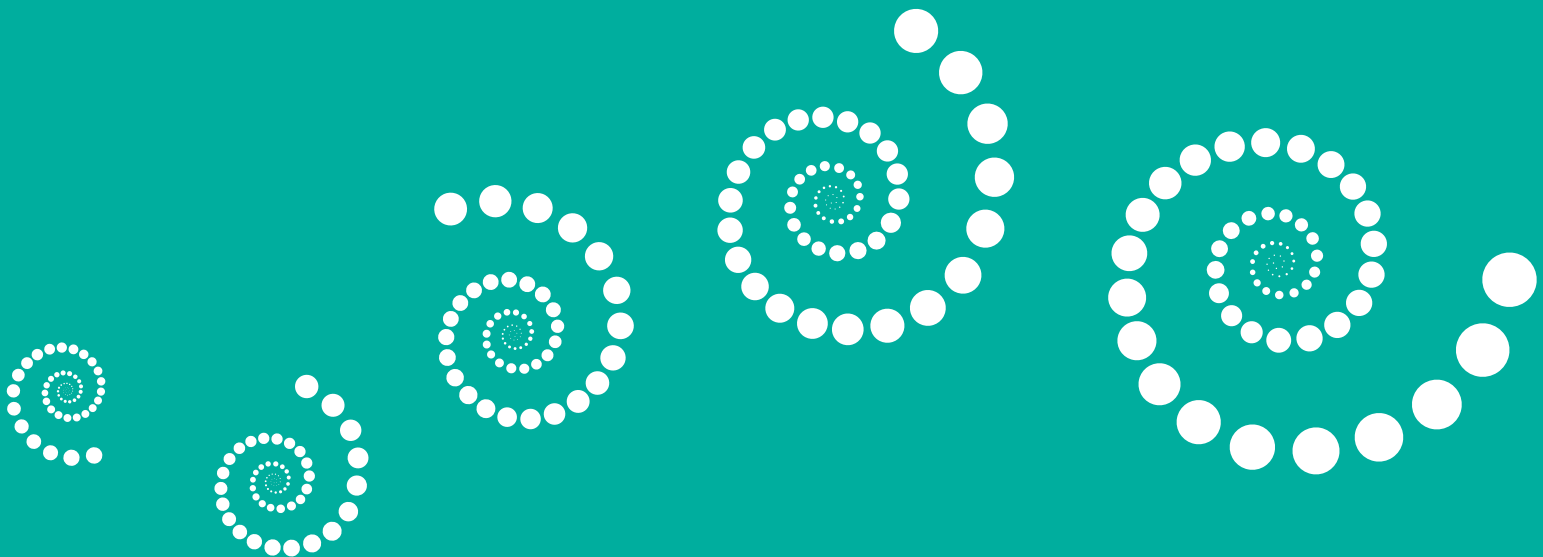


# Annual Report and Accounts

For the year ended 31 March 2009





# NESTA Annual Report and Accounts 2008/09

Annual Report presented to Parliament by the Secretary of State for Business, Innovation and Skills pursuant to section 22(5) of the National Lottery Act 1998. Accounts for the year ended 31 March 2009 presented to Parliament by the Secretary of State for Business, Innovation and Skills on behalf of the Comptroller and Auditor General pursuant to section 23(4) of the National Lottery Act 1998.

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Laid before the Scottish Parliament by the Scottish Ministers.

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## About NESTA

NESTA is the National Endowment for Science, Technology and the Arts – an independent body with a mission to make the UK more innovative. We invest in early-stage companies, inform and shape policy, and deliver practical programmes that inspire others to solve the big challenges of the future.

The unique nature of our endowed funds means that we are able to act differently from others. It allows us to take a longer-term view, and develop ambitious models of innovation that others can replicate or adapt. Our independence and ability to work across different sectors means we are able to bring together ideas from a wide range of perspectives, and to assume a greater burden of risk than others.

NESTA does not work alone. Our success depends on the strength of the partnerships we form with innovators, policymakers, community organisations, educators and other investors. We bring the best ideas, new flows of capital and talented people together, and encourage others to develop them further.

## The year in review: 2008/2009

This report is divided into two parts. The first is a review of 2008/09 (pages 6 to 9), divided into NESTA's three primary areas of activity: Innovation Programmes; Policy and Research; and Investments. The second part (pages 10 to 57) contains the Financial Statements for 2008/09, including the Directors' Report and Management Commentary.

This report complements NESTA's latest Annual Review, 'What impact does NESTA make?', which was published in February 2009 and assesses the effectiveness of NESTA's activities during the calendar year 2008. It can be downloaded (along with previous Annual Reports) from the NESTA website at [www.nesta.org.uk/annual-reports](http://www.nesta.org.uk/annual-reports).

Overview of developments:

Building on the work of the Government's 'Innovation Nation' White Paper, NESTA:

- successfully established an Innovation Research Centre in partnership with DIUS, the Economic and Social Research Council (ESRC) and the Technology Strategy Board;
- launched a Public Services Innovation Laboratory;
- demonstrated its ability to leverage involvement from others and establish effective partnerships;

- made significant progress on gaining acceptance for our design for the UK's new Innovation Index.

NESTA successfully progressed the majority of its experimental programmes to the stage where they yielded some initial lessons and insights. Particularly strong progress was made in our work on how companies can innovate using 'open innovation' processes, and on how mobilising community groups to tackle difficult social issues can generate new ideas. In 2009/10 the aim is to progress this to a set of fully-formed practical toolkits which can be taken up by key stakeholders in the private and public sectors.

## Innovation Programmes

During 2008/09 NESTA's programmes continued to produce a flow of experiment-based learning and practical insights into how businesses, public services, investors, government and others can apply innovative ideas for economic and social benefit.

### Public services innovation

During the first half of 2008/09, we developed plans for NESTA's **Public Services Innovation Lab**, which had been announced in the 'Innovation Nation' White Paper in March 2008. The Lab is designed to test, assess and build a body of evidence on how to foster radical new ideas for innovation in the UK's public services. Its initial focus is on finding solutions to urgent social and environmental challenges such as a rapidly ageing population, climate change and health. We launched The Lab in March 2009.

The **Health Launchpad**, a joint initiative with the Young Foundation, continued its work on developing social enterprises to help reduce the strain on the NHS by shifting the focus of care for long-term conditions from hospitals to the community. During the year, the Launchpad provided support for a number of new healthcare ventures, both commercial and not-for-profit.

In April 2008 we announced the 100 ideas short-listed for the **Big Green Challenge**, NESTA's £1 million prize fund challenging groups of people to find new ways of reducing CO<sub>2</sub> emissions in their communities. Over the year, we helped those groups develop their ideas into detailed delivery plans, and in October announced the ten finalists. They are now putting their plans into practice in their communities, and the winners will be named in early 2010.

## Social investment

Social enterprises can play an important role in tackling some of the social challenges facing the UK. But our research has shown that funding is a significant barrier. During 2008/09 we developed a strand of work to investigate ways of transforming investment in the social enterprise sector. Over the next three years we will work with partners to develop and test new approaches to stimulate the demand for, and supply of, social enterprise capital. Our ambition is to act as a market-maker to help the social finance sector mature and grow.

In November 2008, we invested in and helped launch the **Bridges Social Entrepreneurs Fund**, which will provide up to £1 million in equity capital to ventures that can deliver high social impact as well as solid financial performance. Over time, the fund aims to attract more investment into this sector by demonstrating the real social and economic value of this approach.

## Creative economy

The creative sector is a vital resource for the UK, employing more than a million people and contributing £57 billion a year to the economy. But it is characterised by many small firms, few of which ever reach a significant size. During 2008/09, NESTA continued its work to understand why this is the case, and to find ways of tackling it.

Our **Starter for 6** project continued to deliver training, business advice and mentoring to young Scottish entrepreneurs, building on an established record of success. Independent evaluation found that it added around £2.16 in value for every £1 invested from public funds. The models and materials that we have developed are now being used by other organisations across the UK, and Starter for 6 now has the potential to become a fully-fledged nationwide network of entrepreneurs, providing opportunities not just for learning and support, but collaboration and business development.

In July, we launched **Take 12 – Digital Innovation in Film**, a partnership with the UK Film Council that is working with 12 UK film businesses to explore how small creative businesses can exploit the opportunities provided by digital technology. In 2009 we aim to build the insights from this programme into a more general model of how to support creative businesses in the growth stage.

Also in July, we launched **Raise the Game**, a partnership with Tiga, the national trade association for the games industry. Although often dismissed as a marginal mania, the gaming industry is a huge opportunity for the UK. But

it faces some fundamental challenges, notably a shortage of skilled people, and a lack of early-stage finance for start-ups. Raise the Game provides active support to small-scale games developers to help them grow their businesses, and create and exploit their own intellectual property.

Our research has shown that creative businesses with high growth potential often need specialised help to expand. One idea we are testing is the role of mentoring. In February 2009, we launched the **Creative Business Mentor Network** for companies in the TV production, advertising and digital media sectors. The 20 participating companies will benefit from one-to-one mentoring with some of the most successful business people from the creative sector.

In October 2008 we launched the **Creative Business Catalyst** pilot, which partners MBA students with creative businesses to deliver a specialist, structured programme of business intervention and support.

## Corporate innovation

During 2008/09 we worked with a range of corporate organisations to explore ‘open’ processes of innovation, in which companies look beyond reliance on their own internal R&D departments to work more openly on new ideas with other external organisations. In October, we announced that Procter & Gamble had selected three of the product ideas pitched to them as part of NESTA’s **Corporate Open Innovation Challenge**, identifying a potential market value of \$100 million for each.

During the year, two of the companies taking part in **Corporate Connections** – McLaren and NATS – announced a major new business collaboration in the worldwide air traffic control market. The programme brings together large companies from different sectors to collaborate on common challenges. Other participants included AXA, GlaxoSmithKline, Procter & Gamble, E.ON, Philips and QinetiQ.

In November we launched the **Open Ventures Challenge** to help support the fundraising efforts of Cancer Research UK. The charity invited people across the UK to come up with ideas for generating up to £10 million to support its work, with the emphasis on new commercial and collaborative ventures, rather than conventional fundraising.

**V-Jam**, a partnership with Virgin Atlantic launched in December, focused on how open innovation can be used in a more targeted way, engaging the airline’s end-user customers to create and develop ideas for new products and services.

In 2008/09 we welcomed a new cohort to the popular and successful **Crucible** programme, which brings together researchers from different disciplines to collaborate on shared issues. We have learnt from Crucible that putting people and subject expertise together in unorthodox combinations is a very powerful way to generate new and unexpected ideas. During the year we extended this approach with the launch of **Carbon Crucible**, which focuses on the specific challenge of reducing the carbon footprint of the energy industry.

## Policy & Research

An important area of NESTA's research focus during 2008/09 was on how to measure innovation accurately at the national level. The 'Innovation Nation' White Paper charged NESTA with developing a new **Innovation Index** to capture innovation in the UK's increasingly important services sectors, creative industries and delivery of public services. The Index will be ready in its final form in 2010, with a pilot version tested in 2009. In 2008/09 we successfully completed a preliminary phase of 'mini-projects' to establish a credible design for the overall shape of the Index.

NESTA has argued for several years that much innovation is 'hidden' – it doesn't show up in official statistics about scientific R&D. Our work on '**hidden innovation**' has successfully made the case with policymakers that the current tools for measuring the UK's performance need to be brought in line with how innovation really works in the economy and society.

During 2008/09 we developed this concept further with the idea of 'total innovation'. In May 2008 we published our '**Total Innovation**' report, which focused on high-technology sectors such as aerospace and pharmaceuticals. It revealed the increasing importance of hidden innovation in these sectors, and the surprising ways in which our most innovative firms have adapted to technological change and international competition.

Another important area of research during the year was the role of '**place**' in innovation. Why do some cities and regions perform better than others when it comes to generating and exploiting new ideas? We learnt that the link between new ideas and economic growth is not simple. In October we published our 'Innovation by Adoption' report, which showed that a place's ability to absorb and exploit ideas from elsewhere (its 'absorptive capacity') is just as important as its ability to generate its own ideas.

In December we published our '**Attacking the Recession**' paper, the first of several contributions to the debate on how the UK should respond to the recession, and what role innovation can play in creating longer-term strength in the UK economy and society. In March 2009 we published a second report, 'Demanding Growth', which argued that government policy should focus on innovation and growth, supporting innovative sectors that have the potential for strong growth once the recovery begins.

Also in December, the new £5 million **Innovation Research Centre** was announced, an outcome of the 'Innovation Nation' White Paper. The centre is a collaboration between NESTA, the Economic and Social Research Council, DIUS and the Technology Strategy Board. Jointly hosted by the University of Cambridge and Imperial College London, it will commission research into the role, drivers and impact of innovation.

## Investments

Through NESTA Ventures we demonstrate and gain a practical understanding of how to invest in, manage and support high-growth technology companies. NESTA Capital allows us to gain a practical understanding of how to invest in and manage a fund-of-funds activity. Importantly this also gives us an exceptional insight into different models of investment and allows us to be a cornerstone investor to help launch new funds.

Our data collection and analysis combined with our practical understanding of the market places us in a unique position to influence regional and national innovation, investment and business support policy.

In 2008/09 NESTA Ventures made five new direct investments (totalling £1.2 million) and 14 follow-on investments (totalling £1.7 million). We also sold a direct investment for a profit and now have a portfolio of 50 investee companies.

Through NESTA Capital we made a commitment of £500,000 to one investment fund and now have a portfolio of four funds.

Examples of Investments in 2008/09 include:

- New investment in **Dexela**, to develop medical imagery technology for breast cancer screening.
- New investment in **OSspray**, to help commercialise a bioactive glass for air polishing in dental procedures.

- New investment in **Gnodal**, to develop its high performance ethernet switch technology.
- Further Funding in **Haemostatix**, which is developing a safe substitute for platelet transfusion.
- Further Funding in **Light Blue Optics**, which is developing holographic projection technology.
- Further Funding in **Starbridge**, to continue development of minute fluid handling tools for insulin delivery and drug discovery.
- NESTA Capital investment in **GP Bullhound Sidecar Fund**, which focuses on technology, media and telecoms businesses.

In order to take a more proactive role in fund management and to gain a greater understanding of supporting university spin-outs, in November we were appointed as the manager of the **Kinetique Biomedical Seed Fund**, the first time that we have taken on the role of an FSA-regulated fund manager. Kinetique is a University Challenge Seed Fund, which provides start-up funding for spin-out companies from King's College London and Queen Mary, University of London.

In September 2008 we published our '**Shifting Sands**' report, a detailed investigation of the changing nature of the UK's early-stage venture capital market. It revealed that private sector funding for early-stage investments is getting tighter, and as a result the public sector is becoming much more important. Through this and other research we have provided a major contribution to policy discussions, providing strong evidence to support the case that there is a crisis in venture capital funding and that government support and incentives are urgently needed.

**Jonathan Kestenbaum**  
Chief Executive and  
Accounting Officer

**6 July 2009**

**Sir Chris Powell**  
Chairman

**6 July 2009**

# Directors' Report and Management Commentary

## Constitution

NESTA – the National Endowment for Science, Technology and the Arts – was set up by the National Lottery Act, receiving Royal Assent on 2 July 1998. The composition of the Board and the Executive team is given on pages 12 to 13.

The National Lottery Act 1998 and the Financial Directions, issued by the Secretary of State for the Department for Innovation, Universities and Skills (DIUS) under the National Lottery Act 1998, govern NESTA's operations. NESTA prepares its financial statements in accordance with the Accounts Directions issued by the Secretary of State. A copy of the Accounts Directions can be obtained by writing to NESTA's Chief Operating Officer.

In June 2007 sponsorship responsibility for NESTA passed from the Department for Culture, Media and Sports (DCMS) to DIUS. In June 2009 the Government announced that DIUS and the Department for Business Enterprise and Regulatory Reform (BERR) would be merged to form the new Department for Business, Innovation and Skills (BIS). The effect on NESTA of this change in the sponsor department is expected to be minimal.

## Statutory objects

The statutory objects of NESTA are to support and promote talent, innovation and creativity in the fields of science, technology and the arts.

The objects of NESTA are to be achieved by the following means, namely:

- helping talented individuals (or groups of such individuals) in the fields of science, technology and the arts to achieve their potential;
- helping persons to turn inventions or ideas in the fields of science, technology and the arts into products or services:
  - which can be effectively exploited; and
  - the rights to which can be adequately protected; and
- contributing to public knowledge and appreciation of science, technology and the arts.

## Overview of developments

Building on the work of the Government's Innovation White Paper:

- NESTA successfully established an Innovation Research Centre in partnership with DIUS, the Economic and Social Research Council (ESRC) and the Technology Strategy Board.
- We launched a Public Service Innovation Laboratory.
- We made significant progress on gaining acceptance for our design for the UK's new Innovation Index.

NESTA's core output is practical well-evidenced models of how innovation can happen. NESTA successfully progressed the majority of its models to the stage where they yielded some initial learnings. Particularly strong progress was made in our work on how companies can innovate using 'open innovation' processes, and on how mobilising community groups to tackle difficult social issues can generate new ideas. In 2009/10 the aim is to progress this to a set of fully-formed practical toolkits which can be taken up by key stakeholders in the private and public sectors.

In addition, NESTA made 14 follow-on investments and 5 new direct investments in early-stage companies, totalling £2.9 million in value. It committed to one new investment in early stage-funds to the value of £0.5 million.

NESTA demonstrated its credibility with external funders by leveraging in substantial additional funding:

- NESTA Investments' companies attracted private sector funding at the ratio of over 9:1 for each NESTA pound invested; and
- Our practical projects levered in additional funding of over 100 per cent of the NESTA funding.

## Financial overview

The financial statements on pages 23-57 show the income and expenditure for the year. They reflect the mandatory adoption of financial reporting standards for financial instruments, preparatory to the adoption of International Financial Reporting Standards (IFRS) across the public sector. NESTA is now required to capitalise its investments in early-stage companies and funds rather than treating them as expenditure, and also show unrealised gains or losses from investment valuations in a fair value reserve rather than be included in investment returns, as they have

up to now. This has resulted in the restatement of the 2008 comparatives.

The financial statements also consolidate NESTA's three subsidiary undertakings, which were incorporated in June 2008 to support our work with early-stage companies.

Non-investment activity continued to increase, driven by increased levels of activity in NESTA's practical programmes. Under NESTA's accounts directions, expenditure is recorded on a commitment basis, so is a leading indicator of actual project activity.

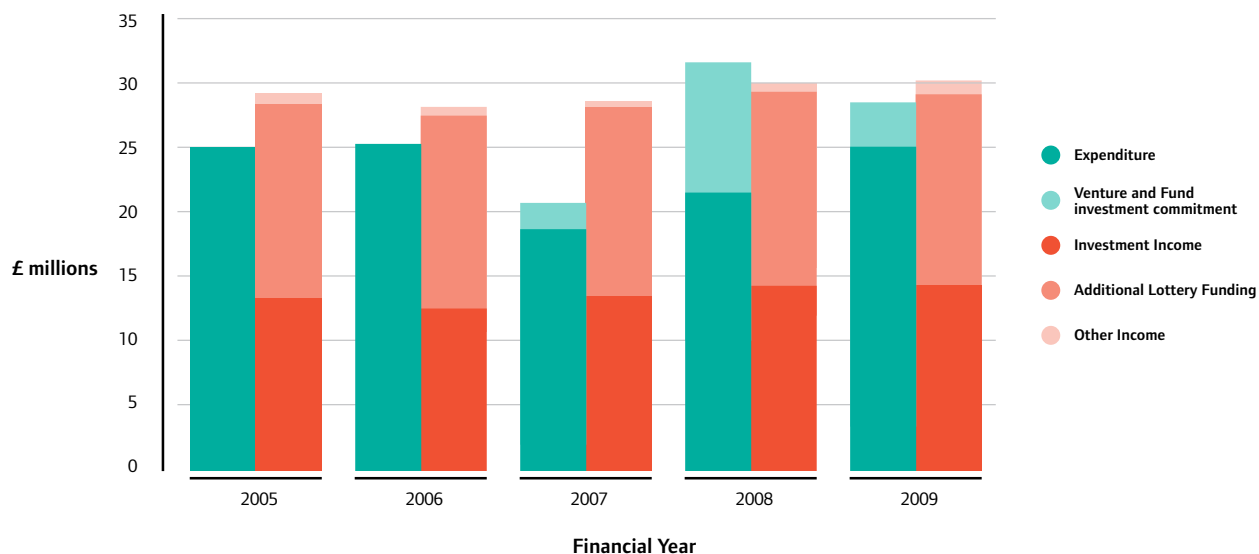
Levels of investment by NESTA Investments fell sharply as deal-flow was substantially affected by the adverse market conditions which developed from summer 2008 onwards, due to the recession and difficulties in financial markets. The comparative ratio of support costs to continuing non-exceptional expenditure fell from 12.6 per cent to 9.5 per cent.

Income levels were slightly higher than the previous year due to higher yields on non-gilt investments, together with some additional external income. Investment income is primarily interest from gilt investments. The total value of gilt and other investment assets at 31 March 2009 was £326 million of which £287 million was invested in gilts and short-term deposits, with the remainder invested in equities, bonds and property. In addition, the total value of NESTA Investments' portfolio holdings was £10.6 million at 31 March 2009. The liberalisation of the Endowment which was agreed last year is currently on hold.

NESTA will continue to receive additional lottery funding of £15 million per year up to and including 2010/11 from the National Lottery in line with a Ministerial agreement in February 2006.

## NESTA Investments

NESTA Investments' return from its portfolio of investments in companies and loans was a loss of £1,903k, comprising profit on sale of investments, and cumulative movements in fair value. In addition, £202k has been received as amounts recovered from loans previously written off and interest thus making a total return loss from direct investments of £1,701k. Total return from NESTA's share of net assets in investment funds was a loss of £173k. In accordance with FRS 26, NESTA's investments are classified as available for sale, and therefore movements in fair value are recognised through the fair value reserve in the balance sheet, except for impairments which are recognised in the Income and Expenditure account. Many private sector venture capital companies adopt a different approach and recognise all in-year movements in the value of investments through the Profit and Loss account thus dealing with total return on investments entirely in the profit and loss account. The negative movements in fair value this year are principally due to the recessionary influence resulting in a lack of third party funding and meaning that a robust view has had to be taken of the prospects for certain investments.



## Organisational structure

Name	Position
Sir Chris Powell	Chairman
Jonathan Kestenbaum	Chief Executive and Accounting Officer

In addition to the Chief Executive, the following were members of the Executive Team during the period from the start of the year to the date of this report:

Name	Date Appointed	Date Resigned	Position
Rachel Grant	February 2009		Executive Director Communications
Helen Gresty	May 2006		Executive Director Innovation Programmes
Richard Halkett	June 2006	September 2008	Executive Director Policy & Research
David Hunter	June 2006		Managing Director NESTA Investments
Daniel Oppenheimer	September 2007		Chief Operating Officer
Michael Stephenson	November 2007	June 2008	Executive Director Communications
Jennifer Weller	September 2008	December 2008	Executive Director Communications
Stian Westlake	January 2009		Executive Director Policy & Research

The following were Trustees during the period from the start of the year to the date of this report:

Name	Date Appointed	Date Retired	Committee & Advisory Board Membership
Sir Chris Powell (Chairman)	October 2003		Investment (Chair)
Sir Michael Barber	February 2006		Innovation Programmes (Chair), Innovation Index Advisory Board
Liam Black	December 2008		Public Services Innovation Laboratory
Professor Marc Clement	July 2006		Investment
Dr Stuart Cosgrove	October 2004	October 2008	
Sherry Coutu	May 2006		Investment, Endowment
Professor Stephen Emmott	June 2008		
Andrew Flanagan	February 2006	March 2009	Finance & Audit (Chair)

Name	Date Appointed	Date Retired	Committee & Advisory Board Membership
Jitesh Gadhia	July 2007		Finance & Audit, Endowment (Chair)
Professor Julia Goodfellow	January 2005	December 2008	
Dr Tracy Long	December 2003		Finance & Audit
Patrick McKenna	December 2006		Endowment
Nick Starr	December 2007		Innovation Programmes
Professor Kathy Sykes	January 2007		Innovation Programmes
Coram Williams	June 2009		Finance & Audit (Chair)

The following were non-Trustee members of Committees and Advisory Boards during the period from the start of the year to the date of this report:

Name	Date Appointed	Committees & Advisory Boards
William Roe	August 2006	Innovation Programmes
David Auckland	August 2006	Innovation Programmes
Tom Hadfield	August 2006	Innovation Programmes
Madeleine Atkins	May 2007	Innovation Programmes
Bettany Hughes	May 2008	Innovation Programmes
Paul Roberts	July 2006	Innovation Programmes, Public Services Innovation Laboratory
Ernie Richardson	November 2006	Investment
Adrian Beecroft	December 2006	Investment
Ian Mclsaac	November 2006	Investment
Mikael Breuer-Weil	May 2008	Endowment
Nick Cavalla	August 2008	Endowment
Anthony Thomas	January 2008	Finance & Audit
Sir David Henshaw	January 2009	Public Services Innovation Laboratory (Chair)
Sir Michael Bichard	January 2009	Public Services Innovation Laboratory
Rosie Boycott	January 2009	Public Services Innovation Laboratory
Andrew Haldenby	January 2009	Public Services Innovation Laboratory
Ed Mayo	January 2009	Public Services Innovation Laboratory
Rita Patel	January 2009	Public Services Innovation Laboratory
Rob Whiteman	January 2009	Public Services Innovation Laboratory
Dawn Austwick	January 2009	Public Services Innovation Laboratory

Name	Date Appointed	Committees & Advisory Boards
Rod Aldridge OBE	January 2009	Public Services Innovation Laboratory
David Nicholson CBE	June 2009	Public Services Innovation Laboratory
Lord David Currie	April 2008	Innovation Index (Chair)
Karen Dunnell	May 2008	Innovation Index
Helen Fleming/Polly Payne	June 2008	Innovation Index
David Godber	May 2008	Innovation Index
Dr Iain Gray	May 2008	Innovation Index
Christine Hewitt	June 2008	Innovation Index
Richard Lambert	May 2008	Innovation Index
Charles Manby	October 2008	Innovation Index
Vicky Pryce	April 2008	Innovation Index
Ceri Smith	June 2008	Innovation Index
Sir Richard Sykes	December 2008	Innovation Index
Professor Nigel Thrift	May 2008	Innovation Index
Andrew Wyckoff	May 2008	Innovation Index

## Creditors

It is NESTA's policy to abide by the DBERR's 'Better Payment Practice Code' and in particular to pay bills in accordance with contract terms. For the year ended 31 March 2009, 92 per cent of undisputed invoices were paid within 30 days or the contractual term (2008: 87 per cent).

## Equal opportunities

NESTA is committed to a policy of equal opportunity in its employment practices. In particular it aims to ensure that no actual or potential employee or awardee receives more or less favourable treatment on the grounds of race, colour, ethnic or national origin, marital status, age, gender, sexual orientation, disability, religious beliefs, political beliefs, economic status or class.

## Employee consultation

NESTA ensures that there are arrangements to promote effective consultation and communication with all staff. Meetings of all staff are held periodically at which matters relating to NESTA's activities are discussed and staff are briefed on matters discussed at the Executive Team, Committee and Trustee meetings.

## Sickness absence

The average number of days lost per employee to sickness absence, for the financial year ending 31 March 2009 was 2 days (2008: 2 days). This is significantly lower than the average for the public sector of 9.8 days per employee per annum.

## Post balance sheet events

The financial statements were authorised for issue by the Board on 1 July 2009.

There were no reportable post balance sheet events between the balance sheet date and 11 July 2009, the date the accounts were certified by the Comptroller and Auditor General. The financial accounts do not reflect events after this date.

## Personal data loss

NESTA has suffered no protected personal data incidents during 2008/09 or prior years, and has made no reports to the Information Commissioner's office.

## Other matters

NESTA maintains a register of interests of members of the Board of Trustees and staff which is available for public inspection by appointment at NESTA's principal office.

NESTA's staff received gifts and hospitality totalling £2,161 (2008: £342) during the financial year.

NESTA's staff gave gifts totalling £291 (2008: £1,156) during the financial year.

## Audit information

As far as the Accounting Officer is aware, there is no relevant audit information of which NESTA's auditors are unaware, and the Accounting Officer has taken all the steps that he ought to have taken to make himself aware of any relevant audit information and to establish that NESTA's auditors are aware of that information.

# Remuneration Report

## Remuneration Committee

The Remuneration Committee is a sub-committee of the Board of Trustees and is incorporated into the Finance and Audit Committee. It consists of non-executive Trustees, all of whom are appointed on terms agreed by Trustees.

The Remuneration Committee was chaired by Andrew Flanagan. Other members of the Remuneration Committee were Dr Tracy Long and Jitesh Gadhia. A secretariat function is provided by the Chief Operating Officer, and the Chief Executive and the Head of Human Resources normally attend. The Remuneration Committee met four times during the year.

The Remuneration Committee's role is to:

- agree a pro-forma employment contract and subsequent changes;
- agree a remuneration and benefit policy including pension provision which will attract, retain and motivate staff;
- agree the terms, conditions and salary levels for all Executive posts and any annual award to staff;
- review any related party transactions of Trustees and staff; and
- hear Executive level disciplinary appeals.

The Remuneration Committee authorised bonus payments for the Chief Executive and Executives. Relevant performance objectives were set by the Chairman or Chief Executive and assessed as part of the individual's annual appraisal, a summary of which was provided to the Committee.

This year the Remuneration Committee endorsed a new employee Flexible Benefits package.

## Chairman, Trustees' and Committee Members' remuneration

NESTA's Chairman, Trustees and Committee Members were entitled to the following remuneration:

- The Chairman is paid a salary of £26,245 (2008: £25,480) for two days per week.

- Trustees were paid an allowance of £209 (2008: £209) per day spent on NESTA business up until 31 December 2008. From 1 January 2009 Trustees are paid an annual salary: £5,000 base, an additional £2,000 for each committee a Trustee sits on, an additional £2,000 if a Trustee chairs a committee and an additional £4,000 for members of the Investment Committee.
- Committee Members were paid an allowance of £168 (2008: £168) per day up until 31 December 2008. From 1 January 2009 Committee members are paid an annual salary of £2,000 and an additional £2,000 if they chair a committee.
- Advisory Board members are unpaid.
- Out-of-pocket expenses are recoverable.

For a list of all Trustees and Committee Members, refer to the Directors' Report and Commentary. Each Trustee and Committee Member, with the exception of the Chairman, was paid between £0 and £7,000 in each applicable year.

### Audited information:

## Executive team remuneration

The salary and allowances for the Executive team were as follows:

- Benefits represent cash payments made under NESTA's flexible benefits scheme. They include childcare subsidy, enhanced benefits (health, learning and science, technology and arts related memberships) and pension/holiday flex.
- All Executives were entitled to a contribution to a personal pension or group defined contribution scheme at a rate of 12 per cent of salary.
- No member of the Executive team received any non-cash benefits (benefits in kind).
- All Executive appointments are on a permanent basis.
- Executive team salaries have been benchmarked against appropriate external markets.
- Bonuses for the Executive team are based upon performance against defined objectives.

	Salary & Benefits 2009 £'000	Pension Contributions £'000	Bonus Payments 2009 £'000	Total 2009 £'000	Salary & Benefits 2008 £'000	Pension Contributions £'000	Bonus Payments 2008 £'000	Total 2008 £'000	Employment Start Date	Employment End Date	Notice Period Months
Jonathan Kestenbaum	168	20	30	218	157	19	32	208	01/11/2005		3
Rachel Grant	13	2	-	15	-	-	-	-	09/02/2009		6
Helen Gresty	86	10	6	102	84	10	8	102	01/06/2004		6
Richard Halkett	41	5	-	46	84	10	8	102	22/06/2006	30/09/2008	3
Tom Hawkins	-	-	-	-	76	6	-	82		06/04/2007	
David Hunter	123	-	17	140	118	-	22	140	05/06/2006		1
Daniel Oppenheimer	91	10	6	107	47	7	4	58	03/09/2007		6
Michael Stephenson	27	3	-	30	33	4	2	39	19/11/2007	26/06/2008	6
Jennifer Weller	29	-	-	29	-	-	-	-	15/09/2008	05/12/2008	6
Stian Westlake	19	3	-	22	-	-	-	-	05/01/2009		6

**Jonathan Kestenbaum**  
Accounting Officer

6 July 2009

# Statement of Accounting Officer's Responsibilities

## Accounting Officer's Responsibilities

Under the National Lottery Act 1998, the Secretary of State for Culture, Media and Sport has directed NESTA to prepare for each financial year a statement of accounts in the form and on the basis set out in the Accounts Directions. In June 2007 sponsorship responsibility for NESTA passed to the Department for Innovation, Universities and Skills. The financial statements are prepared on an accruals basis and must give a true and fair view of the state of affairs of NESTA and of its income and expenditure, recognised gains and losses and cash flows for the financial year.

In preparing the financial statements, the Accounting Officer is required to comply with the requirements of the Government Financial Reporting Manual and in particular to:

- observe the Accounts Directions issued by the Secretary of State, including the relevant accounting and disclosure requirements, and apply suitable accounting policies on a consistent basis;
- make judgements and estimates on a reasonable basis;
- state whether applicable accounting standards as set out in the Government Financial Reporting Manual have been followed, and disclose and explain any material departures in the financial statements; and
- prepare the financial statements on a going concern basis.

The Accounting Officer of the Department for Innovation, Universities and Skills has designated the Chief Executive as Accounting Officer of NESTA. The responsibilities of an Accounting Officer, including responsibility for the propriety and regularity of the public finances for which the Accounting Officer is answerable, for keeping proper records and for safeguarding NESTA's assets, are set out in the Non-Departmental Public Bodies' Accounting Officers' Memorandum issued by HM Treasury and published in Managing Public Money and in the Financial Directions issued by the Secretary of State for Culture, Media and Sport under Section 21 of the National Lottery Act 1998.

**Jonathan Kestenbaum**  
Accounting Officer

**6 July 2009**

# Statement on Internal Control

## Scope of responsibility

As Accounting Officer I am responsible for maintaining a sound system of internal control that supports the achievement of NESTA's policies, aims and objectives, while safeguarding the public funds and assets for which I am personally responsible, in accordance with the responsibilities assigned to me in Managing Public Money. I am accountable to the Secretary of State for Business, Innovation and Skills and to Parliament for ensuring that NESTA distribute their funds with due regularity and propriety and to the Board of Trustees for the economic, efficient and effective use and control of their funds.

The Board of Trustees is responsible for ensuring that through appropriate procedures, systems and personnel, proper financial management and control is achieved.

## The purpose of the system of internal control

The system of internal control is designed to manage risk to a reasonable level rather than to eliminate all risk of failure to NESTA's goals. It can therefore provide only reasonable and not absolute assurance of effectiveness. The system of internal control is based on an ongoing process designed to identify and prioritise the risks to the achievement of NESTA's goals, to evaluate the likelihood of those risks materialising and their consequent impact, and to manage them efficiently and with appropriate and proportionate controls. The system of internal control has been in place at NESTA for the year ended 31 March 2009 and accords with Treasury guidance.

## Capacity to handle risk

NESTA's Chief Operating Officer has lead responsibility at the level of the Executive team for the risk management framework. NESTA's Finance & Audit Committee is responsible for monitoring the implementation of this framework, and for reviewing and reporting to the Board of Trustees annually on the approach to risk management.

The Executive team regularly reviews strategic risks, and individual members of the Executive team are responsible for managing and monitoring these and other operational risks, where appropriate through their teams. Staff actively consider risks as part of the management of individual projects.

## The risk and control framework

The key elements of NESTA's risk management strategy and control framework are set out below.

The Trustees believe that NESTA's mission requires it to have an element of risk-taking in its activities if it is to succeed. Accordingly NESTA's risk appetite is for managed risk-taking rather than simple risk aversion. This includes the recognition that some activities or projects may fail to a greater or lesser extent, and that such failure can be an important source of learning.

Risk management is incorporated into NESTA's strategic and business planning processes.

A budget and budget monitoring system is set in the context of a multi-year strategic planning process. The budget is approved by the Board of Trustees and quarterly financial reports are made to the Finance & Audit Committee.

NESTA's risk management framework sets out the basis for identifying, monitoring and reporting on risk in the context of the organisation's agreed risk appetite. Risk registers are maintained and regularly updated throughout the year as a result of executive and management reviews. Risks are discussed by the Finance & Audit Committee.

NESTA has a number of operational policies under the general headings of governance, financial controls and workplace management. These policies are supported by induction training designed to ensure that NESTA staff are aware of these policies and comply with them appropriately. There is special focus on the proper procurement of goods and services, the management of conflicts of interest and the control of fraud.

NESTA has an internal audit service which operates in accordance with Government Internal Audit Standards. The annual internal audit plans are informed by the risk register, are endorsed by the Finance & Audit Committee and approved by the Accounting Officer. The internal auditors provide an annual report on internal audit activity, an independent opinion on the adequacy and effectiveness of NESTA's system of internal control and recommendations for improvement. All internal audit reports and reviews are considered by the Finance & Audit Committee. Management responses and progress against agreed actions are reported to and monitored by the Finance & Audit Committee on a quarterly basis with an annual review of all outstanding matters. In keeping with best practice, NESTA periodically reviews its internal audit providers.

The Finance & Audit Committee has three Trustee members and a co-opted member who has been selected for his/her effectiveness and experience in this field. Each meeting of the Committee includes an opportunity for a session with internal and external auditors without NESTA staff present.

NESTA also considers its responsibilities on Information Security and Personal Data to be a high priority. We have procedures and data loss prevention technologies in place that minimise the risk of information loss and security breaches. In the last year we have revised our IT policies to ensure they are aligned with DIUS guidelines and the Cabinet Office Data Handling Review, where appropriate. We have issued revised guidance to all staff on the handling of personal data, and all new staff receive a security and data handling induction. We have not had any personal data-related incidents from 2004/2005 through to 2008/2009.

## Review of effectiveness

As Accounting Officer, I have responsibility for reviewing the effectiveness of the system of internal control. My review of the effectiveness of the system of internal control is informed by the work of the internal auditors and the executive managers within the organisation who have responsibility for the development and maintenance of the internal control framework, and comments made by the external auditors in their management letter and other reports. I have been advised on the implications of the result of my review of the effectiveness of the system of internal control by the Board, and the Finance & Audit Committee, and a plan to address weaknesses and ensure continuous improvement of the system is in place.

I have reviewed the work and reports of the internal auditors and system of monitoring and implementation of agreed actions arising from their recommendations, including in particular the annual report of the internal auditors to the Finance & Audit Committee, the responses to their recommendations and their opinion of the effectiveness of NESTA's system of internal control, and have satisfied myself as to its soundness.

I have concluded that, although improvements to systems can always be made and NESTA has an ongoing programme to continuously improve the scope and effectiveness of its systems, there have been no significant internal control problems during the year.

**Jonathan Kestenbaum**  
Accounting Officer

**6 July 2009**

# Certificate and Report of the Comptroller and Auditor General to the Houses of Parliament and the Scottish Parliament

I certify that I have audited the financial statements of the National Endowment for Science, Technology and the Arts (NESTA) for the year ended 31 March 2009 under the National Lottery Act 1998. These comprise the Income and Expenditure Account, the Balance Sheet, the Cash Flow Statement and Statement of Recognised Gains and Losses and the related notes. These financial statements have been prepared under the accounting policies set out within them. I have also audited the information in the Remuneration Report that is described in that report as having been audited.

## Respective responsibilities of the Trustees, Chief Executive and auditor

The Trustees and Chief Executive as Accounting Officer are responsible for preparing the Annual Report, which includes the Remuneration Report, and the financial statements in accordance with the National Lottery Act 1998 and directions made thereunder by the Secretary of State for Innovation, Universities and Skills, with the consent of HM Treasury, and for ensuring the regularity of financial transactions. These responsibilities are set out in the Statement of Accounting Officer's Responsibilities.

My responsibility is to audit the financial statements and the part of the remuneration report to be audited in accordance with relevant legal and regulatory requirements, and with International Standards on Auditing (UK and Ireland).

I report to you my opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with the National Lottery Act 1998 and directions made thereunder by the Secretary of State for Innovation, Universities and Skills, with the consent of HM Treasury. I report to you whether, in my opinion, the information, which comprises the Directors' Report and Management Commentary, included in the Annual Report, is consistent with the financial statements. I also report whether in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

In addition, I report to you if NESTA has not kept proper accounting records, if I have not received all the information and explanations I require for my audit, or if information specified by HM Treasury regarding remuneration and other transactions is not disclosed.

I review whether the Statement on Internal Control reflects NESTA's compliance with HM Treasury's guidance, and I report if it does not. I am not required to consider whether this statement covers all risks and controls, or form an opinion on the effectiveness of NESTA's corporate governance procedures or its risk and control procedures.

I read the other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. This other information comprises all sections of the Annual Report except for the Directors' Report, Management Commentary and the audited part of the Remuneration Report. I consider the implications for my report if I become aware of any apparent misstatements or material inconsistencies with the financial statements. My responsibilities do not extend to any other information.

## Basis of audit opinions

I conducted my audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. My audit includes examination, on a test basis, of evidence relevant to the amounts, disclosures and regularity of financial transactions included in the financial statements and the part of the Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgments made by the Trustees and Chief Executive in the preparation of the financial statements, and of whether the accounting policies are most appropriate to NESTA's circumstances, consistently applied and adequately disclosed.

I planned and performed my audit so as to obtain all the information and explanations which I considered necessary in order to provide me with sufficient evidence to give reasonable assurance that the financial statements and the part of the Remuneration Report to be audited are free from material misstatement, whether caused by fraud or error, and that in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them. In forming my opinion I also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the Remuneration Report to be audited.

## Opinions

In my opinion:

- the financial statements give a true and fair view, in accordance with the National Lottery Act 1998 and directions made thereunder by the Secretary of State for Innovation, Universities and Skills, of the state of NESTA's affairs as at 31 March 2009 and of its surplus, recognised gains and losses and cash flows for the year then ended;
- the financial statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with the National Lottery Act 1998 and directions made thereunder by the Secretary of State for Innovation, Universities and Skills, with the consent of HM Treasury; and
- the Directors' Report and Management Commentary, included within the Annual Report, is consistent with the financial statements.

## Opinion on Regularity

In my opinion, in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

## Report

I have no observations to make on these financial statements.

**Amyas C E Morse**

Comptroller and Auditor General

**National Audit Office**

151 Buckingham Palace Road

Victoria

London

SW1W 9SS

**11 July 2009**

# Group Income and Expenditure Account

For the year ended 31 March 2009

	Notes	Total 2009 £'000	Restated Total 2008 £'000
<b>Income</b>			
Investment income: Gilts	4	13,564	13,519
Investment income: Other	4	737	733
Lottery funding		15,000	15,000
Other income	5	668	666
<b>Total income</b>		<b>29,969</b>	<b>29,918</b>
<b>Less expenditure</b>			
Innovation Programmes	7	11,798	9,235
NESTA Investments	7	3,309	1,963
Policy & Research	7	3,580	3,679
Communications, events and publications	7	4,390	3,845
<b>Direct support of objectives</b>		<b>23,077</b>	<b>18,722</b>
Corporate Services	7	2,419	2,710
<b>Total expenditure</b>		<b>25,496</b>	<b>21,432</b>
Less Notional cost of capital		(2)	(3)
<b>Net surplus after notional costs</b>		<b>4,471</b>	<b>8,483</b>
Reversal of notional costs		2	3
<b>Surplus for the year</b>	2, 3a	<b>4,473</b>	<b>8,486</b>

Refer to Notes 2 and 3a for details on the restatement of the 2008 Income & Expenditure Account.

The Group has no recognised gains or losses other than those shown above and therefore no separate statement of total recognised gains and losses has been presented.

All of the Group's activities derived from continuing operations.

The notes on pages 27 to 57 form an integral part of these financial statements.

# Group Balance Sheet

At 31 March 2009

	Notes	Group 2009 £'000	Parent 2009 £'000	Restated 2008
<b>Fixed assets</b>				
Tangible fixed assets	8a	2,312	2,312	2,795
Intangible fixed assets	8b	92	92	108
<b>Financial assets:</b>				
Gilts	9a	265,708	265,708	202,551
Other investments	9a	39,608	39,608	20,705
Investment in early-stage companies	9b	8,780	8,780	8,018
Loans	9b	722	722	923
Investment in funds	9b	1,075	1,075	328
Deferred investment in companies	9b	651	651	868
Deferred investment in funds	9b	6,328	6,328	6,505
Investment in subsidiaries	10	-	120	-
		<b>325,276</b>	<b>325,396</b>	<b>242,801</b>
<b>Current assets</b>				
Debtors	11	345	344	246
Financial assets: short term deposits	9a	21,153	21,153	98,076
Cash on hand and in bank	21	234	121	329
		<b>21,732</b>	<b>21,618</b>	<b>98,651</b>
<b>Less current liabilities</b>				
Creditors: grants and investments falling due for payment within one year	12	6,063	6,063	7,633
Creditors: other amounts falling due within one year	13	3,751	3,739	2,607
		<b>9,814</b>	<b>9,802</b>	<b>10,240</b>
<b>Net current assets</b>		<b>11,918</b>	<b>11,816</b>	<b>88,411</b>
<b>Total assets less current liabilities</b>		<b>337,194</b>	<b>337,212</b>	<b>331,212</b>
Creditors: grants and investments falling due for payment after one year	12	6,584	6,584	5,871
<b>Net assets</b>		<b>330,610</b>	<b>330,628</b>	<b>325,341</b>

	Notes	Group 2009 £'000	Parent 2009 £'000	Restated 2008
<b>Represented by reserves</b>				
Fair value reserve	16	8,330	8,330	7,534
Accumulated reserve	16	322,280	322,298	317,807
<b>Total reserves</b>		<b>330,610</b>	<b>330,628</b>	<b>325,341</b>

The financial statements, which comprise the income and expenditure account, the balance sheet, the cash flow statement, and the related notes, were approved by the Board of Trustees on 1 July 2009 and signed on their behalf by:

**Jonathan Kestenbaum**  
Accounting Officer

**6 July 2009**

The notes on pages 27 to 57 form an integral part of these financial statements.

# Group Cash Flow Statement

For the year ended 31 March 2009

	Notes	Total 2009 £'000	Restated Total 2008 £'000
<b>Net cash outflow from operating activities</b>			
Payments of grants		(6,005)	(5,129)
Payments for staff and trustees' costs		(6,958)	(6,786)
Payments for other costs*		(11,056)	(7,688)
Project funding received		997	65
Lottery funding		15,000	15,000
Other income		557	548
	20	<b>(7,465)</b>	<b>(3,990)</b>
<b>Returns on investments</b>			
<b>Interest and dividends received</b>		<b>13,462</b>	<b>16,572</b>
<b>Capital expenditure and financial investment</b>			
Payments to acquire tangible and intangible fixed assets		(275)	(269)
Payments to acquire gilt investments		(104,996)	-
Proceeds from sale or maturity of gilt investments		51,230	78,472
Payments to acquire other investments		(25,590)	(445)
Payments for investments in early-stage companies		(2,565)	(2,285)
Payments for investments in loans		(335)	-
Payments for investments in funds		(920)	(328)
Proceeds from sale of investments in companies		358	-
Proceeds from repayment of loans		78	-
		<b>(83,015)</b>	<b>75,145</b>
<b>Increase/(decrease) in cash in hand and cash held as financial assets</b>	21a	<b>(77,018)</b>	<b>87,727</b>

\*Other costs include direct programme costs (programme delivery, mentoring, evaluation), event and publication costs, research costs, and operating costs (including rent, services charges, rates, irrecoverable VAT).

The notes on pages 27 to 57 form an integral part of these financial statements.

# Notes to the Accounts

For the year ended 31 March 2009

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## 1. Accounting policies

### Accounting convention

The financial statements are prepared under the historical cost convention, modified by the revaluation of available-for-sale financial assets and where relevant, the revaluation of tangible fixed assets by reference to current costs at the balance sheet date.

The financial statements have been prepared in accordance with the Accounts Direction issued by the Secretary of State for Culture, Media and Sport (August 2002) with the consent of Treasury in accordance with Section 23 (2) of the National Lottery Act 1998, and so far as appropriate they meet the requirements of the Companies Act, Managing Public Money and the Standards issued and adopted by the Accounting Standards Board.

In accordance with Treasury guidance, the group financial statements have been prepared in accordance with UK GAAP Financial Reporting Standards 25, 26 and 29 (*Financial Instruments: Disclosure & Presentation, Recognition & Measurement, and Disclosures* respectively). These reporting standards are adopted for the first time in the 2008/09 year in preparation for the transition to international financial reporting standards from 2009/10.

### Basis of consolidation

The group financial statements consolidate the financial statements of the National Endowment for Science, Technology and the Arts and all its subsidiary undertakings drawn up to 31 March 2009. There were no subsidiary undertakings in 2008.

On 16 June 2008, NESTA incorporated three legal entities in which to support early-stage companies: NESTA Investment Management LLP, NESTA Partners Ltd, NESTA Kinetique LLP.

NESTA and NESTA Partners Ltd are joint members in NESTA Investment Management LLP. NESTA Investment Management LLP and NESTA Partners Ltd are joint members of NESTA Kinetique LLP. NESTA Investment Management LLP is regulated by the Financial Services Authority and provides fund management services. NESTA Kinetique LLP is the general partner and manager of the Kinetique Biomedical Seed Fund, an external seed fund.

### Income

Income is accounted for on a receivable basis in the year to which it relates.

Investment income includes interest, dividends and realised capital gains or losses from investment financial assets.

Income from gilt investments is the gross interest receivable plus or minus the amortisation of any discount or premium to nominal (redemption) value. The amortisation is calculated on a straight-line basis over the remaining duration of the bond. Where gilts are sold prior to maturity date, any unamortised discount or premium is included in the income statement at the date of sale.

Fluctuations in the fair value of investments are recognised as a charge to equity through the fair value reserve.

Other income comprises royalties received, capital gain on sale of investments in early-stage companies, project funding and sundry other income.

# Notes to the Accounts

For the year ended 31 March 2009

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## Grants expenditure

Grants made by NESTA are recognised in full in the Income and Expenditure Account and Balance Sheet on the date when a binding contract is signed or equivalent obligation created, even if conditional upon future events. Commitments or approvals to fund specific projects not yet contracted (soft commitments) are disclosed by way of note.

## Other expenditure

Other expenditure is recognised when services or goods are received.

Overhead and fixed costs are allocated to each area of programme activity according to a relevant apportionment basis (percentage of total cost, head count, or floor space).

## Financial assets

Under FRS 25 and 26, NESTA classifies all its investments in the category 'available-for-sale' financial assets. The classification reflects the purpose for which the investments were made. Management determines the classification of its investments at initial recognition and will re-evaluate this classification at every reporting date.

Under FRS 26, the carrying value of all investments is at fair value and changes in fair value between accounting periods are charged or credited to equity. For financial assets for which there is no quoted market, fair value is established by using valuation guidelines as detailed below.

Short-term deposits which are held with external investors are presented in the balance sheet as current assets. All other financial assets are presented as fixed assets.

### Available-for-sale financial assets

Available-for-sale financial assets are non-derivative investments that are neither held-for-trading (ie not acquired principally for the purpose of selling in the short term) nor held-to-maturity investments. These financial assets are represented in the balance sheet as: gilts, other investments, investments in early-stage companies, loans, and investments in funds.

Deferred investment in companies and funds represents that portion of NESTA's commitment which remains undrawn at the balance sheet date. The corresponding outstanding commitment is recognised under current or non-current liabilities.

Loans are provided to certain early-stage companies and are recognised as financial assets when repayment of the loan or the option to convert to equity has not expired at the balance sheet date. The loans are included in fixed assets except where repayment is expected within 12 months after the balance sheet date, when they are included as current assets.

### Valuation

The fair values of quoted investments are based on externally reported bid prices at the Balance Sheet date.

The fair value of unquoted investments in early-stage companies is established by using valuation guidelines produced by the British Venture Capital Association (BVCA).

- BVCA guidelines provide for investments to be carried at cost unless there is information indicating an impairment or sufficiently clear evidence to support an increase in valuation. However, in practice NESTA Investments recognises an uplift in estimated value only if there is significant investment from an institutional third-party investor after the first round.
- Where the price of a recent funding round (within previous 12 months) is not available, investments are valued using standard valuation methodologies, as appropriate and in the following order:
  - a. Earnings multiple
  - b. Net asset value
  - c. Discounted cash flow
  - d. Applying BVCA valuation benchmarks
- At each balance sheet date management assesses whether there is objective evidence that a financial asset or a group of financial assets should be revalued. Each investment is reviewed and given a 'health' status:
  - Healthy: value held at cost unless sufficiently clear evidence to support an increase in valuation (for NESTA, only where there is a significant investment from an institutional third-party investor after the first round); company is performing to plan, unlikely to run out of cash within 12 months.
  - Sick: 25-75 per cent value down according to the seriousness of a number of events considered by management; company is performing off-plan, may or may not be recoverable.
  - Terminal – 100 per cent value down, company is performing off-plan, likely to run out of cash within six months, recovery not foreseen, no intervention planned.

Valuation of companies at this early stage of development is an inherently volatile and uncertain process. The valuation guidelines used take a conservative approach and are unlikely to represent the true value of some of the companies with significant potential but are considered to be the best estimate.

Transaction costs incurred by NESTA or management support costs are not included in valuations. They are charged to expenditure in the period in which they are incurred.

Loans to early-stage companies have the same valuation methodology applied as for investments in early-stage companies.

The fair value of investments in funds is valued as NESTA's share of partnership net asset value as stated in the last audited financial statements of each investment fund. Contributions made by NESTA in any period between the date of a fund balance date and NESTA's own balance date for which there is no audited valuation, is valued at cost unless there is information to determine otherwise.

#### Treatment

Investments, loans or contributions to funds are recognised in full in the Balance Sheet on the date when a binding contract is signed or equivalent obligation created, even if conditional upon future events. Undrawn commitments at the date of reporting are recorded as financial assets, either as deferred investments, loans or investment in funds, with a corresponding liability. Commitments or approvals to invest, loan or contribute to funds not yet contracted (soft commitments) are disclosed by way of note.

Unrealised changes in value between accounting periods are charged to equity via a fair value reserve.

When financial assets are sold or derecognised, any fair value adjustments are reversed and reflected in income and expenditure within any capital gains and losses. Financial assets are derecognised when the rights to receive cash flows from the investments have expired or have been transferred with all risks and rewards of ownership.

# Notes to the Accounts

For the year ended 31 March 2009

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Unquoted investments in early-stage companies which have a health status of 'terminal' are treated as impaired and the cost of the impairment charged to the Income & Expenditure Account after a reversal of cumulative fair value adjustments. Any valuation showing a return to an improved health status is credited back to the balance sheet at fair value, through the fair value reserve and not through the income and expenditure account, in accordance with FRS 26.

## Tangible and intangible fixed assets

Tangible and intangible fixed assets are capitalised in the balance sheet at their historic cost and, where necessary, because of materiality, revalued annually by reference to indices published by the Office of National Statistics.

Tangible fixed assets costing less than £500 are written off in the year of purchase.

## Depreciation

Depreciation is provided on all tangible fixed assets. Depreciation is calculated on a straight line basis over the expected useful life of the assets as follows:

- Leasehold improvements – over the life of the lease remaining
- All other assets – three to five years

## Taxation

The National Lottery Act 1998 provides for NESTA to be exempt from tax under the Income and Corporation Taxes Act 1988. HMRC has recognised this exemption. Accordingly, no taxation has been provided for in these financial statements.

## Value Added Tax

Income and Expenditure is recorded net of VAT. Irrecoverable VAT is treated as a separate expenditure item, which, as with all costs applicable to the whole organisation, has been apportioned across the main areas of NESTA activity.

## Pensions

The costs of all employer pension contributions are charged to the Income & Expenditure Account. Certain employees are members of a defined benefit pension scheme. Any known underlying asset or liability is accounted for. Where NESTA is unable to identify its share of the underlying assets and liabilities in a defined benefit scheme, it will be accounted for as if it were a defined contribution scheme in accordance with FRS 17: Retirement Benefits. Refer also to Note 19.

## Operating leases

Rentals payable under operating leases are charged to the Income & Expenditure account on a straight line basis over the term of the lease. Other costs incurred under operating leases are taken into the Income and Expenditure account in the period to which they relate.

## Notional cost of capital

Notional cost of capital employed by NESTA is calculated as 3.5 per cent (2008: 3.5 per cent) of the average non-lottery funded balances employed over the financial year.

## 2. Changes in accounting policy

### Financial assets

The new financial reporting standards have a material impact on the Income & Expenditure Account, Balance Sheet, and the Statement of Cash Flows. The primary changes are as follows:

For all preceding years up to and including 31 March 2008:

- Seed and early-stage investments were charged to programme expenditure and were not capitalised.
- Investments (gilt and other) were recognised in the balance sheet at market (fair) value and fluctuations in market value were charged to income.

The comparative figures in respect of the 31 March 2008 year have been restated to reflect the adjustments required in adopting FRS 25, 26 and 29 and reconciliations and descriptions of the effect of the transition to the financial instrument standards are provided in Notes 3A and 3B.

### Endowment policy

Up to 31 March 2008, NESTA was required by its Financial Directions to maintain a capital element of the Endowment which was non-expendable. Any surplus was available to be drawn down to fund NESTA's ongoing activities. On 1 April 2008, NESTA's Financial Directions were amended to remove this requirement. As a result, NESTA's financial assets at 31 March 2008 have been restated. Cash and short-term deposits are presented as current assets, with all other assets presented as fixed assets.

# Notes to the Accounts

For the year ended 31 March 2009

## 3. Transition statements

### 3a. Restated Income & Expenditure Account

The restated 2008 Income & Expenditure Account surplus of £8,486k reflects a net increase of £4,483k on the originally published 2008 surplus of £4,003. This increase reflects two significant adjustments made to 2008 as if the adoption of FRS 25, 26 and 29 had been applied that year in order to provide a relevant comparison to 2009.

	£'000	2008 £'000
Reported surplus 31 March 2008		4,003
Reversal of 2008 unrealised gains, transferred to fair value reserve	(5,656)	
Reversal of 2008 investment expenditure, transferred to the balance sheet	10,139	4,483
<b>Restated surplus 1 April 2008</b>		<b>8,486</b>

The following shows the adjustments made by the Group in restating its previously published Income and Expenditure Account for the year ending 31st March 2008.

Reconciliation of Income & Expenditure For the year ended 31st March 2008	Notes	31 March 2008	Effect of Transition to FRS 26, 29 £'000	Restated 1 April 2008 £'000
<b>Income</b>				
Investment returns: Gilts		13,519		13,519
Adjustment to market value	(a)	8,250	(8,250)	-
		<b>21,769</b>	<b>(8,250)</b>	<b>13,519</b>
Investment returns: Other	(a)	(1,861)	2,594	733
Lottery funding		15,000		15,000
Other income		666		666
<b>Total income</b>		<b>35,574</b>	<b>(5,656)</b>	<b>29,918</b>

Reconciliation of Income & Expenditure For the year ended 31st March 2008	Notes	31 March 2008	Effect of Transition to FRS 26, 29 £'000	Restated 1 April 2008 £'000
<b>Less expenditure</b>				
Innovation Programmes		9,235		9,235
NESTA Investments	(b)	12,102	(10,139)	1,963
Policy & Research		3,679		3,679
Communications, events and publications		3,845		3,845
<b>Direct support of objectives</b>		<b>28,861</b>		<b>18,722</b>
Corporate Services		2,710		2,710
<b>Total expenditure</b>		<b>31,571</b>	<b>(10,139)</b>	<b>21,432</b>
Less notional cost of capital		(3)		(3)
<b>Net surplus after notional costs</b>		<b>4,000</b>	<b>4,483</b>	<b>8,483</b>
Reversal of notional costs		3		3
<b>Surplus for the year</b>		<b>4,003</b>	<b>4,483</b>	<b>8,486</b>

**(a) Unrealised gains:**

Prior to the adoption of FRS 26 all fluctuations in fair value of gilts and other investments were included as investment income. The investments which generated this income were recognised in the balance sheet at fair value (market value). Under FRS 26 the carrying value of all investments remains at fair value with changes in fair value between accounting periods credited to a Fair Value Reserve. This transition statement shows the effect on the 2007/08 year only. In that year, a net £5,656k of unrealised gains (fair value movement) is transferred to the fair value reserve. The cumulative transfer for all years is £6,770k of unrealised gains – refer also to Note 3(e).

**(b) Investment expenditure:**

Prior to the adoption of FRS 26, all investments in seed and early-stage companies, investment funds and loans were charged to programme expenditure and not capitalised. Under FRS 26 these investments are recognised as financial assets in the balance sheet and measured at fair value. These are now recognised as financial assets in the balance sheet at fair value as either: investment in companies, loans, investment in funds, deferred investment in companies, or deferred investment in funds. In 2007/08, £10.1 million was invested or committed to early-stage companies, loans or investment funds. The cumulative transfer for all years is £16,185k. Refer to Note 3(e).

# Notes to the Accounts

For the year ended 31 March 2009

## 3b. Restated Balance Sheet

The following shows the adjustments made by the Group in restating its previously published Balance Sheet as at 31 March 2008. The adjustments comprise the changes required for the transition to FRS 26 and 29 and the change in the Endowment Policy.

Balance Sheet reconciliation	Notes	31 March 2008 £'000	Adjustments £'000	Restated 1 April 2008 £'000
<b>Fixed assets</b>				
Tangible fixed assets		2,795		2,795
Intangible fixed assets		108		108
Financial assets:				
Gilts		250,000	(47,449)	202,551
Other investments			20,705	20,705
Investment in companies	(c)		8,018	8,018
Loans	(c)		923	923
Investment in funds	(c)		328	328
Deferred investment in companies	(c)		868	868
Deferred investment in funds	(c)		6,505	6,505
		<b>252,903</b>	<b>(10,102)</b>	<b>242,801</b>
<b>Current assets</b>				
Financial assets:				
Gilts		50,174	(50,174)	-
Other investments		21,158	(21,158)	-
Short term deposits		-	98,076	98,076
Debtors		246		246
Cash on hand and in bank		329	-	329
		<b>71,907</b>	<b>26,744</b>	<b>98,651</b>

Balance Sheet reconciliation As at 31st March 2008	Notes	31 March 2008 £'000	Adjustments £'000	Restated 1 April 2008 £'000
<b>Less current liabilities</b>				
Creditors: grants and investments falling due for payment within one year		7,633		7,633
Creditors: other amounts falling due within one year		2,607		2,607
		<b>10,240</b>	-	<b>10,240</b>
<b>Net current assets</b>		<b>61,667</b>	<b>26,744</b>	<b>88,411</b>
<b>Total assets less current liabilities</b>				
Creditors: grants and investments falling due for payment after one year	(c)	6,178	(307)	5,871
<b>Net assets</b>		<b>308,392</b>	<b>16,949</b>	<b>325,341</b>
<b>Represented by reserves</b>				
Fair value reserve	(d)	-	7,534	7,534
Accumulated reserve	(e)	308,392	9,415	317,807
<b>Total reserves</b>		<b>308,392</b>	<b>16,949</b>	<b>325,341</b>

**(c) Financial assets:**

Prior to the adoption of FRS 26, all investments in seed and early-stage companies, loans and investment funds were treated as programme expenditure and not capitalised. Under FRS 26 these investments are recognised as financial assets in the balance sheet and measured at fair value, and classified as either: investment in companies, loans, investment in funds, deferred investment in companies or deferred investment in funds. The transition adjustments recognise the portfolio of investment in companies, funds and loans that are actively managed by the NESTA Investments team.

The deferred investments have a corresponding financial liability.

**(d) Fair value reserve:**

This fair value reserve reflects cumulative unrealised gains and losses to 31 March 2008. They arise from two main groups of financial assets: investments (including gilts and other investments) £6,770k (of which £5,656k relates to the 2007/08 year); investments in companies £764k.

**(e) Accumulated reserve:**

The addition to the Accumulated Reserve reflects the cumulative net transfer out of Income & Expenditure, to the Balance Sheet or Fair Value Reserve:

	£'000	As at 1/4/08 £'000
Reversal from Income, transferred to Fair Value Reserve:		
Cumulative unrealised gains in gilt investments	(4,762)	
Cumulative unrealised gains in other investments	(2,008)	(6,770)
Reversal from Expenditure, transferred to the Balance Sheet:		
Investment in early-stage companies expenditure	7,254	
Investment in loans expenditure	923	
Investment in funds – paid or committed	7,140	
Investment in companies – not paid but committed	868	16,185
<b>Increase to Accumulated Reserve at 1 April 2008</b>		<b>9,415</b>

# Notes to the Accounts

For the year ended 31 March 2009

## 4. Investment income

	2009 £'000	2008 £'000
Gilts:		
Gross interest receivable	14,177	14,945
Amortisation of redemption premium	(891)	(1,426)
Realised gains on sale of gilts	278	-
Total income from gilts	13,564	13,519
Other investments:		
Interest and dividends receivable	708	691
Bank interest	29	42
Total income from other investments	737	733
<b>Total investment income</b>	<b>14,301</b>	<b>14,252</b>

### Gilts:

NESTA has applied an investment policy of buying government gilts and holding them long-term, often to maturity. Such gilts have been purchased at a (premium)/discount to nominal value. This inevitably gives rise to a capital (loss)/profit on redemption, compensated for by higher/(lower) interest income. NESTA's policy is to amortise this (premium)/discount on a straight line basis over the remaining life of the bond.

A realised gain of £278k (2008: £nil) was made on sale of expiring gilts to effect a purchase of longer-term gilts.

### Other investments:

There were no realised capital gains or losses (2008: £0).

## 5. Other income

	2009 £'000	2008 £'000
Project Funding:		
Cabinet Office	45	-
Scottish Arts Council	10	-
South East England Development Agency	100	-
Engineering and Physical Sciences Research Council	2	-
Institute of Physics	4	-
Virgin Atlantic	24	-
One North East RDA	-	40
Highlands and Islands Enterprise Funding	-	11
European Project funding: Early Stage Investors for High Growth Businesses	37	-
Royalty income, loan repayment, interest and dividends from legacy awards	250	42
Realised gain on sale of company in investment portfolio	133	-
Sale of company in investment portfolio	-	428
Other income	63	145
<b>Total other income</b>	<b>668</b>	<b>666</b>

Project Funding is substantially matched against expenditure.

Other income includes amounts received from the provision of services and recharges of expenses.

Loan repayments relate to legacy loans granted which were expensed to programme expenditure in prior years and were not transferred to the balance sheet as a financial asset.

# Notes to the Accounts

For the year ended 31 March 2009

## 6. Staff costs

	2009 £'000	2008 £'000
Salaries and emoluments of directly recruited staff	4,616	5,051
Salaries and allowances of seconded staff	226	133
Trustees' and committee members' remuneration	83	54
Social security costs	617	581
Defined contribution pension payments	385	396
Defined benefit pension payments	21	48
Agency/temporary staff costs	219	159
	<b>6,167</b>	<b>6,422</b>
Other staff costs	792	447
<b>Total Staff Costs</b>	<b>6,959</b>	<b>6,869</b>

Further information on pensions is included in Note 19 and in the Remuneration Report.

Other staff costs include recruitment costs, end of service costs, and staff training costs.

Interest-free season ticket loans were available to all NESTA staff during the year. As at 31 March 2009, eighteen staff had taken up these loans. The value in aggregate of season ticket loans in excess of £2,500 is £nil.

The full time equivalent number of persons employed during the year was as follows:

	Employees 2009	Agency/ contract staff 2009	Secondees 2009	Total 2009	Total 2008
Innovation Programmes	26	2	1	29	32
NESTA Investments	10	-	-	10	11
Policy & Research	10	-	1	11	12
Communications	15	2	-	17	17
Corporate Services/CEO & Trustees Office	21	-	-	21	24
	<b>82</b>	<b>4</b>	<b>2</b>	<b>88</b>	<b>96</b>

## 7. Expenditure

### 7a. Expenditure by activity

Expenditure has been classified by activity: programmes, investment management, policy & research, communications, and corporate services.

Programmes and activities now closed (for example our Invention and Innovation programme) are included within the appropriate activity for the purposes of comparison.

### Innovation Programmes

NESTA's Innovation Programmes focus on people's capacity for innovation – finding the best ways to stimulate curiosity, creativity, inventiveness and enterprise.

Total expenditure for the year on continuing activities was £11,798k (2008: £9,235k).

### NESTA Investments

NESTA Investments supports start-up companies and seed stage funds, either as a limited partner or co-investor, and aims to demonstrate that a commercial return is possible in early-stage investment. They also provide non-financial support (e.g. mentoring and management or board expertise) to our portfolio of growing high-tech businesses. NESTA Investments operates through two arms: NESTA Ventures and NESTA Capital.

See Note 9b for details of active investments held.

Group total expenditure for the year on continuing activities was £3,309k including subsidiary expenditure of £18k for the year (2008: £1,963k). Group expenditure includes a charge of £1,098k (2008: £nil) for impaired investments in early-stage companies at cost.

In addition, direct investments made in companies or funds for the year totalled £3,820k. These are treated as financial assets in the balance sheet. Refer to 9b for further details.

### Policy & Research

NESTA's Policy & Research team aims to shape innovation policies that will help the UK meet national innovation challenges of the 21st century. They use their expert knowledge to influence government and regulatory policy, and consider how policy might support the work of our investment and programme teams.

Total expenditure for the year on continuing activities was £3,580k (2008: £3,679k).

### Communications, events and publications

NESTA's communications, events and publications team supports and works closely with the organisation's external-facing activities. This includes corporate affairs, media and public affairs, high-level events, branding, publications, websites, competitions, and sponsorships.

Total expenditure for the year on continuing activities was £4,390k (2008: £3,845k).

# Notes to the Accounts

For the year ended 31 March 2009

## Corporate Services

Corporate Services includes finance, human resources, information technology, facilities management and legal.

Total expenditure for the year on continuing activities was £2,419k (2008: £2,710k).

### 7b. Expenditure by type

	2009 £'000	2008 £'000
Grants and projects	12,400	9,614
Staff costs	6,959	6,869
Depreciation	662	656
Loss on disposal of assets	21	32
Impairment of investments in early-stage companies	1,098	-
Legal and audit fees	165	316
Operating leases: land and buildings, photocopiers	814	851
Irrecoverable VAT	1,460	988
Other operating costs	1,917	2,106
<b>Total continuing and non-exceptional costs</b>	<b>25,496</b>	<b>21,432</b>
<b>Total expenditure</b>	<b>25,496</b>	<b>21,432</b>

Grants and projects are external costs relating to all activity directly supporting the core mission, including research projects, seminars, publications, investee and recipient training, mentoring, events, dissemination, training academies and grant activities.

Staff costs include salaries, National Insurance, pension and benefit contributions and other staff-related costs such as temporary and contract staff, training and development expenditure, end of service and recruitment costs.

Other operating costs include all centrally administered costs, principally ICT and facilities costs (excluding rent and service charges which are disclosed separately). It also includes other costs not centrally administered, principally travel and entertaining, consulting and other professional fees.

## 7c. Further information

<b>Net surplus is stated after charging:</b>	<b>2009 £'000</b>	<b>2008 £'000</b>
Auditor's remuneration – National Audit Office statutory audit services	37	29
– IFRS review, other services	4	1
Auditor's remuneration – Audit of subsidiaries	8	-
– Non-audit services	1	-
Staff travel, subsistence and hospitality	197	366
Trustee travel and subsistence	16	24

## 8a. Tangible Fixed Assets

<b>Group &amp; Parent</b>	<b>Leasehold improvement £'000</b>	<b>Computer hardware £'000</b>	<b>Office equipment £'000</b>	<b>Fixtures &amp; fittings £'000</b>	<b>Total £'000</b>
<b>Cost or valuation</b>					
At 1 April 2008	2,405	695	219	374	3,693
Additions	6	121	-	8	135
Disposals	-	(13)	-	(18)	(31)
Transfers in/(out)	-	-	-	(1)	(1)
<b>At 31 March 2009</b>	<b>2,411</b>	<b>803</b>	<b>219</b>	<b>363</b>	<b>3,796</b>
<b>Depreciation</b>					
At 1 April 2008	338	330	133	97	898
Charge for the year	251	216	52	75	594
Disposals in year	-	-	-	(8)	(8)
<b>At 31 March 2009</b>	<b>589</b>	<b>546</b>	<b>185</b>	<b>164</b>	<b>1,484</b>
<b>Net Book Value</b>					
<b>At 31 March 2009</b>	<b>1,822</b>	<b>257</b>	<b>34</b>	<b>199</b>	<b>2,312</b>
At 31 March 2008	2,067	365	86	277	2,795

Assets have not been revalued at 31 March 2009 as their current cost does not differ materially from the historic cost. There is no material difference between the net book values of assets on a current cost and on an historic cost basis.

# Notes to the Accounts

For the year ended 31 March 2009

## 8b. Intangible Fixed Assets

<b>Group and Parent</b>	<b>Computer software £'000</b>	<b>Total £'000</b>
<b>Cost or valuation</b>		
At 1 April 2008	1,191	1,191
Additions	67	67
Transfers in/(out)	(21)	(21)
<b>At 31 March 2009</b>	<b>1,237</b>	<b>1,237</b>
<b>Depreciation</b>		
At 1 April 2008	1,083	1,083
Charge for the year	68	68
Transfers in/(out)	(6)	(6)
<b>At 31 March 2009</b>	<b>1,145</b>	<b>1,145</b>
<b>Net Book Value at 31 March 2009</b>	<b>92</b>	<b>92</b>
Net Book Value At 31 March 2008	108	108

## 9a. Investments

NESTA invests in government gilts and deposits held with the Commissioners for the Reduction of The National Debt in the UK. Other investments in equities, property funds and bonds are held separately with commercial investment managers. Other than short-term deposit investments, all investments are shown as fixed assets.

	Group and Parent		Group and Parent	
	Cost	Market value	Cost	Market value
	2009	2009	2008	2008
	£'000	£'000	£'000	£'000
Cash and short-term deposits	20,207	20,212	97,313	97,623
Government Stocks – up to one year	-	-	48,939	50,737
Government Stocks – two to five years	144,769	156,532	147,107	151,814
Government Stocks – over five years	104,827	109,176	-	-
<b>Total gilts</b>	<b>269,803</b>	<b>285,920</b>	<b>293,359</b>	<b>300,174</b>
Cash and short-term deposits	941	941	453	453
UK equities	14,479	11,174	14,010	14,871
Property funds	4,650	3,903	4,650	5,834
Bonds	25,000	24,531	-	-
<b>Total other investments</b>	<b>45,070</b>	<b>40,549</b>	<b>19,113</b>	<b>21,158</b>
<b>Total gilt and other investments</b>	<b>314,873</b>	<b>326,469</b>	<b>312,472</b>	<b>321,332</b>
<b>Represented in the Balance Sheet as:</b>		<b>Group and Parent</b>		<b>Group and Parent</b>
		<b>Market value 2009</b>		<b>Market value 2008</b>
		<b>£'000</b>		<b>£'000</b>
Fixed asset – financial asset, gilts		265,708		202,551
Fixed asset – financial asset, other investments		39,608		20,705
Current assets – financial asset, short-term deposits		21,153		98,076
		<b>326,469</b>		<b>321,332</b>

# Notes to the Accounts

For the year ended 31 March 2009

## 9b. Investments in seed and early-stage companies and funds

NESTA Investments has made equity, participating or convertible loan or quasi-equity investments in a portfolio of early-stage, start-up companies, and made contributions to early-stage investment funds.

During the year 19 investments were made into new and existing portfolio companies at a total cost of £2.9m and five contributions were made to investment funds at a total cost of £920k.

A summary of the portfolio of investments held at 31st March 2009 is set out below:

### i. Investments in early-stage companies – cost

Company	Cash investment to 31 March 2009 £'000	Cash investment to 31 March 2009 £'000	Cash investment to 31 March 2009 £'000		
Light Blue Optics Ltd	658	Meciria Ltd	372	Scyron Ltd	200
Tideway Systems Ltd	500	Haemostatix Ltd	367	Cardiak Ltd	196
MMIC Solutions Ltd	500	Camrivox Ltd	320	Smart Surgical Appliances	190
Dexela Limited	500	OSsray Ltd	300	Plasma Clean Ltd	185
Cellcentric Ltd	500	Surface Generation Ltd	250	Orthogem Ltd	174
Veryan Medical Ltd	431	Gnodal Ltd	250	Cytox Ltd	150
Quotient Diagnostics Ltd	416	Advanced Transport Systems Ltd	250	Spiral Gateway Ltd	145
Starbridge Systems Ltd	406	Micrima Ltd	248	Thermal Energy Systems Ltd	125
ProVision Communication Technologies Ltd	405	Hypertag Ltd	238	Dialog Devices Ltd	125
AquaPharm Bio-Discovery Ltd	400	ProKyma Technologies Ltd	235	Odontis Ltd	110
Ashe Morris Ltd	375	St Andrews Fuel Cells Ltd	219	ROBAT Ltd	105
Symetrica Ltd	374	Probe Scientific Ltd	211	Six To Start Ltd	100
				Bluegnome Ltd	100
				Investments over £100k	10,630
				Other investments of less than £100k	726
				<b>Total investment at cost</b>	<b>11,356</b>
				<b>Number of companies invested in</b>	<b>50</b>

Using valuation guidelines produced by the British Venture Capital Association (BVCA) and in line with best practice, NESTA estimates the value of this portfolio to be £9,502k as at 31 March 2009 comprising equity investments at £8,780k and convertible loans at £722k. These are represented in the balance sheet as financial assets and are made up as follows:

<b>Investments in early-stage companies – fair value</b>	<b>Investment in companies 2009 £'000</b>	<b>Convertible loans 2009 £'000</b>	<b>Total 2009 £'000</b>
At 1 April 2008	8,018	923	8,941
Additions	2,565	335	2,900
Conversion	250	(250)	-
Repayments	-	(78)	(78)
Sales	(225)	-	(225)
Impairment	(1,018)	(80)	(1,098)
Fair value movement – gain/(loss)	(810)	(128)	(938)
<b>Total investment at fair value represented in the Balance Sheet</b>	<b>8,780</b>	<b>722</b>	<b>9,502</b>

At balance sheet date NESTA had deferred investments in early-stage companies totalling £651k (2008: £868k). These represent commitments made by NESTA but are undrawn at 31 March 2009.

BVCA guidelines provide for investments to be carried at cost unless there is information indicating an impairment or sufficient evidence to support an increase in valuation. However, in practice NESTA Investments includes in its estimated value an uplift in valuation only if there is significant investment from an institutional third-party investor after the first round.

It should be noted that the majority of the companies are not at a stage of generating significant earnings or in many cases even revenues. Valuation of companies at this early stage of development is an inherently volatile and uncertain process. The valuation guidelines used take a conservative approach and are unlikely to represent the true value of some of the companies with significant potential but are considered to be the best estimate.

Transaction costs incurred by NESTA or management support costs are not included in valuations.

<b>ii. Investment in funds – cost</b>	<b>Cash investment 2009 £'000</b>	<b>Deferred investment in funds 2009 £'000</b>
Pentech Fund II	269	2,731
IP Venture Fund	205	296
The UMIP Premier Fund	525	2,975
GP Bullhound Sidecar Ltd	174	326
Seedcamp	75	-
<b>Total investment at cost</b>	<b>1,248</b>	<b>6,328</b>

# Notes to the Accounts

For the year ended 31 March 2009

Deferred investment funds of £6,328k (2008: £6,505k) represent commitments made by NESTA to funds which are undrawn at balance sheet date.

<b>Investment in funds – fair value</b>	<b>Fair Value 2009 £'000</b>
At 1 April 2008	328
Additions	920
Fair value movement – gain/(loss)	(173)
<b>Total investment in funds at fair value 31 March 2009</b>	<b>1,075</b>

## 10. Investment in subsidiaries

During the year NESTA contributed £120k toward NESTA Investment Management LLP's Members' Capital.

On 16 June 2008, NESTA incorporated three legal entities in which to support early-stage companies: NESTA Investment Management LLP, NESTA Partners Ltd, NESTA Kinetique LLP. NESTA and NESTA Partners Ltd are joint members in NESTA Investment Management LLP. NESTA Investment Management LLP and NESTA Partners Ltd are joint members in NESTA Kinetique LLP. NESTA Investment Management LLP is regulated by the Financial Services Authority and provides fund management services. NESTA Kinetique LLP is the general partner and manager of the Kinetique Biomedical Seed Fund, an external seed fund of which King's College and Queen Mary College, London, are also limited partners.

Both NESTA Kinetique LLP and NESTA Partners Ltd have no trading activity for the year ended 31 March 2009 and have nil assets, liabilities and reserves. The trading results for NESTA Investment Management LLP are included in the Group results.

## 11. Debtors

	<b>Group 2009 £'000</b>	<b>Parent 2009 £'000</b>	<b>Group &amp; Parent 2008 £'000</b>
Trade debtors	34	114	144
Prepayments	104	104	95
Accrued income	174	174	-
Other debtors	33	33	15
Less provision for doubtful debts	-	(81)	(8)
<b>Total Debtors</b>	<b>345</b>	<b>344</b>	<b>246</b>

NESTA is owed £81k by its subsidiary, NESTA Investment Management LLP, for certain start-up costs and management services. This has been provided for as a doubtful debt as payment is contingent on NESTA Investment Management LLP generating sufficient profits to repay these amounts.

NESTA is required to disclose the value of any debtor balances with other bodies within the Whole of Government Accounts (WGA) boundary. At balance sheet date there were no material balances held with other WGA bodies.

## 12. Creditors: Grants and Investments

Contracted commitments	Group & Parent at 1 April 2008 £'000	New commitments £'000	Commitments paid £'000	De-commitments £'000	Group & Parent at 31 March 2009 £'000
Innovation Programmes	4,792	4,421	(5,182)	(195)	3,836
NESTA Investments	7,791	3,359	(3,911)	(164)	7,075
Policy & Research	1,228	1,377	(810)	(59)	1,736
<b>Total</b>	<b>13,811</b>	<b>9,157</b>	<b>(9,903)</b>	<b>(418)</b>	<b>12,647</b>

Payments under contracted commitments are expected to be made as follows:

	Within 1 year £'000	1 to 2 years £'000	2 to 3 years £'000	3 to 4 years £'000	4 to 5 years £'000	Total £'000
Innovation Programmes	2,876	609	351	-	-	3,836
NESTA Investments	2,451	2,312	2,312	-	-	7,075
Policy & Research	736	250	250	250	250	1,736
<b>Total</b>	<b>6,063</b>	<b>3,171</b>	<b>2,913</b>	<b>250</b>	<b>250</b>	<b>12,647</b>

Payments under contracted commitments are disclosed in the balance sheet as: due for payment within one year £6,063k; due for payment after one year £6,584k (2008: £7,633k and £5,871k respectively).

Grants committed or approved but not yet contracted are set out in Note 15.

# Notes to the Accounts

For the year ended 31 March 2009

## 13. Creditors: other amounts falling due within one year

	Group 2009 £'000	Parent 2009 £'000	Group & Parent 2008 £'000
Trade creditors	12	11	659
Taxation and social security	156	156	177
Other creditors	45	45	24
Accruals and deferred income	3,538	3,527	1,747
<b>Total Trade and other payables</b>	<b>3,751</b>	<b>3,739</b>	<b>2,607</b>

NESTA is required to disclose the value of any year-end creditor balances with other bodies within the Whole of Government Accounts (WGA) boundary. There were year-end balances held with the following organisations, inclusive of VAT:

	2009 £'000
Balances with government bodies	1,548
Balances with English local government bodies	30
Balances with National Health Service bodies	31
	<b>1,609</b>
Balances with bodies external to government	14,789
<b>Total Creditors and Grant and Investment Commitments</b>	<b>16,398</b>

## 14. Provisions and contingent liabilities

### Defined Benefit Pension:

Section 75 of the Pensions Act provides that a statutory debt may become due from an employer in a multi-employer final salary scheme if it ceases to employ any employees who are active members in the scheme. NESTA's membership of the PSATSITA pension scheme (see Note 19) may give rise to such a liability.

It is uncertain when such a liability will crystallise, and were it to do so, what the size of the liability would be. The next actuarial valuation of the pension fund is due for 31 March 2010 at which time NESTA can estimate its potential contingent liability. The last valuation completed for 31 March 2007 is not a reliable estimate of any future liability. At balance sheet date NESTA had one active member and 38 deferred members in the scheme.

### Dilapidations:

The lease agreement for the rental property at 1 Plough Place expires in 2021. Due to uncertainty in timing and amount, no estimate for a contingent liability for dilapidations has been made.

## 15. Grants and investments committed or approved but not yet contracted

Grants and investments committed or approved (soft commitments) are not treated as liabilities until contracted.

<b>Soft commitments</b>	<b>Group &amp; Parent at 1 April 2008 £'000</b>	<b>Approvals £'000</b>	<b>Contracted £'000</b>	<b>Cancelled/ Withdrawn £'000</b>	<b>Group &amp; Parent at 31 March 2009 £'000</b>
Innovation Programmes	2,062	3,788	(4,421)	(816)	613
NESTA Investments	1,239	3,650	(3,359)	(178)	1,352
Policy & Research	91	1,286	(1,377)	-	-
<b>Total</b>	<b>3,392</b>	<b>8,724</b>	<b>(9,157)</b>	<b>(994)</b>	<b>1,965</b>

Cancelled/withdrawn soft commitments vary from year to year (2008: £563k; 2007: £1,417). Many soft commitments do not reach the point of formal, contracted hard commitment. Common reasons include: the breaking down of contract negotiations where NESTA and the organisation do not agree final terms; the organisation accepting an offer from an alternative funding body; or the organisation not raising additional funds required to complete larger rounds of financing.

# Notes to the Accounts

For the year ended 31 March 2009

## 16. Reserves

Group	Notes	Accumulated Reserve £'000	Fair Value Reserve £'000	Group Total £'000
<b>Balance at 31 March 2008</b>		<b>308,392</b>	-	<b>308,392</b>
Adjustments for first time adoption of FRS 26, 29:				
Fair value gains/(losses) on 'available-for-sale' financial assets:				
Gilts	3(d)		4,762	4,762
Other investments	3(d)		2,008	2,008
Investments in early-stage companies	3(d)		764	764
Net reversal of expenditure from prior years	3(e)	9,415		9,415
<b>Balance at 1 April 2008</b>		<b>317,807</b>	<b>7,534</b>	<b>325,341</b>
Fair value gains/(losses) on 'available-for-sale' financial assets:				
Gilts			8,432	8,432
Other investments			(6,525)	(6,525)
Investments in early-stage companies			(810)	(810)
Loans			(128)	(128)
Investments in funds			(173)	(173)
Retained surplus for the year		4,473		4,473
<b>Balance at 31 March 2009 – Group</b>		<b>322,280</b>	<b>8,330</b>	<b>330,610</b>

Parent	Accumulated Reserve £'000	Fair Value Reserve £'000	Group Total £'000
<b>Balance at 1 April 2008</b>	<b>317,807</b>	<b>7,534</b>	<b>325,341</b>
Fair value gains/(losses) on 'available-for-sale' financial assets:			
Gilts		8,432	8,432
Other investments		(6,525)	(6,525)
Investments in early-stage companies		(810)	(810)
Loans		(128)	(128)
Investments in funds		(173)	(173)
Retained surplus for the year	4,491		4,491
<b>Balance at 31 March 2009 – Parent</b>	<b>322,298</b>	<b>8,330</b>	<b>330,628</b>

## 17. Capital commitments

There are no amounts committed or contracted in respect of capital expenditure at 31 March 2009 (2008: £59k).

## 18. Operating lease commitments

At 31 March 2009, NESTA had an annual commitment under operating leases as follows:

	Less than 1 year to expiry	1-5 years to expiry	More than 5 years to expiry	2009 £'000	2008 £'000
<b>Land and Buildings:</b>					
Plough Place, London			12 yrs 3 mths	709	709
Scotswood Road, Newcastle Upon Tyne				-	7
West Bute Street, Cardiff				-	6
Scion House, Stirling				-	10
<b>Other Leases:</b>					
Photocopiers		2 yrs		19	19
<b>Total</b>				<b>728</b>	<b>751</b>

In addition to the premises mentioned above, NESTA maintains a regional office in Dundee, on a short-term lease.

# Notes to the Accounts

For the year ended 31 March 2009

## 19. Pensions

NESTA offers employees a 12 per cent contribution, on a defined contribution basis, to a personal pension scheme or group stakeholder scheme. NESTA is also a member of the Pension Scheme for Administration and Technical Staff in the Arts ("PSATSITA"). The scheme is a multi-employer, trustee-administered defined benefit scheme whose fund is independently managed and invested by a leading fund management company. This scheme is now closed to new members. NESTA's total contribution made in respect of the period, for all schemes, totalled £406k, including outstanding contributions of £41k.

As NESTA is unable to identify its share of the underlying assets and liabilities in the PSATSITA scheme, it has been accounted for as if it were a defined contribution scheme in accordance with FRS17: Retirement Benefits. An Actuarial Valuation of the pension fund takes place every three years. The market value of the whole scheme assets at 31 March 2007 was £10,200k, representing 100 per cent of the estimated liabilities of the scheme. The surplus or deficit on the scheme affects the size of contributions made by NESTA and its staff. These are currently 19.4 per cent and 5.5 per cent of pensionable earnings respectively. The total annual pension is calculated as 1/60ths of final pensionable earnings for each year of service and index linked to the Retail Prices Index, with a maximum increase of 5 per cent per annum. On retirement 3/80ths of the final pensionable earnings for each year of service may be taken as a lump sum.

## 20. Reconciliation of surplus for the year to net cash outflow from operating activities

	2009 £'000	2008 £'000
Surplus for the year	4,473	8,486
Investment returns – interest and dividends	(14,301)	(14,252)
Depreciation	662	656
Loss on disposal of assets	21	32
Impairment of investment portfolio	1,098	-
(Increase)/Decrease in debtors	(99)	(74)
(Increase)/Decrease in deferred financial assets	394	-
Increase/(Decrease) in grants and investments due	(857)	657
Increase/(Decrease) in other creditors	1,144	505
<b>Net cash outflow from operating activities</b>	<b>(7,465)</b>	<b>(3,990)</b>

## 21a. Analysis of net cash in hand and cash held in investments

	Group 2009 £'000	Group 2008 £'000	Movement £'000
At bank and in hand	234	92	142
Held in escrow	-	237	(237)
Included in bank and in hand	234	329	(95)
Included in current assets: financial assets, short-term deposits	21,153	98,076	(76,923)
<b>Total</b>	<b>21,387</b>	<b>98,405</b>	<b>(77,018)</b>

	Parent 2009 £'000	Parent 2008 £'000	Movement £'000
At bank and in hand	121	92	29
Held in escrow	-	237	(237)
Included in bank and in hand	121	329	(208)
Included in current assets: financial assets, short-term deposits	21,153	98,076	(76,923)
<b>Total</b>	<b>21,274</b>	<b>98,405</b>	<b>(77,131)</b>

The movement largely represents cash received from maturing gilt investments in 2007/08 and reinvested in 2008/09.

## 21b. Reconciliation of net cashflow to movement in net funds

	Group 2009 £'000	Parent 2009 £'000	2008 £'000
Decrease in cash on hand	(95)	(208)	(102)
Cash inflow/(outflow) from increase in liquid resources	(76,923)	(76,923)	87,829
Movement in net funds	(77,018)	(77,131)	87,727
Net funds 1 April 2008	98,405	98,405	10,678
<b>Net funds 31 March 2009</b>	<b>21,387</b>	<b>21,274</b>	<b>98,405</b>

# Notes to the Accounts

For the year ended 31 March 2009

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## 22. Financial instruments

FRS 29: Financial Instruments: Disclosures requires an explanation of the role which financial instruments have had during the period in creating or changing the risks which the Trustees of NESTA face in undertaking their role. For NESTA, financial instruments include all investments made and cash held on short-term deposit. Short-term debtors and creditors have minimal financial risk and are not separately disclosed. The key relevant risks are set out below.

### Liquidity risks

In 2009, £14,434k (48 per cent) of NESTA's income derived from the returns accruing on its financial assets investments. The remaining income is Lottery funding of £15,000k (50 per cent) and project funding and other income of £535k (2 per cent).

NESTA is satisfied that it has sufficient certainty over future income and liquid resources in the form of cash and short-term deposits of £21,387k and regular coupon returns from gilt investments and is therefore not exposed to significant liquidity risks.

### Interest Rate risks

For gilt investment to 31 March 2008, NESTA had a policy of buying five-year plus gilts on a rolling basis and holding them to maturity. In the current year, as gilt parcels have matured and with low yield rates for five-year gilts, longer-term gilts have been purchased to provide more sustainable levels of income. The purchasing of gilts inherently reduces NESTA's economic exposure to short-term interest rate risks, although reported results may be volatile due to the policy of revaluing such investments to prevailing market prices.

Cash on hand used to fund operating activity is predominantly held with the Commissioners for the Reduction of the National Debt and attracts base rate interest income. Based on average cash holdings, a drop in the interest rate by 0.5 per cent would reduce income by approximately £75k per annum.

## Interest Rate profile

The following table shows the interest rate profile of NESTA's financial assets.

	Group & Parent Market value £'000	Weighted average interest rate %	Weighted average period for which rate is fixed
<b>Financial Assets at 31 March 2009</b>			
Fixed rate	265,708	5.08%	10 years, 1 month
Floating rate	20,553	4.62%	
Non-interest bearing assets	57,764		
	<b>344,025</b>		
<b>Financial Assets at 31 March 2008</b>			
Fixed rate	202,551	5.29%	2 years, 6 months
Floating rate	98,076	4.98%	
Non-interest bearing assets	37,347		
	<b>337,974</b>		

All assets are denominated in sterling. The book value equals the fair value for all assets held. Interest rates on gilts expected to be held to maturity are gross redemption yields and include expected capital gains or losses to redemption.

The assets above are included in the Balance Sheet as:	2009 £'000	2008 £'000
Fixed assets, financial assets	322,872	239,898
Current assets, financial assets	21,153	98,076
<b>Total</b>	<b>344,025</b>	<b>337,974</b>

## Inflation Rate risks

NESTA is exposed to cost inflation, particularly in relation to staff costs. At the same time, the majority of its investments are held in fixed income gilts that do not provide any form of cover against changes in inflation. Whilst this is not considered a substantial risk to effective operations in the short term, assuming no substantial and unexpected increase in inflation, it does pose challenges to NESTA in the medium to longer term. NESTA is continuing to work on increasing the effective purchasing power of its investments to be better protected for the future.

# Notes to the Accounts

For the year ended 31 March 2009

## Credit risks

NESTA is not exposed to any significant credit risk. Over 80 per cent of its financial assets are managed by the Commissioners for the Reduction of the National Debt and invested in government gilts. A further 12 per cent of financial assets are held by large institutional investors. The remaining financial assets make up NESTA's portfolio of investments in early-stage companies, loans or funds which are actively managed, re-valued annually, and any impairment treated as expenditure.

## Foreign Exchange risks

NESTA is not exposed to any material foreign exchange risks. The majority of financial assets are denominated in sterling.

## 23. Related parties

NESTA is an NDPB of the Department for Innovation, Universities and Skills (DIUS, now BIS). NESTA had no material financial transactions with DIUS during the year.

NESTA has had material transactions with other Government Departments and other central Government bodies, namely: the Department for Culture, Media and Sport which is parent department for the Big Lottery Fund (BLF), and the Commissioners for the Reduction of the National Debt.

The following related party transactions occurred during the period:

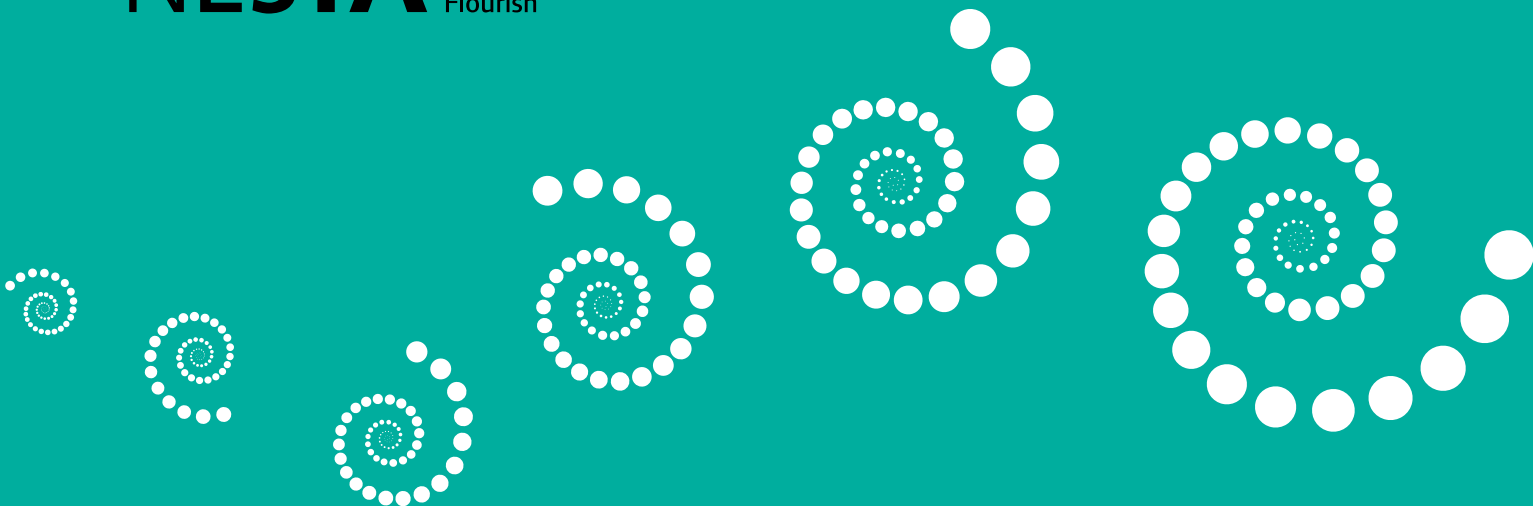
Organisation	Relationship with recipient organisation	Transaction type	Transactions for the year £'000	Outstanding commitment £'000
<b>Trustees of NESTA</b>				
Cancer Research UK	Venture Board Member	Grant (Innovation Programmes)	90	40
Library House	Director	Procurement of services	49	-
Royal National Theatre	Chief Executive	Procurement of services, Grant (Innovation Programmes)	76	75

Organisation	Relationship with recipient organisation	Transaction type	Transactions for the year £'000	Outstanding commitment £'000
<b>Committee Members of NESTA</b>				
Ignite Futures Ltd	Board Member	Procurement of services	12	-
National Council for Graduate Entrepreneurship	Director	Grant (Innovation Programmes)	150	
Gnodal Ltd	Investor, Director	NESTA Investment in company	250	-
MTI Partners	CEO, Managing Director of the fund manager of a NESTA Investment in early-stage fund	NESTA Investments, investment in early-stage fund	-	2,975
<b>Employees of NESTA</b>				
British Business Angel Association	Director	Sponsorship, procurement	5	-
Design Council	Council Member	Grant (Innovation Programmes)	63	43
Royal Shakespeare Company	Governing Board Member	Sponsorship	36	-
Royal Society of the encouragement of Arts, Manufactures and Commerce	Advisory Committee member	Project support	24	-
Young Foundation	Spouse of Director	Procurement of services, Grants (Innovation Programmes and Research)	68	332

NESTA is satisfied that the above-mentioned transactions were entered into in the ordinary course of business, and on arms' length terms.







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