PATHEON UK LIMITED

Report and Accounts

31 October 2001

ERNST & YOUNG



A47
COMPANIES HOUSE
0702
30/08/02

Registered number: 3764421

DIRECTORS
R Tedford
A Braca
D Watchorn (resigned 31 October 2001)
J Blaker (appointed 31 October 2001)

SECRETARY
R Tedford

REGISTERED OFFICE
Kingfisher Drive
Covingham
Swindon
Wiltshire
SN3 5BZ

BANKERS
HSBC
The Forum
Marlborough Road
Swindon
SN3 1QN

SOLICITORS
Macfarlanes
10 Norwich Street
London
EC4A 1BD

AUDITORS
Ernst & Young LLP
Apex Plaza
Reading
Berkshire
RG1 1YE

ERNST & YOUNG

DIRECTORS' REPORT

The directors present their report and accounts for the year ended 31 October 2001.

PRINCIPAL ACTIVITY, REVIEW OF THE BUSINESS AND FUTURE DEVELOPMENTS

The principal activity of the company is one of providing commercial manufacturing and development services of prescription and over-the-counter drugs to the international pharmaceutical industry.

In June 2001 a new Pharmaceutical Development Services (PDS) facility was officially opened at the Swindon facility. This fully supports the strategy of the company to increase the development services aspect of the business and in so doing to provide further added value for our clients. Pharmaceutical development services include dosage form development, analytical methods development, pilot batch manufacture of new products for the regulatory drug approval process and the provision of scale-up services designed to show that a drug can be manufactured in commercial volumes. All costs associated with setting up and running the PDS operation have been written off to the Profit and Loss account as incurred.

RESULTS AND DIVIDENDS

The profit for the year, after taxation, amounted to £629,000 (2000: £1,266,000). A preference dividend of £120,000 was paid during the year. No ordinary dividends were recommended by the directors.

DISABLED EMPLOYEES

The company gives full consideration to applications for employment from disabled persons where the requirements of the job can be adequately fulfilled by a handicapped or disabled person. Where existing employees become disabled, it is the group's policy wherever practical to provide continuing employment under normal terms and conditions and to provide training and career development and promotion to disabled employees wherever appropriate.

EMPLOYEE INVOLVEMENT

During the year the policy of providing employees with information through various media was established. A quarterly newsletter is produced and all employee meetings are conducted through monthly sessions. In addition, regular focus group sessions are conducted between management and employees to allow for a free flow of information and ideas. A bonus scheme for all employees is in operation that is linked to financial performance of the company.

DIRECTORS AND THEIR INTERESTS

The directors who served during the year are shown on page 2. No director had any disclosable interest in the share capital of the company during the year.

AUDITORS

On 28 June 2001, Ernst & Young, the Company's auditor, transferred its entire business to Ernst & Young LLP, a limited liability partnership incorporated under the Limited Liability Partnerships Act 2000. The Directors consented to treating the appointment of Ernst & Young as extending to Ernst & Young LLP with effect from 28 June 2001. A resolution to re-appoint Ernst & Young LLP as the company's auditor will be put to the forthcoming Annual General Meeting.

On behalf of the board

Robert C. Tedford
Director

Date: 28 August 2002

ERNST & YOUNG

STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE ACCOUNTS

Company law requires the directors to prepare accounts for each financial period which give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing those accounts, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed; and
- prepare the accounts on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and to enable them to ensure that the accounts comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

ERNST & YOUNG

ERNST & YOUNG

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF PATHEON UK LIMITED

We have audited the company's financial statements for the year ended 31 October 2001, which comprise the Profit and Loss Account, Statement of Total Recognised Gains and Losses, Balance Sheet and the related notes 1 to 24. These financial statements have been prepared on the basis of the accounting policies set out therein.

Respective responsibilities of directors and auditors

As described in the Statement of Directors' Responsibilities the company's directors are responsible for the preparation of the financial statements in accordance with applicable United Kingdom law and accounting standards.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards.

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

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it.

Basis of audit opinion

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

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

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the company as at 31 October 2001 and of its profit for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Ernst & Young LLP

Registered Auditor
Reading

30 August 2002

PROFIT AND LOSS ACCOUNT
for the year ended 31 October 2001

	Notes	2001 £'000	2000 £'000
TURNOVER	2	28,131	29,671
Change in stocks of finished goods and work in progress		(510)	1,987
Raw materials and consumables		(9,743)	(13,703)
Staff costs	5	(12,621)	(10,555)
Depreciation and amortisation		(590)	(518)
Other operating charges		(4,150)	(3,541)
Interest payable and similar charges	6	(171)	(1,071)
Interest receivable and similar income	7	410	-
PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION	3	756	2,270
Tax on profit on ordinary activities	8	127	1,004
PROFIT FOR THE FINANCIAL YEAR		629	1,266
Preference dividends payable on non-equity shares	9	120	110
PROFIT RETAINED FOR THE FINANCIAL YEAR		509	1,156

STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES
for the year ended 31 October 2001

There were no recognised gains and losses other than the profit attributable to shareholders of £629,000 in the year ended 31 October 2001 (2000: £1,266,000).

ERNST & YOUNG

BALANCE SHEET
at 31 October 2001

	Notes	*31 October 2001* £'000	*31 October 2000* £'000
FIXED ASSETS			
Intangible asset	10	(17,446)	(18,404)
Tangible assets	11	31,417	28,143
		13,971	9,739
CURRENT ASSETS			
Stocks	12	4,230	4,471
Debtors	13	4,157	5,265
Cash at bank and in hand		-	1,715
		8,387	11,451
CREDITORS: amounts falling due within one year	14	16,241	15,759
NET CURRENT (LIABILITIES)/ASSETS		(7,854)	(4,308)
TOTAL ASSETS LESS CURRENT LIABILITIES		6,117	5,431
CREDITORS: amounts falling due after more than one year			
Loans	15	1,861	1,782
Obligations under finance leases and hire purchase contracts	16	26	38
		1,887	1,820
PROVISIONS FOR LIABILITIES AND CHARGES			
Deferred taxation	17	465	355
		3,765	3,256
CAPITAL AND RESERVES			
Called up share capital	18	2,100	2,100
Profit and loss account	19	1,665	1,156
Shareholders' funds:			
Equity		1,765	1,256
Non equity		2,000	2,000
		3,765	3,256

The accounts were approved by the Board of Directors on 8 August 2002 and signed on its behalf by

R Tedford

Robert C. Tedford, Director

ERNST & YOUNG

NOTES TO THE ACCOUNTS
at 31 October 2001

1. ACCOUNTING POLICIES

Accounting convention
The accounts have been prepared in accordance with applicable accounting standards and under the historical cost convention.

Depreciation
Depreciation is provided on all tangible fixed assets at rates calculated to write off the cost or valuation, less estimated residual value, of each asset evenly over its expected useful life, as follows:

Buildings	40	Years
Computer Hardware	4	Years
Computer Software	3	Years
Plant and Equipment	15	Years
Laboratory Equipment	5	Years
Furniture and Fittings	10	Years
Change Parts	5	Years

Goodwill
Goodwill is the difference between the consideration paid for the acquired entity and the aggregated amount of the fair value of that entity's identifiable assets and liabilities. Negative goodwill up to the fair values of the non-monetary assets acquired is recognised in the profit and loss account in the period in which the non-monetary assets are recovered, whether through depreciation or sale.

Stocks
Stocks are stated at the lower of cost and net realisable value.

Deferred taxation
Deferred taxation is provided using the liability method on all timing differences, including those relating to pensions and other post retirement benefits, to the extent they are expected to reverse in the future without being replaced, calculated at the rate at which it is anticipated the timing differences will reverse.

Deferred tax assets are only recognised if recovery without replacement by equivalent debit balances is reasonably certain.

Foreign currencies
Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies are translated at the rate of exchange ruling at the balance sheet date.

All exchange differences are taken to the profit and loss account.

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

Assets held under finance leases, which are leases where substantially all the risks and rewards of ownership of the asset have passed to the company, are capitalised in the balance sheet and are depreciated over their useful lives. The capital elements of the future obligations under the leases are included as liabilities in the balance sheet. The interest element of the rental obligations are charged to profit & loss account over the periods of the leases and represent a constant proportion of the balance of capital repayments outstanding.

ERNST & YOUNG

NOTES TO THE ACCOUNTS
at 31 October 2001

1 ACCOUNTING POLICIES (continued)

Cash flow statement
The company has adopted the provisions under FRS1 (Revised) and has not prepared a cash flow statement.

Pensions
The company operates a defined benefit pension scheme which requires contributions to be made to a separately administered trust fund. Contributions to these funds are charged in the profit and loss account so as to spread the cost of pensions over the employees working lives with the company.

2. TURNOVER
Turnover, which is stated net of value added tax, represents the amount derived from the provision of goods and services which fall within the company's continuing ordinary activities. Turnover is attributable to one continuing activity, the provision of manufacturing and development services to the pharmaceutical industry.

The analysis by geographic market is as follows.

	2001	*2000*
	£'000	*£'000*
United Kingdom	8,274	3,513
Other geographical regions	19,857	26,158
	28,131	29,671

3. PROFIT ON ORDINARY ACTIVITIES BEFORE TAX
This is stated after charging/(crediting):

	2001	*2000*
	£'000	*£'000*
Depreciation of owned fixed assets	1,547	1,415
Depreciation of assets held under finance lease	1	1
Amortisation of negative goodwill	(958)	(898)
Auditors' remuneration	19	18
Operating lease rentals – plant and machinery	31	39

4. DIRECTORS' REMUNERATION
The directors did not receive any remuneration for their services during the year to 31 October 2001. None of the directors were members of the pension scheme.

ERNST & YOUNG

NOTES TO THE ACCOUNTS
at 31 October 2001

5. STAFF COSTS

	2001	*2000*
	£'000	*£'000*
Wages and salaries	10,660	8,857
Social security costs	771	672
Other pension costs	1,190	1,026
	12,621	10,555

The average monthly number of employees during the year was as follows:

	2001	*2000*
	No.	*No.*
Production & service	254	194
Administration and other	245	239
	499	433

6. INTEREST PAYABLE AND SIMILAR CHARGES

	2001	*2000*
	£'000	*£'000*
Interest payable to group undertakings	110	52
Finance charges payable under finance leases	2	1
Loss on foreign exchange	-	1,005
Bank charges	59	13
	171	1,071

7. INTEREST RECEIVABLE AND SIMILAR INCOME

	2001	*2000*
	£'000	*£'000*
Bank interest receivable	48	-
Gain on foreign exchange	362	-
	410	-

ERNST & YOUNG

NOTES TO THE ACCOUNTS
at 31 October 2001

8. TAX ON PROFIT ON ORDINARY ACTIVITIES

	2001 *£'000*	*2000* *£'000*
UK corporation tax	-	649
Prior Year Adjustment	17	-
Deferred taxation	110	355
	127	1,004

9. DIVIDENDS

	2001 *£'000*	*2000* *£'000*
Non-equity dividend on preference shares:		
Interim dividend	60	50
Final dividend	60	60
	120	110

10. INTANGIBLE ASSET

	Negative Goodwill *£'000*
Cost:	
At 1 November 2000	(19,302)
At 31 October 2001	(19,302)
Amortisation:	
At 1 November 2000	898
Written back during the year	958
At 31 October 2001	1,856
Net book value:	
31 October 2001	(17,446)
1 November 2000	(18,404)

Negative goodwill arising on the acquisition of the trade and assets of Hoechst Marion Roussel (HMR) Swindon is being written back to profit and loss in line with the period in which the non-monetary assets are recovered, whether through depreciation or sale.

ERNST & YOUNG

11. TANGIBLE FIXED ASSETS

	Land and buildings £'000	*Plant and machinery* £'000	*Fixtures and fittings* £'000	*Total* £'000
Cost:				
At 1 November 2000	15,350	14,088	121	29,559
Additions	5	4,812	5	4,822
At 31 October 2001	15,355	18,900	126	34,381
Depreciation:				
At 1 November 2000	336	1,069	11	1,416
Provided during the year	371	1,161	16	1,548
At 31 October 2001	707	2,230	27	2,964
Net book value:				
At 31 October 2001	14,648	16,670	99	31,417
At 1 November 2000	15,014	13,019	110	28,143

The net book value of plant and machinery above includes an amount of £66,000 in respect of assets held under finance leases.

12. STOCKS

	2001 £'000	*2000* £'000
Raw material	2,753	2,484
Engineering stores	407	387
Work in process	1,070	1,600
	4,230	4,471

13. DEBTORS

	2001 £'000	*2000* £'000
Trade debtors	3,611	4,511
Amounts due to parent undertaking	63	-
Corporation Tax	73	-
Prepayments	410	754
	4,157	5,265

ERNST & YOUNG

NOTES TO THE ACCOUNTS
at 31 October 2001

14. CREDITORS: amounts falling due within one year

	2001	*2000*
	£'000	*£'000*
Obligations under finance leases and hire purchase contracts (note 16)	14	14
Overdraft	1,642	-
Trade creditors	1,759	2,180
Amounts due to parent undertaking	10,811	11,355
Corporation tax	-	323
Other taxes and social security costs	177	163
Accruals	1,838	1,724
	16,241	15,759

The bank overdraft is secured by mortgage on leasehold property and both fixed and floating charges over certain of the company's other assets.

15. LOANS

	2001	*2000*
	£'000	*£'000*
FRF 20,000,000 from Patheon France at 5% per annum, wholly repayable in April 2002	-	1,782
£1,861,299 from Patheon Europe Rt. at Libor plus 2%, wholly repayable in July 2006	1861	-

ERNST & YOUNG

16. OBLIGATIONS UNDER FINANCE LEASES AND HIRE PURCHASE CONTRACTS

The maturity of these amounts is as follows:

	2001 *£'000*	*2000* *£'000*
Amounts payable:		
Within one year	14	14
In two to five years	31	45
	45	59
Less: finance charges allocated to future periods	7	7
	38	52
Finance leases are analysed as follows:		
Current obligations	12	14
Non-current obligations	26	38
	38	52

17. PROVISIONS FOR LIABILITIES AND CHARGES

The movement in deferred taxation during the current year is as follows:

	2001 *£'000*	*2000* *£'000*
At 1 November 2000	355	-
Charge for the year (note 8)	110	355
At 31 October 2001	465	355

Deferred taxation provided in the accounts and the amounts not provided are as follows:

	Provided		*Not provided*	
	2001 *£'000*	*2000* *£'000*	*2001* *£'000*	*2000* *£'000*
Capital allowances in advance of depreciation	855	355	-	-
Other timing difference	(390)	-	(194)	(300)
	465	355	(194)	(300)

No deferred tax asset has been recognised in relation to the foreign exchange loss arising on the intercompany loan due to the uncertainty that foreign exchange gains will be made on the loan in the future.

ERNST & YOUNG

NOTES TO THE ACCOUNTS
at 31 October 2001

18. SHARE CAPITAL

	Authorised		Allotted, called-up and fully paid	
	2001	*2000*	*2001*	*2000*
	No	*No*	*£'000*	*£'000*
Ordinary shares of £1 each	2,000,000	2,000,000	100	100
6% preference shares of £1 each	8,000,000	8,000,000	2,000	2,000

The preference shares were issued at par. They carry a dividend right of 6% per annum payable half yearly in April and October. The dividend rights are cumulative. On a winding up of the company the preference shares have the right to receive, in preference to ordinary shareholders, £1 per share plus any accrued dividend. The preference shares carry voting rights at meetings of 1 vote per share whereas the ordinary shares carry 100 votes per share.

19. RECONCILIATION OF SHAREHOLDERS' FUNDS AND MOVEMENTS ON RESERVES

	Share capital	*Profit and loss account*	*Total*
	£'000	*£'000*	*£'000*
At 31 October 2000	2,100	1,156	3,256
Profit for the year	-	509	509
At 31 October 2001	2,100	1,665	3,765

20. OTHER FINANCIAL COMMITMENTS

The company had annual commitments under non-cancellable operating leases as set out below:

	2001	*2000*
	£'000	*£'000*
Operating leases which expire		
Within one year	16	-
In two to five years	303	57
	319	57

21. RELATED PARTY TRANSACTIONS

Patheon UK is a 100% owned subsidiary of Patheon Inc. and accordingly is not required to disclose related party transactions with companies within the same group.

ERNST & YOUNG

22. CAPITAL COMMITMENTS

Amounts contracted for but not provided in the accounts amounted to £1.4 million as at 31st October 2001.

23. PENSIONS

In line with the requirements of FRS17, published by the Accounting Standards board in November 2000, details in respect of the scheme are provided below in accordance with both SSAP24 and FRS17.

(a) SSAP24

Patheon UK operates a defined benefit scheme with contributions being paid into a separately administered trust fund. Pension costs are determined with the advice of an independent actuary.

The Patheon UK Pension Plan scheme was established by the company following the acquisition by Patheon Inc. of the HMR Swindon facility. A bulk transfer of assets from the HMR scheme to the Patheon UK Scheme to cover pension liabilities associated with the past service of members transferring to the new scheme, as at the date of acquisition, is being finalised between the respective actuaries.

Total pension costs for the period under SSAP 24 are disclosed in note 5 to the accounts.

(b) FRS17 "Retirement Benefits" Disclosures

An actuarial valuation is being undertaken as at 30 September 2001. This valuation was updated to 31 October 2001, by an independent qualified actuary in accordance with the transitional arrangements of FRS17. As required by FRS17, the defined benefit liabilities have been measured using the projected unit method.

The major assumptions used by the actuary to calculate scheme liabilities at 31 October 2001 under FRS 17 were (in normal terms):

Rate of increase in salaries	4.05%
Rate of increase of pensions in payment	2.30%
Discount rate	5.60%
Inflation assumption	2.30%

The assets in the scheme and the expected rate of return were:

	Long-term rate of return expected at 31 October 2001 %	*Value at 31 October 2001 £'000*
Equities	7.50%	15,770
Bonds	4.40%	2,560
Other	4.40%	190
Total market value of assets		18,520
Actuarial present value of liabilities		(24,520)
Deficit in the scheme		(6,000)
Related deferred tax asset		1,800
Net pension liability		(4,200)

ERNST & YOUNG

23. PENSIONS (CONTINUED)

Note that the figures include assets and liabilities anticipated to be transferred from HMR Pension and Life Assurance Scheme under the terms of the sale and purchase agreement relating to the acquisition of Patheon UK Limited from HMR. The actual market value of the assets in the plan at 31 October 2001 was £1.44m.

The reconciliation of net assets and reserves under FRS 17 is as follows:

	2001 £'000
Net assets	
Net assets as stated in balance sheet excluding pension liability	3,765
Pension liability	(4,200)
Net assets including pension liability	(435)
Reserves	
Profit and loss reserve excluding pension liability	1,665
Pension liability under FRS 17	(4,200)
Profit and loss reserve including amounts relating to defined benefit scheme deficit	(2,535)

The company has agreed, subject to review at future actuarial valuations of the scheme, to pay to the scheme contributions at 15% of pensionable salaries.

24. ULTIMATE PARENT UNDERTAKING

The company's ultimate parent company is Patheon Inc., a company incorporated in Canada. The smallest and largest group of which the company is a member and for which group accounts are prepared is Patheon Inc. A copy of the group accounts can be obtained from the headquarters at the following address: -

Patheon Inc.
2100 Syntex Court
Mississauga
Ontario, L5N 7K9
Canada

ERNST & YOUNG