# OCTOPUS TITAN VCT 2 PLC

**ANNUAL REPORT**
**FOR THE YEAR ENDED 31 OCTOBER 2009**
**COMPANY NO: 06397765**

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# FINANCIAL HEADLINES

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| 8.0% | Total return for the year to 31 October 2009 |
| 96.1p | Net asset value per share at 31 October 2009 |
| 1.0p | Dividends paid since launch |
| 0.5p | Proposed final dividend for the year to 31 October 2009 |
| 8 | New qualifying investments in the year amounting to £2.5 million |

# SHAREHOLDER INFORMATION AND CONTACT DETAILS

## Financial Calendar

The Company's financial calendar is as follows:

| | |
|---|---|
| 31 March 2010 | Annual General Meeting |
| 23 April 2010 | 2009 final dividend paid |
| June 2010 | Half-yearly results to 30 April 2010 published |
| February 2011 | Annual results for the year to 31 October 2010 announced; Annual Report and financial statements published |
| April 2011 | 2010 final dividend paid |

## Dividends

Dividends will be paid by the Registrar on behalf of the Company. Shareholders who wish to have dividends paid directly into their bank account rather than by cheque to their registered address can complete a mandate form for this purpose. Queries relating to dividends, shareholdings and requests for mandate forms should be directed to the Company's Registrar, Capita Registrars, by calling 0871 6640300 (calls cost 10p per minute plus network extras), or by writing to them at:

Capita Registrars
The Registry
34 Beckenham Road
Beckenham
Kent
BR3 4BR

The table below shows the Net Asset Value per share (NAV) and lists the dividends that have been paid since the launch of Octopus Titan VCT 2 plc:

| Period Ended | NAV | Dividends paid in period | NAV + cumulative dividends |
|---|---|---|---|
| 30 April 2008 | 95.0p | – | 95.0p |
| 31 October 2008 | 89.9p | – | 89.9p |
| 30 April 2009 | 91.5p | 0.5p | 92.0p |
| 31 October 2009 | 96.1p | 0.5p | 97.1p |

The proposed final dividend of 0.5p will, if approved by shareholders, be paid on 23 April 2010 to shareholders on the register on 5 March 2010.

## Share Price

The Company's share price is published daily in the Financial Times and its FTSE classification is 'Investment Companies' 'VCTs'. They can also be found on various financial websites with the following TIDM/EPIC code:

| | Ordinary Shares |
|---|---|
| TIDM/EPIC code | OTV2 |
| Latest share price (3 February 2010) | 85.0p per share |

## Buying and Selling Shares

The Company's Ordinary shares can be bought and sold in the same way as any other company quoted on the London Stock Exchange via a stockbroker. There may be tax implications in respect of selling all or part of your holdings, so shareholder's should contact their independent financial adviser if they have any queries.

The Company operates a policy of buying its own shares for cancellation as they become available. The Company is, however, unable to buy back shares directly from shareholders. If you are considering selling your shares or trading in the secondary market, please contact the Company's Corporate Broker, Matrix Corporate Capital ('Matrix').

Matrix is able to provide details of close periods (when the Company is prohibited from buying in shares) and details of the price at which the Company has bought in shares. Matrix can be contacted as follows:

Chris Lloyd
0203-206-7176 chris.lloyd@matrixgroup.co.uk

Paul Nolan
0203-206-7177 paul.nolan@matrixgroup.co.uk

## Notification of Change of Address

Communications with shareholders are mailed to the registered address held on the share register. In the event of a change of address or other amendment this should be notified to the Company's Registrar, Capita Registrars, under the signature of the registered holder.

## Other Information for Shareholders

Previously published Annual Reports and Half-yearly Reports are available for viewing on the Investment Manager's website at www.octopusinvestments.com by navigating to Services, Investor Services, Venture Capital Trusts, Octopus Titan VCT 2. All other statutory information will also be found there.

## Warning to Shareholders

Many companies are aware that their shareholders have received unsolicited phone calls or correspondence concerning investment matters. These are typically from overseas based 'brokers' who target UK shareholders offering to sell them what often turn out to be worthless or high risk shares in US or UK investments. They can be very persistent and extremely persuasive. Shareholders are therefore advised to be very wary of any unsolicited advice, offer to buy shares at a discount or offer for free company reports.

Please note that it is very unlikely that either the Company or the Company Registrar would make unsolicited telephone calls to shareholders and that any such calls would relate only to official documentation already circulated to shareholders and never in respect of investment 'advice'.

If you are in any doubt about the veracity of an unsolicited phone call, please call either the Investment Manager or the Registrar at the numbers provided on page 48.

# ABOUT OCTOPUS TITAN VCT 2 PLC

**Octopus Titan VCT 2 plc ('Titan 2', 'Company' or 'Fund') is a venture capital trust which aims to provide shareholders with attractive tax-free dividends and long-term capital growth, by investing in a diverse portfolio of predominately unquoted companies. The Company is managed by Octopus Investments Limited ('Octopus' or 'Manager').**

Titan 2 was incorporated on 12 October 2007 with the first allotment of equity being 19 December 2007. In collaboration with Octopus Titan VCT 1 plc ('Titan 1'), the Funds raised over £30.8 million in aggregate (£29.5 million net of expenses) through an Offer for subscription which closed on 16 May 2008. Titan 2 invests primarily in unquoted UK smaller companies and aims to deliver absolute returns on its investments.

Further details of the Fund's progress are discussed in the Chairman's Statement and Investment Manager's Review on pages 6 to 17.

## Venture Capital Trusts (VCTs)

VCTs were introduced in the Finance Act 1995 to provide a means for private individuals to invest in unlisted companies in the UK. Subsequent Finance Acts have introduced changes to VCT legislation. The tax benefits currently available to eligible new investors in VCTs include:

- up-front income tax relief of 30%
- exemption from income tax on dividends paid
- exemption from capital gains tax on disposals of shares in VCTs.

The Company has been provisionally approved as a VCT by HM Revenue & Customs. In order to maintain its approval the Company must comply with certain requirements on a continuing basis. By the end of the Company's third accounting period at least 70% of the Company's investments must comprise 'qualifying holdings' of which at least 30% must be in eligible Ordinary shares. A 'qualifying holding' consists of up to £1 million invested in any one year in new shares or securities in an unquoted company (including companies listed on AIM) which is carrying on a qualifying trade and whose gross assets do not exceed £7 million at the time of investment, and whose total number of employees is less than 50, also at the time of investment. The Company will continue to ensure its compliance with these qualification requirements.

# FINANCIAL SUMMARY

| | **As at 31 October 2009** | **As at 31 October 2008** |
|---|---|---|
| Net assets (£'000s) | 15,014 | 14,036 |
| Return on ordinary activities after tax (£'000s) | 1,133 | (722) |
| Net asset value per share | 96.1p | 89.9p |
| Dividend per share – paid and proposed since launch | 1.5p | 0.5p |

# CHAIRMAN'S STATEMENT

I am pleased to present the Company's second Annual Report for the year ended 31 October 2009.

## Performance

I am delighted to be able to report a positive total return (being the change in NAV plus cumulative dividends paid) for the year of 8.0% comprising an increase in NAV of 6.2p to 96.1p, plus dividends paid of 1.0p. This has been driven primarily by a recovery in the value of the Company's liquid resources, as well as a strong overall performance in the two Octopus Open Ended Investment Companies ('OEICs'), offset by the reduction in fair values of three investments.

The Fund is now invested in ten unquoted companies and one AIM-quoted company (including the investment held in The Key Revolution which is currently in administration). The focus continues to be to invest in a broad range of unquoted UK smaller companies with the potential for high growth in order to generate income and capital growth over the long-term. By value, 26.0% of the Company's net assets are in unquoted investments, 3.2% in AIM-quoted investments and 32.4% in Octopus OEICS, leaving 38.4% currently in cash or cash equivalents.

## Investment Portfolio

The year under review, particularly the first half, has been challenging for many businesses, with the impact of the credit crunch combining with a worsening of the economic environment. Inevitably, this has had an impact on the portfolio and, as a result, three investments have had reductions in fair value. That said, we are optimistic about both the progress and potential of our portfolio companies but as yet it is too early to recognise any significant uplift in value in all but two of these.

During the year, the Fund made eight new investments totalling £2.47 million and two follow-on investments into The Key Revolution and True Knowledge for £230,000 and £350,000 respectively. All of these investments are discussed in more detail in the Investment Manager's Review on pages 8 to 17 in which you will see that we have made investments in a diverse range of companies in some exciting market sectors. In the case of Zoopla, we have been able to recognise an uplift in value following the new investment but, unfortunately, we have had to make a reduction in fair value (to £nil) in respect of our investment in The Key Revolution, following the appointment of Administrators in December. On balance however, the Investment Manager is encouraged by the performance of the portfolio and the good flow of investment opportunities which it is seeing.

Further details about the portfolio, including new investments can be found in the Investment Manager's Review on pages 8 to 17.

## Cash and Liquid Resources

Since the unprecedented market turmoil we saw in the second half of 2008 and first quarter of 2009, I am delighted to report that our portfolio of bonds, floating rate notes and cash-plus funds has significantly recovered in value, up more than 7% over the year. As you may recall, we created such a portfolio to invest your cash whilst awaiting deployment into suitable qualifying investments. As I reported in my first Annual Report, the values of some of these instruments had fallen in 2008. With advice from our cash manager, Goldman Sachs, we have continued to hold these investments and propose to do so until maturity which is in line with the timetable for making investments to achieve our qualifying threshold. Indeed, at the time of writing, two of our bonds have successfully matured at par.

The yield on our cash, which is held in highly liquid, low risk cash funds, has reduced due to the continued decline in UK interest rates. Unfortunately, this is just a factor of the historically low interest rate environment we find ourselves in. Given our requirements over the coming months for liquidity to make new investments, the Board has taken the view that it is in the best interest of shareholders to preserve capital by keeping a high level of cash in such low risk money market funds.

## Open Ended Investment Companies (OEICs)

The Company's investments in the two Octopus Partner OEICs have also seen significant uplifts in valuation over the year to 31 October 2009. The Absolute Return Fund and the UK Smaller Companies Fund have increased in value 46% and 34% respectively. The Absolute Return Fund is the number one performing fund in its sector, and indeed has gained 81% since Titan 2 first invested in March 2008, when that particular OEIC launched. The Board has met with the respective fund managers and believe it is in the best interests to continue to hold investments in these OEICs for the foreseeable future, as set out in the original prospectus. Further details of these OEICs may be found at www.octopusinvestments.com where monthly factsheets are available.

## Dividend

It is your Board's policy to strive to maintain a regular dividend flow where possible. Our primary aim is to create distributable capital gains. We anticipate declaring modest dividends in the early years although these are likely to be smaller than originally envisaged due to the substantial reduction in interest rates during the last 12 months. Taking this into account, for the year ended 31 October 2009, a final dividend of 0.5p per share has been proposed. Subject to shareholder approval at the Annual General Meeting, this dividend will be paid on 23 April 2010 to those shareholders on the register on 5 March 2010. This will take dividends for the year ended 31 October 2009 to 1.0p per share (2008: 0.5p per share).

## VCT Qualifying Status

PricewaterhouseCoopers LLP provides the Board and Investment Manager with advice concerning ongoing compliance with Her Majesty's Revenue & Customs (HMRC) rules and regulations concerning VCTs. The Board has been advised that Titan 2 is in compliance with the conditions laid down by HMRC for maintaining approval as a VCT. This is discussed further on page 5.

A key requirement now is to achieve the 70% qualifying investment level prior to 31 October 2010. As at 31 October 2009, over 35.0% of the portfolio, as measured by HMRC rules, was invested in VCT qualifying investments. In view of the current investment activity, the Board continues to be confident that the 70% target will be met by the required date.

## Investment Management Agreement

The Board announced on 20 October 2009 that the Investment Management Agreement between Titan 2 and Octopus Ventures Limited had been novated to Octopus Investments Limited. This change was made as a result of an internal reorganisation of the Octopus group and the terms of the Investment Management Agreement and the composition of the fund management team within Octopus responsible for managing the Company's assets remain unchanged.

## Annual General Meeting

The Company's Annual General Meeting will take place on 31 March 2010 at 2.30 p.m. I look forward to welcoming you to the meeting which will be held at the Company's registered office, and the offices of Octopus Investments Limited, at 8 Angel Court, London, EC2R 7HP.

## Outlook

Octopus launched a further Fund (Octopus Titan VCT 3 plc) in 2008 and has recently launched a fourth Fund (Octopus Titan VCT 4 plc) during the current tax year. This will give the Titan VCT family a significant presence in the marketplace which we believe will be an advantage for all of us. The Octopus team now has uncommitted resources of £39 million for investment in emerging companies in our defined market sectors.

Despite the recent improvement in stock markets, we remain cautious about the wider economic environment and the impact this may have on portfolio companies. This could be reflected directly through trading performance or indirectly through the availability of credit. We also need to ensure that, where appropriate, our portfolio companies have sufficient resources to take advantage of the opportunities that will present themselves. Our Investment Manager is seeing a high level of new investment opportunities and we will continue to maintain our strategy of seeking to keep an appropriate level of liquidity in the Fund to provide support for the existing portfolio.

John Hustler
Chairman
3 February 2010

# INVESTMENT MANAGER'S REVIEW

## Personal Service

At Octopus, we focus on both managing your investments and keeping you informed throughout the investment process. We are committed to providing our investors with regular and open communication. Our updates are designed to keep you informed about the progress of your investment. During this time of economic upheaval, we consider it particularly important to be in regular contact with our investors and are working hard to manage your money in the current climate.

Octopus Investments Limited was established in 2000 and has a strong commitment to both smaller companies and to VCTs. We currently manage 17 VCTs, including this Company, and manage over £230m in the VCT sector. Octopus has over 100 employees and has been voted as 'Best VCT Provider of the Year' by the financial adviser community for the last four years.

## Investment Policy

The investment approach of Titan 2 is not designed to deliver a return that is measured against a stock market index. Instead, the focus of Titan 2 is on generating absolute returns over the medium term. In order to achieve this goal, the Fund will focus on providing early stage, development and expansion funding to unquoted companies with a typical deal size of £0.2 million to £1 million.

## Investment Strategy

The investee companies are those that we believe have great potential but need some financial support to realise it. Each company that we target will have the potential to create a large business by taking a relatively modest market share. We are particularly interested in businesses that address current market trends and aim to create a balanced investment portfolio spanning multiple industries and business sectors.

We expect that the portfolio of holdings built by Titan 2 will encompass investments in 20–25 predominantly unquoted companies, with a focus on the environmental, technology, media, telecoms and consumer lifestyle and wellbeing sectors. It is envisaged that, at the end of the three year initial investment period, 75–85% of the proceeds of the Offer will be invested in a range of qualifying investments with 15–25% invested in a combination of cash, OEICs* managed by Octopus and money market securities managed by third party specialists.

## Portfolio Review

As at 31 October 2009 the NAV stood at 96.1p, compared to 89.9p at 31 October 2008, and when adding back the 1p of cumulative dividends paid, this represents a positive total return of 8.0%. Recent improvements in the economy have created a better environment for the companies in the portfolio. There is a sense that the worst of the recession is over and that we may be on the road to recovery. We are excited about the potential in the market for smaller private companies, including those in your portfolio.

At this point in time, small growing businesses have an opportunity to work nimbly in a rocky economic landscape and both grow and take market share. We work with each company, providing expertise and guidance to help them achieve their goals. As an example of a business taking advantage of the economic environment, portfolio company Zoopla recently made a series of acquisitions, including the websites Hot Property, Think Property and the Property Finder Group, which have added significantly to Zoopla's proposition, user base and brand profile. Given the company's progress, we made a further investment into Zoopla in October of £205,000.

The following events occurred between the balance sheet date and the signing of these financial statements:

- 8 January 2010: £499,998 investment into Calastone
- 9 January 2010: A previous £201,440 non-qualifying investment in Zoopla became qualifying.

## Outlook

At the time of writing, we are actively engaged with a number of new businesses and expect to be completing these investments early in 2010. Historically, a time of great pressure for small business is frequently the first two quarters coming out of recession. It is at this time that cash flow remains constrained, but there is the opportunity to return to growth. As a result, this is a good time to be making investments and providing financial capital to those businesses that we believe have the opportunity to grow significantly. Times of disruption in industries are also the times when there are the greatest opportunities to make a significant

*Titan 2 has invested in two OEICs managed by Octopus, the CF Octopus Partner Fund – (Absolute Return) and the CF Octopus Partner Fund – (UK Smaller Companies).

difference to the way in which an industry is structured, or a service is delivered. There are, and will always be, significant challenges as a result of the size and nature of the businesses we invest into. They are often at the forefront of new ideas within their industry sectors, which can leave them exposed, and we recognise the risks associated with investing into such businesses. However, it is precisely these sorts of businesses that can change the way in which we live our lives, or the way in which we do business, thus creating large successful businesses from our investment. As a result, we look forward with expectation to the coming year.

If you have any questions on any aspect of your investment, please call one of the team on 0800 316 2347.

Alex Macpherson

Octopus Investments Limited
3 February 2010

## Investment Portfolio

| Qualifying investments | Sector | Investment at cost 31 October 2009 (£'000) | Movement in valuation (£'000) | Fair value at 31 October 2009 (£'000) | % equity held by Titan 1 | % equity managed by Octopus |
|---|---|---|---|---|---|---|
| **Zoopla Limited** | Media | 764 | 277 | 1,041 | 5.0% | 16.7% |
| **True Knowledge Limited** | Media | 1,032 | - | 1,032 | 3.1% | 38.8% |
| **Calastone Limited** | Technology | 635 | - | 635 | 7.5% | 23.5% |
| **e-Therapeutics plc** | Consumer lifestyle & wellbeing | 450 | 27 | 477 | 0.3% | 5.1% |
| **Surrey Nanosystems Limited** | Technology | 300 | - | 300 | 4.9% | 28.5% |
| **GetOptics Limited** | Consumer lifestyle & wellbeing | 285 | - | 285 | 4.9% | 27.1% |
| **Nature Delivered Limited** | Consumer lifestyle & wellbeing | 275 | - | 275 | 4.8% | 24.2% |
| **Phase Vision Limited** | Technology | 200 | - | 200 | 8.9% | 49.0% |
| **Phasor Solutions Limited** | Technology | 100 | (25) | 75 | 2.0% | 30.7% |
| **The Skills Market Limited** | Technology | 100 | (50) | 50 | 4.9% | 15.7% |
| **The Key Revolution Limited** | Telecommunications | 641 | (641) | - | 12.4% | 35.9% |
| **Total qualifying investments** | | **4,782** | **(412)** | **4,370** | | |
| **Money market securities** | | 5,242 | (35) | 5,207 | | |
| **OEICs** | | 3,542 | 1,320 | 4,862 | | |
| **Cash at bank** | | 578 | - | 573 | | |
| **Total investments** | | **14,144** | **873** | **15,012** | | |
| **Net current assets** | | - | - | 2 | | |
| **Total net assets** | | | | **15,014** | | |

## Valuation Methodology

The investments held by Titan 2 are all early stage businesses with growth opportunities. As a result, the methodology used in fair valuing the investments is the transaction price of the recent investment round. Subsequent adjustment to the fair value has then been made according to the significant under or over performance of the business.

Quoted investments are valued at market bid price. No discounts are applied.

If you would like to find out more regarding the The International Private Equity and Venture Capital ('IPEVC') Valuation Guidelines, please visit their website at: www.privateequityvaluation.com.

# INVESTMENT MANAGER'S REVIEW (continued)

**Sector Analysis**

TOTAL QUALIFYING INVESTMENTS BY BOOK COST

**Media**

**Telecommunications**

**Consumer lifestyle & wellbeing**

**Technology**

TOTAL QUALIFYING INVESTMENTS BY VALUE

## Review of Investments

During the year, the Fund made eight new investments amounting to £2.47 million and two follow-on investments into The Key Revolution and True Knowledge for £230,000 and £350,000 respectively.

Quoted and unquoted investments are valued in accordance with the accounting policy set out on page 37, which takes account of current industry guidelines for the valuation of venture capital portfolios and is compliant with International Private Equity and Venture Capital Valuations guidelines and current financial reporting standards.

### Zoopla Limited

Zoopla is an award-winning online property information service and community website, presenting information on house pricing and free valuation estimates, for sale listings, and local community information. Zoopla has become the UK's leading website for house prices and value data, as it provides the most comprehensive source of residential property market information. It is also the UK's most active property community, with over a million user contributions to its website in 2008. It recently launched estate agent listings on a pay-for-performance basis and expects to become one of the premier UK websites for those interested in the property market. We would encourage you to view the website at www.zoopla.co.uk.

In August 2009, Zoopla announced the purchase of The PropertyFinder Group, from News International Ltd and REA Group, which includes propertyfinder.com, one of the best-known and most-visited property websites in the country, with over 2 million unique visitors per month, as well as other online property assets including HotProperty.co.uk and UKPropertyshop.co.uk. This purchase comes hot on the heels of its acquisition in July of ThinkProperty.com from Guardian Media Group. The integration of the two companies took place in the autumn of 2009. These acquisitions have accelerated the company's growth and Zoopla currently holds the number 2 slot in Nielson's analysis of property portals.

| | |
|---|---|
| **Initial investment date:** | January 2009 |
| **Cost:** | £764,206 |
| **Valuation:** | £1,041,696 |
| **Equity held:** | 5.0% |
| **Equity held by all funds managed by Octopus:** | 16.7% |
| **Last audited accounts:** | N/A |

**Further information can be found at the company's website www.zoopla.co.uk**

### True Knowledge Limited

True Knowledge has developed an internet search engine website that answers questions. Finding information on the internet currently involves a process of trial and error, hoping that the search engine retrieves the information you're looking for. True Knowledge has devised technology that resolves this fundamental problem by operating along a more intuitive system. It intelligently answers questions asked on any topic in plain English. It can be used just like a conventional search engine, but users can also add knowledge directly to it. There are currently over 220 million facts in the database, which is being continually expanded.

The company has launched a plug in for the Mozilla Firefox browser where True Knowledge sits on top of the search results provided by Google. Having dramatically improved performance response times, the company's focus is now on securing paying customers. There has also been considerable interest in True Knowledge's ability to answer questions in relation to local search and the company is now providing information to Siri for its local search solution on the iPhone.

| | |
|---|---|
| **Initial investment date:** | July 2008 |
| **Cost:** | £1,031,783 |
| **Valuation:** | £1,031,783 |
| **Equity held:** | 3.1% |
| **Equity held by all funds managed by Octopus:** | 38.8% |
| **Last audited accounts:** | 31 July 2009 |
| **Loss before interest & tax:** | (£1,478,219) |
| **Net current assets:** | £462,892 |

**Further information can be found at the company's website www.trueknowledge.com**

# INVESTMENT MANAGER'S REVIEW (continued)

## Calastone Limited

Calastone is the UK's only independent transaction service for the mutual fund industry. It enables buyers and sellers of mutual funds on different platforms to communicate orders electronically by providing a universal message communication and 'translation' service. This is being welcomed in an industry which has not previously been able to invest in the real-time exchange of information between participants. Orders are commonly communicated by fax or telephone with a high level of manual re-keying and manual error correction. Calastone's 'translation' service means that neither the transmitter nor receiver need purchase additional technology or change their existing systems. Furthermore, there is no barrier or cost of entry.

Over the last few months, the company has been signing clients on a regular basis and, during August 2009, was able to announce a significant milestone in sending its one millionth message across its network. Calastone has also recently announced an offering into the settlement market further extending its services to its client base.

| | |
|---|---|
| **Initial investment date:** | October 2008 |
| **Cost:** | £634,746 |
| **Valuation:** | £634,746 |
| **Equity held:** | 7.5% |
| **Equity held by all funds managed by Octopus:** | 23.5% |
| **Last audited accounts:** | N/A |

**Further information can be found at the company's website www.calastone.com**

## e-Therapeutics plc

e-Therapeutics is an AIM-listed, drug discovery and development company. It focuses on three core areas: the discovery of new drugs; discovering novel uses for existing drugs; and analysis of the interactions between different drugs. The company has developed a unique drug discovery technology that enables it to assess drug candidates for high efficacy and safety ahead of clinical trials. The use of this technology dramatically reduces the time between drug discovery and market applicability, and reduces the risks associated with clinical trials.

The company is currently progressing with the preclinical and clinical development of a number of innovative drug candidates to which the new technology was applied. The treatments are now at an advanced stage of testing, validating the therapeutic attributes that e-Therapeutics' drug discovery system predicted for each candidate. The development and commercialisation of the company's drug candidates that have generated clinical data will be supported initially by licensing these to partners operating in smaller pharmaceutical markets.

e-Therapeutics announced their results in July with news of the continued development of its drug pipeline. The company has also announced a placing of approximately 10% of the issued shares to Gartmore at 38p per share, a premium to the Fund's entry price of 26%.

| | |
|---|---|
| **Initial investment date:** | March 2009 |
| **Cost:** | £450,000 |
| **Valuation:** | £477,000 |
| **Equity held:** | 0.3% |
| **Equity held by all funds managed by Octopus:** | 5.1% |
| **Last audited accounts:** | 24 July 2009 |
| **Loss before tax:** | (£1,957,000) |
| **Net assets:** | £947,000 |

**Further information can be found at the company's website www.etherapeutics.com**

## Surrey Nanosystems Limited

Surrey NanoSystems was founded in November 2006 in partnership with the University of Surrey's Advanced Technology Institute. The company is a pioneer in the development of highly advanced equipment and processes for growing carbon nanotubes (CNTs). CNTs are molecular-scale tubes of graphitic carbon that possess extraordinary electronic and mechanical properties.

Surrey NanoSystems is unique in its ability to consistently grow CNTs at temperatures as low as 350°C. Historically, nanotechnology specialists have been unable to grow CNTs below 700°C, preventing their use in a range of other applications, due to the damage high temperatures cause to other materials used in semiconductor chips. For this reason, NanoGrowth®, the company's unique growth technology, represents a major breakthrough for the rapidly developing field of nanoelectronics, the future manufacture of high-performance semiconductor chips and their use in a far broader range of sectors.

| | |
|---|---|
| **Initial investment date:** | July 2009 |
| **Cost:** | £300,009 |
| **Valuation:** | £300,009 |
| **Equity held:** | 4.9% |
| **Equity held by all funds managed by Octopus:** | 28.5% |
| **Last audited accounts:** | N/A |

**Further information can be found at the company's website www.surreynanosystems.com**

## GetOptics Limited

GetOptics is an online retailer of contact lenses. It is a new company formed to acquire Getlenses and Postoptics. Following the investment, GetOptics is the largest online retailer of contact lenses in the UK. With a turnover of £6.5 million and 25–30% market share of the online market, the company will have unrivalled buying power in the e-commerce lens market, founded on very good relations with contact lens manufacturers.

As a result of the combination, GetOptics will have the opportunity to grow with minimal capital expenditure over the coming years and the chance to roll out best practices learned across the business in marketing, business development, supply chain management and systems.

| | |
|---|---|
| **Initial investment date** | September 2009 |
| **Cost:** | £285,000 |
| **Valuation:** | £285,000 |
| **Equity held:** | 4.9% |
| **Equity held by all funds managed by Octopus:** | 27.1% |
| **Last audited accounts:** | N/A |

**Further information can be found at the company's website www.postoptics.co.uk**

# INVESTMENT MANAGER'S REVIEW (continued)

## Nature Delivered Limited (trading as Graze)

Graze is the first UK company to deliver healthy and nutritionally balanced food by post straight to the home or office. The company was founded in April 2007 and has over 15,000 existing customers who regularly place orders via its website. Graze's snack boxes cost only £2.99 and are sent by Royal Mail for next day delivery.

The Graze product range includes over 100 products to choose from, all free from artificial colourings, flavourings and preservatives. Customers can also place orders for personalised boxes, specifically tailored to meet their tastes, dietary and nutritional requirements.

Graze promotes a varied and balanced diet through facilitating the intake of a wide variety of smaller portions of natural, high-energy foods throughout the day. Its boxes contain up to three portions of fruit and vegetables, in line with the National Health Service's recognised 'five-a-day' scheme. Its product is very much in tune with customer needs and the demands of modern living, as people become ever more conscious of health and convenience.

| | |
|---|---|
| **Initial investment date:** | June 2009 |
| **Cost:** | £275,000 |
| **Valuation:** | £275,000 |
| **Equity held:** | 4.8% |
| **Equity held by all funds managed by Octopus:** | 24.2% |
| **Last audited accounts:** | N/A |

**Further information can be found at the company's website www.graze.com**

## Phase Vision Limited

Phase Vision is a manufacturer of optical inspection solutions for high-speed, three-dimensional shape measurement with micro-scale accuracy. The company has developed (and patented) a unique optical approach to the measurement of very large (>100cm) industrial items with free-form or curved surfaces, such as ship propellers and aircraft wings to tighten manufacturing tolerances, increase throughput and reduce waste.

Phase Vision's metrology solutions are more cost efficient than current laser processes, and accurately measure mechanical systems to micron level, thus providing superior performance. Phase Vision's systems use a fringe projection approach and comprise of one or more projector/camera units that project, and image, patterns of light onto the object to be measured. Sophisticated algorithms are then used to accurately calculate the dimension of the object. Phase Vision's clients include some of the biggest names in the automotive, aerospace, chemical and medical device engineering sectors. The market for large-scale measurement with micro-scale accuracy is estimated to be worth around £2 billion per year, with growth of around 6% per annum.

Since Octopus' investment, the business has strengthened its organisational structure, and built more robust manufacturing and financial controls into its processes. Development of the product continues and nears completion, while the management are also gaining increased traction with another large tier one potential customer.

| | |
|---|---|
| **Initial investment date:** | May 2009 |
| **Cost:** | £199,984 |
| **Valuation:** | £199,984 |
| **Equity held:** | 8.9% |
| **Equity held by all funds managed by Octopus:** | 49.0% |
| **Last audited accounts:** | N/A |

**Further information can be found at the company's website www.phasevision.com**

### Phasor Solutions Limited

Phasor provides flat panel phased array antennae at a fraction of the cost associated with traditional phased array technology. Phased array products are groups of antennae constituting a radar system that enhances and controls signal strength. They are used across many industries, including travel and engineering and can facilitate communication signals. Phasor has the potential to transform the 'communication on the move' market through its phased array product offering. Phasor develops phased array antennae with multiple commercial uses, which include enabling moving host units, such as trains and airplanes, to deliver broadband Internet access and high-speed communications. Additionally, Phasor's product range, which will be expanded to include radars, has numerous other applications in both the aerospace and military sectors.

Phasor received its first production chips from the foundry and the team have been testing these together with a specialist semiconductor design consultancy. Whilst this is a time delay, the effect on cash flow is less significant than expected.

**Initial investment date:** March 2009
**Cost:** £99,992
**Valuation:** £74,994
**Equity held:** 2.0%
**Equity held by all funds managed by Octopus:** 30.7%
**Last audited accounts:** N/A

**Further information can be found at the company's website www.phasorsolutions.com**

### The Skills Market Limited (trading as iProfile)

The company, formerly known as SkillsMarket, works with recruiters to make the business of finding and placing the right people a lot simpler and quicker. The company's website enables candidates to transform any static CV into a dynamic professional profile kept up-to-date by candidates themselves. The aim of iProfile is to bring the traditional CV template into the 21st Century.

Recruiters save time and money on CV processing by searching up-to-date databases and unleash the potential of candidate information - making it more accurate and responsive, with the ability to search and sort in real-time, transforming the efficiency of recruitment processes.

The company was affected by the economic environment and therefore required an injection of capital. Titan 2 invested at this time in order to take advantage of a turnaround in the company and the general recruiting market.

**Initial investment date:** July 2009
**Cost:** £100,000
**Valuation:** £50,000
**Equity held:** 4.9%
**Equity held by all funds managed by Octopus:** 15.7%
**Last audited accounts:** N/A

**Further information can be found at the company's website www.iprofile.com**

# INVESTMENT MANAGER'S REVIEW (continued)

## The Key Revolution Limited

The work of The Key Revolution heralded the move towards 'cloud computing'. Its patented technology enables Internet users to securely authenticate themselves and access their own files on any computer, then clear their text or data. The highly innovative Mobiu key device combines both SIM card and chip and pin features. Lost or stolen Mobiu keys can also be deactivated, ensuring total security.

Unfortunately, it took The Key Revolution longer to establish itself in the market place than previously anticipated, predominantly due to the poor economic environment and the company struggled to make sales. Titan 2 loaned the business £75,000 in August 2009 to afford it time to secure additional funding from an alternative investor. Unfortunately, despite initial positive messages, no funding was found. As such, the company has unfortunately had to take the decision to be placed into administration in December 2009.

| | |
|---|---|
| **Initial investment date:** | May 2008 |
| **Cost:** | £641,026 |
| **Valuation:** | £0 |
| **Equity held:** | 12.4% |
| **Equity held by all funds managed by Octopus:** | 35.9% |
| **Last audited accounts:** | 31 March 2009 |
| **Loss before interest:** | (£1,317,418) |
| **Net assets:** | £173,595 |

**Further information can be found at the company's website www.thekeyrevolution.com**

## How Octopus creates and delivers value for the shareholders of Octopus Titan VCT 2 plc

Octopus Titan VCT 2 plc focuses on providing early stage, development and expansion funding to predominantly unquoted companies with a typical deal size of £0.2 million to £2 million, in aggregate from the four Titan funds managed by Octopus. The focus is on establishing a portfolio of Qualifying Investments in companies that have the potential to achieve a high level of profitability through the combination of:

**Scalability**
The potential to deliver services to significant numbers of new customers at very low incremental cost and to generate repeat sales from customers.

**Scope**
The ability to expand into complementary areas by leveraging customer and/or distributor relationships, new product development or brand positioning.

**Pricing power**
An ability to charge high and defensible prices for its products or services as a result of having intellectual property rights, a strong brand and/or a dominant position in a market niche.

The Investment Manager looks to identify opportunities where the people involved – the entrepreneur, management team, investors, advisers and any other significant stakeholders – have a record of success. Although the Fund has the ability to invest across a wide range of industries, the focus will be on several principal sectors:

- environment
- technology
- media
- telecoms
- consumer lifestyle and wellbeing.

## Investment Process

The Investment Manager follows a multi-stage process prior to making Qualifying Investments in unquoted companies.

**Initial screening**
If the initial review of the business plan is positive, a meeting is held with the management team of the business in order to assess the team in terms of its ability to achieve the objectives set out in the business plan. The proposition is then discussed and reviewed with the other members of the Octopus team and a decision is taken as to whether to continue discussions with the company with a view to making an investment.

**Due diligence**
Prior to making an investment, due diligence is carried out on the potential investee company. The due diligence process includes a review of the investee company's technology, discussions with customers and suppliers, competitive analysis, assessment of the capabilities of the management team and financial analysis. In addition, the input of existing Octopus clients is also sought, where appropriate, as the client base may include individuals who have or have had senior roles in a range of organisations giving them industry knowledge and experience that is relevant to an assessment of the capabilities of the potential investee company.

Additionally, Octopus also draws on professional input from lawyers, accountants and other specialists as required in order to conduct the due diligence and draw up the required legal documentation in order to complete an investment.

**Post-investment monitoring**
Octopus will usually appoint a director to the board of each investee company. The majority of the investments are expected to be held for approximately five years. There may, however, be opportunities to exit profitably on shorter timescales. The Investment Manager will conduct a regular review of the portfolio, during which each investee company will be assessed in terms of its commercial and financial progress, its strategic positioning, requirement for further capital, progress towards an eventual exit and its current and prospective valuation.

As each company matures, the exit considerations become more specific, with a view to establishing a definitive action plan in order to achieve a successful sale of the investment. Throughout the cycle of an investment the Investment Manager will remain proactive in determining the appropriate time and route to exit. It is expected that the majority of exits will be by means of trade sale.

# DETAILS OF DIRECTORS

### John Hustler
### (Non-Executive Chairman – Age 63)

John joined Peat Marwick, now KPMG, in 1965 and became a Partner in 1983. Since leaving KPMG in 1993 to form Hustler Venture Partners Limited, he has advised and been a director of a number of growing companies. He is presently Chairman of Northern Venture Trust plc, a director of Northern 3 VCT plc and Hygea VCT plc and Chairman of Renaissance Re Syndicate Management Limited. He was also a member of the Council of The Institute of Chartered Accountants in England and Wales and Chairman of its Corporate Finance Faculty from 1997-2000 and is a member of the Council of the British Venture Capital Association.

### Mark Faulkner
### (Non-Executive Director – Age 42)

Mark has worked in finance for more than twenty years. In 1991, Mark founded a financial advisory firm providing investment advice to high net worth individuals. This firm merged with Roundhouse Financial Services LLP in 2000 and Mark is now a principal partner of the combined business. In 2003, he co-founded Hibridge Capital, a specialist investment firm that combines investment banking and private client financial advisory expertise in one entity.

### Matt Cooper
### (Non-Executive Director – Age 43)

Matt is the Chairman of Octopus Investments. Prior to joining Octopus, Matt was the Principal Managing Director of Capital One Bank (Europe) plc where he was responsible for all aspects of the company's strategic direction and day-to-day operations in Europe. He led the UK portion of the business from start-up to two million customers, generating revenues of over £275 million and employing over 2,000 people. Matt is also Chairman of Perfect Pizza Limited and Imaginatik Plc and a non-executive director of 10Duke Software Limited, MyDish Limited, Global Collect and nine other VCTs.

# DIRECTORS' REPORT

The Directors present their report and the audited financial statements for the year ended 31 October 2009.

The Board announced on 20 October 2009 that the Investment Management Agreement between Titan 2 and Octopus Ventures Limited had been novated to Octopus Investments Limited. This change was made as a result of an internal reorganisation of the Octopus group and shareholders were advised that the terms of the Investment Management Agreement and the composition of the fund management team within Octopus that has responsibility for managing the Company's assets remained unchanged.

This report has been prepared by the Directors in accordance with the requirements of s415 of the Companies Act 2006. The Company's independent auditor is required by law to report on whether the information given in the Directors' Report (including the Business Review) is consistent with the financial statements. The auditor's opinion is included in their report on page 31.

## Principal Activity and Status

The principal activity of the Company is to invest in a diversified portfolio of UK smaller companies in order to generate capital growth over the long-term as well as an attractive tax-free dividend stream. The Company has been granted provisional approval as a VCT by HMRC.

In order to maintain approved status, the Company must comply on a continuing basis with the provisions of s274 of the Income Tax Act 2007. By the end of the third accounting period, the Company is required to hold at least 70% of its investments (as defined in the legislation) in VCT qualifying holdings, of which at least 30% must comprise eligible Ordinary shares.

For this purpose, a 'VCT qualifying holding' consists of up to £1 million invested in any one year in new shares or securities of a UK-quoted company (which may be quoted on AIM) or unquoted company which is carrying on a qualifying trade, and whose gross assets and number of employees at the time of investment do not exceed a prescribed limit. The definition of 'qualifying trade' excludes certain activities such as property investment and development, financial services and asset leasing.

The Directors are required by the Articles of Association to propose an Ordinary Resolution at the Company's Annual General Meeting in 2018 that the Company should continue as a VCT for a further five-year period, and at each fifth subsequent Annual General Meeting thereafter. If any such Resolution is not passed, the Directors shall within four months convene a general meeting to consider the proposals for the reorganisation or winding-up of the Company.

## Review of Business Activities

The Directors are required by s417 of the Companies Act 2006 to include a Business Review to shareholders. The Business Review is set out below and also includes the Chairman's Statement on pages 6 and 7, and the Investment Manager's Review on pages 8 to 17 by reference.

The purpose of this review is to provide shareholders with a snapshot summary setting out the business objectives of the Company, the Board's strategy to achieve those objectives, the risks faced, the regulatory environment and the key performance indicators used to measure performance.

The following events occurred between the balance sheet date and the signing of these financial statements:

- 8 January 2010: £499,998 investment into Calastone
- 9 January 2010: A previous £201,440 non-qualifying investment in Zoopla became qualifying.

## Performance and Key Performance Indicators

As a VCT, the Company's objective is to provide shareholders with an attractive income and capital return by investing its funds in a broad spread of unquoted UK companies which meet the relevant criteria for VCTs. The Board has a number of performance measures to assess the Company's success in meeting its objectives.

Performance, measured by the change in NAV and total return per share, is also measured against the FTSE All-Share index and the FTSE UK Smaller Companies index. This is shown in the graphs on page 29 of the Directors' Remuneration Report. These indices have been adopted as an informal benchmark. Investment performance, cash returned to shareholders and share price are also measured against the Company's peer group of the other generalist VCTs.

The Chairman's Statement, on pages 6 to 7, includes a review of the Company's activities and future prospects; further details are also provided within the Investment Manager's Review on pages 8 to 17.

# DIRECTORS' REPORT (continued)

**Results and dividend**

| | Year ended 31 October 2009 £'000 | Period Ended 31 October 2008 £'000 |
|---|---|---|
| Net return attributable to shareholders | 1,133 | (722) |
| Appropriations: Final dividend proposed 0.5p (2008 – 0.5p) per share | 77 | 78 |

The proposed final dividend will, if approved by shareholders, be paid on 23 April 2010 to shareholders on the register on 5 March 2010.

## Objective and Investment Policy

The objective of the Company is to invest in a broad range of UK smaller companies in order to generate income and capital growth over the long-term. The Company's investment strategy is designed to deliver absolute returns on its investments rather than a performance measured against the market indices. On an ongoing basis, it is intended that approximately 80% of the Company will be invested in qualifying holdings across a range of sectors, with the remainder held in cash, OEICs and money market securities.

The Directors control the overall risk of the portfolio by ensuring that the Company has exposure to a diversified range of companies from a number of different sectors. In order to limit the risk to the portfolio that is derived from any particular investment, no more than 15% of the Company will be invested in any one investment.

The Company will not borrow money for the purposes of making investments. The investment decisions made must adhere to the HMRC qualification rules as stated in the above section. The Directors will continually monitor the investment process and ensure compliance with the investment policy. Further details of the Company's risk management policies are provided in note 16 to the financial statements.

No material changes may be made to the Company's investment policy described above without the prior approval of shareholders by the passing of an Ordinary Resolution.

## VCT Regulation

Compliance with required rules and regulations is considered with all investment decisions made. The company is further monitored on a continual basis to ensure compliance. The main criteria to which the company must adhere include:

- at least 70% of investments must be made in qualifying shares or securities
- at least 30% of the 70% of qualifying investments must be invested into Ordinary shares with no preferential rights
- no single investment made can exceed 15% of the total company value
- a minimum of 10% of each qualifying investment must be in Ordinary shares with no preferential rights.

## Principal Risks, Risk Management and Regulatory Environment

The Board carries out a regular review of the risk environment in which the Company operates. The main areas of risk identified by the Board are as follows:

**VCT qualifying status risk:** the Company is required at all times to observe the conditions laid down in the Income Tax Act 2007 for the maintenance of approved VCT status. The loss of such approval could lead to the Company losing its exemption from corporation tax on capital gains, to investors being liable to pay income tax on dividends received from the Company and, in certain circumstances, to investors being required to repay the initial income tax relief on their investment.

The Investment Manager keeps the Company's VCT qualifying status under continual review and reports to the Board regularly throughout the year. The Board has also retained PricewaterhouseCoopers LLP to undertake an independent VCT status monitoring role.

**Investment risk:** the majority of the Company's investments will be in small- and medium-sized companies which are VCT-qualifying holdings, which by their nature entail a higher level of risk and lower liquidity than investments in large quoted companies.

The Directors and the Manager aim to limit the risk attached to the portfolio as a whole by careful selection and timely realisation of investments, by carrying out rigorous due diligence procedures and by maintaining a wide spread of holdings in terms of financing stage, industry sector and geographical location. The Board reviews the investment portfolio with the Manager on a regular basis.

**Financial risk:** as most of the Company's investments involve medium- to long-term commitment and are relatively illiquid, the Directors consider that it is inappropriate to finance the Company's activities through borrowing. Accordingly, they seek to maintain a proportion of the Company's assets in cash or cash equivalents in order to be in a position to take advantage of new investment opportunities.

The Company has very little exposure to foreign currency risk and does not enter into derivative transactions. The Company has cash deposits which are held on the balance sheet of HSBC Bank plc and in cash funds managed by Goldman Sachs. The risk of loss to this cash is deemed to be low.

**Regulatory:** the Company is required to comply with the Companies Act, the rules of the UK Listing Authority and United Kingdom Accounting Standards. Breach of any of these might lead to suspension of the Company's Stock Exchange listing, financial penalties or a qualified audit report.

**Reputational:** inadequate or failed controls might result in breaches of regulation or loss of shareholder trust.

**Competitive risk:** retention of key personnel within Octopus is vital to the success of the Company. Incentives to the Manager's key staff are continuously monitored.

**Internal control risk:** the Board reviews annually the system of internal controls, financial and non-financial, operated by the Company and the Manager. These include controls designed to ensure that the Company's assets are safeguarded and that proper accounting records are maintained.

The Board seeks to mitigate the internal risks by setting policy, regular review of performance, enforcement of contractual obligations and monitoring progress and compliance. In the mitigation and management of these risks, the Board applies rigorously the principles detailed in the 'Turnbull' guidance. Details of the Company's internal controls are contained in the Corporate Governance section on pages 24 to 27.

Further details of the Company's risk management policies are provided in note 16 to the financial statements.

## Directors

The Directors of the Company during the period and their interests (in respect of which transactions are notifiable under Disclosure and Transparency Rule 3.1.2R) in the issued Ordinary shares of 10p are shown in the table below:

| | 31 October 2009 | 31 October 2008 |
|---|---|---|
| John Hustler (Chairman) | 5,275 | 5,275 |
| Mark Faulkner | 5,275 | 5,275 |
| Matt Cooper | 5,275 | 5,275 |

All of the Directors' shares were held beneficially. There have been no changes in the Directors' share interests between 31 October 2009 and the date of this report.

John Hustler retires by rotation and, being eligible, offers himself for re-election. The Board has considered provision A.7.2 of the Combined Code 2008 and believes that Mr Hustler continues to be effective and to demonstrate commitment to his role, the Board and the Company. The Board therefore has no hesitation in recommending him for re-election at the forthcoming Annual General Meeting.

Brief biographical notes on the Directors are given on page 18.

## Directors' and Officers' Liability Insurance

The Company has maintained directors' and officers' liability insurance cover on behalf of the Directors and Company Secretary. The Company's Articles of Association, provide, subject to provisions of UK legislation, an indemnity for directors in respect of costs which they may incur relating to the defence of any proceedings brought against them arising out of their positions as directors, in which they are acquitted or judgement is given in their favour by the Court.

## Whistleblowing

The Board has considered and implemented arrangements in accordance with the Combined Code's recommendations, to encourage staff of the Manager or Secretary of the Company to raise concerns, in confidence, within their organisation about possible improprieties in matters of financial reporting or other matters. It is therefore satisfied that adequate arrangements are in place to allow an independent investigation, and follow on action where necessary, to take place within the organisation.

## Management

Octopus Investments Limited acts as Investment Manager to the Company. The principal terms of the Company's management agreement with Octopus are set out in notes 3 & 19 to the financial statements.

Matt Cooper is Chairman of Octopus Investments Limited, which also provides secretarial, administrative and custodian services to the Company. Liquid resources (being cash, OEICs and money market securities) are managed by Goldman Sachs International and Octopus Investments Limited.

As required by the Listing Rules, the Directors confirm that, in their opinion, the continuing appointment of Octopus as Investment Manager is in the best interest of the shareholders as a whole. In reaching this conclusion the Directors have taken into account the performance of the investment portfolio and the efficient and effective service provided by Octopus to the Company.

The Company has established a performance incentive scheme whereby the Investment Manager is entitled to an annual performance-related incentive fee in the event that certain performance criteria are met, commencing at the end of the 2011 financial year. Further details of this scheme are disclosed within note 19 to the financial statements. Given the current economic climate, the Directors do not anticipate that the criteria will be met in the medium term.

# DIRECTORS' REPORT (continued)

## Share Issues and Open Offers

There are no open offers and no shares were issued in the year.

## Share Buy Backs

No buy backs were made during the year.

## Share Capital, Rights Attaching to the Shares and Restrictions on Voting and Transfer

The Company's Ordinary share capital as at 31 October 2009 is 15,616,881 Ordinary share of 10p each.

Subject to any suspension or abrogation of rights pursuant to relevant law or the Company's Articles of Association, the shares confer on their holders the following principal rights:

(a) the right to receive out of profits available for distribution such dividends as may be agreed to be paid (in the case of a final dividend in an amount not exceeding the amount recommended by the Board as approved by shareholders in a general meeting or in the case of an interim dividend in an amount determined by the Board). All dividends unclaimed for a period of 12 years after having become due for payment are forfeited automatically and cease to remain owing by the Company;

(b) the right, on a return of assets on a liquidation, reduction of capital or otherwise, to share in the surplus assets of the Company remaining after payment of its liabilities pari passu with the other holders of Ordinary shares; and

(c) the right to receive notice of and to attend and speak and vote in person or by proxy at any general meeting of the Company.

On a show of hands every member present or represented and voting has one vote and on a poll every member present or represented and voting has one vote for every share of which that member is the holder; the appointment of a proxy must be received not less than 48 hours before the time of the holding of the relevant meeting or adjourned meeting or, in the case of a poll taken otherwise than at or on the same day as the relevant meeting or adjourned meeting, be received after the poll has been demanded and not less than 24 hours before the time appointed for the taking of the poll.

These rights can be suspended. If a member, or any other person appearing to be interested in shares held by that member, has failed to comply within the time limits specified in the Company's Articles of Association with a notice pursuant to s793 of the Companies Act 2006 (notice by the Company requiring information about interests in its shares), the Company can until the default ceases suspend the right to attend and speak and vote at a general meeting and if the shares represent at least 0.25% of their class the Company can also withhold any dividend or other money payable in respect of the shares (without any obligation to pay interest) and refuse to accept certain transfers of the relevant shares.

Shareholders, either alone or with other shareholders, have other rights as set out in the Company's Articles of Association and in company law.

A member may choose whether his shares are evidenced by share certificates (certificated shares) or held in electronic (uncertificated) form in CREST (the UK electronic settlement system). Any member may transfer all or any of his shares, subject in the case of certificated shares, to the rules set out in the Company's Articles of Association or in the case of uncertificated shares to the regulations governing the operation of CREST (which allow the Directors to refuse to register a transfer as therein set out); the transferor remains the holder of the shares until the name of the transferee is entered in the Register of Members.

The Directors may refuse to register a transfer of certificated shares in favour of more than four persons jointly or where there is no adequate evidence of ownership or the transfer is not duly stamped (if so required). The Directors may also refuse to register a share transfer if it is in respect of a certificated share which is not fully paid up or on which the Company has a lien provided that, where the share transfer is in respect of any share admitted to the Official List maintained by the UK Listing Authority, any such discretion may not be exercised so as to prevent dealings taking place on an open and proper basis, or if in the opinion of the Directors (and with the concurrence of the UK Listing Authority) exceptional circumstances so warrant, provided that the exercise of such power will not disturb the market in those shares. Whilst there are no squeeze-out and sell out rules relating to the shares in the Company's Articles of Association, shareholders are subject to the compulsory acquisition provisions in s974 to s991 of the Companies Act 2006.

## Appointment and Replacement of Directors

A person may be appointed as a Director of the Company by the shareholders in a general meeting by Ordinary Resolution (requiring a simple majority of the persons voting on the relevant Resolution) or by the Directors; no person, other than a Director retiring by rotation or otherwise, shall be appointed or reappointed a Director at any general meeting unless he is recommended by the Directors or, not less than seven nor more than 42 clear days before the date appointed for the meeting, notice is given to the

Company of the intention to propose that person for appointment or re-appointment in the form and manner set out in the Company's Articles of Association.

Each Director who is appointed by the Directors (and who has not been elected as a Director of the Company by the members at a general meeting held in the interval since his appointment as a Director of the Company) is to be subject to election as a Director of the Company by the members at the first Annual General Meeting of the Company following his appointment. At each Annual General Meeting of the Company one-third of the Directors for the time being, or if their number is not three or an integral multiple of three the number nearest to but not exceeding one-third, are to be subject to re-election.

The Companies Act allows shareholders in a general meeting by Ordinary Resolution (requiring a simple majority of the persons voting on the relevant Resolution) to remove any Director before the expiration of his or her period of office, but without prejudice to any claim for damages which the Director may have for breach of any contract of service between him or her and the Company.

A person also ceases to be a Director if he or she resigns in writing, ceases to be a Director by virtue of any provision of the Companies Act, becomes prohibited by law from being a Director, becomes bankrupt or is the subject of a relevant insolvency procedure, or becomes of unsound mind, or if the Board so decides following at least six months' absence without leave or if he or she becomes subject to relevant procedures under the mental health laws, as set out in the Company's Articles of Association.

## Powers of the Directors

Subject to the provisions of the Companies Act, the Memorandum and Articles of Association of the Company and any directions given by shareholders by Special Resolution, the Articles of Association specify that the business of the Company is to be managed by the Directors, who may exercise all the powers of the Company, whether relating to the management of the business or not. In particular the Directors may exercise on behalf of the Company its powers to purchase its own shares to the extent permitted by shareholders.

## International Financial Reporting Standards

As the Company is not part of a group it is not mandatory for it to comply with International Financial Reporting Standards. The Company does not anticipate that it will voluntarily adopt International Financial Reporting Standards.

## Creditor Payment Policy

The Company's payment policy for the forthcoming financial year is to agree terms of payment before business is transacted and to settle accounts in accordance with those terms. The Company does not follow any code or standard with regard to creditor payment practice. At 31 October 2009 there were £nil trade creditors (2008: £nil).

## Environmental Policy

The company always makes full effort to conduct its business in a manner that is responsible to the environment. This responsibility is always maintained in investment decisions where possible.

## Going Concern

The Company's business activities and the factors likely to affect its future performance and position are set out in the Chairman's Statement and Investment Manager's Review on pages 6 to 17. Further details on the management of financial risk may be found in note 16 to the Financial Statements.

The Board receives regular reports from the Manager and the Directors believe that, as no material uncertainties leading to significant doubt about going concern have been identified, it is appropriate to continue to adopt the going concern basis in preparing the financial statements.

The assets of the Company consist mainly of securities which are readily realisable and, accordingly, the Company has adequate financial resources to continue in operational existence for the foreseeable future.

## Substantial Shareholdings

As at the date of this report, no disclosures of major shareholdings had been made to the Company under Disclosure and Transparency Rule 5 (Vote Holder and Issuer Notification Rules).

## Annual General Meeting

Notice convening the 2010 Annual General Meeting of the Company and a form of proxy in relation to the meeting can each be found at the end of this document.

## Independent Auditor

Grant Thornton UK LLP offer themselves for re-appointment as auditor. A Resolution to re-appoint Grant Thornton UK LLP will be proposed at the forthcoming Annual General Meeting.

## Directors' Authority to Allot Shares, to Disapply Pre-Emption Rights

The authority proposed under Resolution 6 is required so that the Directors may offer existing shareholders the opportunity to add to their investment or to offer to potential shareholders an opportunity to invest in the Company in a tax-efficient manner without the Company having to incur substantial costs. Any consequent modest increase in the size of the Company will, in the opinion of the Directors, be in the interests of shareholders generally. Any issue proceeds will be available for investment in line with the Company's

# DIRECTORS' REPORT (continued)

investment policy and may be used, in part, to purchase Ordinary shares in the market.

Resolution 6 renews the Directors' authority to allot Ordinary shares. This would enable the Directors until April 2011, to allot up to 1,561,688 Ordinary shares (representing approximately 10% of the Company's issued share capital as at 31 October 2009).

Resolution 7 renews and extends the Directors' authority to allot equity securities for cash without pre-emption rights applying in certain circumstances. This Resolution would authorise the Directors, until the date falling 15 months after the date of the passing of the Resolution or, if earlier, the conclusion of the next Annual General Meeting of the Company, to issue Ordinary shares for cash without pre-emption rights applying by way of an offer to existing shareholders, or re-issuing shares out of Treasury up to a maximum of 1,561,688 Ordinary shares (representing approximately 10% of the Company's issued share capital as at 31 October 2009). This power will be exercised only if, in the opinion of the Directors, it would be in the best interests of shareholders, as a whole.

## Directors' Authority to Make Market Purchase of its Own Shares

The authority proposed under Resolution 8 is required so that the Directors may make purchases of up to approximately 5% of the Company's issued share capital and Resolution 8 seeks renewal of such authority until the next Annual General Meeting (or the expiry of 15 months, if earlier). The price paid for shares will not be less than the nominal value nor more than the maximum amount permitted to be paid in accordance with the rules of the UK Listing Authority in force as at the date of purchase. This power will be exercised only if, in the opinion of the Directors, a repurchase would be in the best interests of shareholders as a whole. Any shares repurchased under this authority will either be cancelled or held in Treasury for future re-sale in appropriate market conditions.

## Corporate Governance

The Board of Octopus Titan VCT 2 plc has considered the principles and recommendations of the Association of Investment Companies Code of Corporate Governance (AIC Code) by reference to the Association of Investment Companies Corporate Governance Guide for Investment Companies (AIC Guide).

The AIC Code, as explained by the AIC Guide, addresses all the principles set out in the 2008 Combined Code, as well as setting out additional principles and recommendations on issues that are of specific relevance to the Company. The Board considers that reporting against principles and recommendations of the AIC Code, by reference to the AIC Guide (which incorporates the Combined Code), will provide better information to shareholders.

The Company is committed to maintaining high standards in corporate governance. The Directors consider that the Company has, throughout the period under review, complied with the provisions set out in the 2008 Combined Code on Corporate Governance with the exceptions set out in the Compliance Statement on page 26.

## Board of Directors

The Company has a Board of three non-executive Directors, two of whom are considered to be independent. Matt Cooper is not considered to be independent due to his role as Chairman of the Company's Investment Manager. The Board meets regularly on a quarterly basis, and on other occasions as required, to review the investment performance and monitor compliance with the investment policy laid down by the Board.

The Board has a formal schedule of matters specifically reserved for its decision which include:

- the consideration and approval of future developments or changes to the investment policy, including risk and asset allocation;
- consideration of corporate strategy;
- approval of the appropriate dividend to be paid to the shareholders;
- the appointment, evaluation, removal and remuneration of the Manager;
- the performance of the Company, including monitoring of the discount of the NAV to the share price; and
- monitoring shareholder profiles and considering shareholder communications.

The Chairman leads the Board in the determination of its strategy and in the achievement of its objectives. The Chairman is responsible for organising the business of the Board, ensuring its effectiveness and setting its agenda, and has no involvement in the day-to-day business of the Company. He facilitates the effective contribution of the Directors and ensures that they receive accurate, timely and clear information and that they communicate effectively with shareholders.

The Company Secretary is responsible for advising the Board through the Chairman on all governance matters. All of the Directors have access to the advice and services of the Company Secretary, who has administrative responsibility for the meetings of the Board and its committees. Directors may also take independent professional advice at the Company's expense where necessary in the performance of their duties.

The Company's Articles of Association and the schedule of matters reserved to the Board for decision provide that the appointment and removal of the Company Secretary is a matter for the full Board.

During the year the following were held:

| | Full Board meetings held | No. of meetings attended | Audit Committee meetings held | Audit Committee meetings attended |
|---|---|---|---|---|
| John Hustler | 5 | 5 | 2 | 2 |
| Mark Faulkner | 5 | 4 | 2 | 2 |
| Matt Cooper | 5 | 3 | 2 | N/A |

Additional meetings were held as required to address specific issues including considering recommendations from the Investment Manager. A brief biographical summary of each Director is given on page 18.

The Company's Articles of Association require that one third of Directors should retire by rotation each year and seek re-election at the Annual General Meeting, and that Directors appointed by the Board should seek re-appointment at the next Annual General Meeting. All Directors are required to submit themselves for re-election at least every three years. This practice was followed during the year under review.

| | Date of Original Appointment | Due date for Re-election |
|---|---|---|
| John Hustler | 31/10/2008 | AGM 2010 |
| Mark Faulkner | 31/10/2008 | AGM 2011 |
| Matt Cooper | 31/10/2008 | AGM 2012 |

The Board has appointed two committees to make recommendations to the Board in specific areas:

## Audit Committee:

**Mark Faulkner**
**John Hustler**

The Audit Committee, chaired by Mark Faulkner, consists of two independent Directors. The Audit Committee believes Mark Faulkner possesses appropriate and relevant financial experience as per the requirements of the Combined Code. The Board considers that the members of the Committee are independent and have collectively the skills and experience required to discharge their duties effectively.

The Audit Committee's terms of reference include the following roles and responsibilities:

- reviewing and making recommendations to the Board in relation to the Company's published financial statements and other formal announcements relating to the Company's financial performance;
- reviewing and making recommendations to the Board in relation to the Company's internal control (including internal financial control) and risk management systems;
- periodically considering the need for an internal audit function;
- making recommendations to the Board in relation to the appointment, re-appointment and removal of the external auditor, and approving the remuneration and terms of engagement of the external auditor;
- reviewing and monitoring the external auditor's independence and objectivity and the effectiveness of the audit process, taking into consideration relevant UK professional regulatory requirements;
- monitoring the extent to which the external auditor is engaged to supply non-audit services; and
- ensuring that the Investment Manager has arrangements in place for the investigation and follow-up of any concerns raised confidentially by staff in relation to propriety of financial reporting or other matters.

The Committee reviews its terms of reference and its effectiveness annually and recommends to the Board any charges required as a result of the review. The terms of reference are available on request from the Company Secretary. The Committee meets twice per year and has direct access to Grant Thornton UK LLP, the Company's external auditor. The Audit Committee has reviewed the non-audit services provided by the external auditor and does not believe they are sufficient to influence their independence or objectivity.

The Company does not have an independent internal audit function as it is not deemed appropriate given the size of the Company and the nature of the Company's business. However, the Committee considers annually whether there is a need for such a function and if so would recommend this to the Board.

During the year ended 31 October 2009, the Audit Committee discharged its responsibilities by:

- reviewing and approving the external auditor's terms of engagement and remuneration;
- reviewing the external auditor's plan for the audit of the Company's financial statements, including identification of key risks and confirmation of auditor independence;

# DIRECTORS' REPORT (continued)

- reviewing Octopus Investments Limited's statement of internal controls in relation to the Company's business and assessing the effectiveness of those controls in minimising the impact of key risks;
- reviewing periodic reports on the effectiveness of Octopus Investments Limited's compliance procedures;
- reviewing the appropriateness of the Company's accounting policies;
- reviewing the Company's draft annual financial and interim results statement prior to Board approval; and
- reviewing the external auditor's detailed reports to the Committee on the annual financial statements.

### Nomination Committee:

**John Hustler**
**Mark Faulkner**

The Nomination Committee considers the selection and appointment of Directors and makes recommendations to the Board as to the level of Directors' fees.

It has not yet been necessary for the Committee to meet and so terms of reference will be agreed if and when appropriate. The Board does not have a separate remuneration committee as the Company has no employees or executive Directors. Detailed information relating to the remuneration of Directors is given in the Directors' remuneration report.

### Internal Control

The Directors have overall responsibility for keeping under review the effectiveness of the Company's systems of internal controls. The purpose of these controls is to ensure that proper accounting records are maintained, the Company's assets are safeguarded and the financial information used within the business and for publication is accurate and reliable; such a system can only provide reasonable and not absolute assurance against material misstatement or loss. The system of internal controls is designed to manage rather than eliminate the risk of failure to achieve the business objectives. The Board regularly reviews financial results and investment performance with its Investment Manager.

Octopus identifies the investment opportunities for the consideration of the Board who ultimately makes the decision whether to proceed with that opportunity. Octopus monitors the portfolio of investments and makes recommendations to the Board in terms of suggested disposals and further acquisitions.

Octopus is engaged to carry out the accounting function and retains physical custody of the documents of title relating to unquoted investments. Octopus regularly reconciles the client asset register with the physical documents.

The Directors confirm that they have established a continuing process throughout the year and up to the date of this report for identifying, evaluating and managing the significant potential risks faced by the Company and have reviewed the effectiveness of the internal control systems. As part of this process an annual review of the internal control systems is carried out in accordance with the Financial Reporting Council guidelines for internal control.

Internal control systems include the production and review of monthly bank and management accounts. All outflows made from the VCT's accounts require the authority of two signatories from Octopus. The VCT is subject to a full annual audit whereby the auditor is the same auditor as other VCTs managed by the Investment Manager. Further to this, the Audit Partner has open access to the Directors of the VCT and the Investment Manager is subject to regular review by the Octopus Compliance Department.

### Financial Risk Management Objectives and Policies

The Company is exposed to the risks arising from its operational and investment activities. Further details can be found in note 16 to the financial statements.

### Relations with Shareholders

Shareholders have the opportunity to meet the Board at the Annual General Meeting. In addition to the formal business of the Annual General Meeting, the Board is available to answer any questions a shareholder may have.

The Board is also happy to respond to any written queries made by shareholders during the course of the year and can be contacted at 8 Angel Court, London, EC2R 7HP. Alternatively, the team at Octopus is happy to answer any questions you may have and can be contacted on 0800 316 2396.

### Compliance Statement

The Listing Rules require the Board to report on compliance with the 48 Combined Code provisions throughout the accounting year. The preamble to the Combined Code does, however, acknowledge that some provisions may have less relevance for investment companies. With the exception of the limited items outlined below, the Company has complied throughout the accounting year to 31 October 2009 with the provisions set out in the 2008 Combined Code.

1. New Directors do not receive a full, formal and tailored induction on joining the Board. Such matters are addressed on an individual basis as they arise.

2. Due to the size of the Board and the nature of the Company's business, a formal performance evaluation process for the Board, its committees, the individual Directors and the Chairman has not been put in place or a formal evaluation been undertaken. Specific performance issues are dealt with as they arise.

3. The Company has two independent Directors, John Hustler and Mark Faulkner as defined by the Combined Code issued in 2008. Matt Cooper holds directorships of other companies with the same Investment Manager and with the Investment Manager itself. The Board considers that all Directors have sufficient experience to be able to exercise proper judgement within the meaning of the Combined Code.

4. The Company does not have a Chief Executive Officer or senior independent Director. The Board does not consider this necessary for the size of the Company.

5. The Company conducts a formal review as to whether there is a need for an internal audit function. However, the Directors do not consider that an internal audit would be an appropriate control for a VCT.

6. The non-executive Directors do not have service contracts, whereas the recommendation is for fixed-term renewable contracts.

7. The Company has no major shareholders so shareholders are not given the opportunity to meet any new non-executive Directors at a specific meeting other than the Annual General Meeting.

8. The Company does not have a remuneration committee given the size of the Company and as such the whole board deal with any matters of this nature.

By order of the Board

Celia L Whitten, FCIS
Company Secretary
3 February 2010

# DIRECTORS' REMUNERATION REPORT

## Introduction

This report is submitted in accordance with s420 - 422 of the Companies Act 2006, in respect of the year ended 31 October 2009. An Ordinary Resolution for the approval of this report will be put to the members at the forthcoming Annual General Meeting.

The Company's auditor, Grant Thornton UK LLP, is required to give its opinion on certain information included in this report; this comprises the Directors' emoluments section below only. Their report on these and other matters is set out on page 31.

## Consideration by the Directors of Matters Relating to Directors' Remuneration

The Board as a whole considers Directors' remuneration and has not appointed a separate committee in this respect. The Board has not sought advice or services from any person in respect of its consideration of Directors' remuneration during the year (although the Directors expect from time to time to review the fees against those paid to the boards of directors of other VCTs).

## Statement of the Company's Policy on Directors' Remuneration

The Board consists entirely of non-executive Directors, who meet at least four times a year and on other occasions as necessary, to deal with the important aspects of the Company's affairs. Directors are appointed with the expectation that they will serve for, at least, a period of three years. All Directors retire at the first general meeting after election and thereafter one third of all Directors are subject to retirement by rotation at subsequent Annual General Meetings. Re-election will be recommended by the Board but dependent upon shareholder vote.

Each Director received a letter of appointment. A Director may resign by notice in writing to the Board at any time. None of the Directors are entitled to compensation payable upon early termination of their contract other than in respect of any unexpired notice period.

The Company's policy is that the fees payable to the Directors should reflect the time spent by the Board on the Company's affairs and the responsibilities borne by the Directors. They should be sufficient to attract candidates of high calibre to be recruited. The policy is for the Chairman of the Board to be paid higher fees than the other Directors in recognition of his more onerous role. The policy is to review these rates from time to time, although such review will not necessarily result in any changes.

The Company's policy is for the Directors to be remunerated in the form of fees, payable quarterly in arrears. The fees are not specifically related to the Directors' performance, either individually or collectively. There are no long-term incentive schemes, share option schemes or pension schemes in place. The Board is also entitled to be repaid all reasonable travelling, subsistence and other expenses incurred by them respectively whilst conducting their duties as Directors, however no other remuneration or compensation was paid or payable by the Company during the year to any of the current Directors.

## Company Performance

The Board is responsible for the Company's investment strategy and performance, although the management of the Company's investment portfolio is delegated to the Investment Manager through the Investment Management Agreement, as referred to in the Directors' Report.

The graph below compares the NAV return and total return (including dividends and up-front tax relief, rebased to 100) of Titan 2 over the period from October 2007 to October 2009, with the total return from a notional investment (rebased to 100) in the FTSE AIM All-Share index and the FTSE SmallCap index over the same period. These indices are considered to be the most appropriate broad equity market indices for comparative purposes. However, the Directors wish to point out that VCTs are not able to make qualifying investments in companies quoted on the main market in their observance of the VCT rules.

## Octopus Titan VCT 2 plc – Portfolio performance

## Directors' Emoluments (Information Subject to Audit)

Amount of each Directors' emoluments:

**Directors' fees**

| | Year ended 31 October 2009 £ | Period ended 31 October 2008 £ |
|---|---|---|
| John Hustler (Chairman) | 15,000 | 13,000 |
| Mark Faulkner | 10,000 | 8,000 |
| Matt Cooper | 8,000 | 7,000 |
| Total | 33,000 | 28,000 |

The Directors do not receive any other form of emoluments in addition to the Directors' fees.

By order of the Board

Celia L Whitten, FCIS
Company Secretary
3 February 2010

# DIRECTORS' RESPONSIBILITY STATEMENT

The Directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable laws and regulations.

Company law requires the Directors to prepare financial statements for each financial year which give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company. Under that law the Directors have elected to prepare financial statements in accordance with United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

In preparing these financial statements, 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 UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping adequate accounting records that disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. 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.

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

Insofar as each of the Director's is aware:

- there is no relevant audit information of which the Company's auditor is unaware;
- the Directors have taken all steps that they ought to have taken to make themselves aware of any relevant audit information and to establish that the auditor is aware of that information.

To the best of my knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company; and
- the management report includes a fair review of the development and performance of the business and the position of the Company, together with a description of the principal risks and uncertainties that it faces.

On behalf of the Board

John Hustler
Chairman
3 February 2010

# REPORT OF THE INDEPENDENT AUDITOR

## Independent auditor's report to the members of Octopus Titan VCT 2 plc

We have audited the financial statements of Octopus Titan VCT 2 plc for the year ended 31 October 2009 which comprise the income statement, the reconciliation of movements in shareholders' funds, the balance sheet, the cash flow statement, and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice - GAAP).

This report is made solely to the Company's members, as a body, in accordance with Sections 495, 496 and 497 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

## Respective Responsibilities of Directors and Auditors

As explained more fully in the Directors' Responsibility Statement set out on page 30, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

## Scope of the Audit of the Financial Statements

A description of the scope of an audit of financial statements is provided on the APB's website at www.frc.org.uk/apb/scope/UKP.

## Opinion of Financial Statements

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 October 2009 and of its profit for the year then ended;
- have been properly prepared in accordance with UK GAAP; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

## Opinion of Other Matters Prescribed by the Companies Act 2006

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

## Matters on Which We Are Required to Report by Exception

We have nothing to report in respect of the following:

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

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

Under the Listing Rules, we are required to review:

- the Directors' Statement, set out on page 23, in relation to going concern; and
- the part of the Corporate Governance Statement relating to the Company's compliance with the nine provisions of the 2008 Combined Code specified for our review.

Tracey James
Senior Statutory Auditor
for and on behalf of Grant Thornton UK LLP
Statutory Auditor, Chartered Accountants
Oxford
3 February 2010

# INCOME STATEMENT

| | Notes | Year to 31 October 2009 Revenue £'000 | Capital £'000 | Total £'000 |
|---|---|---|---|---|
| Loss on disposal of fixed asset investments | 10 | – | (315) | (315) |
| Gain on disposal of current asset investments | 12 | – | 45 | 45 |
| Loss on valuation of fixed asset investments | 10 | – | (206) | (206) |
| Gain on valuation of current asset investments | 12 | – | 1,676 | 1,676 |
| Income | 2 | 437 | – | 437 |
| Investment management fees | 3 | (73) | (208) | (281) |
| Other expenses | 4 | (223) | – | (223) |
| **Return on ordinary activities before tax** | | **141** | **992** | **1,133** |
| Taxation on return on ordinary activities | 6 | – | – | – |
| **Return on ordinary activities after tax** | | **141** | **992** | **1,133** |
| **Earnings per share – basic and diluted** | **8** | **0.9p** | **6.4p** | **7.3p** |

- The 'Total' column of this statement is the profit and loss account of the Company; the supplementary revenue return and capital return columns have been prepared under guidance published by the Association of Investment Companies.
- All revenue and capital items in the above statement derive from continuing operations.
- The accompanying notes are an integral part of the financial statements.
- The Company has only one class of business and derives its income from investments made in shares and securities and from bank and money market funds

The Company has no recognised gains or losses other than the results for the year as set out above.

# INCOME STATEMENT

| | Notes | Period to 31 October 2008 Revenue £'000 | Capital £'000 | Total £'000 |
|---|---|---|---|---|
| Loss on valuation of fixed asset investments | 10 | - | (215) | (215) |
| Loss on valuation of current asset investments | 12 | - | (437) | (437) |
| Income | 2 | 326 | - | 326 |
| Investment management fees | 3 | (55) | (164) | (219) |
| Other expenses | 4 | (177) | - | (177) |
| **Return on ordinary activities before tax** | | **94** | **(816)** | **(722)** |
| Taxation on return on ordinary activities | 6 | - | - | - |
| **Return on ordinary activities after tax** | | **94** | **(816)** | **(722)** |
| **Earnings per share – basic and diluted** | **8** | **1.0p** | **(8.3)p** | **(7.3)p** |

- The 'Total' column of this statement is the profit and loss account of the Company; the supplementary revenue return and capital return columns have been prepared under guidance published by the Association of Investment Companies.
- All revenue and capital items in the above statement derive from continuing operations.
- The accompanying notes are an integral part of the financial statements.
- The Company has only one class of business and derives its income from investments made in shares and securities and from bank and money market funds.

The Company has no recognised gains or losses other than the results for the year as set out above.

# RECONCILIATION OF MOVEMENTS IN SHAREHOLDERS' FUNDS

| | Year ended 31 October 2009 £'000 | Period ended 31 October 2008 £'000 |
|---|---|---|
| Shareholders' funds at start of year | 14,036 | - |
| Return on ordinary activities after tax | 1,132 | (722) |
| Issue of equity (net of expenses) | - | 14,758 |
| Dividends paid | (155) | - |
| **Shareholders' funds at end of period** | **15,014** | **14,036** |

# BALANCE SHEET

| | Notes | As at 31 October 2009 £'000 | £'000 | As at 31 October 2008 £'000 | £'000 |
|---|---|---|---|---|---|
| Fixed asset investments* | 10 | | 4,370 | | 1,837 |
| Current assets: | | | | | |
| Debtors | 11 | 96 | | 162 | |
| Investments* | 12 | 10,069 | | 11,663 | |
| Cash at bank | | 573 | | 461 | |
| | | 10,738 | | 12,286 | |
| Creditors: amounts falling due within one year | 13 | (94) | | (87) | |
| Net current assets | | | 10,644 | | 12,199 |
| **Net assets** | | | **15,014** | | **14,036** |
| Called up equity share capital | 14 | 1,562 | | 1,562 | |
| Share premium | 15 | - | | 13,196 | |
| Special distributable reserve | 15 | 13,196 | | - | |
| Capital reserve – gains and losses on disposals | 15 | (407) | | (164) | |
| – holding gains and losses | 15 | 583 | | (652) | |
| Revenue reserve | 15 | 80 | | 94 | |
| **Total equity shareholders' funds** | | | **15,014** | | **14,036** |
| **Net asset value per share** | **9** | | **96.1p** | | **89.9p** |

*At fair value through profit and loss

The accompanying notes are an integral part of the financial statements.

The statements were approved by the Directors and authorised for issue on 3 February 2010 and are signed on their behalf by:

John Hustler
Chairman

Company No: 06397765

# CASH FLOW STATEMENT

| | Notes | Year to 31 October 2009 £'000 | Period to 31 October 2008 £'000 |
|---|---|---|---|
| **Net cash inflow/(outflow) from operating activities** | | 6 | (145) |
| **Financial investment:** | | | |
| Purchase of fixed asset investments | 10 | (3,054) | (2,052) |
| **Management of funds:** | | | |
| Purchase of current asset investments | 12 | (2,146) | (24,433) |
| Sale of current asset investments | 12 | 5,461 | 12,333 |
| **Dividends paid** | | (155) | - |
| **Financing:** | | | |
| Issue of shares | | - | 15,443 |
| Share issue expenses | | - | (685) |
| **Increase in cash resources at bank** | | **112** | **461** |

# RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET FUNDS

| | Year to 31 October 2009 £'000 | Period to 31 October 2008 £'000 |
|---|---|---|
| Increase in cash resources at bank | 112 | 461 |
| Movement in cash equivalent securities | (1,594) | 11,663 |
| Opening net funds | 12,124 | - |
| **Net funds at 31 October** | **10,642** | **12,124** |

**Net funds at 31 October comprised:**

| | 31 October 2009 £'000 | 31 October 2008 £'000 |
|---|---|---|
| Cash at bank | 573 | 461 |
| Bonds | 4,083 | 6,701 |
| Money market funds | 1,124 | 1,529 |
| OEICs | 4,862 | 3,433 |
| **Net funds at 31 October** | **10,642** | **12,124** |

# RECONCILIATION OF OPERATING PROFIT/(LOSS) BEFORE TAXATION TO CASH FLOW FROM OPERATING ACTIVITIES

| | Year to 31 October 2009 £'000 | Period to 31 October 2008 £'000 |
|---|---|---|
| Return on ordinary activities before tax | 1,133 | (722) |
| Loss on disposal of fixed asset investments | 315 | - |
| Gain on disposal of current asset investments | (45) | - |
| Loss on valuation of fixed asset investments | 206 | 215 |
| (Gain)/loss on valuation of current asset investments | (1,676) | 437 |
| Decrease/(Increase) in debtors | 66 | (162) |
| Increase in creditors | 7 | 87 |
| **Inflow/(outflow) from operating activities** | **6** | **(145)** |

# NOTES TO THE FINANCIAL STATEMENTS

## 1. Principal Accounting Policies

**Basis of accounting**

The financial statements have been prepared under the historical cost convention, except for the measurement at fair value of certain financial instruments, and in accordance with UK Generally Accepted Accounting Practice (UK GAAP), and the Statement of Recommended Practice (SORP) 'Financial Statements of Investment Trust Companies' (revised 2009).

The principal accounting policies have remained unchanged from those set out in the Company's 2008 Annual Report and financial statements. A summary of the principal accounting policies is set out below.

The Company has designated all fixed asset investments as being held at fair value through profit and loss; therefore all gains and losses arising from investments held are attributable to financial assets held at fair value through profit and loss. Accordingly, all interest income, fee income, expenses and impairment losses are attributable to assets designated as being at fair value through profit and loss.

The preparation of the financial statements requires Management to make judgements and estimates that affect the application of policies and reported amounts of assets, liabilities, income and expenses. Estimates and assumptions mainly relate to the fair valuation of the fixed asset investments particularly unquoted investments. Estimates are based on historical experience and other assumptions that are considered reasonable under the circumstances. The estimates and the assumptions are under continuous review with particular attention paid to the carrying value of the investments.

Capital valuation policies are those that are most important to the depiction of the Company's financial position and that require the application of subjective and complex judgements, often as a result of the need to make estimates about the effects of matters that are inherently uncertain and may change in subsequent periods. The critical accounting policies that are declared will not necessarily result in material changes to the financial statements in any given period but rather contain a potential for material change. The main accounting and valuation policies used by the Company are disclosed below. Whilst not all of the significant accounting policies require subjective or complex judgements, the Company considers that the following accounting policies should be considered critical.

Investments are regularly reviewed to ensure that the fair values are appropriately stated. Quoted investments are valued in accordance with the bid price on the relevant date, unquoted investments are valued in accordance with current International Private Equity and Venture Capital ('IPEVC') valuation guidelines, although this does rely on subjective estimates such as appropriate sector earnings multiples, forecast results of investee companies, asset values of subsidiary companies and liquidity or marketability of the investments held.

Although the Company believes that the assumptions concerning the business environment and estimate of future cash flows are appropriate, changes in estimates and assumptions could require changes in the stated values. This could lead to additional changes in fair value in the future.

**Investments**

Purchases and sales of investments are recognised in the financial statements at the date of the transaction (trade date).

These investments will be managed and their performance evaluated on a fair value basis in accordance with a documented investment strategy and information about them has to be provided internally on that basis to the Board. Accordingly, as permitted by FRS 26, the investments will be designated as fair value through profit and loss (FVTPL) on the basis that they qualify as a group of assets managed, and whose performance is evaluated, on a fair value basis in accordance with a documented investment strategy. The Company's investments are measured at subsequent reporting dates at fair value.

In the case of investments quoted on a recognised stock exchange, fair value is established by reference to the closing bid price on the relevant date or the last traded price, depending upon convention of the exchange on which the investment is quoted. This is consistent with the International Private Equity and Venture Capital (IPEVC) guidelines.

# NOTES TO THE FINANCIAL STATEMENTS (continued)

In the case of unquoted investments, fair value is established by using measures of value such as the price of recent transactions, earnings multiple and net assets. This is consistent with IPEVC valuation guidelines.

Gains and losses arising from changes in fair value of investments are recognised as part of the capital return within the income statement and allocated to the capital reserve - holding gains/(losses).

In the preparation of the valuations of assets the Directors are required to make judgements and estimates that are reasonable and incorporate their knowledge of the performance of the investee companies.

**Current asset investments**
Current asset investments comprise money market funds, bonds and OEICs and are designated as FVTPL. Gains and losses arising from changes in fair value of investments are recognised as part of the capital return within the income statement and allocated to the capital reserve - gains/(losses) on disposal.

The current asset investments are all invested with the Company's cash manager and are readily convertible into cash at the choice of the Company. The current asset investments are held for trading, are actively managed and the performance is evaluated on a fair value basis in accordance with a documented investment strategy. Information about them has to be provided internally on that basis to the Board.

**Income**
Investment income includes interest earned on bank balances and money market securities and includes income tax withheld at source. Dividend income is shown net of any related tax credit.

Dividends receivable are brought into account when the Company's right to receive payment is established and there is no reasonable doubt that payment will be received. Fixed returns on debt and money market securities are recognised on a time apportionment basis so as to reflect the effective yield, provided there is no reasonable doubt that payment will be received in due course.

**Expenses**
All expenses are accounted for on an accruals basis. Expenses are charged wholly to revenue with the exception of the investment management fee, which has been charged 25% to the revenue account and 75% to the capital reserve to reflect, in the Directors' opinion, the expected long-term split of returns in the form of income and capital gains respectively from the investment portfolio.

**Revenue and capital**
The revenue column of the income statement includes all income and revenue expenses of the Company. The capital column includes gains and losses on disposal and holding gains and losses on investments. Gains and losses arising from changes in fair value of investments are recognised as part of the capital return within the income statement and allocated to the appropriate capital reserve on the basis of whether they are readily convertible to cash in full at the balance sheet date.

**Taxation**
Corporation tax payable is applied to profits chargeable to corporation tax, if any, at the current rate. The tax effect of different items of income/gain and expenditure/loss is allocated between capital and revenue return on the 'marginal' basis as recommended in the SORP.

Deferred tax is recognised on an undiscounted basis in respect of all timing differences that have originated but not reversed at the balance sheet date. Where transactions or events have occurred at that date that will result in an obligation to pay more, or a right to pay less tax, with the exception that deferred tax assets are recognised only to the extent that the Directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing can be deducted.

**Cash and liquid resources**
Cash, for the purposes of the cash flow statement, comprises cash in hand and deposits repayable on demand, less overdrafts payable on demand. Liquid resources are current asset investments which are disposable without curtailing or disrupting the business and are either readily convertible into known amounts of cash at or close to their carrying values or traded in an active market. Liquid resources comprise term deposits of less than one year (other than cash), government securities, investment grade bonds and investments in money market managed funds, as well as OEICs.

**Loans and receivables**
The Company's loans and receivables are initially recognised at cost and subsequently measured at fair value, being amortised cost using the effective interest rate method.

**Financing strategy and capital structure**
FRS 29 'Financial Instruments: Disclosures' comprises disclosures relating to financial instruments.

We define capital as shareholders' funds and our financial strategy in the medium term is to manage a level of cash that balances the risks of the business with optimising the return on equity. The Company currently has no borrowings nor does it anticipate that it will drawdown any borrowing facilities in the future to fund the acquisition of investments.

**Financial instruments**
The Company's principal financial assets are its investments and the policies in relation to those assets are set out above. Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the entity after deducting all of its financial liabilities. Where the contractual terms of share capital do not have any terms meeting the definition of a financial liability then this is classed as an equity instrument. Dividends and distributions relating to equity instruments are debited direct to equity

Capital management is monitored and controlled using the internal control procedures set out on page 26 of this report. The capital being managed includes equity and fixed-interest investments, cash balances and liquid resources including debtors and creditors.

The company does not have any externally imposed capital requirements.

**Dividends**
Dividends payable are recognised as distributions in the financial statements when the Company's liability to make payment has been established. This liability is established for interim dividends when they are declared by the Board, and for final dividends when they are approved by the shareholders.

## 2. Income

| | **Year to 31 October 2009 £'000** | **Period to 31 October 2008 £'000** |
|---|---|---|
| Money market funds & OEICs | 311 | 174 |
| Bond interest receivable | 118 | 107 |
| Bank interest receivable | – | 45 |
| Loan note interest receivable | 8 | – |
| | **437** | **326** |

## 3. Investment Management Fees

| | **Year to 31 October 2009** | | | **Period to 31 October 2008** | | |
|---|---|---|---|---|---|---|
| | **Revenue £'000** | **Capital £'000** | **Total £'000** | **Revenue £'000** | **Capital £'000** | **Total £'000** |
| Investment management fee | 73 | 208 | 281 | 45 | 135 | 180 |
| Irrecoverable VAT thereon | – | – | – | 10 | 29 | 39 |
| **Total fees** | **73** | **208** | **281** | **55** | **164** | **219** |

For the purposes of the revenue and capital columns in the income statement, the management fee has been allocated 25% to revenue and 75% to capital, in line with the Board's expected long-term return in the form of income and capital gains respectively from the Company's investment portfolio.

Octopus provides investment management and accounting and administration services to the Company under a management agreement. This agreement runs for a period of five years with effect from 2 November 2007 and may be terminated at any time thereafter by not less than 12 months' notice given by either party. No compensation is payable in the event of terminating the agreement by either party, if the required notice period is given. The fee payable, should insufficient notice be given, will be equal to the fee that would have been paid should continuous service be provided, or the required notice period was given. The basis upon which the management fee is calculated is disclosed within note 19 to the financial statements.

In his budget statement on 12 March 2008, the Chancellor of the Exchequer announced that the Finance Act 2008 would contain draft legislation exempting VCTs from VAT on management fees with effect from 1 October 2008. This legislation was passed in October 2008 and, as such, all VCTs are now exempt from paying VAT on management fees from this date.

# NOTES TO THE FINANCIAL STATEMENTS (continued)

## 4. Other Expenses

| | Year to 31 October 2009 £'000 | Period to 31 October 2008 £'000 |
|---|---|---|
| Accounting and administration services | 46 | 32 |
| Directors' remuneration | 33 | 28 |
| Fees payable to the Company's auditor for the audit of the financial statements | 9 | 8 |
| Fees payable to the Company's auditor for other services – tax compliance | 2 | 2 |
| Legal and professional expenses | 1 | 38 |
| Trail commission | 78 | 46 |
| Other expenses | 54 | 23 |
| | **223** | **177** |

Total annual running costs are capped at 3.2% of net assets (excluding irrecoverable VAT). For the year to 31 October 2009 the running costs were 2.7% (2008: 2.1%) of net assets.

## 5. Directors' Remuneration

| | Year to 31 October 2009 £'000 | Period to 31 October 2008 £'000 |
|---|---|---|
| Directors' emoluments | | |
| John Hustler (Chairman) | 15 | 13 |
| Mark Faulkner | 10 | 8 |
| Matt Cooper | 8 | 7 |
| | **33** | **28** |

None of the Directors received any other remuneration from the Company during the year. The Company has no employees other than non-executive Directors. The average number of non-executive Directors in the year was three (2008: three).

## 6. Tax on Ordinary Activities

The corporation tax charge for the period was £nil (2008: £nil).

Factors affecting the tax charge for the current year:
The current tax charge for the period differs from the standard rate of corporation tax in the UK of 28% (2008: 29%).

The differences are explained below.

Current tax reconciliation:

| | Year to 31 October 2009 £'000 | Period to 31 October 2008 £'000 |
|---|---|---|
| Return on ordinary activities before tax | 1,133 | (722) |
| Current tax at 28% (2008: 29%) | 318 | (209) |
| Income not taxable for tax purposes | (366) | - |
| Expenses not deductible for tax purposes | - | 188 |
| Unrelieved tax losses | 48 | 21 |
| **Total current tax charge** | **-** | **-** |

Excess management charges of £241,000 (2008: £69,000) have been carried forward at 31 October 2009 and are available for offset against future taxable income subject to agreement with HMRC. The company has not recognised the deferred tax asset of £67,000 (2008: £19,000) in respect of these excess management charges.

Approved VCTs are exempt from tax on capital gains within the Company. Since the Directors intend that the Company will continue to conduct its affairs so as to maintain its approval as a VCT, no current deferred tax has been provided in respect of any capital gains or losses arising on the revaluation or disposal of investments.

## 7. Dividends

| | Year to 31 October 2009 £'000 | Period to 31 October 2008 £'000 |
|---|---|---|
| **Recognised as distributions in the financial statements for the period** | | |
| Previous year's final dividend | 78 | – |
| Current period's interim dividend | 77 | – |
| | **155** | **-** |
| Paid and proposed in respect of the period | | |
| Interim dividend paid – 0.5p per share (2008: 0.0p per share) | 78 | - |
| Proposed final dividend – 0.5p per share (2008: 0.5p per share) | 78 | 78 |
| | **156** | **78** |

The final dividend of 0.5p per share for the year ended 31 October 2009, subject to shareholder approval at the Annual General Meeting, will be paid on 23 April 2010 to those shareholders on the register on 5 March 2010.

## 8. Earnings per Share

The total earnings per share is based on 15,616,881 (31 October 2008: 9,832,696) shares, being the weighted average number of shares in issue during the year, and a return for the year totalling £1,134,000 (31 October 2008: £(722,000)).

The revenue and capital earnings per share are based on 15,616,881 (31 October 2008: 9,382,696) shares, being the weighted average number of shares in issue during the year, and a revenue return for the year totalling £142,000 (31 October 2008: £94,000) and a capital return for the year totalling £992,000 (31 October 2008: £(816,000)).

There are no potentially dilutive capital instruments in issue and, therefore no diluted returns per share figures are relevant. The basic and diluted earnings per share are therefore identical.

## 9. Net Asset Value per Share

The calculation of NAV as at 31 October 2009 is based on 15,616,881 (31 October 2008: 15,616,881) Ordinary shares in issue at that date.

## 10. Fixed Asset Investments

| | £'000 | £'000 |
|---|---|---|
| Valuation and net book amount: | | |
| Book cost as 1 November 2008 | 2,052 | |
| Cumulative revaluation | (215) | |
| Valuation at 1 November 2008 | | 1,837 |
| Movement in the year: | | |
| Purchases at cost | 3,054 | |
| Loss on realisation of investments | (315) | |
| Revaluation in year | (206) | |
| **Valuation at 31 October 2009** | | **4,370** |
| Book cost at 31 October 2009: | | |
| – Ordinary shares | 3,641 | |
| – Loan notes/other securities | 1,140 | |
| Revaluation to 31 October 2009: | | |
| – Ordinary shares | (259) | |
| – Loan notes/other securities | (152) | |
| **Valuation at 31 October 2009** | | **4,370** |

Further details of the fixed asset investments held by the Company are shown within the Investment Manager's Review on pages 8 to 17.

# NOTES TO THE FINANCIAL STATEMENTS (continued)

## 10. Fixed Asset Investments (continued)

All investments are designated as fair value through profit or loss at the time of acquisition, and all capital gains or losses on investments so designated. Given the nature of the Company's venture capital investments, the changes in fair value of such investments recognised in these financial statements are not considered to be readily convertible to cash in full at the balance sheet date and accordingly these gains are treated as holding gains or losses.

When the Company revalues the investments still held during the period, any gains or losses arising are credited / charged to the Capital reserve – holding gains/(losses).

When an investment is sold any balance held on the Capital reserve – holding gains/(losses) is transferred to the Capital reserve – gains/(losses) on disposal as a movement in reserves.

At 31 October 2009 there were no commitments in respect of investments approved by the Manager but not yet completed.

## 11. Debtors

| | 31 October 2009 £'000 | 31 October 2008 £'000 |
|---|---|---|
| Prepayments | 9 | 5 |
| Accrued income | 88 | 157 |
| | **97** | **162** |

## 12. Current Asset Investments

Current asset investments at 31 October 2009 comprised bonds, money market funds and OEICs.

| | £'000 | £'000 |
|---|---|---|
| Valuation and net book amount: | | |
| Book cost as 1 November 2008 | | |
| – Bonds | 5,442 | |
| – Money Market Funds | 3,116 | |
| – OEICs | 3,542 | |
| | | 12,100 |
| Revaluation as at 1 November 2008 | | |
| – Bonds | (232) | |
| – Money Market Funds | (96) | |
| – OEICs | (109) | |
| | | (437) |
| **Valuation as at 31 October 2009** | | **11,663** |
| Purchase at cost: | | |
| – Bonds | – | |
| – Money Market Funds | 2,146 | |
| – OEICs | – | |
| | | 2,146 |
| Disposal proceeds | | |
| – Bonds | (1,512) | |
| – Money Market Funds | (3,949) | |
| – OEICs | – | |
| | | (5,461) |

## 12. Current Asset Investments (continued)

| | £'000 | £'000 |
|---|---|---|
| Profit/(loss) in year on realisation of investments: | | |
| – Bonds | 86 | |
| – Money Market Funds | (41) | |
| – OEICs | – | |
| | | 45 |
| Revaluation in the year | | |
| – Bonds | 298 | |
| – Money Market Funds | (51) | |
| – OEICs | 1,429 | |
| | | 1,676 |
| **Valuation as at 31 October 2009** | | **10,069** |
| Book cost as at 31 October 2009 | | |
| – Bonds | 3,930 | |
| – Money Market Funds | 1,120 | |
| – OEICs | 3,542 | |
| | | 8,592 |
| Revaluation as at 31 October 2009 | | |
| – Bonds | 153 | |
| – Money Market Funds | 4 | |
| – OEICs | 1,320 | |
| | | 1,477 |
| **Valuation as at 31 October 2009** | | **10,069** |

## 13. Creditors: Amounts Falling Due Within One Year

| | 31 October 2009 £'000 | 31 October 2008 £'000 |
|---|---|---|
| Accruals | 94 | 79 |
| Other creditors | – | 8 |
| | **94** | **87** |

## 14. Share Capital

| | 31 October 2009 £'000 | 31 October 2008 £'000 |
|---|---|---|
| Authorised: | | |
| 50,000,000 Ordinary shares of 10p | 5,000 | 5,000 |
| Allotted and fully paid up: | | |
| 15,616,881 Ordinary shares of 10p | 1,562 | 1,562 |

The capital of the Company is managed in accordance with its investment policy with a view to the achievement of its investment objective as set on page 20. The Company is not subject to any externally imposed capital requirements.

# NOTES TO THE FINANCIAL STATEMENTS (continued)

## 15. Reserves

| | Share Premium £'000 | Special distributable reserve £'000 | Capital reserve gains/(losses) on disposal £'000 | Capital reserve holding gains/(losses) £'000 | Revenue reserve £'000 | Total £'000 |
|---|---|---|---|---|---|---|
| As at 1 November 2008 | 13,196 | – | (164) | (652) | 94 | 12,474 |
| Return for the year | – | – | – | – | 141 | 141 |
| Management fees allocated as capital expenditure | – | – | (208) | – | – | (208) |
| Share premium account cancelled | (13,196) | 13,196 | – | – | – | - |
| Current period gains/losses on disposal | – | – | (270) | – | – | (270) |
| Prior period holding gains/losses now crystallised | – | – | (10) | 10 | – | - |
| Current period gains/losses on fair value of investments | – | – | 245 | 1,225 | – | 1,470 |
| Dividends paid | – | – | – | – | (155) | (155) |
| **Balance as at 31 October 2009** | – | 13,196 | (407) | 583 | 80 | 13,452 |

When the Company revalues its investments during the period, any gains or losses arising are credited/ charged to the income statement. Changes in fair value of investments held are then transferred to the capital reserve – holding gains/(losses). When an investment is sold any balance held on the capital reserve – holding gains/(losses) reserve is transferred to the capital reserve – gains/(losses) on disposal as a movement in reserves.

Following the company's petition which was heard on 19 August 2009, the Companies Court ordered that the Special Resolution passed by the shareholders on 17 October 2007 to effect the cancellation of the share premium account be confirmed. The Order relating to the same was duly registered by the Registrar of Companies on 20 August 2009. The purpose of the cancellation was to create a reserve which will be capable of being used by the Company for the purpose of making repurchases of its own shares in the market with a view to narrowing the discount at which the Company's Ordinary shares trade to NAV. This reserve can also be used to pay capital dividends.

## 16. Financial Instruments and Risk Management

The Company's financial instruments comprise equity and fixed interest investments, cash balances and liquid resources including debtors and creditors. The Company holds financial assets in accordance with its investment policy of investing mainly in a portfolio of VCT-qualifying unquoted securities whilst holding a proportion of its assets in cash or near-cash investments in order to provide a reserve of liquidity.

Fixed asset investments (see note 10) are valued at fair value. Unquoted investments are carried at fair value as determined by the Directors in accordance with current venture capital industry guidelines. The fair value of all other financial assets and liabilities is represented by their carrying value in the balance sheet. The Directors believe that the fair value of the assets are held at the year end is equal to their book value.

In carrying on its investment activities, the Company is exposed to various types of risk associated with the financial instruments and markets in which it invests. The most significant types of financial risk facing the Company are price risk, interest rate risk, credit risk and liquidity risk. The Company's approach to managing these risks is set out below together with a description of the nature and amount of the financial instruments held at the balance sheet date.

**Market risk**

The Company's strategy for managing investment risk is determined with regard to the Company's investment objective, as outlined on page 20. The management of market risk is part of the investment management process and is a central feature of venture capital investment. The Company's portfolio is managed with regard to the possible effects of adverse price movements and with the objective of maximising overall returns to shareholders. Investments in unquoted companies, by their nature, usually involve a higher degree of risk than investments in companies quoted on a recognised stock exchange, though the risk can be mitigated to a certain extent by diversifying the portfolio across business sectors and asset classes. The overall disposition of the Company's assets is regularly monitored by the Board.

Details of the Company's investment portfolio at the balance sheet date are set out on page 8 to 17. An analysis of investments between debt and equity instruments is given in note 10.

## 16. Financial Instruments and Risk Management (continued)

29.2% (2008: 13.1%) by value of the Company's net assets comprises investments in unquoted companies held at fair value. The valuation methods used by the Company include the application of a price/earnings ratio derived from listed companies with similar characteristics, and consequently the value of the unquoted element of the portfolio can be indirectly affected by price movements on the London Stock Exchange. A 10% overall increase in the valuation of the unquoted investments at 31 October 2009 would have increased net assets and the total return for the year by £437,000 (2008: £183,700) an equivalent change in the opposite direction would have reduced net assets and the total return for the year by the same amount.

67.3% (2008: 83.1%) by value of the Company's net assets comprises of OEICs and money market securities held at fair value. A 10% overall increase in the valuation of the OEICs and money market securities at 31 October 2009 would have increased net assets and the total return for the year by £1,007,000 (2008: £1,166,000) an equivalent change in the opposite direction would have reduced net assets and the total return for the year by the same amount.

**Interest rate risk**
Some of the Company's financial assets are interest-bearing, of which some are at fixed rates and some variable. As a result, the Company is exposed to fair value interest rate risk due to fluctuations in the prevailing levels of market interest rates.

**Fixed rate**
The table below summarises weighted average effective interest rates for the fixed interest-bearing financial instruments:

| | As at 31 October 2009 | | | As at 31 October 2008 | | |
|---|---|---|---|---|---|---|
| | **Total fixed rate portfolio by value £'000** | **Weighted average interest rate %** | **Weighted average time for which rate is fixed in years** | **Total fixed rate portfolio by value £'000** | **Weighted average interest rate %** | **Weighted average time for which rate is fixed in years** |
| Listed fixed interest | | | | | | |
| Listed fixed interest investments | 2,483 | 4.90% | 0.6 | 3,680 | 4.85% | 1.2 |
| Fixed rate investments in unquoted companies | 987 | 10.6% | 3.5 | 160 | 10.00% | 5.0 |
| | **3,470** | | | **3,840** | | |

Due to the relatively short period to maturity of the fixed rate investments held within the portfolio, it is considered that an increase or decrease of 1% in interest rates as at the reporting date would not have had a significant effect on the Company's net assets or total return for the period.

**Floating rate**
The Company's floating rate investments comprise cash held on interest-bearing deposit accounts, libor rate on one loan note and, where appropriate, within interest-bearing money market securities. The benchmark rate which determines the rate of interest receivable on such investments is the bank base rate, which was 0.5% at 31 October 2009. The amounts held in floating rate investments at the balance sheet date were as follows:

| | **31 October 2009 £'000** | **31 October 2008 £'000** |
|---|---|---|
| Floating rate notes | 1,599 | 1,529 |
| Floating-rate investments in unquoted companies | 315 | - |
| Cash on deposit & money market funds | 2,234 | 3,481 |
| | **4,148** | **5,010** |

A 1% increase in the base rate would increase income receivable from these investments and the total return for the period by £41,000.

# NOTES TO THE FINANCIAL STATEMENTS (continued)

## 16. Financial Instruments and Risk Management (continued)

**Credit risk**

There were no significant concentrations of credit risk to counterparties at 31 October 2009. By cost, no individual investment exceeded 10.9% (2008: 11.2%) of the Company's net assets at 31 October 2009.

Credit risk is the risk that a counterparty to a financial instrument will fail to discharge an obligation or commitment that it has entered into with the Company. The Investment Manager and the Board carry out a regular review of counterparty risk. The carrying values of financial assets represent the maximum credit risk exposure at the balance sheet date.

At 31 October 2009 the Company's financial assets exposed to credit risk comprised the following:

| | 31 October 2009 £'000 | 31 October 2008 £'000 |
|---|---|---|
| Investments in fixed interest instruments | 2,483 | 3,680 |
| Investments in floating rate instruments | 1,599 | 1,529 |
| Cash on deposit & money market funds | 2,229 | 3,481 |
| Fixed rate investments in unquoted companies | 987 | 160 |
| Accrued dividends and interest receivable | 89 | 157 |
| | **7,392** | **9,007** |

Credit risk relating to listed money market securities is mitigated by investing in a portfolio of investment instruments of high credit quality, comprising securities issued by the UK Government and major UK companies and institutions. Credit risk relating to loans to and preference shares in unquoted companies is considered to be part of market risk.

Those assets of the Company which are traded on recognised stock exchanges are held on the Company's behalf by third party custodians (Goldman Sachs International in the case of listed money market securities and Charles Stanley Limited in the case of quoted equity securities). Bankruptcy or insolvency of a custodian could cause the Company's rights with respect to securities held by the custodian to be delayed or limited.

Credit risk arising on the sale of investments is considered to be small due to the short settlement and the contracted agreements in place with the settlement lawyers.

The Company's interest-bearing deposit and current accounts are maintained with Goldman Sachs International and HSBC PLC.

**Liquidity risk**

The Company's financial assets include investments in unquoted equity securities which are not traded on a recognised stock exchange and which generally may be illiquid. They also include investments in AIM-quoted companies, which, by their nature, involve a higher degree of risk than investments on the main market. As a result, the Company may not be able to realise some of its investments in these instruments quickly at an amount close to their fair value in order to meet its liquidity requirements, or to respond to specific events such as deterioration in the creditworthiness of any particular issuer.

The Company's listed money market securities are considered to be readily realisable as they are of high credit quality as outlined above.

The Company's liquidity risk is managed on a continuing basis by the Investment Manager in accordance with policies and procedures laid down by the Board. The Company's overall liquidity risks are monitored on a quarterly basis by the Board.

The Company maintains sufficient investments in cash and readily realisable securities to pay accounts payable and accrued expenses. At 31 October 2009 these investments were valued at £10,600,000.

## 17. Post Balance Sheet Events

The following events occurred between the balance sheet date and the signing of these financial statements:

- 8 January 2010: £499,998 investment into Calastone.
- 9 January 2010: A previous £201,440 non-qualifying investment in Zoopla became qualifying.

## 18. Contingencies, Guarantees and Financial Commitments

Provided that the intermediary continues to act for the client and the client continues to be the beneficial owner of the shares, intermediaries will be paid an annual trail commission of 0.5% of the initial net asset value.

There were no other contingencies, guarantees or financial commitments as at 31 October 2009.

## 19. Related Party Transactions

Octopus Titan VCT 2 plc has employed Octopus Investments Limited since 20 October 2009 as the Investment Manager, prior to this, the agreement was held with Octopus Ventures Limited. Matt Cooper, a non-executive Director of Octopus Titan VCT 2 plc, is also Chairman of Octopus Investments. Octopus Titan VCT 2 plc has paid Octopus £281,000 (2008: £180,000) in the year as a management fee and there is £nil outstanding at the balance sheet date. The management fee is payable quarterly in advance and is based on 2.0% of the net asset value calculated at annual intervals as at 31 October.

Octopus Investments Limited provides accounting, administrative and company secretarial services to the Company, payable quarterly in advance for a fee of 0.3% of the net asset value calculated at annual intervals as at 31 October. During the year £46,000 (2008: £32,000) was paid to Octopus Investments Limited and there is £nil outstanding at the balance sheet date, for the accounting and administrative services.

In addition, Octopus is entitled to performance related incentive fees. The incentive fees are designed to ensure that there are significant tax-free dividend payments made to shareholders as well as strong performance in terms of capital and income growth, before any performance-related incentive fee payment is made. Therefore, only if by the end of a financial year (commencing no earlier than close of the 2011 financial year), declared distributions per share have reached 40p in aggregate and if the Performance Value at that date exceeds 130p per share, a performance incentive fee equal to 20% of the excess of such Performance Value over 100p per share will be payable to Octopus.

If, on a subsequent financial year end, the Performance Value of Octopus Titan VCT 2 plc falls short of the Performance Value on the previous financial year end, no incentive fee will arise. If, on a subsequent financial year end, the performance exceeds the previous best Performance Value of Octopus Titan VCT 2 plc, the Investment Manager will be entitled to 20% of such excess in aggregate.

# DIRECTORS AND ADVISERS

## Board of Directors
John Hustler (Chairman)
Mark Faulkner
Matt Cooper

## Company Number
Registered in England & Wales
No 06397765

## Secretary and Registered Office
Celia L Whitten FCIS
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## Investment and Administration Manager
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(calls cost 10p per minute plus network extras)
www.capitaregistrars.com

# NOTICE OF ANNUAL GENERAL MEETING

Notice is hereby given that the Annual General Meeting of Octopus Titan VCT 2 plc will be held at 8 Angel Court, London EC2R 7HP on Wednesday, 31 March 2010 at 2.30 p.m. for the following purposes:

## Ordinary Business

To consider and if thought fit, pass Resolutions 1-5 as Ordinary Resolutions:

1. **To receive and adopt the financial statements for the year to 31 October 2009 and the Directors' and Auditor's Reports thereon.**

2. **To approve a final dividend of 0.5 pence per share.**

3. **To approve the Directors' Remuneration Report.**

4. **To re-elect John Hustler as a Director.**

5. **To re-appoint Grant Thornton UK LLP as auditor of the Company and to authorise the Directors to determine their remuneration.**

## Special Business

To consider and, if thought fit, pass Resolution 6 as an Ordinary Resolution and Resolutions 7 and 8 as Special Resolutions:

6. **AUTHORITY TO ALLOT RELEVANT SECURITIES**
   THAT the Directors be and are generally and unconditionally authorised in accordance with s551 of the Companies Act 2006 to exercise all the powers of the Company to allot shares in the Company up to a maximum nominal amount of £156,169 (representing approximately 10% of the Ordinary share capital in issue at today's date) such authority to expire at the later of the conclusion of the Company's Annual General Meeting next following the passing of this Resolution and the expiry of 15 months from the passing of the relevant Resolution (unless previously revoked, varied or extended by the Company in a general meeting but so that such authority allows the Company to make offers or agreements before the expiry thereof, which would or might require relevant securities to be allotted after the expiry of such authority).

7. **EMPOWERMENT TO MAKE ALLOTMENTS OF EQUITY SECURITIES**
   TO empower the Directors pursuant to s571 of the Companies Act 2006 to allot or make offers or agreements to allot equity securities (as defined in s560(1) of the said Act) for cash pursuant to the authority referred to in Resolution 6 as if s561 (1) of the said Act did not apply to any such allotments and so that:

   (a) reference to allotment in this Resolution shall be construed in accordance with s560(2) of the said Act; and

   (b) the power conferred by this Resolution shall enable the Company to make any offer or agreement before the expiry of the said power which would or might require equity securities to be allotted after the expiry of the said power and the Directors may allot equity securities in pursuance of such offer or agreement notwithstanding the expiry of such power.

   And this power, unless previously varied, revoked or renewed, shall come to an end at the conclusion of the Annual General Meeting of the Company next following the passing of this Resolution or, if earlier, on the expiry of 15 months from the passing of this Resolution.

**8. AUTHORITY TO MAKE MARKET PURCHASES**

THAT the Company be and is hereby generally and unconditionally authorised to make market purchases (within the meaning of s693(4) of the Act) of Ordinary shares of 1 0p each in the Company ('Ordinary shares') provided that:

(a) the maximum number of Ordinary shares so authorised to be purchased shall not exceed 5% of the present issued Ordinary share capital of the Company;

(b) the minimum price which may be paid for an Ordinary share shall be 10p;

(c) the maximum price, exclusive of expenses, which may be paid for an Ordinary share is an amount equal to 105% of the average of the middle market quotations for an Ordinary share taken from the London Stock Exchange Daily Official List for the five business days immediately preceding the day on which the Ordinary share is contracted to be purchased;

(d) the authority conferred comes to an end at the conclusion of the next Annual General Meeting of the Company or upon the expiry of 15 months from the passing of this Resolution, whichever is the later; and

(e) that the Company may enter into a contract to purchase its Ordinary shares under this authority prior to the expiry of this authority which would or might be completed wholly or partly after the expiry of this authority.

By order of the Board

8 Angel Court
London
EC2R 7HP

Celia L Whitten FCIS
Company Secretary
3 February 2010

## NOTES:

(a) A member entitled to attend and vote at the Annual General Meeting may appoint one or more proxies to attend and vote on his or her behalf. A proxy need not be a member.

(b) A form of proxy is enclosed which, to be effective, must be completed and delivered to the registrars of the Company, Capita Registrars, Proxies Department, The Registry, 34 Beckenham Road, Beckenham, Kent BR3 4TU so as to be received by no later than 48 hours before the time the Annual General Meeting is scheduled to begin. The completion and return of the form of proxy will not affect the right of a member to attend and vote at the Annual General Meeting.

(c) Copies of the Directors' Letters of Appointment, the Register of Directors' Interests in the Ordinary shares of the Company kept in accordance with the Listing Rules Articles of Association will be available for inspection at the registered office of the Company during usual business hours on any weekday from the date of this notice until the Annual General Meeting, and at the place of that meeting for at least 15 minutes prior to the commencement of the meeting until its conclusion, as well as on the Investment Manager's website www.octopusinvestments.com.

Perivan Financial Print 217068

# PROXY FORM OCTOPUS TITAN VCT 2 PLC ANNUAL GENERAL MEETING 31 MARCH 2010 AT 2.30 P.M.

I/We ______________________________________________
(BLOCK CAPITALS PLEASE)

of [address] ______________________________________________

being a member of Octopus Titan VCT 2 plc, hereby appoint the Chairman of the meeting or,

Name of Proxy ______________________________ Number of Shares ______________

as my/our proxy and vote for me/us on my/our behalf at the Annual General Meeting of the Company to be held on 31 March 2010, notice of which was sent to shareholders with the Directors' Report and the accounts for the year to 31 October 2009, and at any adjournment thereof. The proxy will vote as indicated below in respect of the Resolutions set out in the notice of meeting.

Please indicate by ticking the box if this proxy appointment is one of multiple appointments being made. ☐

For the appointment of one or more proxy, please refer to the explanatory note 4 overleaf.

| Resolution number | | For | Against | Withheld |
|---|---|---|---|---|
| **Ordinary Business** | | | | |
| 1. | To receive, consider and adopt the financial statements for the year ended 31 October 2009 | ☐ | ☐ | ☐ |
| 2. | To approve a final dividend of 0.5 pence per share | ☐ | ☐ | ☐ |
| 3. | To approve the Directors' Remuneration Report | ☐ | ☐ | ☐ |
| 4. | To re-elect John Hustler as a Director | ☐ | ☐ | ☐ |
| 5. | To re-appoint Grant Thornton UK LLP as auditor and authorise the Directors to agree their remuneration | ☐ | ☐ | ☐ |
| **Special Business** | | | | |
| 6. | To authorise the Directors to allot shares under s551 of the Companies Act 2006 (Ordinary Resolution) | ☐ | ☐ | ☐ |
| 7. | To disapply s561 of the Companies Act 2006 and allot shares on a non-rights issue basis (Special Resolution) | ☐ | ☐ | ☐ |
| 8. | To authorise the Directors to make market purchases of its own shares (Special Resolution) | ☐ | ☐ | ☐ |

Signed: ______________________________ Dated: ______________________2010

If you are unable to attend the AGM and wish to pass on any comments to the Board, please use the box below:

NOTES

1. To be valid, the proxy form must be received by the Registrars of Octopus Titan VCT 2 plc at, Capita Registrars, Proxies Department, PO Box 25, Beckenham, Kent BR3 4BR no later than 48 hours before the commencement of the meeting. If delivering by courier please use the full address of Capita set out in the notice.

2. Where this form of proxy is executed by a corporation it must be either under its seal or under the hand of an officer or attorney duly authorised.

3. Every holder has the right to appoint some other person(s) of their choice, who need not be a shareholder as his proxy to exercise all or any of his rights, to attend, speak and vote on their behalf at the meeting. If you wish to appoint a person other than the Chairman, please insert the name of your chosen proxy holder in the space provided. If the proxy is being appointed in relation to less than your full voting entitlement, please enter next to the proxy holder's name the number of shares in relation to which they are authorised to act as your proxy. If left blank your proxy will be deemed to be authorised in respect of your full voting entitlement. (or if this proxy form has been issued in respect of a designated account for a shareholder, the full voting entitlement for that designated account).

4. To appoint more than one proxy, you may photocopy this form. Please indicate next to the proxy holder's name the number of shares in relation to which they are authorised to act as your proxy. Please also indicate by ticking the box provided if the proxy instruction is one of multiple instructions being given. All forms must be signed and should be returned together in the same envelope.

5. The 'Vote Withheld' option is provided to enable you to abstain on any particular Resolution. However, it should be noted that a 'Vote Withheld' is not a vote in law and will not be counted in the calculation of the proportion of the votes 'For' and 'Against' a Resolution.

6. If the proxy form is signed and returned without any indication as to how the proxy shall vote, the proxy will exercise his/her discretion as to whether and how he/she votes.

7. Pursuant to regulation 41 of the Uncertificated Securities Regulations 2001, entitlement to attend and vote at the meeting and the number of votes which may be cast thereat will be determined by reference to the Register of Members of the Company at 6 p.m. on the day which is two days before the day of the meeting or adjourned meeting. Changes to entries on the Register of Members after that time shall be disregarded in determining the rights of any person to attend and vote at the meeting.

8. The address on the envelope containing this notice is how your address appears on the Register of Members. If this information is incorrect please ring the Registrar's helpline on 0871 664 0300. (calls cost 10p per minute plus network extras, lines are open 8.30 a.m.–5.30 p.m. Monday–Friday) to request a change of address form).

9. The completion and return of this form will not preclude a member from attending the meeting and voting in person.

PLEASE USE THE REPLY PAID ENVELOPE PROVIDED