on AIM to comply with the disclosure requirements of Directors' Remuneration Report Regulations 2013 or to comply with the UKLA Listing Rules and the disclosure provisions under schedule 8 to SI 2008/410 of the large and medium-sized companies and groups (accounts and reports) regulations 2008 certain disclosures are not included below.

Unaudited information
Remuneration report
The Board has applied the principles of good governance relating to Directors' remuneration as described below.

Remuneration committee
The remuneration committee comprises the Non-executive Directors under the chairmanship of Sandy Shaw. The committee's constitution and operation is compliant with the provisions of the UK Corporate Governance Code on Corporate Governance. When setting its remuneration policy for Executive Directors, the committee gives consideration to the provisions and principles of the UK Corporate Governance Code.

Remuneration policy for Executive Directors
The remuneration policy has been designed to ensure that Executive Directors receive appropriate incentive and reward given their performance, responsibility and experience. When assessing this, the remuneration committee looks to ensure that the policy aligns the interests of the Executive Directors with those of shareholders.

The Company's remuneration policy for Executive Directors is to:
- consider the individual's experience and the nature, complexity and responsibilities of their work in order to set a competitive salary that attracts and retains management of the highest quality
- link individual remuneration packages to the Company's long-term performance through bonus schemes and long-term share-based plans
- provide post-retirement benefits through payment into defined contribution pension schemes
- provide employment-related benefits including life assurance and medical insurance.

Remuneration of Executive Directors
Executive Directors' remuneration is considered annually. In addition, the remuneration committee undertakes a comprehensive review using external advisors every three years. The current remuneration package is based on such a review commissioned by the remuneration committee at the end of 2013. This review looked at the overall remuneration package for executives and made recommendations based on benchmarking with other companies similar in size, industry and stage of development. The basic components of this package are set out below.

<u>Base salary</u>
The base salary is reviewed annually at the beginning of each year. The review process undertaken by the remuneration committee has regard to the development of the Company and the contribution that individuals will continue to make. Consideration is also given to the need to retain and motivate individuals, and available information on the package levels in comparable organisations.

<u>Annual performance incentive</u>
All Executive Directors are eligible, at the discretion of the remuneration committee, for an annual bonus. The target bonus award for each individual is based on a percentage of base salary for each individual. In the case of the CEO, this percentage is 100%; for the other executives, this percentage is 75%. The maximum award for stretch target performance is twice the target amount. The remuneration committee sets performance targets for bonus awards at the beginning of each year. Awards are determined by both the performance of the individual and the Company as a whole at the end of each year. The performance targets for the Company comprise measures of certain financial, as well as technical and business development goals.

<u>Pensions and other benefits</u>
The Company contributes to individuals' defined contribution pension plans.

Other benefits provided are life assurance, private medical insurance and relocation allowances where applicable, in line with the Company's standard policies. In the case of Mr Lipski, who is located in the USA, he is entitled to the standard medical benefits provided to all of the Company's US full-time employees.

Directors' remuneration report (continued)

During 2013, Mr Lipski relocated from Plain City to Houston and the Company paid for the costs of relocation for himself and his family including housing rental costs for a defined period of time to facilitate this move. Rental costs continued part way through 2014 and have now ceased. Where these costs were taxable, the Company paid grossed up costs. These costs are included in the other benefits category in the analysis shown below. The review of the CEO's base salary in 2014 included recognition of a cost of living adjustment associated with this move to Houston.

ELTIP awards
As part of its comprehensive review of executive remuneration in 2013 and 2014, the remuneration committee concluded that a revised long term incentive plan needed to be adopted for the executives going forward. Following extensive consultation with both advisors and the major investors in the Company, a new ELTIP scheme was adopted in 2014 subject to obtaining relevant approval from shareholders for revised headroom limits for the number of awards that could be issued under the share plan scheme. This approval was obtained at a general meeting of shareholders in February 2015, following which, the Company made ELTIP awards to its executives under the new scheme in February 2015 for both 2014 and 2015.

The new ELTIP scheme (within NELTIP in note 15) has the following features:
- awards include both time vesting and performance vesting elements
- the performance criteria are designed to align with shareholder interests and are based on compound annual growth of the Company's market capitalisation excluding fund raising subsequent to 1 January 2015
- targets set for achievement of the maximum award are designed to be stretching
- a minimum performance threshold below which none of the performance awards vest
- pro rata vesting of award between minimum and stretch targets, up to maximum award amount
- all awards are subject to the detailed rules within the Velocys employee option plan and include malus and clawback provisions.

In the case of the CEO, it was determined that the ELTIP would comprise a single 5 year award, intended to ensure focus on growth targets over a longer horizon. This award includes an element that vests on a time basis (30% of the award), with the remainder related to performance. Of the performance component, no awards vest unless a minimum threshold performance is met with pro rata vesting between 0 -100% for performance between the minimum threshold and the maximum stretch target.

In the case of the other Executive Directors, the awards are made annually, based on a multiple of base salary and have a three year performance period. Of these awards, 23% vest on a time basis. For the remaining performance based awards, 30% vest at a threshold level of performance with additional awards vesting pro rata for performance between the minimum and the maximum stretch target.

Remuneration policy for Non-executive Directors
The remuneration of the Non-executive Directors is determined by the Board as a whole, based on a review of current practices in other equivalent companies. The Non-executive Directors do not receive any pension payments towards private arrangements, nor do they participate in any of the bonus schemes. Remuneration is based on a fixed fee, plus a separate fee for any additional consulting services.

Each Non-executive Director has a service agreement that is reviewed annually by the Board. All Non-executive Directors retire by rotation and are subject to re-election every 3 years at the annual general meeting.

Audited information
Directors' remuneration

The Directors' received the following remuneration in relation to the year to 31 December 2014.

Name of Director	Salary and fees £	Bonus £	Other benefits £	EBT payment £	**2014** Totals £	Pension contributions £	2013 Totals £	2013 Pension £
Executive								
Roy Lipski *	289,346	576,596	77,320	–	943,262	16,095	541,017	14,050
Susan Robertson	187,500	195,117	929	–	383,546	13,181	272,371	11,547
Paul Schubert	165,687	128,311	24,226	195,349	513,573	4,734	131,773	4,890
Non-executive								
Pierre Jungels	80,000	–	–	–	80,000	–	66,500	–
Sandy Shaw	45,000	–	–	–	45,000	–	40,000	–
Andrew Jamieson	45,000	–	–	–	45,000	–	40,000	–
Jan Verloop	43,705	–	–	–	43,705	–	39,281	–
Julian West	45,000	–	–	–	45,000	–	22,500	–
Aggregate emoluments and pension contributions	901,238	900,024	102,475	195,349	2,099,086	34,010	1,153,442	30,487

* Includes Company-reimbursed relocation costs associated with the move to Houston as described above.

Directors' share options

Aggregate emoluments disclosed above include amounts paid through the employee benefit trust (EBT) in relation to share options exercised during the year. They do not however include any amounts relating to share based awards that are not exercised during the year. Such amounts are included in the share-based payments award included in the financial statements, details of which are provided in note 15.

In December 2014, Dr Schubert exercised 277,100 options. These resulted in a net gain of £368,000 inclusive of a bonus award through the employee benefit trust, shown in the remuneration table above.

ELTIP awards made in 2015 relating to 2014

Due to the need to obtain shareholder approval for the revised share plan, awards under the revised ELTIP plan for 2014 were not made until 26 February 2015. However, these were included in the calculation of the share-based payment charge for 2014. The awards were as follows:

Name of Director	Award type	Shares under award	% with performance conditions	Exercise price (£)	Earliest date of exercise	Date of expiry
Roy Lipski	RSU *	7,000,000	70%	n/a	02/01/19	02/01/20
Susan Robertson	Option	245,881	77%	£0.01	02/01/17	26/02/25
Paul Schubert	RSU *	187,826	77%	n/a	02/01/17	02/01/18

Also on 26 February, further awards were made to two executives, representing the ELTIP annual awards for the year commencing 1 January 2015, as follows:

Name of Director	Award type	Shares under award	% with performance conditions	Exercise price (£)	Earliest date of exercise	Date of expiry
Susan Robertson	Option	205,508	77%	£0.01	02/01/18	26/02/25
Paul Schubert	RSU *	156,985	77%	n/a	02/01/18	02/01/19

* Restricted share units

Details of all Directors' shareholdings are disclosed on page 10 in the Directors' report.

Directors' remuneration report (continued)

Details of all options held by the Directors at 31 December 2014 are as follows.

Name of Director	At 31 December 2013	Granted	Exercised	Lapsed	At 31 December 2014	Exercise price (£)	Earliest date of exercise	Date of expiry	Exercisable at 31 December 2014
Roy Lipski									
Bonus 2009	342,000	–	–	–	342,000	0.01	31/03/10	31/03/20	342,000
ELTIP 2008	100,000	–	–	–	100,000	0.01	24/01/11	19/11/18	100,000
ELTIP 2009	140,000	–	–	–	140,000	0.01	31/01/12	04/11/19	140,000
ELTIP 2011	625,000	–	–	–	625,000	0.58	20/09/11	20/09/21	625,000
ELTIP 2012	818,000	–	–	–	818,000	0.49	01/01/15	01/02/22	–
ELTIP 2012	613,000	–	–	–	613,000	0.49	01/01/12	01/02/22	613,000
ELTIP 2013	1,126,563	–	–	–	1,126,563	1.59	01/01/16	12/04/23	–
ELTIP 2013	281,640	–	–	–	281,640	1.59	12/04/13	12/04/23	187,760
ELTIP 2014	–	986,306	–	–	986,306	1.64	01/01/17	01/04/24	–
ELTIP 2014	–	246,576	–	–	246,576	1.64	01/04/14	01/04/24	82,192
Total	4,046,203	1,232,882	–	–	5,279,085				2,089,952
Susan Robertson									
EMI	62,893	–	–	–	62,893	1.59	29/10/10	01/04/18	62,893
Bonus 2008	42,105	–	–	–	42,105	0.01	31/03/09	31/03/19	42,105
Bonus 2010	37,655	–	–	–	37,655	0.01	20/03/11	20/03/21	37,655
ELTIP 2009	105,000	–	–	–	105,000	0.01	31/01/12	21/11/19	105,000
ELTIP 2011	390,625	–	–	–	390,625	0.01	20/09/11	20/09/21	390,625
ELTIP 2012	365,000	–	–	–	365,000	0.49	01/01/15	01/02/22	–
ELTIP 2012	273,803	–	–	–	273,803	0.49	01/01/12	01/02/22	273,803
ELTIP 2013	502,930	–	–	–	502,930	1.59	01/01/16	12/04/23	–
ELTIP 2013	125,732	–	–	–	125,732	1.59	12/04/13	12/04/23	83,821
ELTIP 2014	–	440,316	–	–	440,316	1.64	01/01/17	01/04/24	–
ELTIP 2014	–	110,079	–	–	110,079	1.64	01/04/14	01/04/24	36,693
Total	1,905,743	550,395	–	–	2,456,138				1,032,595
Paul Schubert									
EMI	320,513	–	(112,619)	–	207,894	0.56	04/10/14	04/10/21	207,894
ELTIP 2012	119,000	–	–	–	119,000	0.49	01/01/15	01/02/22	–
ELTIP 2012	52,600	–	(52,600)	–	–	–	–	–	–
ELTIP 2013	502,930	–	–	–	502,930	1.59	01/01/16	12/04/23	–
ELTIP 2013	125,733	–	(83,822)	–	41,911	1.59	01/01/15	12/04/23	–
ELTIP 2014	–	336,711	–	–	336,711	1.64	01/01/17	01/04/24	–
ELTIP 2014	–	84,178	(28,059)	–	56,119	1.64	01/01/15	01/04/24	–
Total	1,120,776	420,889	(277,100)	–	1,264,565				207,894
Andrew Jamieson									
2010	6,500	–	–	–	6,500	0.01	31/03/11	31/03/21	6,500
2012	10,204	–	–	–	10,204	0.01	20/04/12	19/04/22	10,204
2013	3,390	–	–	–	3,390	0.01	01/05/13	05/01/23	3,390
Total	20,094	–	–	–	20,094				20,094

The market price of the parent company's shares as at 31 December 2014 was 144p (2013: 145p) and the range during the year was 140p to 237p (2013: 124p to 201p). Details of options and the cost of share-based payments are given in note 15.

Statement of directors' responsibilities

The Directors are responsible for preparing the annual report, the Strategic report, the Director's report, the Directors' remuneration report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have prepared the financial statements for the parent company (Velocys plc) and the Company (Velocys plc and its subsidiaries) 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 Company and of the parent company, and of the profit or loss of the Company for that period. In preparing these financial statements, the Directors are required to:

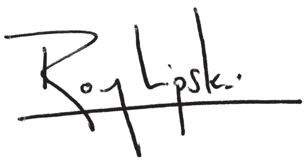
- select suitable accounting policies and then apply them consistently
- make judgements and accounting estimates that are reasonable and prudent
- state whether applicable IFRSs as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial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

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and of Velocys plc and enable them to ensure that the financial statements and the Directors' remuneration report comply with the Companies Act 2006 and, as regards the Company financial statements, Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Company and of Velocys plc and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

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

The Directors consider that the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's performance, business model and strategy.

On behalf of the Board



Roy Lipski
Chief executive
27 April 2015

Independent auditors' report
to the members of Velocys plc

Report on the financial statements

Our opinion

In our opinion, Velocys plc's group financial statements and 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 2014 and of the group's loss and the group's and 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
- have been prepared in accordance with the requirements of the Companies Act 2006.

What we have audited

Velocys plc's financial statements comprise:

- the consolidated and parent company statement of financial position as at 31 December 2014
- the consolidated income statement and consolidated statement of comprehensive income for the year then ended
- the consolidated and parent company statement of cash flows for the year then ended
- the consolidated and parent company statement of changes in equity for the year then ended, and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

The financial reporting framework that has been applied in the preparation of the financial statements is applicable law and IFRSs as adopted by the European Union.

In applying the financial reporting framework, the directors have made a number of subjective judgements, for example in respect of significant accounting estimates. In making such estimates, they have made assumptions and considered future events.

Opinion on other matter prescribed by the Companies Act 2006

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

Other matters on which we are required to report by exception

Adequacy of accounting records and information and explanations received

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 company, or returns adequate for our audit have not been received from branches not visited by us, or
- the company financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

Directors' remuneration

Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of directors' remuneration specified by law are not made. We have no exceptions to report arising from this responsibility

Responsibilities for the financial statements and the audit

Our responsibilities and those of the directors

As explained more fully in the Statement of directors' responsibilities set out on page 19, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) ("ISAs (UK & Ireland)"). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

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

What an audit of financial statements involves

We conducted our audit in accordance with ISAs (UK & Ireland). An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the group's and the parent company's circumstances and have been consistently applied and adequately disclosed
- the reasonableness of significant accounting estimates made by the directors, and
- the overall presentation of the financial statements.

We primarily focus our work in these areas by assessing the directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the financial statements.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

In addition, we read all the financial and non-financial information in the Annual report and accounts 2014 to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Sam Taylor (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Reading
27 April 2015

Consolidated income statement
for the year ended 31 December 2014

	Note	2014 £'000 Before exceptional items	2014 £'000 Exceptional items (note 4)	2014 £'000 Total	2013 £'000
Revenue	6	1,736	(1,742)	(6)	4,753
Cost of sales		(536)	1,742	1,206	(3,300)
Gross profit		1,200	–	1,200	1,453
Unfunded research and development costs		(11,163)	–	(11,163)	(10,477)
Share-based payments	15	(3,407)	–	(3,407)	(2,782)
Other administrative expenses		(9,853)	(1,328)	(11,181)	(6,339)
Total administrative expenses		(24,423)	(1,328)	(25,751)	(19,598)
Operating loss	10	(23,223)	(1,328)	(24,551)	(18,145)
Finance income	7	1,225	–	1,225	419
Finance costs	8	(29)	–	(29)	(364)
Other income	9	56	–	56	58
Finance income, net		1,252	–	1,252	113
Loss before income tax		(21,971)	(1,328)	(23,299)	(18,032)
Income tax credit	13	929	–	929	1,111
Loss for the financial year attributable to the owners of Velocys plc		(21,042)	(1,328)	(22,370)	(16,921)
Loss per share attributable to the owners of Velocys plc					
Basic and diluted loss per share (pence)	16	(17.24)		(18.33)	(14.60)

The notes on pages 30 to 59 are part of these consolidated financial statements.

The Company has elected to take the exemption under Section 408 of the Companies Act 2006 to not present the parent company income statement and statement of comprehensive income. The loss for the parent company for the year was £5,649,000 (2013: loss £6,323,000).

Consolidated statement of comprehensive income
for the year ended 31 December 2014

	2014 £'000 Before exceptional items	2014 £'000 Exceptional items (note 4)	2014 £'000 Total	2013 £'000
Loss for the year	(21,042)	(1,328)	(22,370)	(16,921)
Other comprehensive expense				
Items that will be reclassified subsequently to profit or loss when specific conditions are met				
Foreign currency translation differences	1,108	–	1,108	(269)
Total comprehensive expense for the year	(19,934)	(1,328)	(21,262)	(17,190)

The notes on pages 30 to 59 are part of these consolidated financial statements.

Consolidated statement of financial position
as at 31 December 2014

	Note	**2014** £'000	2013 £'000
Assets			
Non-current assets			
Intangible assets	17	28,347	24,971
Property, plant and equipment	18	4,065	2,084
Investments	20	1,711	–
		34,123	27,055
Current assets			
Trade and other receivables	21	653	1,112
Current income tax asset		1,778	1,750
Inventory	22	291	263
Derivative financial instruments	27	435	–
Short term investments – funds held on deposit	23	28,083	11,875
Cash and cash equivalents	23	31,693	14,475
		62,933	29,475
Total assets		97,056	56,530
Liabilities			
Current liabilities			
Trade and other payables	24	(10,902)	(6,021)
Derivative financial instruments	27	–	(263)
Borrowings	26	(267)	(104)
		(11,169)	(6,388)
Non-current liabilities			
Trade and other payables	25	(69)	(232)
Borrowings	26	(999)	(1,192)
Deferred tax	14	(269)	–
		(1,337)	(1,424)
Total liabilities		(12,506)	(7,812)
Net assets		84,550	48,718
Capital and reserves attributable to owners of Velocys plc			
Called up share capital	29	1,419	1,164
Share premium account	29	149,225	95,793
Merger reserve		369	369
Share-based payment reserve		13,220	9,813
Foreign exchange reserve		(2,151)	(3,259)
Accumulated losses		(77,532)	(55,162)
Total equity		84,550	48,718

The notes on pages 30 to 59 are part of these consolidated financial statements.

The financial statements on pages 22 to 59 were approved by the Board of Directors and authorised for issue on 27 April 2015. They were signed on its behalf by:

Susan Robertson
Chief financial officer

Company number 5712187

Velocys plc statement of financial position
as at 31 December 2014

	Note	2014 £'000	2013 £'000
Assets			
Non-current assets			
Investments in subsidiaries	19	128,752	77,355
Current assets			
Trade and other receivables	21	76	–
Current income tax asset		1,357	1,300
Total assets		130,185	78,655
Current liabilities			
Trade and other payables	24	(85)	–
Total liabilities		(85)	–
Net assets		130,100	78,655
Capital and reserves attributable to owners of Velocys plc			
Called up share capital	29	1,419	1,164
Share premium account	29	149,225	95,793
Share-based payment reserve		13,220	9,813
Accumulated losses		(33,764)	(28,115)
Total equity		130,100	78,655

The notes on pages 30 to 59 are part of these consolidated financial statements.

The financial statements on pages 22 to 59 were approved by the Board of Directors and authorised for issue on 27 April 2015. They were signed on its behalf by:

Susan Robertson
Chief financial officer

Company number 5712187

Consolidated statement of changes in equity
as at 31 December 2014

	Called up share capital £'000	Share premium account £'000	Share-based payments reserve £'000	Merger reserve £'000	Foreign exchange reserve £'000	Accumulated losses £'000	Total equity £'000
Balance at 1 January 2013	914	66,662	7,031	369	(2,990)	(38,241)	33,745
Comprehensive income							
Loss for the year	–	–	–	–	–	(16,921)	(16,921)
Other comprehensive income							
Foreign currency translation differences	–	–	–	–	(269)	–	(269)
Total comprehensive expense	–	–	–	–	(269)	(16,921)	(17,190)
Transactions with owners							
Share-based payments – value of employee services	–	–	2,782	–	–	–	2,782
Proceeds from share issues	250	29,131	–	–	–	–	29,381
Total transactions with owners	250	29,131	2,782	–	–	–	32,163
Balance at 1 January 2014	1,164	95,793	9,813	369	(3,259)	(55,162)	48,718
Comprehensive income							
Loss for the year	–	–	–	–	–	(22,370)	(22,370)
Other comprehensive income							
Foreign currency translation differences	–	–	–	–	1,108	–	1,108
Total comprehensive expense	–	–	–	–	1,108	(22,370)	(21,262)
Transactions with owners							
Share-based payments – value of employee services	–	–	3,407	–	–	–	3,407
Proceeds from share issues	247	51,785	–	–	–	–	52,032
Issue of ordinary shares in relation to business combination	8	1,647	–	–	–	–	1,655
Total transactions with owners	255	53,432	3,407	–	–	–	57,094
Balance at 31 December 2014	1,419	149,225	13,220	369	(2,151)	(77,532)	84,550

The notes on pages 30 to 59 are part of these consolidated financial statements.

Velocys plc statement of changes in equity
as at 31 December 2014

	Called up share capital £'000	Share premium account £'000	Share-based payments reserve £'000	Accumulated losses £'000	Total equity £'000
Balance at 1 January 2013	914	66,662	7,031	(21,792)	52,815
Comprehensive income					
Loss for the year	–	–	–	(6,323)	(6,323)
Total comprehensive expense	–	–	–	(6,323)	(6,323)
Transactions with owners					
Share-based payments – value of employee services	–	–	2,782	–	2,782
Proceeds from share issues	250	29,131	–	–	29,381
Total transactions with owners	250	29,131	2,782	–	32,163
Balance at 1 January 2014	1,164	95,793	9,813	(28,115)	78,655
Comprehensive income					
Loss for the year	–	–	–	(5,649)	(5,649)
Total comprehensive income	–	–	–	(5,649)	(5,649)
Transactions with owners					
Share-based payments – value of employee services	–	–	3,407	–	3,407
Proceeds from share issues	247	51,785	–	–	52,032
Issue of ordinary shares in relation to business combination	8	1,647	–	–	1,655
Total transactions with owners	255	53,432	3,407	–	57,094
Balance at 31 December 2014	1,419	149,225	13,220	(33,764)	130,100

The notes on pages 30 to 59 are part of these consolidated financial statements.

Consolidated statement of cash flows
for the year ended 31 December 2014

	Note	2014 £'000	2013 £'000
Cash flows from operating activities			
Operating loss before taxation		(24,551)	(18,145)
Depreciation and amortisation		909	878
Loss on disposal of property, plant and equipment		11	–
Loss on disposal of intangible assets		154	–
Impairment of intangible assets		1,328	–
Share-based payments		3,407	2,782
(Gain) loss on derivative financial instruments		(698)	263
Changes in working capital (excluding the effects of exchange differences on consolidation)			
– Trade and other receivables		282	702
– Trade and other payables		2,507	2,331
– Inventory		(8)	62
Tax credits (paid) received		901	(39)
Other		–	6
Net cash used in operating activities		(15,758)	(11,160)
Cash flows from investing activities			
Purchase of property, plant and equipment		(1,544)	(971)
Purchase of intangible assets		(429)	(418)
Investment in GTL JV		(1,613)	–
Interest received		358	197
Interest paid		(37)	(38)
Proceeds from sale of fixed assets		56	52
Increase in funds placed on deposit	23	(16,208)	(11,875)
Net cash used in investing activities		(19,417)	(13,053)
Cash flows from financing activities			
Net proceeds of issuance of ordinary shares		51,570	29,381
(Decrease) increase in borrowing	26	(104)	70
Net cash generated from financing activities		51,466	29,451
Net increase in cash and cash equivalents		16,291	5,238
Cash and cash equivalents at beginning of year	23	14,475	9,451
Exchange gains (losses) on cash and cash equivalents		927	(214)
Cash and cash equivalents at end of year		31,693	14,475

The notes on pages 30 to 59 are part of these consolidated financial statements.

Velocys plc statement of cash flows
for the year ended 31 December 2014

	2014 £'000	2013 £'000
Cash flows from operating activities		
Loss before income tax	(7,999)	(7,743)
Movement in intercompany balances	(44,219)	(21,638)
Changes in working capital (excluding the effects of exchange differences on consolidation)		
– Trade and other receivables	(78)	–
– Trade and other payables	85	–
Cash consumed by operations	(52,211)	(29,381)
Tax credit received	641	–
Net cash used in operating activities	(51,570)	(29,381)
Cash flows from financing activities		
Net proceeds of issuance of ordinary shares	51,570	29,381
Net cash generated from financing activities	51,570	29,381
Net movement in cash and cash equivalents	–	–
Cash and cash equivalents at beginning of year	–	–
Cash and cash equivalents at end of year	–	–

The notes on pages 30 to 59 are part of these consolidated financial statements.

Notes to the financial statements

1. General information

Velocys plc is a company incorporated in England and Wales and domiciled in England. It operates through its subsidiaries Velocys Technologies Limited and Velocys (USA Holdings) LLC, which holds Velocys, Inc. and Velocys Project Solutions, LLC, and collectively they are referred to in the Notes to the financial statements as the "Company", with Velocys plc as the "parent company". The nature of the Company's operations and its principal activities are set out in the summary on the inside front cover and on the highlights page, and in the Chairman's statement, the Chief executive's report and the Strategic report on pages 2 to 9.

The parent company is a public limited company that is listed on AIM.

2. Accounting policies

The principal accounting policies applied in the preparation of these consolidated and parent company financial statements are summarised below. The policies have been consistently applied to all the years presented unless otherwise stated.

Basis of preparation

The consolidated and parent company financial statements have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU), IFRIC Interpretations and the Companies Act 2006 applicable to companies reporting under IFRS and Article 4 of the IAS Regulation. The consolidated and parent company financial statements have been prepared under the historical cost convention, as modified for fair value required under IFRS and measured in accordance with IFRS 13 'Fair value measurement'.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Company's accounting policies. Areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in note 3.

Going concern

The Directors have, at the time of approving the financial statements, a reasonable expectation that the Company and the parent company have adequate resources to continue in operational existence for the foreseeable future. Thus they continue to adopt the going concern basis of accounting in preparing the financial statements.

Accounting developments

The following new standards, amendments to standards and interpretations are mandatory for the first time for the financial year beginning 1 January 2014:

- Amendments to IAS 36, 'Impairment of assets', on the recoverable amount disclosures for non-financial assets. This amendment removed certain disclosures of the recoverable amount of cash generating units which had been included in IAS 36 by the issue of IFRS 13. The amendment was not mandatory for the Company until 1 January 2014, however the Company decided to early adopt the amendment as of 1 January 2013. The amendment does not impact on the disclosures given in the financial information.

The following new standards, amendments to standards and interpretations are mandatory for the first time for the financial year beginning 1 January 2014, but are not currently relevant for the Company:

- IFRS 10, 'Consolidated financial statements' builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent company. The Company has assessed that this will not impact the entities of the Company.
- IFRS 11, 'Joint arrangements'. This standard provides for a more realistic reflection of joint arrangements by focusing on the rights and obligations of the arrangement, rather than its legal form. There are two types of joint arrangements: joint operations and joint ventures. Proportional consolidation of joint ventures is no longer allowed. This standard was considered in relation to the investment in GTL JV, however the investment has been classified as assets available for sale. Therefore, the change to the standard has no impact on the Company.
- IFRS 12 'Disclosure of interests in other entities'. This standard includes the disclosure requirements for all forms of interest in other entities, including joint arrangements, associates, special purpose vehicles and other off balance sheet vehicles. The standard is not applicable to the Company.
- IAS 27 (revised 2011), 'Separate financial statements'. This clarifies the point that the consequential amendments from IAS 27 to IAS 21 'The effect of changes in foreign exchanges rates', IAS 28 'Investments in associates', and IAS 31 'Interests in joint ventures', apply prospectively for annual periods beginning on or after 1 July 2009. The amendment does not impact the Company.

- IAS 28 (revised 2011), 'Investments in associates and joint ventures'. This standard includes the requirements for joint ventures, as well as associates, to be equity accounted following the issue of IFRS 11. The amendment does not impact the Company.
- Amendments to IFRS 10, 'Consolidated financial statements', IFRS 12 and IAS 27 for investment entities. These amendments mean that many funds and similar entities will be exempt from consolidating most of their subsidiaries. These amendments are not currently relevant to the Company.
- Amendments to IFRS 10, IFRS 11 and IFRS 12. These amendments provide additional transition relief to IFRSs 10, 11 and 12, limiting the requirement to provide adjusted comparative information to only the preceding comparative period. These amendments are not currently relevant to the Company.
- IAS 32 (amendment), 'Financial instruments – Presentation' on asset and liability offsetting. This amendment clarifies some of the requirements for offsetting financial assets and financial liabilities on the balance sheet. The amendment is not applicable to the Company.
- IFRIC 21 'Levies'. This is not applicable to the Company.
- Amendment to IAS 19 regarding defined benefit plans. The standard is not applicable to the Company as there is no defined benefit pension scheme. This is applicable for accounting periods beginning on or after 1 July 2014.

The following new standards, amendments to standards and interpretations are mandatory for the first time for the financial year beginning 1 January 2015 or later, but are not currently relevant for the Company:

- IFRS 9 'Financial instruments', on 'Classification and measurement' (effective 1 January 2015). This is the first part of a new standard on classification and measurement of financial assets that will replace IAS 39. IFRS 9 has two measurement categories: amortised cost and fair value. All equity instruments are measured at fair value. A debt instrument is measured at amortised cost only if the entity is holding it to collect contractual cash flows and the cash flows represent principal and interest. Otherwise it is at fair value through profit or loss. Amortised cost accounting will also be applicable for most financial liabilities, with bifurcation of embedded derivatives. The main change is that in cases where the fair value option is taken for financial liabilities, the part of a fair value change due to an entity's own credit risk is recorded in other comprehensive income rather than the income statement, unless this creates an accounting mismatch. The Company is yet to assess the impact of IFRS 9 on its financial information. The Company will also consider the impact of the remaining phases of IFRS 9 when completed by the Board.
- IFRS 14 'Regulatory deferral accounts' (effective from 1 January 2016). This is not currently relevant to the Company.
- IFRS 15 'Revenue from contracts with customers' (effective from 1 January 2017). The IASB and FASB have jointly issued a converged standard on the recognition of revenue from contracts with customers. The standard will improve the financial reporting of revenue and improve comparability of the top line in financial statements globally. The Company has not chosen to early adopt this standard, but it is considered relevant for future accounting periods.
- Amendments to IAS 16 and IAS 38 'Clarification of acceptable methods of depreciation and amortisation' (effective from 1 January 2016). In this amendment the IASB has clarified that the use of revenue-based methods to calculate the depreciation of an asset is not appropriate because revenue generated by an activity that includes the use of an asset generally reflects factors other than the consumption of the economic benefits embodied in the asset. The IASB has also clarified that revenue is generally presumed to be an inappropriate basis for measuring the consumption of the economic benefits embodied in an intangible asset. The Company has adopted the units-of-production method of amortisation with the measured unit being reactors sold. The Company did not recognise expense in 2014 but expects amortisation to begin in 2015 based on projected delivery dates for commercial reactors. As a result no change to the accounting policy will be required.

Financial risk management policies

Financial risk management policies are set out in the Strategic report on pages 8 and 9.

Significant accounting policies

Consolidation – subsidiaries

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Company. The cost of an acquisition is measured as the fair value of the assets acquired, equity instruments issued and liabilities incurred or assumed at the date of exchange plus, for acquisitions completed prior to 1 January 2010, costs directly attributable to the acquisition. For acquisitions completed on or after 1 January 2010, directly attributable costs are expensed. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the acquiring company's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement. Acquired subsidiaries are consolidated from the date on which control of the subsidiary is transferred to the Company.

Notes to the financial statements (continued)

Intercompany transactions, balances and unrealised gains and losses on transactions between Company entities are eliminated. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Company.

Contingent consideration is initially measured at fair value on the acquisition date and classified as a liability. It is remeasured at fair value at the balance sheet date and any change in value is recognised directly in the consolidated income statement.

Exceptional items
Items that are material because of their size or nature, and/or that are non-recurring are considered as exceptional items. Exceptional items are presented with the line items to which they best relate. During 2014, exceptional items have been included in the consolidated income statement.

Segment reporting
Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The person or persons responsible for allocating resources and assessing performance of the operating segments has been identified as the Senior management team, who take operational decisions.

Foreign currency translation
Functional and presentation currency
Items included in the financial statements of each of the Company's entities 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 sterling (£), which is Velocys plc's functional and the Company's presentation currency.

Transactions and balances
Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the consolidated income statement. Foreign exchange gains and losses that relate to borrowings and cash and cash equivalents are presented in the income statement within 'finance income' or 'finance costs'.

Entities within the Company
The results and financial position of all the Company entities (none of which has the currency of a hyper-inflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet
- income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the rate on the dates of the transactions), and
- all resulting exchange differences are recognised as a movement within equity.

On consolidation, exchange differences arising from the translation of the net investment in foreign operations are taken to shareholders' equity.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

Cash and cash equivalents including short term deposits
Cash and cash equivalents includes cash in hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities on the balance sheet.

Bank accounts held that have an original maturity of more than three months, or that are subject to significant restrictions over access, are not presented as cash and cash equivalents. Such amounts are shown separately as short term investments or other financial assets with appropriate disclosure of the related terms.

Inventory
Inventories are stated at the lower of cost or net realisable value. Cost is determined on a first-in, first-out basis and includes transport and handling costs. In the case of manufactured products, cost includes all direct expenditure

including production overheads. Where necessary, provision is made for obsolete, slow-moving and defective inventories. Items purchased for use in externally funded research and development contracts are expensed to that contract immediately. Items held for the Company's own development are also expensed when acquired. Items purchased for ongoing commercial sale are held in inventory and expensed when used or sold.

Leases
Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

The Company leases certain property, plant and equipment. Leases under which the Company incurs substantially all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalised on commencement of the lease at the lower of the fair value of the leased property and the present value of the minimum lease payments.

Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The corresponding rental obligations, net of finance charges, are included in other long-term payables. The interest element of the finance cost is also charged to the income statement over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The property, plant and equipment acquired under finance leases is depreciated over the shorter of the useful life of the asset and the lease term.

Revenue recognition
Revenue is measured at the fair value of consideration received or receivable, and represents amounts receivable for goods and services provided in the normal course of business, net of trade discounts, value added tax and other sales-related taxes after eliminating sales within the Company.

Revenue is recognised only when the collection of related receivables is probable. When uncertainty arises about the collectability of an amount that has already been recorded in revenue, any provision required as a result of that uncertainty is recognised as an expense and not a reduction in revenue.

Revenue related to FT reactors and catalyst
Prior to 2014 the Company recognised revenue and costs from its FT reactors over the manufacturing period, where the right to consideration was accrued on a percentage of completion basis under IAS 11. In 2014, after the restructuring of a major supply agreement, which provides a more consistent measure of the cost of each reactor, the Company changed its method, and now recognises FT reactor revenue and costs when substantially all risk and reward associated with the reactor has passed to the customer under IAS 18 (see note 4); this will be upon delivery of reactors. The supplier agreement to which changes were made, was the first of its kind into which Velocys had entered, and was designed to cover the manufacture of the first eight commercial reactors. As this process developed and evolved the partners agreed that it would be appropriate for the contract to be amended to reflect this evolution.

Catalyst sales income will be recognised monthly, whilst the service element will be recognised when services are provided. Licence fee revenue will be recognised on commencement of the contract provided that the fair value of the licence fee can be determined. However, if no reliable fair value can be determined, any revenue associated with the licence fee will be deferred and recognised in line with the reactor sales.

Other revenue
Revenue from development contracts is measured in accordance with the Company's policy on development contracts. Revenue from most development contracts is earned on a time and materials basis, supplemented by milestones, and is recognised as the work is performed. In a situation where a contract is for fixed services and value, and where the outcome of a development contract can be estimated reliably, revenue and costs are recognised by reference to the stage of completion of the contract activity at the balance sheet date. This is normally measured as the proportion of costs incurred for work performed to date relative to the estimated total costs, except where this would not be representative of the stage of completion.

Where the outcome of a development contract cannot be estimated reliably, contract revenue is recognised to the extent that contract costs incurred are expected to be recoverable. Contract expenses are recognised as costs in the year in which they are incurred. When it is probable that total contract costs will exceed revenue, the total expected loss is recognised as an expense immediately.

Notes to the financial statements (continued)

Contracts for development work may include either upfront payments or milestone payments, payable on successful attainment of defined milestones. Where upfront non-refundable payments are received on signature of an agreement, such payments are deferred and amortised over the life of the agreement to which it relates. For milestone payments, revenue is only recognised when the milestone has been successfully achieved and no further obligations remain.

Grants are recognised as income over the periods necessary to match them, on a systematic basis, with the costs that they are intended to compensate. Grant income is not recognised until the conditions for their receipt have been complied with and there is assurance that the grant will be received. Where a grant is received to fund the acquisition of property, plant and equipment, the income is deferred and recognised over the useful economic life of the related asset.

Interest income is accrued on a time basis by reference to the principal outstanding and at the effective interest rate applicable.

Provisions
Provisions for claims are recognised when the Company has a present constructive or legal obligation as a result of past events, and it is probable that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated. Provisions are measured at the present value of the expenditures expected to be required to settle the obligation.

Intangible assets
Licences
Purchased licences are capitalised at the present value of the minimum licence payments. Amortisation will commence when related revenue starts to be earned and it will be charged in equal annual instalments over the life of the patents to which the licences relate. Provision is made for any impairment.

Patents and trademarks
Patents and trademarks are included at cost less accumulated amortisation and amortised in equal annual instalments over a period of 20 years, which is their estimated useful economic life. Provision is made for any impairment. Where patent expenditure is funded by arrangements with development partners, the costs of such patents are not capitalised, but are expensed as cost of sales.

Goodwill
Goodwill represents the excess of the cost of an acquisition over the fair value of the Company's share of the identifiable net assets of the acquired subsidiary at the date of acquisition. Goodwill on acquisitions of subsidiaries is included in 'Intangible assets'. Goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment reviews are performed more frequently if events or changes in circumstances indicate a potential impairment. Impairment losses on goodwill are not reversed. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose, identified according to operating segment.

Software
Purchased software is measured initially at cost and is amortised on a straight-line basis over its estimated useful life of 3 years. Provision is made for any impairment.

In process technology
In process technology consists of purchased intangibles and capitalised development costs and is carried at cost less accumulated amortisation and impairment losses. When the development phase is completed and delivery of commercial reactors has commenced, amortisation of the intangibles will begin. The Company uses the units-of-production method of amortisation with the measured unit being reactors sold. The Company expects amortisation to begin in 2015 based on projected delivery dates for commercial reactors.

Purchased intangibles
Purchased intangibles arose from the acquisition of Velocys, Inc. and Pinto Energy, LLC, now known as Velocys Project Solutions (VPS). These purchased intangibles are valued using discounted cash flow valuations of the projected future benefits arising from the technology acquired. See "Impairment of non-financial assets" below.

Capitalised development costs
Development costs are normally charged to the income statement in the year they are incurred except in those circumstances where, during the development phase of a project, the Company is able to identify an intangible asset and demonstrate that the asset will generate probable future economic benefits. In such cases, provided the criteria defined under IAS 38 are met, the costs are capitalised as in process technology. The costs in respect of funded projects are recognised to the extent that the costs meet the relevant criteria, net of any amounts reimbursed by research partners.

Development costs are amortised, from the point the asset is available for use in the manner intended by management, on a straight-line time basis or other appropriate basis over the period of its expected benefit. See "Impairment of non-financial assets" below.

Impairment of non-financial assets
Assets that have an indefinite useful life, for example goodwill and investments, are not subject to amortisation and are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date. Assets that are not yet being amortised are reviewed for impairment on an annual basis.

Property, plant and equipment
Property, plant and equipment is stated at cost, net of depreciation and any provision for impairment. Cost includes the original purchase price of the asset and the costs attributable to bringing the asset to its working condition for its intended use. Depreciation is provided on all property, plant and equipment at rates calculated to write off the cost or valuation, less estimated residual value, of each asset on a straight-line basis over its expected useful life, as follows: plant and machinery, 3-10 years. No depreciation is provided on land or assets under construction. Residual value is calculated on prices prevailing at the balance sheet date. Residual values and useful lives are reviewed annually and adjusted if appropriate, at each balance sheet date.

Expenditure funded by research partners is only capitalised where there are no significant rights acquired by that third party over the asset and the asset has a clear enduring use beyond the specific funding project, these are regularly reviewed.

Investments
Investments are shown at cost less provision for impairment. See "Impairment of non-financial assets" above.

Share-based payments
Velocys plc issues share options to certain Company employees, which are accounted for as equity settled. Equity settled share-based payments are measured at fair value (excluding the effect of non market-based vesting conditions) at the date of grant. The fair value determined at the grant date of the equity settled share-based payments is expensed on a straight-line basis over the vesting period, based on the Company's estimate of shares that will eventually vest and adjusted for the effect of non market-based vesting conditions.

Fair value of executive share options with market performance conditions attached is measured using a Monte Carlo pricing model. The expected life used in the model is assumed to be the earliest point at which the shares may vest. Fair value of all other share options is measured by use of the Black-Scholes pricing model. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations. Under both models, when options are exercised the proceeds received, net of attributable transaction costs, are credited to share capital and premium.

For executive options with market performance conditions attached the recognition period covers the period of service and the vesting period; for all other options the recognition period is the vesting period.

At each balance sheet date, the Company revises its estimates of the number of options that are expected to vest. It recognises the impact of the revision to original estimates, if any, in the income statement with a corresponding adjustment to reserves.

Notes to the financial statements (continued)

The grant by the parent company of options of its equity instruments to employees of subsidiary undertakings is treated as a capital contribution. The fair value of employee services received, measured by reference to the grant date fair value, is recognised as an increase to investments in subsidiary undertakings with a corresponding credit to equity.

Short term employee benefits
Accruals are included to reflect the cost of short term compensation to employees for absences such as paid leave.

Pension costs
The Company operates various defined contribution pension schemes for its employees. The amount charged to the income statement in respect of pension costs and other post-retirement benefits is the contributions payable in the year. Differences between contributions payable and contributions actually paid are shown as either accruals or prepayments in the balance sheet. The Company has no further payment obligations once the contributions have been paid.

Taxation
Current tax, including UK corporation tax and foreign tax, is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised using the liability method, on temporary differences arising between the tax basis of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affected neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised. Deferred income tax is provided on temporary differences arising on investments in subsidiaries except where the timing of the reversal of the temporary difference is controlled by the parent company and it is probable that the temporary difference will not reverse in the foreseeable future.

Financial instruments
Trade receivables
Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments (more than 30 days overdue) are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognised in the income statement within 'cost of sales'. When a trade receivable is uncollectible, it is written off against the allowance account for trade receivables. Subsequent recoveries of amounts previously written off are credited against 'cost of sales' in the income statement.

Trade payables
Trade payables are stated at fair value and subsequently held at amortised cost.

Financial liabilities and equity instruments
Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the Company after deducting all of its liabilities.

Borrowings
Interest bearing loans and overdrafts are initially recorded at fair value, taken as proceeds received net of direct issue costs and thereafter at amortised cost. Finance charges, including premiums payable on settlement or redemption and direct issue costs, are recognised in the income statement using the effective interest method and are added to the carrying amount of the instrument to the extent that they are not settled in the period in which they arise.

Provisions

Provisions are recognised when the Company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount has been reliably estimated.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

Derivative financial instruments

The Company enters into forward contracts and options to fund its US operations. Derivative financial instruments are classified as current assets or current liabilities where they have a maturity period within 12 months. Where derivative financial instruments have a maturity period greater than 12 months, they are classified within either non-current assets or non-current liabilities. Financial assets and liabilities are initially recognised and subsequently measured at fair value. The gain or loss on re-measurement to fair value is recognised immediately in the income statement, in net finance income.

Financial assets

The Company classifies its financial assets in the following categories: at fair value through profit or loss, loans and receivables and available-for-sale. The classification depends on the nature of the asset and the purpose for which the assets were acquired. Management determines the classification of its financial assets at initial recognition.

Classification

- Financial assets at fair value through profit or loss are financial assets held for trading. A financial asset is classified in this category if it is acquired principally for the purpose of selling in the short term. Derivatives are also categorised as held for trading. Assets in this category are presented as current assets if they are expected to be realised within 12 months after the balance sheet date, otherwise they are classified as non-current.
- Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included as current assets, except for maturities greater than 12 months after the balance sheet date which are presented as non-current assets. Loans and receivables are presented as 'trade and other receivables' (note 21) and 'cash and cash equivalents' (note 23) on the balance sheet.
- Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless the investment matures or management intends to dispose of the assets within 12 months after the balance sheet date.

Recognition and measurement

Regular purchases and sales of financial assets are recognised on the trade date – the date on which the Company commits to purchase or sell the asset. Investments are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognised at fair value, and transaction costs are expensed in the consolidated income statement. Financial assets are de-recognised when the rights to receive cash flows from the investments have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership. Available-for-sale financial assets and assets held at fair value through profit and loss are subsequently carried at fair value. Loans and receivables are subsequently carried at amortised cost using the effective interest method.

Gains or losses arising from changes in the fair value of the 'financial assets at fair value through profit or loss' category are presented in the income statement in the period in which they arise. Dividend income from 'financial assets at fair value through profit or loss' is recognised in the income statement as part of other income when the Company's right to receive payments is established.

Changes in the fair value of monetary and non-monetary securities classified as available for sale are recognised in other comprehensive income.

When securities classified as available for sale are sold or impaired, the accumulated fair value adjustments recognised in equity are included in the income statement as 'Gains and losses from investment securities'.

Interest on available-for-sale securities calculated using the effective interest method is recognised in the consolidated income statement as part of finance income. Dividends on available-for-sale equity instruments are recognised in the income statement as part of other income when the Company's right to receive is established.

Notes to the financial statements (continued)

3. Critical accounting estimates and judgements

The preparation of financial information in conformity with IFRS requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the reporting date and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from those estimates. Estimates and assumptions that have a significant risk of causing material adjustment to the carrying amounts of assets and liabilities within the next financial period are discussed below.

Valuation of acquired intangible assets

Estimation of the fair values of acquired intangible assets requires assumptions as to value, future life and future cash flows for impairment tests. There is a high degree of judgement required in making these assumptions, which impact both the initial fair value acquired and the carrying value as at the balance sheet date (see note 17).

At 31 December 2014, the carrying value of the Company's intangible assets was £28,347,000 (2013: £24,971,000). The impairment charge for the year includes £1,328,000 in 2014 (2013: nil). The Company acquired intangible assets valued at £3,209,000 through the acquisition of Velocys Projects Solutions in 2014 (see note 30).

Revenue recognition and cost of sales

In order to recognise revenue, the fair value of each component of the Fischer-Tropsch process is identified, which includes the sale of the reactor, an initial licence fee, the sale of catalyst and ongoing engineering services. This fair value is based on the sales contract and historical actual data.

Once the fair value of the components has been determined, revenue is recognised in line with the underlying nature of the contract. Revenue for the reactor is recognised upon delivery. Where the fair value of the licence fee can be determined this is recognised on commencement of the contract. However, if no reliable fair value can be determined any revenue associated with the licence fee is deferred and recognised in line with the reactor sales. Catalyst sales income is recognised monthly, whilst the service element is recognised when services are provided.

Where the underlying costs associated with any component cannot be estimated, any profit element identified is deferred until such time as the costs can be reliably estimated.

Investments

The carrying value of investments is considered in the context of market capitalisation and future forecast earnings.

Share-based payments

The fair value calculation of share-based payments requires several assumptions and estimates, details of which are disclosed in note 15. Such assumptions and estimates could change and could affect the amount recorded.

4. Exceptional items

Items that are material because of their size or nature, and/or that are non-recurring are considered as exceptional items and are presented with the line items to which they best relate. During the year, exceptional items, as detailed below, have been included in the consolidated income statement.

	2014 £'000	2013 £'000
Impairment of intangible assets	(1,328)	–
Reversal of revenue	(1,742)	–
Reversal of cost of sales	1,742	–
	(1,328)	–

The impairment of intangible assets relates to the full impairment of one of the Company's six cash-generating units (see note 17).

The revenue reversed was generated in the Americas.

The reversals of revenue and costs of sales are related to the restructuring of a major multi-year supply contract for FT reactor cores which was formally agreed in early 2015. The terms of the revised agreement, which provides a more consistent measure of cost of each reactor, resulted in a change in the method of recognising the revenue and costs related to the build of the commercial reactors. The Company will now recognise revenue and costs upon delivery of the commercial reactors under IAS 18 and no longer use the percentage of completion method under IAS 11. The reversals of revenue and costs of sales represent the unwinding of the percentage of completion method for 2013.

None of the exceptional items described above has any cashflow impact.

5. Segmental information

The chief operating decision-maker has been identified as the Senior management team ("SMT"). This committee reviews the Company's internal reporting in order to assess performance and allocate resources. The SMT has determined the operating segments based on these reports.

The SMT considers that the business comprises a single activity which is the design and development of technology for synthetic fuels production. The SMT reviews the Company's profit or loss and its cash flows, assets and liabilities on a Company-wide basis. In carrying out these reviews, the SMT considers all material items of income and expenditure that are directly attributable to individual commercial projects and development programmes. The internal management reports do not allocate assets and liabilities or shared overheads to individual products or projects.

Based on the above considerations, there is considered to be one reportable segment, synthetic fuels. The business is segmented on the basis that the key end use market is that of synthetic fuels production. At this stage, the synthetic fuels segment represents over 90% of the business and therefore represents the only material segment.

Internal and external reporting is on a consolidated basis, with purchases and sales between subsidiaries eliminated on consolidation. Therefore, the segmental and financial information is the same as that set out in the consolidated income statement, consolidated statement of comprehensive income, the consolidated statement of financial position, the consolidated statement of cash flows and the consolidated statement of changes in equity.

The SMT assesses the performance of the operating segment based on a measure of operating loss.

The Company's operating segment operates in three main geographical areas. Revenue before exceptional items is allocated based on the country in which the customer is located.

	2014			2013		
	Europe £'000	Americas £'000	Asia Pacific £'000	Europe £'000	Americas £'000	Asia Pacific £'000
Total revenue before exceptional items	207	1,090	439	45	1,924	2,784

Revenues during the year were generated in the United Kingdom and United States.

Non-current assets, consisting primarily of goodwill, other intangible assets, investment in GTL JV and property, plant and equipment, totalling £33,157,000 (2013: £26,039,000) were located in the United States. All other non-current assets were held in the United Kingdom.

6. Revenue from partners

The majority of revenue before exceptional items of the Company is derived from a small number of significant commercial customers and development partners, who are not related parties. The total amounts recognised from partners where revenue comprises 10% or more of Company revenue before exceptional items is as follows.

	2014 £'000	2013 £'000
Partner 1	532	2,783
Partner 2	312	1,835
Partner 3	250	–
Partner 4	183	–
Partners less than 10%	459	135
Total before exceptional items	1,736	4,753

Notes to the financial statements (continued)

7. Finance income

	2014 £'000	2013 £'000
Interest income on bank deposits	164	419
Net fair value gains on forward foreign exchange contracts	394	–
Foreign exchange gains	667	–
	1,225	419

8. Finance costs

	2014 £'000	2013 £'000
Unwinding of discount on deferred licence payments payable	(8)	20
Interest on finance leases	12	11
Interest on borrowings	25	27
Foreign exchange losses	–	306
	29	364

During the year the licence against which interest payments had been accrued was cancelled.

9. Other income

	2014 £'000	2013 £'000
Sale of fixed assets	56	58
	56	58

10. Expenses by nature

	2014 £'000	2013 £'000
Employee benefit expense (see note 12)	14,014	11,217
Sub-contractor and consultant costs	2,714	1,664
Depreciation of property, plant and equipment: owned (note 18)	680	703
Depreciation of property, plant and equipment: leased (note 18)	48	37
Amortisation of intangible assets (note 17)	181	138
Operating lease payments – plant and machinery	13	7
Operating lease payments – other	418	413
Patent and other IP costs	914	1,213
Materials expense	2,018	4,077
Services	811	1,050
Other expenses	3,148	2,379
Total costs of sales, unfunded research and development costs, share-based payments and other administrative expenses before exceptional items	24,959	22,898

11. Auditors remuneration

	2014 £'000	2013 £'000
Fees payable to Company's auditors for the audit of parent company and consolidated financial statements	26	25
Fees payable for the audit of Company's subsidiaries pursuant to legislation	55	59
Fees payable to the Company's auditors for other services		
– Tax services	23	18
	104	102

12. Employee benefit expense

The average monthly number of Company employees (including Executive Directors) was as follows.

	2014 number	2013 number
Research, design and development	79	69
Administration	26	22
Total average headcount	105	91

Their aggregate remuneration comprised the following items.

	2014 £'000	2013 £'000
Wages and salaries	9,684	7,719
Social security costs	649	504
Other pension costs	252	207
Severance expense	22	5
Share-based payments granted to Directors and employees	3,407	2,782
	14,014	11,217

Details of Directors' remuneration are given in the audited information in the remuneration report on pages 17-18, which forms part of these financial statements.

13. Income tax

Company	**2014** £'000	2013 £'000
Current tax:		
R&D tax credit	(929)	(1,111)
Income tax total	(929)	(1,111)

Due to the availability of losses incurred in the year, there is no charge to corporation tax. The Company recovered £929,000 through R&D tax credits (2013: £1,111,000). A claim of £978,000 for the year ending 31 December 2013 was submitted to HMRC during 2014 and settled in January 2015.

The actual tax charge for the current and previous year is higher (2013: higher) than the theoretical amount that would arise using the weighted average tax rate applicable to the results of the consolidated entities, for the reasons set out in the following reconciliation.

Company	**2014** £'000	2013 £'000
Loss on ordinary activities before tax	(23,299)	(18,145)
Tax calculated at domestic tax rates applicable to losses in the respective countries	(6,184)	(4,875)
Tax effects of:		
– Expenses not deductible for tax purposes	401	9
– Unutilised tax losses	5,783	4,866
– R&D tax credit relating to prior years	(129)	(236)
– R&D tax credit	(800)	(875)
Current tax total	(929)	(1,111)

The weighted average applicable tax rate was 27.3% (2013: 27.3%).

The standard rate of corporation tax in the United Kingdom changed from 23% to 21% with effect from 1 April 2014. Accordingly, profits in the United Kingdom were taxed at an effective rate of 21.5%. Legislation to reduce the main rate of corporation tax from 21% to 20% from 1 April 2015 was included in the Finance Act 2013, substantively enacted on 2 July 2013, and consequently deferred tax balances have been re-measured.

Notes to the financial statements (continued)

14. Deferred tax

The movement in deferred tax in the year was as follows.

Company	**2014** £'000	2013 £'000
Deferred tax brought forward	–	–
Purchase of intangible assets through acquisition of subsidiary (see note 30)	269	–
Deferred tax carried forward	269	–

Company	**2014** £'000	2013 £'000
Unrecognised		
Deferred tax assets		
– Trading losses	(16,298)	(14,860)
– Equity settled options	(1,081)	(1,097)
	(17,379)	(15,957)

At 31 December 2014 the Company had a net unrecognised deferred tax asset of £16,298,000 (2013: £14,860,000) arising from trading losses from incorporation. No recognition (2013: nil) of the net deferred tax asset has been made at 31 December 2014 on the grounds of uncertainty over its recoverability in light of the Company's nascent revenue streams and commitment to continued investment in research and development and therefore there is no impact on the current or prior year income statement.

Of this unrecognised deferred tax asset, £10,929,000 (2013: £9,911,000) is anticipated to remain available indefinitely to offset against future taxable trading profits of the companies in which the losses arose. The remainder has expiry dates between 2023 and 2033 (2013: 2023 and 2033).

15. Share-based payments

Equity settled share option scheme

The Company has four share option schemes that cover all employees. The number of shares outstanding at 31 December 2014 and the expense recognised in the profit and loss for these schemes, along with bonus and other schemes, are as follows.

	2014		2013	
Scheme	Options outstanding	Income statement £'000	Options outstanding	Income statement £'000
EMI	4,179,111	308	3,811,236	163
ELTIP	1,520,000	–	1,595,000	27
NELTIP	8,006,636	3,068	5,603,325	2,301
Velocys, Inc.	130,062	3	202,415	4
Bonus	421,760	–	421,760	–
Other	92,129	28	232,264	287
Total	14,349,698	3,407	11,866,000	2,782

EMI scheme

The EMI scheme covers all employees of the Company. Options are exercisable at a price equal to the mid-market value of the parent company's ordinary shares on the day prior to grant and vest after the earlier of three, four or five years from grant or date of joining the Company. Options expire after 10 years and are forfeited if the employee leaves the Company before the options vest.

Movements in the number of EMI scheme share options outstanding and their related weighted average exercise prices are as follows.

	2014		2013	
	Weighted average exercise price	Number of options	Weighted average exercise price	Number of options
At 1 January	80.17p	3,811,236	60.90p	3,351,010
Granted	180.64p	1,264,000	145.45p	903,200
Forfeited	78.12p	(350,934)	59.72p	(375,300)
Exercised	86.89p	(545,191)	63.43p	(67,674)
At 31 December	119.33p	4,179,111	80.17p	3,811,236

Of the 4,179,111 options outstanding at 31 December 2014, 740,705 were exercisable (2013: 191,740). The weighted average exercise price of the exercisable shares was 67.84p (2013: 95.38p).

Share options outstanding at the end of the year have the following expiry dates and exercise prices.

		2014		2013	
Year of expiry	Range of exercise price	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
2017	124.00p	16,129	124.00p	16,129	124.00p
2018	159.00p	62,893	159.00p	62,893	159.00p
2019	54.50p	10,000	54.50p	12,523	119.78p
2020	56.01 – 57.50p	51,748	56.19p	100,195	70.66p
2021	50.22 – 59.50p	1,506,141	57.73p	2,091,296	55.29p
2022	46.36 – 156.00p	468,200	76.21p	638,200	66.49p
2023	126.19 – 179.79p	984,000	152.82p	890,000	145.15p
2024	146.00 – 257.40p	1,080,000	194.65p	–	–
Total	46.36 – 257.40p	4,179,111	119.33p	3,811,236	80.17p

The weighted average fair value of options granted during the year determined using the Black-Scholes valuation model was 52.46p (2013: 38.21p) per option. The significant inputs into the model were as follows.

	2014	2013
Weighted average share price at grant date	180.64	145.45
Weighted average exercise price	180.64	145.45
Expected volatility (i)	30%	30%
Annual risk free rate	3%	3%
Dividend yield	0%	0%
Expected life	4.0 years	4.0 years

(i) The expected volatility was determined by reference to comparable companies and review of historic actual volatility based on statistical analysis of daily share prices since the date of Velocys plc's listing on AIM.

Total expense recognised in the income statement for share options granted to Directors and employees was £308,000 in 2014 (2013: £163,000).

Executive Long Term Incentive Plan (ELTIP)

The ELTIP scheme covers executives of the Company. Options are exercisable at a price of 1p or at a price equal to the mid-market value of the parent company's ordinary shares on the day prior to the grant. Options vest after a period of one, two or three years from grant, expire after 10 years and are forfeited if the employee leaves the Company before the options vest.

Notes to the financial statements (continued)

Movements in the number of ELTIP share options outstanding and their related weighted average exercise prices are as follows.

	2014		2013	
	Weighted average exercise price	Number of options	Weighted average exercise price	Number of options
At 1 January	31.71p	1,595,000	31.71p	1,595,000
Exercised	58.00p	(75,000)	–	–
At 31 December	30.41p	1,520,000	31.71p	1,595,000

Of the 1,520,000 options outstanding at 31 December 2014, 1,520,000 were exercisable (2013: 1,595,000). The weighted average exercise price of the exercisable shares was 30.41p (2013: 31.71p).

Share options outstanding at the end of the year have the following expiry dates and exercise prices.

		2014		2013	
Year of expiry	Range of exercise price	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
2018	1.00p	100,000	1.00p	100,000	1.00p
2019	1.00p	245,000	1.00p	245,000	1.00p
2021	1.00 – 58.00p	1,175,000	39.05p	1,250,000	40.19p
Total	1.00 – 58.00p	1,520,000	30.41p	1,595,000	31.71p

No share options were issued in 2014 (2013: nil). Total expense recognised in the income statement for share options granted to Directors and employees was £nil in 2014 (2013: £27,000).

At the time of exercising their share options, executives of the Company may apply to an employee benefit trust managed by Oxford Catalysts Trustees Limited for a distribution in respect of the exercise value of their options. The trustees then request a contribution from the Company in respect of the grant made. The total value of funds distributed to executives by Oxford Catalysts Trustees Limited during the year in respect of ELTIP options was £nil (2013: nil).

New Executive Long Term Incentive Plan (NELTIP)

Under the NELTIP scheme 2,567,791 share options were granted to executives of the Company in April 2014 after certain performance conditions relating to the year ended 31 December 2013 were satisfied. The fair value of the share options was recognised over a period combining the year during which performance was measured, the time from the end of that year to the options' grant date, and the vesting period. Award of options in respect of the year ended 31 December 2013 was announced on 27 February 2014.

Options awarded up to 2014 are, subject to the Board's decision, exercisable at a price either equal to the mid-market value of the parent company's ordinary shares on the day prior to the grant, or to the nominal value of the shares. Options vest immediately, or after a period of one, two or three years from grant, they expire after 10 years and are forfeited if the employee leaves the Company before the options vest.

Options to be awarded in respect of 2014 are divided into time lapse options and market performance options. For the CEO time lapse options represent 30% of the potential total award, for the rest of the Senior management team they represent 23%. Time lapse options vest two years after the conclusion of the period over which performance is measured. The market performance conditions on which the rest of the award is based pertain to the Compound Annual Growth Rate of the Company's market capitalisation excluding fund raising subsequent to 1 January 2015. Market performance options for the CEO are measured after 5 years from the start of the service period, with a possible re-measurement one year later. Market performance options for other executives are measured after 3 years from the start of the service period, with possible re-measurements one, and two years later. Options are subject to the discretion of the Board if the employee leaves the Company before the options vest.

Movements in the number of NELTIP share options outstanding and their related weighted average exercise prices are as follows.

	2014		2013	
	Weighted average exercise price	Number of options	Weighted average exercise price	Number of options
At 1 January	108.92p	5,603,325	49.00p	2,587,103
Granted	97.54p	2,567,791	159.00p	3,052,222
Exercised	124.59p	(164,481)	49.00p	(36,000)
At 31 December	125.96p	8,006,635	108.92p	5,603,325

Of the 8,006,635 options outstanding at 31 December 2014, 1,485,503 were exercisable (2013: 906,215). The weighted average exercise price of the exercisable shares was 83.89p (2013: 73.70p). Options for 2011 were granted in 2011 whereas options for 2012 were granted in April 2013.

Share options outstanding at the end of the year have the following expiry dates and exercise prices.

		2014		2013	
Year of expiry	Range of exercise price	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
2022	49.00p	2,498,503	49.00p	2,551,103	49.00p
2023	159.00p	2,968,400	159.00p	3,052,222	159.00p
2024	153.00 – 163.50p	2,539,732	163.05p	–	–
Total	49.00 – 163.50p	8,006,635	125.96p	5,603,325	108.92p

No options had been granted under this scheme in respect of the financial year ending 31 December 2014, however on 27 February 2015 it was announced that up to 7,588,613 options would be awarded subject to the satisfaction of certain market conditions over the vesting period. The weighted average fair value of the market performance options and the time lapse options to be granted in respect of year ended 31 December 2014 using respectively the Monte Carlo and Black-Scholes valuation models is 155.00p (2013: 100.91p) per option. The significant inputs into the model were as follows.

	2014	2013*
Weighted average share price at grant date	155.00p	163.50p
Weighted average exercise price	0.01p	64.20p
Expected volatility (i)	46%	30%
Annual risk free rate	1.03%	3%
Dividend yield	0%	0%
Expected life	3.77 years	3.6 years

(i) The expected volatility under Black-Scholes was determined by reference to comparable companies and review of historic actual volatility based on statistical analysis of daily share prices since the date of Velocys plc's listing on AIM. The expected volatility under Monte Carlo was calculated using statistical analysis of historic share prices over an equivalent period to the vesting period.

* This number was estimated in 2013 and adjusted according to the final award.

Total expense recognised in the income statement for share options granted to Directors and employees was £1,390,000 in 2014 (2013: £1,452,000). In addition, an expense of £1,678,000 relating to shares to be granted for the year ended 31 December 2014 has been accrued within the share-based payments charge (2013: £849,000).

At the time of exercising their share options, executives of the Company may apply to an employee benefit trust managed by Oxford Catalysts Trustees Limited for a distribution in respect of the exercise value of their options. The trustees then request a contribution from the Company in respect of the grant made. The total value of funds distributed to executives by Oxford Catalysts Trustees Limited during the year in respect of NELTIP options was £205,000 (2013: nil).

Notes to the financial statements (continued)

Velocys, Inc. scheme

The Velocys, Inc. Stock Compensation Plan ("Pre-Acquisition Scheme") was acquired as part of the acquisition of Velocys, Inc. by Velocys plc, formerly Oxford Catalysts Group PLC, on 20 November 2008. The scheme was started in 2001 and covers all US based employees. Prior to the acquisition, Velocys, Inc.'s board of directors granted non-qualified share options to employees with expiry 10 years from grant date. The options' exercise price was equal to the stock's fair market value at the date of grant. Options are forfeited if an employee leaves the Company. Generally, options vest as follows.

After 1 year of service from vest start date:	25% of grant
Each month subsequent to 1 year of service:	1/48th of grant

Pursuant to the terms and conditions of the acquisition of Velocys, Inc., each vested and unvested Pre-Acquisition Scheme option existing on the acquisition date was converted into 0.3659 of a Velocys plc, formerly Oxford Catalyst Group PLC, option (the ratio of the value of one share of Velocys, Inc. stock to one share of Velocys plc, formerly Oxford Catalyst Group PLC stock) with a corresponding increase to the exercise price. Share options are exercisable in US dollars.

During 2011, the Company reviewed employee incentives and concluded that the Pre-Acquisition Scheme options did not provide the intended incentive or retention value for its employees due to significant shifts in the market price since the original grants. Consequently, holders of these options were offered the opportunity to forfeit their options and have new options issued. All such new issues vest in three years and expire 10 years from date of grant.

Details of the share options outstanding under the Pre-Acquisition Scheme are as follows.

	2014		2013	
	Weighted average exercise price	Number of options	Weighted average exercise price	Number of options
At 1 January	$0.94	202,415	$0.94	344,291
Forfeited	$0.77	(951)	$1.10	(61,976)
Exercised	$0.86	(71,402)	$0.77	(79,900)
At 31 December	$1.00	130,062	$0.95	202,415

Of the options outstanding presented above, 130,062 (2013: 70,536) were exercisable as of 31 December 2014. The weighted average share price of the exercisable shares was $0.91 (2013: $0.99).

Share options outstanding at the end of the year have the following expiry dates and exercise prices.

		2014		2013	
Year of expiry	Range of exercise price per share	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
2014	$0.77	–	–	951	$0.77
2015	$0.77	27,410	$0.77	60,367	$0.77
2017	$2.21 – $2.54	9,218	$2.45	9,218	$2.45
2021	$0.93	93,434	$0.93	131,879	$0.93
Total	$0.77 – $2.54	130,062	$1.00	202,415	$0.95

Total expense recognised in the income statement for share options granted under the Velocys, Inc. plan was £3,000 (2013: £4,000).

Bonus shares

The Company previously maintained two bonus share schemes for certain executives: one in respect of employees of Velocys Technologies Limited and one in respect of employees of Velocys, Inc. Under both schemes, the value of the bonus was based upon the executive's salary as well as the Company and the executive achieving certain targets throughout the year. No awards were, or will be, made under these schemes during, or in respect of, 2014.

The Velocys Technologies Limited bonus share scheme awarded nominal value share options (1p) that were issued subsequent to the end of previous financial years. The awards vested on the date of grant and expire 10 years thereafter. Details of the bonus shares outstanding under the Velocys Technologies Limited bonus share scheme are as follows.

	2014		2013	
	Exercise price	Number of options	Exercise price	Number of options
At 1 January	1.00p	421,760	1.00p	421,760
At 31 December	1.00p	421,760	1.00p	421,760

Velocys Technologies Limited bonus share options outstanding at the end of the year have the following expiry dates.

		2014	2013
Year of expiry	Exercise price	Number of options	Number of options
2019	1.00p	42,105	42,105
2020	1.00p	342,000	342,000
2021	1.00p	37,655	37,655
Total	1.00p	421,760	421,760

The Velocys, Inc. bonus share scheme consists of deferred shares awarded subsequent to year end at a nominal price of 1p. 20% of the award is granted on each anniversary of the date of award. Shares remaining to be granted in future years totalled 16,418. No bonus share awards were made in respect of 2014 (2013: 4,214 shares).

The share-based payment expense for the year includes a cost of £nil (2013: £nil) relating to shares granted under either the Velocys Technologies Limited or the Velocys, Inc. bonus share schemes.

Other share options
Since 2011 the Board has approved the granting of share options to a small number of consultants who provide a strategic service to the business.

Movements in the number of consultants' share options outstanding and their related weighted average exercise prices are as follows.

	2014		2013	
	Weighted average exercise price	Number of options	Weighted average exercise price	Number of options
At 1 January	58.38p	232,264	23.37p	527,054
Granted	145.25p	21,375	21.44p	75,210
Forfeited	–	–	1.00p	(70,000)
Exercised	73.99p	(161,510)	1.00p	(300,000)
At 31 December	51.15p	92,129	58.38p	232,264

Of the 92,129 options outstanding at 31 December 2014, 70,969 were exercisable (2013: 189,944). The weighted average exercise price of the exercisable shares was 66.10p (2013: 72.65p). An estimated further 11,750 options will be granted to consultants at the start of 2015 in respect of the year ended 31 December 2014. The weighted average exercise price of these options is 143.50p.

Notes to the financial statements (continued)

Share options outstanding at the end of the year have the following expiry dates and exercise prices.

Year of expiry	Range of exercise price	2014 Number of options	2014 Weighted average exercise price	2013 Number of options	2013 Weighted average exercise price
2021	1.00p	6,500	1.00p	146,850	81.28p
2022	1.00p	10,204	1.00p	10,204	39.71p
2023	1.00 – 53.10p	54,050	29.44p	75,210	1.00p
2024	145.25p	21,375	145.25p	–	–
Total	1.00 – 145.25p	92,129	51.15p	232,264	58.38p

The weighted average fair value of options granted during the year determined using the Black-Scholes valuation model was 0.92p (2013: 126.43p) per option. All 2014 options were granted at market price with immediate vesting, whereas most 2013 options were granted at 1p and with a 1 or 2 year vesting period. The weighted average fair value of estimated options to be granted in 2015 in respect of 2014 was 1.00p per option. The significant inputs into the model were as follows.

	2014	2013
Weighted average share price at grant date	145.25p	147.85p
Weighted average exercise price	145.25p	21.44p
Expected volatility (i)	30%	30%
Annual risk free rate	3%	3%
Dividend yield	0%	0%
Expected life	0.01 years	0.8 years

(i) The expected volatility was determined by reference to comparable companies and review of historic actual volatility based on statistical analysis of daily share prices since the date of Velocys plc's listing on AIM.

The share-based payment expense for the year includes a cost of £28,000 (2013: £249,000) related to options granted to consultants. An expense of £nil relating to the year ended 31 December 2014 has been accrued within the share-based payment charge.

Share-based payments charge
The total charge for share-based payments during the year was £3,407,000 (2013: £2,782,000) of which £2,864,000 (2013: £1,786,000) relates to options granted to Directors and the remainder to other employees.

16. Loss per share
The basic loss per share is calculated by dividing the loss attributable to owners of the parent company by the weighted average number of ordinary shares in issue during the year.

	2014	2013
Loss attributable to owners of Velocys plc (£'000s)	(22,370)	(16,921)
Weighted average number of ordinary shares in issue	122,062,050	115,929,849
Basic and diluted loss per share (pence)	(18.33)	(14.60)

Diluted loss per share is calculated by adjusting the weighted average number of shares in issue to assume conversion of all potential dilutive shares. Share options have not been included in the number of shares used for the purpose of calculating diluted loss per share since these would be anti-dilutive for the period presented. There are no other potentially dilutive instruments. Details of share options are given in note 15.

17. Intangible assets

Company 2014	Goodwill £'000	In process technology £'000	Patents, licence and trademarks £'000	Customer contracts £'000	Software £'000	Total £'000
Cost						
At 1 January 2014	4,062	19,440	1,752	–	211	25,465
Additions	–	–	329	–	100	429
Disposals	–	–	(167)	–	–	(167)
Acquisition of subsidiary	1,865	–	–	1,344	–	3,209
Foreign exchange movement	31	1,170	81	129	17	1,428
At 31 December 2014	5,958	20,610	1,995	1,473	328	30,364
Accumulated amortisation						
At 1 January 2014	–	–	382	–	112	494
Charge for the year	–	–	138	–	43	181
Disposals	–	–	(13)	–	–	(13)
Impairment	–	1,328	–	–	–	1,328
Foreign exchange movement	–	–	21	–	6	27
At 31 December 2014	–	1,328	528	–	161	2,017
Net book amount						
At 31 December 2014	5,958	19,282	1,467	1,473	167	28,347

2013	Goodwill £'000	In process technology £'000	Patents, licence and trademarks £'000	Customer contracts £'000	Software £'000	Total £'000
Cost						
At 1 January 2013	4,147	19,844	1,454	–	128	25,573
Additions	–	–	328	–	90	418
Foreign exchange movement	(85)	(404)	(30)	–	(7)	(526)
At 31 December 2013	4,062	19,440	1,752	–	211	25,465
Accumulated amortisation						
At 1 January 2013	–	–	277	–	91	368
Charge for the year	–	–	114	–	24	138
Foreign exchange movement	–	–	(9)	–	(3)	(12)
At 31 December 2013	–	–	382	–	112	494
Net book amount						
At 31 December 2013	4,062	19,440	1,370	–	99	24,971

In process technology is yet to be brought into use and hence is not being amortised. The Company will amortise in process technology using the units-of-production method under IAS 16. The unit of measure will be number of reactors sold.

Intangible assets in use are amortised over their expected useful lives and are reviewed when there is an indication that impairment may have occurred.

Goodwill and 'In process technology' intangible assets that are not yet ready for use are subject to an annual impairment review. The impairment review for In process technology is performed for each 'Cash generating unit' (CGU) identified in accordance with the Company's accounting policy. It had been determined that there were initially six CGUs, each representing a separate technology stream for which distinct revenue streams are either being currently generated or are anticipated in the future. One CGU was fully impaired in 2014; this represented one of the Company's non-core technologies, which is still believed to offer prospective future revenue, but which the Company does not currently have the intention to pursue.

Goodwill of £4,062,000 (2013: £4,147,000) originates from the acquisition of Velocys, Inc. in 2008. Goodwill of £1,865,000 (2013: £nil) originates from the acquisition of Velocys Projects Solutions in 2014. Customer contracts represents the discounted value of expected future income to be received by the Company upon obtaining a final investment decision by outside investors currently being sought to invest in the Ashtabula project (see note 30).

Notes to the financial statements (continued)

It is not possible to allocate goodwill to each individual CGU as goodwill is considered to relate to the synthetic fuel group of CGUs as a whole. This group represents an operating segment as described in further detail within the segmental disclosures in note 4.

An impairment test is a comparison of the carrying value of the assets of the CGU (or group of CGUs for goodwill) with their recoverable amount. Where the recoverable amount is less than the carrying value, an impairment results. The Company has carried out its annual impairment testing at 31 December each year. The recoverable amounts of the CGUs are determined based on the value in use ('VIU') calculations for all but one of the technology streams, which due to the stage of its development has been measured at the estimated fair value less cost to sell. The VIU calculation is based upon the estimated discounted future cash flows to be generated by the respective technology stream.

Key assumptions
The key assumptions in the VIU calculations are the discount rate applied and sales and gross margin forecasts for the period of the expected useful life of the technology.

Sales and gross margin forecasts
Future sales forecasts are based upon the commercialisation of the Company's technology in what is an emerging and nascent market. Forecast sales and gross margin levels are therefore dependent upon speed of uptake of the Company's technology, the size of the markets and the penetration achieved in those markets.

In all cases the approved budget for the following financial year forms the initial basis for the forecasts. Growth rate assumptions have then been applied to revenue for periods of between 6 and 7 years for each CGU. Revenue growth beyond this period has not been assumed in the VIU calculations as it is difficult at this stage to assess a long term growth rate. An expected useful life for each technology stream has been estimated of 15 years in each case.

Discount rate
The discount rate applied to each CGU represents a pre-tax rate that reflects market assessment of the time value of money at the balance sheet date and the risks specific to each CGU. The pre-tax discount rates applied to each CGU was 25% in 2014 (2013: between 25% and 30%).

Summary of results
During the year, goodwill and in process technology intangible assets were tested for impairment and it was determined that one of the six CGUs was fully impaired resulting in an impairment charge of £1,328,000 (2013: nil).

For the remaining five CGUs, the forecasts used in the impairment review as at 31 December 2014 indicate significant headroom when comparing recoverable amount against carrying value. However, given the early stage of adoption there remains a significant level of judgment involved in making the assumptions for revenues and margins.

Amortisation of intangible assets is charged to other administrative expenses in the consolidated income statement. Under no reasonable scenario is an impairment expected to arise in relation to the remaining intangible assets.

Parent company
The parent company has no intangible assets (2013: nil).

18. Property, plant and equipment

Company 2014	Assets under construction £'000	Land £'000	Plant and machinery £'000	Total £'000
Cost				
At 1 January 2014	160	–	6,953	7,113
Additions	1,203	23	318	1,544
Disposals	–	–	(450)	(450)
Assets acquired on acquisition of subsidiary	–	940	–	940
Transfers to plant and machinery	(630)	–	630	–
Foreign exchange	45	90	376	511
At 31 December 2014	778	1,053	7,827	9,658
Accumulated depreciation				
At 1 January 2014	–	–	5,029	5,029
Charge for the year	–	–	728	728
Disposals	–	–	(439)	(439)
Foreign exchange	–	–	275	275
At 31 December 2014	–	–	5,593	5,593
Net book amount				
At 31 December 2014	778	1,053	2,234	4,065

2013	Assets under construction £'000	Land £'000	Plant and machinery £'000	Total £'000
Cost				
At 1 January 2013	200	–	6,264	6,464
Additions	418	–	553	971
Disposals	–	–	(185)	(185)
Transfers to plant and machinery	(456)	–	456	–
Foreign exchange	(2)	–	(135)	(137)
At 31 December 2013	160	–	6,953	7,113
Accumulated depreciation				
At 1 January 2013	–	–	4,568	4,568
Charge for the year	–	–	740	740
Disposals	–	–	(185)	(185)
Foreign exchange	–	–	(94)	(94)
At 31 December 2013	–	–	5,029	5,029
Net book amount				
At 31 December 2013	160	–	1,924	2,084

The costs of leased assets included above is £214,000 (2013: £225,000). The net book amount of leased assets included above is £121,000 (2013: £162,000). Depreciation is charged to other administrative expenses in the consolidated income statement.

Parent company
The parent company has no property, plant or equipment (2013: nil).

As at 31 December 2014, the Company had entered into contractual commitments for the acquisition of property, plant and equipment amounting to £60,000 (2013: £24,000).

Notes to the financial statements (continued)

19. Investments in subsidiaries

Velocys plc	2014 Loan to subsidiaries £'000	2014 Capital contributions to subsidiaries £'000	2014 Total investment in subsidiaries £'000	2013 Loan to subsidiaries £'000	2013 Capital contributions to subsidiaries £'000	2013 Total investment in subsidiaries £'000
Investments in subsidiaries						
At 1 January	47,948	29,407	77,355	26,040	26,625	52,665
Movement in loans	47,080	–	47,080	23,858	–	23,858
Capital contributions		5,525	5,525	–	2,782	2,782
Foreign exchange	(1,208)	–	(1,208)	(1,950)	–	(1,950)
At 31 December	93,820	34,932	128,752	47,948	29,407	77,355

The Directors believe the carrying value of the investments is supported by their expected future cash flows. Investments include long term loans to Velocys, Inc., Velocys Technologies Limited and Velocys (USA Holdings) LLC. Investments are stated at cost.

The parent company has direct investments in the following subsidiary undertakings.

Subsidiary undertakings	Country of incorporation or principal business address	Principal activity	% Holding (all ordinary share capital)
Velocys Technologies Limited	England and Wales	Design and development of catalysts, and exploitation of platform catalyst technologies	100
Velocys (USA Holdings) LLC	Ohio, USA	Holding company for US subsidiaries	100
Oxford Catalysts Trustees Limited	England and Wales	Holds assets and makes distributions in respect of employee remuneration	100

The following companies are significant subsidiaries of the Company whose immediate parent is not Velocys plc.

Subsidiary undertakings	Country of incorporation or principal business address	Principal activity	% Holding (all ordinary share capital)
Velocys, Inc.	Delaware, USA	Design, development and exploitation of its microchannel technologies	100
Velocys Project Solutions, LLC	Delaware, USA	Project development of smaller scale GTL plants	100
Ashtabula Energy, LLC	Delaware, USA	Project development of smaller scale GTL plant in Ashtabula, Ohio	100
JAB Land-Ashtabula	Ohio USA	Hold land for small scale GTL plant in Ashtabula Ohio	100

Velocys plc has an investment in the following dormant subsidiary.

Dormant subsidiary	Incorporated	Principal activity	% Holding
Oxford Catalysts UK Limited	England and Wales (07671880)	Dormant company	100

20. Investments

	2014 £'000	2013 £'000
Investment in GTL JV	1,613	–
Foreign exchange	98	–
	1,711	–

Available for sale financial assets purchased for cash in 2014 represent the acquisition of an 8.6% minority interest in a GTL joint venture. In 2014 the Company entered into an exclusive joint venture (GTL JV) with established players in the gas and energy markets to develop GTL plants using a combination of renewable biogas (including landfill gas) and natural gas. The investment is measured at fair value on the balance sheet date and any changes in value are included in the consolidated income statement. The investment was remeasured at 31 December 2014 and there was no change in value. This is a level 3 fair value measurement. The investment is denominated in US dollars. The Company is committed to a further investment of £1,653,000. The parent company had no investments (2013: nil).

21. Trade and other receivables

	Company	
	2014 £'000	2013 £'000
Current		
Trade receivables	43	102
Prepayments and accrued income	420	797
Other receivables	190	213
	653	1,112

The fair value of trade and other receivables is not materially different to the book value above (2013: not materially different). The majority of the trade receivables are due from large multinational groups and hold a low credit risk. The maximum exposure to credit risk at the reporting date is the carrying value of each class of receivable plus cash balances held. The Company does not hold any collateral as security (2013: nil).

The parent company had trade and other receivables of £76,000 (2013: nil).

As at 31 December 2014 Company trade receivables of nil (2013: £71,000) were past due but not impaired. The aging analysis for the 2013 amounts past the due date, which were received in full in 2014, is as follows.

	Company	
	2014 £'000	2013 £'000
Up to 3 months	–	71
	–	71

The parent company had no trade and other receivables past due but not impaired (2013: nil).

Trade receivables outstanding at year end represent approximately 9 days' sales (2013: 8 days).

The Company believes that the full amount of trade receivables recognised is recoverable after allowance has been made for doubtful debts. At 31 December 2014, the parent company had no overdue trade receivables (2013: nil). The other classes within trade and other receivables do not contain impaired assets (2013: nil).

Notes to the financial statements (continued)

The allowance for doubtful debt at 31 December 2013 related to two smaller companies who no longer appear to be in a position to pay. This amount was written off in 2014. Details of the allowance for doubtful debt are as follows:

Allowance for doubtful debt included in trade receivables	2014 £'000	2013 £'000
Provision		
At 1 January	–	90
At 31 December	–	90

Trade and other receivables are denominated in the following currencies:

	2014 £'000	2013 £'000
UK sterling	331	662
US dollars	322	450
	653	1,112

22. Inventory

	Company	
	2014 £'000	2013 £'000
Raw materials and consumables	8	–
Finished goods	283	263
Total	291	263

The parent company has no inventory.

23. Short term investments, cash and cash equivalents

	Company	
	2014 £'000	2013 £'000
Short term bank deposits	28,083	11,875
Cash at bank and in hand	31,693	14,475
Total cash and cash equivalents	59,776	26,350

Under IFRS 7, cash held on term deposits of greater than 3 months has been classified as a short term investment.

Both short term investments, and cash and cash equivalents, are denominated in UK sterling and in US dollars, as follows:

UK sterling denominated:

	Company	
	2014 £'000	2013 £'000
Short term bank deposits	21,000	11,875
Cash at bank and in hand	24,039	8,813
	45,039	20,688

US dollar denominated:

	Company	
	2014 £'000	2013 £'000
Short term bank deposits	7,083	–
Cash at bank and in hand	7,654	5,662
	14,737	5,662

The parent company has no cash or cash equivalents (2013: nil).

24. Trade and other payables: current

	Company	
	2014 £'000	2013 £'000
Trade payables	728	1,526
Other payables	875	–
Other taxation and social security	62	65
Accruals	3,260	3,600
Deferred income	4,214	830
Deferred consideration	1,763	–
	10,902	6,021

The parent company has trade and other payables of £85,000 (2013: nil).

The fair value of trade and other payables are not considered to be materially different to their carrying values based on discounted cash flows. In circumstances in which an award for costs from an external entity is subject to a final settlement, such as awarded costs from a court judgement, the Company does not recognise awarded amounts until the settlement is finalised and are therefore included in other payables.

25. Trade and other payables: non-current

	Company	
	2014 £'000	2013 £'000
Accruals	69	96
Deferred licence payments	–	136
	69	232

The parent company has no non-current trade and other payables (2013: nil).

The deferred licence payments payable represented the discounted value of the minimum licence payments due under the terms of a licence agreement between Velocys and ISIS Innovations Limited, the technology transfer office of the University of Oxford, which was cancelled during 2014. In 2013 the discounted value of these payments was included in intangible assets.

The fair value of trade and other payables are not considered to be materially different to their carrying values based on discounted cash flows.

26. Borrowings

The parent company had no borrowings in 2014 (2013: nil). Maturity of borrowings for the Company is as follows.

	Company	
	2014 £'000	2013 £'000
Within 1 year	267	104
Within 2 to 5 years	999	969
Greater than 5 years	–	223
	1,266	1,296

Notes to the financial statements (continued)

On 1 December 2009, Velocys plc's wholly owned subsidiary, Velocys, Inc. (Velocys) entered into a loan agreement with the State of Ohio (the State) allowing Velocys to borrow up to $2.25 million to fund qualified capital projects. Under this loan agreement a qualified capital project is one that is for research and development purposes, is completed by 30 June 2010 (subsequently extended to 31 August 2012) and the costs of which are at least 25% funded by Velocys. The interest rate for the loan is 2.00% per annum with a service fee of 0.25% of the principal balance. The loan is repaid to the State using a blended payment schedule as follows:

- for the first five years of the loan, the principal is paid in consecutive monthly instalments based upon an original amortisation over 20 years with any interest accrued during that particular month
- for the remaining term of the loan, the principal is paid in consecutive monthly instalments based upon the remaining term of the loan (5 years) with any interest accrued during that particular month.

The loan is secured by all plant and machinery acquired using the loan proceeds as well as a guarantee of payment provided by the Company. The gross book value of the capital projects secured is £2,116,000 (2013: £1,994,000). The loan was fully drawn down in 2012. After repayments of principal, the amount outstanding on the loan as at 31 December 2014 is £1,138,000 (2013: £1,134,000).

All remaining borrowings arise from finance lease obligations. The fair values of borrowings are not considered to be materially different to their carrying values based on discounted cash flows.

27. Derivative financial instruments

The Company sells sterling and buys US dollars to fund its operations in the United States, for which purpose it makes use of forward contracts and options. At 31 December 2014 the notional principal amounts of the outstanding forward foreign exchange contracts were £14,000,000 (2013: £4,000,000), and the notional principal amount of outstanding forward foreign exchange options was £nil (2013: £1,000,000). All the outstanding contracts will mature during 2015. Gains and losses against the US dollar exchange rate as at 31 December 2014 are recognised in Finance income in the consolidated income statement and in Current assets in the consolidated statement of financial position.

28. Financial instruments

	31 December 2014			
Company	Loans and receivables	Assets at fair value through profit and loss	Available for sale	Total
Assets as per balance sheet				
Available-for-sale financial assets	–	–	1,711	1,711
Derivative financial instruments	–	435	–	435
Trade and other receivables excluding non-financial assets	233	–	–	233
Short term investments – funds held on deposit	28,083	–	–	28,083
Cash and cash equivalents	31,693	–	–	31,693
	60,009	435	1,711	62,155

	31 December 2013			
Company	Loans and receivables	Assets at fair value through profit and loss	Available for sale	Total
Assets as per balance sheet				
Trade and other receivables excluding non-financial assets	315	–	–	315
Short term investments – funds held on deposit	11,875	–	–	11,875
Cash and cash equivalents	14,475	–	–	14,475
	26,665	–	–	26,665

The credit risk of short term investments and cash and cash equivalents, summarised in the following table, is assessed using an external credit rating agency's long-term ratings.

	2014		2013	
Short-term bank deposits, cash at bank and in hand	£	%	£	%
Aa3	11,504	19%	–	–
A1	8,951	15%	–	–
A2	27,496	46%	18,402	70%
A3	11,825	20%	7,948	30%
	59,776		26,350	

	31 December 2014		
Company	Liabilities at fair value through the profit and loss	Other financial liabilities at amortised cost	Total
Liabilities as per balance sheet			
Borrowings	–	1,139	1,139
Trade and other payables excluding non-financial liabilities	–	3,366	3,366
Finance lease liabilities	–	127	127
	–	4,632	4,632

	31 December 2013		
Company	Liabilities at fair value through the profit and loss	Other financial liabilities at amortised cost	Total
Liabilities as per balance sheet			
Borrowings	–	1,134	1,134
Derivative financial instruments	263	–	263
Trade and other payables excluding non-financial liabilities	–	1,662	1,662
Finance lease liabilities	–	162	162
	263	2,958	3,221

29. Called up share capital

Company and parent company	Number of shares (thousands)	Ordinary shares £'000	Share premium £'000
At 1 January 2013	91,432	914	66,662
Employee share options scheme: shares issued	500	5	99
Fund raising January 2013	24,479	245	29,032
At 31 December 2013	116,411	1,164	95,793
Employee share options scheme: shares issued	1,018	10	506
Investment by Shiloh Industries	601	6	1,197
Consideration for purchase of Pinto Energy, LLC	755	8	1,647
Fund raising October 2014	23,111	231	50,082
At 31 December 2014	141,896	1,419	149,225

A total of 13,927,937 (2013: 11,702,661) options to subscribe for ordinary shares of Velocys plc have been granted and are outstanding at 31 December 2014 under the employee options schemes operated within the Company and contracts for options granted to a limited number of consultants. Details are given in note 15.

On 11 March 2014 the Company issued 601,326 shares in Velocys plc at £2.00 per share to Shiloh Industries, Inc. as part of a manufacturing partnership agreement between the companies. The shares represent 0.4% of issued share capital. On 25 June 2014 the Company issued 754,887 shares in Velocys plc at £2.19 to the shareholders of Pinto Energy, LLC, now known as Velocys Projects Solutions, as consideration for the purchase of 100% of its ordinary share capital. These shares represent 0.5% of issued share capital. On 20 October 2014 the Company issued

Notes to the financial statements (continued)

23,111,111 shares in Velocys plc at £2.25 per share to raise £52 million before related transaction expenses of £1.7 million. These shares represent 16.3% of issued share capital. All of the ordinary shares issued have the same rights as the other shares in issue.

30. Acquisition of a subsidiary
On 25 June 2014, the Company acquired 100% membership interest in a projects development company, Pinto Energy, LLC, subsequently rebranded Velocys Project Solutions (VPS), along with its Ashtabula GTL project and pipeline of other opportunities.

Through its acquisition the Company has expanded its commercial operations to actively pursue project development opportunities. VPS is one of the leading project developers of smaller scale GTL in North America. Through its most advanced project to date, VPS is developing a facility for a GTL plant to produce approximately 4,800 barrels per day (bpd) on an 80 acre industrial site that it owns near the Port of Ashtabula, Ohio, USA. Final investment decision in the Ashtabula plant by outside investors currently being solicited by VPS and the Company is expected towards the end of 2015. Future expansions could see installed capacity upwards of 10,000 bpd at the site. In addition to Ashtabula, VPS has a pipeline of smaller scale GTL projects it is seeking to develop throughout North America.

Goodwill of £1,865,000 arising from the acquisition is attributable to the acquired pipeline of potential projects. The deferred consideration of £1,763,000 arose on the acquisition of Velocys Project Solutions and is due within one year.

The following table summarises the consideration for VPS, the fair values of the assets acquired and liabilities assumed at the acquisition date.

Consideration at 25 June 2014	Fair value £'000
Equity	1, 655
Cash	462
Deferred consideration	1,763
Total consideration	3,880
Recognised amount of identifiable assets acquired and liabilities assumed	
Land	940
Other intangible assets	1,344
Total identifiable net assets	2,284
Deferred tax liability	(269)
Goodwill arising on acquisition	1,865
Total	3,880

The total purchase consideration of £3,880,000 comprised an upfront amount of £1,655,000 through the issue of 754,887 shares in Velocys plc, £462,000 paid in cash for outstanding obligations and deferred consideration of £1,763,000 that will also be settled by the issue of shares in Velocys plc. The deferred consideration is contingent on the achievement of final investment decision on the plant in Ashtabula. A discount has been applied to the deferred consideration based on the Company's estimate of the percentage likelihood of achieving final investment decision within a specified time period.

Acquisition costs have been charged to Other administrative expenses in the consolidated income statement for 2014. There were no acquisitions in the year ended 31 December 2013.

The fair value of the 754,887 shares issued as the consideration paid for VPS was based on an average of the published share price from 17 June 2014 to 24 June 2014.

The deferred consideration arrangement requires the Company to pay, in shares of Velocys plc, to the former owners of VPS contingent upon the achievement of final investment decision on the plant in Ashtabula in a specified timeframe. The fair value of the deferred consideration was £1,763,000. The fair value estimates are based on a discount rate of 25%. This is a level 3 fair value measurement.

Other intangibles of £1,344,000 represents the discounted value of future income to be received by the Company upon obtaining a final investment decision by outside investors currently being sought to invest in the Ashtabula project (see note 30). The fair value estimates are based on a discount rate of 63% reflecting the probable level of the eventual fee as well as the likelihood of the project proceeding; this is a level 3 fair value measurement.

31. Commitments

Capital commitments are disclosed in note 18.

Operating lease commitments

The Company leases various offices under non-cancellable operating lease agreements. The lease terms are between 2 and 5 years and the majority of lease agreements are renewable at the end of the lease period at market rate.

	2014 £'000	2013 £'000
Future aggregate minimum lease payments under non-cancellable property leases:		
– Within one year	412	377
– Between one and five years	1,419	1,478
– After more than five years	575	842
	2,406	2,697

	2014 £'000	2013 £'000
Future commitments under non-cancellable operating plant and equipment leases:		
– Within one year	1	1
– Between one and five years	3	4
	4	5

32. Pension arrangements

The Company operates a number of defined contribution schemes for which the pension cost charge for the year amounted to £252,000 (2013: £207,000).

33. Related party transactions

The parent company has the following amounts due from its subsidiaries:

Balances with subsidiary companies	**2014** £'000	2013 £'000
Velocys Technologies Limited	78,565	41,740
Velocys (USA Holdings) LLC	1,711	–
Velocys, Inc.	13,544	6,208
Total due from subsidiaries	93,820	47,948

All amounts are unsecured and have no fixed date of repayment.

Oxford Catalysts Trustees Limited

At the time of exercising their share options, executives of the Company may apply to the employee benefit trust managed by Oxford Catalysts Trustees Limited for a distribution in respect of the exercise value of their options. The trustees then request a contribution from the Company in respect of the grant made. The total value of funds contributed by the Company to Oxford Catalysts Trustees Limited during the year was £205,000 (2013: nil).

Directors, secretary and advisors to the Company

Velocys plc registration no.	5712187
Registered office	115e Olympic Avenue Milton Park Abingdon Oxfordshire OX14 4SA
Directors	Dr Pierre Jungels (Non-executive Chairman) Roy Lipski (Chief executive) Susan Robertson (Chief financial officer) Dr Paul F. Schubert (Chief operating officer) Dr Andrew Jamieson (Non-executive Director) Dr Jan Verloop (Non-executive Director) Sandy Shaw (Non-executive Director) Julian West (Non-executive Director and since 9 January 2015 Senior independent Director)
Company secretary	Susan Robertson
Brokers & nominated advisors	Numis Securities Limited The London Stock Exchange Building 10 Paternoster Square St Pauls London EC4M 7LT
Registrars	Capita Asset Services The Registry 34 Beckenham Road Beckenham Kent BR3 4TU
Bankers	Barclays Bank Plc Wytham Court 11 West Way Oxford OX2 0JB
Public relations	Camarco 107 Cheapside London EC2V 6DN
Independent auditors	PricewaterhouseCoopers LLP One Reading Central 23 Forbury Road Reading RG1 3JH

Velocys plc
115e Olympic Avenue
Milton Park
Abingdon
OX14 4SA
United Kingdom

Registered Number: 5712187