

Company Registration No. 4018752

KOBALT MUSIC GROUP LIMITED

Report and Consolidated Financial Statements

30 June 2010



(- 24/03/2011)

KOBALT MUSIC GROUP LIMITED

REPORT AND FINANCIAL STATEMENTS 2010

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KOBALT MUSIC GROUP LIMITED

REPORT AND FINANCIAL STATEMENTS 2010

OFFICERS AND PROFESSIONAL ADVISERS

DIRECTORS

W B A Ahdritz
J Ekelund
A J Palm
J P Fitzherbert-Brockholes
T Bunting
T Teichman

SECRETARY

J P Fitzherbert-Brockholes

REGISTERED OFFICE

4 Valentine Place
London
SE1 8QH

BANKERS

The Royal Bank of Scotland plc
62-63 Threadneedle Street
London
EC2R 8LA

AUDITOR

Deloitte LLP
Chartered Accountants and Statutory Auditor
Cambridge

KOBALT MUSIC GROUP LIMITED

CHAIRMAN'S STATEMENT

I am delighted to report that Kobalt Music Group's rapid growth continues, with gross revenues up 29% in the year ended 30 June 2010 compared to the prior year and net publisher share (NPS) up 18%. This growth has been achieved despite the continuing difficulties in the wider music publishing market, which for a decade has been impacted by the on-going decline in the recorded music market, but now has been further hit by the global recession.

Against this background Kobalt continues to deliver significant growth both through signing new deals and the ongoing delivery of new compositions from its existing client base. In the calendar year 2010 Kobalt signed 174 new agreements further extending its number of clients and so both its catalogue and potential for growth. Major recent signings include rock legends Pearl Jam, indie superstar Beck and hit-making writer/producer duo Future Cuts. It is also relevant to understand that in the same period 283 existing clients delivered over 14,000 new works from around 3,000 writers which in itself contributed to growing revenue. Client retention rates continue to be extremely high at 98%.

Our clients have continued to have much success in the charts around the world. Kobalt reached 11.9% airplay market share in Quarter 4 2010 in the US, surpassing Warner Chappell on 11.2%. This is the first time since records began in 2005 that an independent publisher has beaten one of the majors in the most important market in the world. This follows on from Germany where Kobalt has passed Warner Chappell in several quarters over the last couple of years. We do not manage Kobalt focused on delivering market share - revenue growth is our key metric. However our high market share is a strong marketing signal of Kobalt's success and the level of clients that we administer.

Examples of successful Kobalt-administered songs are the Grammy winning song "Halo" performed by Beyonce co-written by Kobalt client Ryan Tedder, Ke\$ha's hits "TiK ToK", "Blah Blah Blah" and "Your Love is my Drug", Jay-Z and Alicia Keys' "Empire State of Mind", Keri Hilson's "Knock You Down", as well as Dizzie Rascal and James Corden's "Shout for England". Max Martin and Dr Luke continue to write a number of the biggest hits on the charts like "Teenage Dream" and "California Gurls" performed by Katy Perry, and "Dynamite" performed by Taio Cruz.

Over the last year we have gone direct into Singapore, Vietnam and Malaysia. In July we took the decision to further expand our direct collection network to 40 territories from the current 30 territories which will put us in line with the biggest majors' direct collection infrastructure. The major step in this plan was taken in September 2010 when we opened a full service office in Sydney covering Australia and New Zealand. The new office proved its worth straight away with the signing of up-and-coming Australian act Art vs Science.

We are pleased with last year's results both financially and operationally. However it is important that we continue to launch new services, underpinned by our innovative and unique technology built in house over 10 years. By doing this we will carry on being a world leading and innovative publisher, setting new standards for how copyright management should be carried out most efficiently and cost effectively for our customers on a global scale. We look forward to further success for Kobalt in the next financial year and beyond.

2011 has started strongly and Kobalt continues to set new landmarks in its growth, chart positions and client gains.

Finally, I would like to thank, on behalf of the Board and all shareholders, the innovative, highly committed and focused Kobalt management team and staff at Kobalt's offices worldwide, for all their outstanding work in the past year. The year was a great success thanks to their efforts.

Thomas Teichman

Chairman

24 March 2011

KOBALT MUSIC GROUP LIMITED

DIRECTORS' REPORT

The directors present their annual report and the audited financial statements for the year ended 30 June 2010

BUSINESS REVIEW AND PRINCIPAL ACTIVITIES

The group's principal activity is music publishing. The group head office is in London, with other offices in New York, Los Angeles, Nashville, Sydney, Stockholm and Berlin.

There have not been any significant changes in the group's principal activity in the year under review. The directors are not aware, at the date of this report, of any likely major changes in the group's activities in the next year.

As shown in the group's profit and loss account on page 8, the group's sales have increased by 29.0% over the prior year while gross margin has decreased by one percentage point. However, gross profit increased in absolute terms by £834k, an increase which was not matched by a corresponding increase in operating costs. This has resulted in loss after tax of £1,889k as opposed to the previous year's £2,363k.

The board monitors the company's performance in a number of ways including key performance indicators. The key financial performance indicators together with the information for the prior year are as follows:

	2010	2009
Increase in turnover	29.0%	85.0%
Gross profit	£5,428k	£4,594k
Gross profit percentage	11.2%	12.2%
Operating loss	£(1,516k)	£(2,116k)
Average employees	76	69

The group also uses certain non-financial performance indicators, one of which is the number of employees. The increase in employee numbers during the year is the result of the group's rapid growth in activity.

The balance sheet on page 9 of the financial statements shows that the group's cash position remains healthy. The group is financed by working capital, loans and equity.

PRINCIPAL RISKS AND UNCERTAINTIES

The risks and uncertainties facing the group are detailed below:

Revenue generation The on-going demand for the music administered by the group is unpredictable and as such the level at which this music will generate revenue in future periods is uncertain.

The group seeks to mitigate this risk by seeking to make its roster as wide-ranging as possible. This means that the group's revenue is not unduly affected by fluctuations in the popularity of certain genres of music, or of specific writers and artists. The fact that the group collects royalties worldwide minimises its exposure to specific territories.

Client acquisition and retention The decisions of potential clients to sign with Kobalt or of existing clients to remain with Kobalt are complex and involve the consideration of many factors. As such it is uncertain how many new clients the group will sign and what proportion of existing clients will extend their agreements.

In recent years the group has increased its sales efforts, particularly in the USA which is the world's largest market. Furthermore, the group has additional finance available to enable it to provide the advances which larger prospective clients often require.

The group makes constant efforts to improve its service offering, particularly in the areas of transparency and technological innovation. This serves to help retain existing clients as well as encouraging new clients to join Kobalt.

KOBALT MUSIC GROUP LIMITED

DIRECTORS' REPORT

PRINCIPAL RISKS AND UNCERTAINTIES (continued)

Market environment There are uncertain economic conditions at present and the record industry is experiencing declining sales volumes and depressed profitability. The extent and timing of any response by the record labels to this threat is uncertain. In addition, as the major music publishers are also record companies, it is not clear how they will respond to this and what competitive action they may take to defend their publishing interests.

The group monitors the latest developments in the industry by means of research, review of trade publications, and membership of industry organisations and forums. Kobalt's state of the art royalty processing and analysis systems arguably allow it to adapt more quickly to industry changes than more traditional publishers.

Changing distribution The new channels for music distribution could significantly change the operational or financial dynamics of music publishing.

Again Kobalt's technological expertise makes it well-placed to adapt to new distribution channels. The high level of automation in its royalty processing makes assimilating new sources of revenue and/or royalty information less time-consuming and costly.

Third party suppliers Kobalt relies on a number of important third party suppliers to operate successfully. Any failure in the provision of these services may adversely impact Kobalt's business.

In recent years Kobalt has sought to institute direct collection in as many territories as possible, thereby minimising its exposure to the failure of third parties. However, the nature of music publishing makes it impossible to avoid reliance on some third parties, especially royalty collection societies.

FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The group's activities expose it to a number of financial risks including currency risk, credit risk and liquidity risk. The use of financial derivatives is governed by the group's policies approved by the board of directors, which provide written principles on the use of financial derivatives to manage these risks. The group does not use derivative financial instruments for speculative purposes.

Currency risk

The group's activities expose it to some risk of changes in foreign currency exchange rates. Other than in exceptional circumstances, the group does not feel it necessary to hedge against these exposures.

Credit risk

Royalties due to Kobalt are often from large and established organisations and there is considered to be a low risk that these debts will not be recovered.

The group is exposed to credit risk when it makes advances to clients. These advances are subject to detailed financial analysis and a full commercial assessment.

Liquidity risk

The group uses a bank loan and overdraft facility to ensure that sufficient funds are available for ongoing operations and future developments. A convertible loan of £4m was also received by the group during the year. This subsequently converted to equity post year end.

The group regularly prepares and updates cash flow forecasts which monitor its financing requirements. The group maintains a close relationship with its existing lenders whilst regularly assessing the possibility of obtaining finance from other sources.

CHARITABLE DONATIONS

During the year the Group made charitable donations of £13k (2009 - £19k)

KOBALT MUSIC GROUP LIMITED

DIRECTORS' REPORT

DIRECTORS

The directors who served during the year were as follows

W B A Ahdritz

J Ekelund

Newmedia Spark Directors Limited (resigned 30 April 2010)

A J Palm

J P Fitzherbert-Brockholes

C Broadhurst (resigned 1 October 2009)

T Bunting

T Teichman (appointed 1 May 2010)

DIRECTORS' RESPONSIBILITIES STATEMENT

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

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the group and company and of the profit or loss of the group for that period. In preparing these financial statements, the directors are required to

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

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and 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

AUDITOR

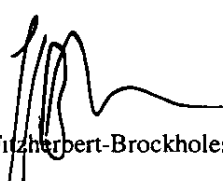
Each of the persons who is a director at the date of approval of this annual report confirms that

- so far as the director is aware, there is no relevant audit information of which the company's auditor is unaware, and
- the director has taken all the steps that he ought to have taken as a director to make himself aware of any relevant audit information and to establish that the company's auditor is aware of that information

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

Deloitte LLP have expressed their willingness to continue in office as auditor and a resolution to reappoint them as auditor will be proposed at the forthcoming Annual General Meeting

Approved by the Board of Directors
and signed on behalf of the Board


J P Fitzherbert-Brockholes
Secretary

24 March 2011

INDEPENDENT AUDITOR'S REPORT TO THE DIRECTORS OF KOBALT MUSIC GROUP LIMITED

We have audited the financial statements of Kobalt Music Group Limited for the year ended 30 June 2010 which comprise the consolidated profit and loss account, the consolidated and company balance sheets, the consolidated cash flow statement and the related notes 1 to 18. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 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 auditor

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

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of whether the accounting policies are appropriate to the group's and the parent company's circumstances and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates made by the directors, and the overall presentation of the financial statements.

Opinion on financial statements

In our opinion the financial statements

- give a true and fair view of the state of the group's and the parent company's affairs as at 30 June 2010 and of the group's loss for the year then ended,
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

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

**INDEPENDENT AUDITOR'S REPORT TO THE DIRECTORS OF
KOBALT MUSIC GROUP LIMITED (continued)**

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us, or
- the parent company financial statements 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

AJ Swarbrick

Andrew Swarbrick BA FCA (Senior Statutory Auditor)
For and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
Cambridge, United Kingdom

25 March 2011

KOBALT MUSIC GROUP LIMITED

CONSOLIDATED PROFIT AND LOSS ACCOUNT

Year ended 30 June 2010

	Note	2010 £'000	2009 £'000
TURNOVER	2	48,679	37,730
Cost of sales		(43,251)	(33,136)
Gross profit		5,428	4,594
Administrative expenses		(6,944)	(6,710)
OPERATING LOSS		(1,516)	(2,116)
Interest receivable and similar income	5	1	1
Interest payable and similar charges	6	(76)	(43)
LOSS ON ORDINARY ACTIVITIES BEFORE TAXATION		(1,591)	(2,158)
Tax on loss on ordinary activities	7	(298)	(201)
LOSS ON ORDINARY ACTIVITIES AFTER TAXATION		(1,889)	(2,359)
Minority interest		-	(4)
LOSS FOR THE FINANCIAL YEAR	17	(1,889)	(2,363)

All activities derive from continuing operations

There are no recognised gains and losses other than as shown above. Therefore no statement of total recognised gains and losses is presented.

KOBALT MUSIC GROUP LIMITED

CONSOLIDATED BALANCE SHEET 30 June 2010

	Note	£'000	2010 £'000	£'000	2009 £'000
ASSETS EMPLOYED					
FIXED ASSETS					
Tangible assets	10		1,097		964
CURRENT ASSETS					
Debtors	12		14,481		12,716
Cash at bank and in hand			8,556		3,907
			23,037		16,623
CREDITORS: amounts falling due within one year	13		(23,328)		(19,380)
NET CURRENT LIABILITIES			(291)		(2,757)
TOTAL ASSETS EMPLOYED LESS CURRENT LIABILITIES			806		(1,793)
FINANCED BY					
CREDITORS: amounts falling due after more than one year	14		4,056		-
CAPITAL AND RESERVES					
Called up share capital	16	250		242	
Share premium account	17	11,046		10,768	
Share option reserve	17	874		728	
Profit and loss account	17	(15,420)		(13,531)	
SHAREHOLDERS' DEFICIT	17		(3,250)		(1,793)
			806		(1,793)

The financial statements of Kobalt Music Group Limited, registered number 4018752, were approved by the Board of Directors and authorised for issue on 24 March 2011.

Signed on behalf of the Board of Directors



Director

J P Fitzherpert-Brockholes

KOBALT MUSIC GROUP LIMITED

**BALANCE SHEET
30 June 2010**

	Note	2010 £'000	2009 £'000
ASSETS EMPLOYED			
FIXED ASSETS			
Tangible assets	10	935	807
Investments	11	119	119
		<u>1,054</u>	<u>926</u>
CURRENT ASSETS			
Debtors	12	20,136	11,333
Cash at bank and in hand		850	1,082
		<u>20,986</u>	<u>12,415</u>
CREDITORS: amounts falling due within one year	13	<u>(8,111)</u>	<u>(4,446)</u>
NET CURRENT ASSETS		<u>12,875</u>	<u>7,969</u>
TOTAL ASSETS EMPLOYED		<u>13,929</u>	<u>8,895</u>
FINANCED BY			
CREDITORS: amounts falling due after more than one year	14	4,056	-
CAPITAL AND RESERVES			
Called up share capital	16	250	242
Share premium account	17	11,046	10,768
Share option reserve	17	874	728
Profit and loss account	17	<u>(2,297)</u>	<u>(2,843)</u>
SHAREHOLDERS' FUNDS	17	<u>9,873</u>	<u>8,895</u>
		<u>13,929</u>	<u>8,895</u>

The financial statements of Kobalt Music Group Limited, registered number 4018752, were approved by the Board of Directors and authorised for issue on 24 March 2011.

Signed on behalf of the Board of Directors



Director

J P Fitzherpert-Brockholes

KOBALT MUSIC GROUP LIMITED

CONSOLIDATED CASH FLOW STATEMENT Year ended 30 June 2010

	Note	2010 £'000	2009 £'000
Net cash inflow from operating activities	1	<u>1,062</u>	<u>2,070</u>
Returns on investments and servicing of finance			
Interest received		1	1
Interest paid		<u>(76)</u>	<u>(43)</u>
Net cash outflow from returns on investments and servicing of finance		<u>(75)</u>	<u>(42)</u>
Taxation		<u>(298)</u>	<u>(201)</u>
Capital expenditure and financial investment			
Payments to acquire tangible fixed assets		<u>(240)</u>	<u>(143)</u>
Net cash outflow from capital expenditure and financial investment		<u>(240)</u>	<u>(143)</u>
Net cash inflow before financing		<u>449</u>	<u>1,684</u>
Financing			
Issue of convertible loan stock		4,000	-
Share capital issued		286	91
Capital element of finance lease rental payments		<u>(6)</u>	<u>(7)</u>
Net cash inflow from financing		<u>4,280</u>	<u>84</u>
Increase in cash	2/3	<u><u>4,729</u></u>	<u><u>1,768</u></u>

KOBALT MUSIC GROUP LIMITED

NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT Year ended 30 June 2010

	2010 £'000	2009 £'000
1. RECONCILIATION OF OPERATING LOSS TO NET CASH INFLOW FROM OPERATING ACTIVITIES		
Operating loss	(1,516)	(2,116)
Depreciation of tangible assets	392	355
Loss on disposal of fixed assets	1	-
Capitalised labour costs	(286)	(375)
Increase in debtors	(1,765)	(2,736)
Increase in creditors	4,090	6,710
Share option payment charge	146	232
Net cash inflow from operating activities	<u>1,062</u>	<u>2,070</u>

2. ANALYSIS OF NET FUNDS

	At 1 July 2009 £	Cash flow £	At 30 June 2010 £
Cash at bank and in hand	3,907	4,649	8,556
Bank overdrafts	(80)	80	-
	<u>3,827</u>	<u>4,729</u>	<u>8,556</u>
Finance leases	(6)	6	-
Convertible loan stock	-	(4,000)	(4,000)
Net funds	<u>3,821</u>	<u>735</u>	<u>4,556</u>

3 RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET FUNDS

	2010 £'000	2009 £'000
Increase in cash in the year	4,729	1,768
Cash inflow from change in debt and lease financing	(3,994)	7
Movement in net funds in the year	<u>735</u>	<u>1,775</u>
Opening net funds	3,821	2,046
Closing net funds	<u>4,556</u>	<u>3,821</u>

KOBALT MUSIC GROUP LIMITED

NOTES TO THE FINANCIAL STATEMENTS

Year ended 30 June 2010

1. ACCOUNTING POLICIES

The principal accounting policies are summarised below. They have been applied consistently throughout the year and the preceding year.

Basis of accounting

The financial statements are prepared under the historical cost convention and in accordance with applicable United Kingdom accounting standards.

The group's business activities, together with the factors likely to affect its future development, performance and position are set out in the directors' report on pages 3 and 4.

Going concern

The group has in place an agreed £4m bank borrowing facility, renewed in January 2011, which is available for the period through to 31 December 2011. The directors are not aware of any reason why this facility will not be renewed when it expires.

The directors have prepared projected cash flow information for the period ending 30 June 2012 and beyond. These projections anticipate that the group will be able to operate solely from cash generated from trading revenue. No further capital injections to the group are expected or considered necessary.

The directors acknowledge the group is trading in an uncertain economic environment, although it is their belief that the group is well positioned to meet its business objectives. They have examined the results of sensitivity analysis on their forecasts to assess the effect on cash given certain downside scenarios. The directors expect that the group will be cash generating for the next 12 months and beyond.

Based on the above, the directors have concluded that the group will continue in operational existence for the foreseeable future even if there are significant reductions in its planned revenues over this period. The directors therefore consider it appropriate to prepare the financial statements on a going concern basis.

Turnover

Turnover represents 12 months' worth of royalties. Part of this will be represented by an accrual the company makes for approximately 3 months of royalty revenue, the receipt of which will occur in the first quarter post year end.

Basis of consolidation

The group financial statements consolidate the financial statements of Kobalt Music Group Limited and its subsidiary undertakings (as listed in note 11). All entities have an accounting year end of 30 June 2010.

Fixed asset investments

Fixed asset investments are stated at cost. The carrying values of investments are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable.

Convertible loan notes

The component parts of compound instruments issued by the group are classified separately as financial liabilities and equity in accordance with the substance of the contractual arrangement. On initial recognition the financial liability component is recorded at its fair value. At the date of issue, in the case of a convertible bond denominated in the local currency of the issuer that may be converted into a fixed number of equity shares, the fair value of the liability component is estimated using the prevailing market interest rate for a similar non-convertible instrument. The equity component is determined by deducting the amount of the liability component from the fair value of the compound instrument as a whole. Where applicable, this is recognised and included in equity and is not subsequently remeasured.

KOBALT MUSIC GROUP LIMITED

NOTES TO THE FINANCIAL STATEMENTS

Year ended 30 June 2010

1. ACCOUNTING POLICIES (continued)

Depreciation

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

Fixtures and fittings	20% per annum
Office equipment	33% per annum
Computer equipment	33% per annum
Purchased software	20% to 33% per annum
Proprietary software	20% per annum

The carrying values of tangible fixed assets are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable

Taxation

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

Deferred tax is provided in full on timing differences, which result in an obligation at the balance sheet date to pay more tax, or a right to pay less tax, at a future date, at rates expected to apply when they crystallise based on current tax rates and law. Timing differences arise from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in financial statements. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered. Deferred tax assets and liabilities are not discounted.

Pension costs

Kobalt Music Group Limited operates a defined contribution stakeholder pension scheme. The group does not make any contributions to this scheme and so no cost to the group is involved.

Foreign currencies

The financial statements of overseas subsidiary undertakings are translated at the rate of exchange ruling at the balance sheet date. The exchange difference arising on the retranslation of opening net assets is taken directly to reserves. All other translation differences are taken to the profit and loss account with the exception of differences on foreign currency borrowings to the extent that they are used to finance or provide a hedge against group equity investments in foreign currency enterprises, which are taken directly to reserves together with the exchange difference on the net investment in these enterprises. Tax charges and credits attributable to exchange differences on those borrowings are also dealt with in reserves.

Leasing and hire purchase agreements

Assets held under finance leases and hire purchase contracts are capitalised in the balance sheet and are depreciated over their useful lives.

The interest element of the rental obligations is charged to the profit and loss account over the period of the lease and represents a constant proportion of the balance of capital repayments outstanding.

Rentals paid under operating leases are charged to income on a straight line basis over the lease term.

Royalty advances

Advances in respect of royalties payable, which are non-refundable but recoupable, comprise advances to clients under contract. These advances are included as prepayments. Specific provisions are made against these advances where the outstanding advance at the balance sheet date exceeds future expected royalty earnings.

KOBALT MUSIC GROUP LIMITED

NOTES TO THE FINANCIAL STATEMENTS Year ended 30 June 2010

1. ACCOUNTING POLICIES (continued)

Share-based payment

The group has applied the requirements of FRS 20 Share-based Payment. In accordance with the transitional provisions, FRS 20 has been applied to all grants of equity instruments after 7 November 2002 that were unvested as of 1 July 2006.

The group has issued equity-settled share-based payments to certain employees and suppliers. Equity-settled share-based payments are measured at fair value at the date of grant. The fair value determined at the grant date of the equity-settled share-based payments is expensed on a straight-line basis over the vesting period, based on the group's estimate of shares that will eventually vest and adjusted for the effect of non market-based vesting conditions.

Fair value is measured by use of the Black-Scholes pricing model. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations.

2. TURNOVER

Turnover, which is stated net of value added tax, represents amounts earned in respect of the group's continuing activity as stated in the directors' report.

An analysis of turnover by geographical market is given below.

	2010 £'000	2009 £'000
United Kingdom	6,938	6,703
Rest of Europe	14,877	12,393
North America	23,290	16,419
Rest of World	3,574	2,215
	<u>48,679</u>	<u>37,730</u>

3. INFORMATION REGARDING DIRECTORS AND EMPLOYEES

	2010 £'000	2009 £'000
Directors' remuneration		
Directors' emoluments	<u>492</u>	<u>992</u>
Emoluments of highest paid director	<u>311</u>	<u>786</u>
	No	No
Average number of persons employed by the group during the year was:		
Management	8	8
Administration	46	40
Synchronisation and creative	22	21
	<u>76</u>	<u>69</u>
	£'000	£'000
Staff costs during the year (including directors)		
Wages and salaries	3,628	3,080
Social security costs	360	318
Share-based payment charges	146	232
	<u>4,134</u>	<u>3,630</u>

KOBALT MUSIC GROUP LIMITED

NOTES TO THE FINANCIAL STATEMENTS

Year ended 30 June 2010

4. OPERATING LOSS

	2010 £'000	2009 £'000
Operating loss is after charging:		
Depreciation of fixed assets		
Owned assets	386	348
Leased assets	6	7
Loss on disposal of fixed assets	1	-
Operating lease rentals		
Land and buildings	311	223
Plant and machinery	16	12
Foreign exchange losses	177	229
The analysis of auditor's remuneration is as follows		
Fees payable to the company's auditor for the audit of the group's annual accounts	50	47
Other services relating to tax	63	38
	<u> </u>	<u> </u>

5. INTEREST RECEIVABLE AND SIMILAR INCOME

	2010 £'000	2009 £'000
Bank interest receivable	1	1
	<u> </u>	<u> </u>

6. INTEREST PAYABLE AND SIMILAR CHARGES

	2010 £'000	2009 £'000
Bank loans and overdraft	19	34
Finance lease interest	-	1
Convertible loan interest	56	-
Other interest payable	1	8
	<u> </u>	<u> </u>
	76	43
	<u> </u>	<u> </u>

KOBALT MUSIC GROUP LIMITED

NOTES TO THE FINANCIAL STATEMENTS

Year ended 30 June 2010

7. TAX ON LOSS ON ORDINARY ACTIVITIES

	2010 £'000	2009 £'000
Current tax		
United Kingdom corporation tax based on the result for the year at 28% (2009 - 28%)	-	3
Double tax relief		
Non-reclaimable withholding tax on royalty payments received	298	198
	<u>298</u>	<u>198</u>
Total current tax	<u>298</u>	<u>201</u>

The standard rate of tax for the year, based on the United Kingdom standard rate of corporation tax is 28% - 2009 - 28%) The actual tax charge for the current year and the previous year differs from the standard tax rate for the reasons set out in the following reconciliation

	2010 £'000	2009 £'000
Loss on ordinary activities before tax	(1,591)	(2,158)
	<u>(1,591)</u>	<u>(2,158)</u>
Tax on loss on ordinary activities at standard rate	(445)	(604)
Factors affecting charge for the year		
Expenses not deductible for tax purposes	184	115
Capital allowances in (excess) deficit of depreciation	(32)	66
Other timing differences	-	9
Tax losses carried forward	440	857
Net non-reclaimable withholding tax on royalty payments received	298	143
Losses utilised	(147)	(385)
	<u>298</u>	<u>201</u>
Total actual amount of current tax	<u>298</u>	<u>201</u>

Deferred taxation

The parent company and various subsidiaries have, subject to agreement by HMRC, tax losses available for offset against future taxable profits arising from the same trades. These losses have an approximate value of £7.2 million (2009 - £6.1 million). Consequently, potential deferred taxation assets arise in these companies which have not been recognised in the financial statements due to the uncertainty of future profits against which these losses may be offset.

In June 2010 the UK Government announced that it would introduce legislation that would reduce the corporation tax rate to 27% with effect from 1 April 2011. This legislation was substantively enacted on 27 July 2010. The effective tax rate for the period to 30 June 2011 is expected to reduce accordingly.

KOBALT MUSIC GROUP LIMITED

NOTES TO THE FINANCIAL STATEMENTS

Year ended 30 June 2010

8. SHARE BASED PAYMENTS

Equity-settled share options

The company provides incentives in the form of share options to many employees of the group as well as a small number of key suppliers. Options are exercisable at a price equal to or greater than the latest issued or traded price of the company's shares on the date of grant. The vesting period is between one to three years. If the options remain unexercised after a period of between five and ten years from the date of grant the options expire. Some options are forfeited if the employee leaves the group.

Details of the share options outstanding during the year are as follows

	2010	Weighted average exercise price (in £)	2009	Weighted average exercise price (in £)
	Number of share options		Number of share options	
Outstanding at beginning of year	1,273,329	3.35	1,099,702	2.83
Granted during the year	78,680	6.00	212,820	6.00
Forfeited during the year	(11,357)	2.82	(8,683)	2.40
Exercised during the year	-		(30,510)	3.00
Expired during the year	-		-	
	<u>1,340,652</u>	3.51	<u>1,273,329</u>	3.35
Outstanding at the end of the year				
Exercisable at the end of the year	<u>1,330,969</u>	3.49	<u>1,213,677</u>	3.21

The inputs into the Black-Scholes option pricing model for options granted within the relevant period are as follows

Year ended 30 June	2010	2009
Weighted average share price	£4.63	£5.55
Weighted average exercise price	£6.00	£6.00
Expected volatility	25%	25%
Weighted average expected life	4.2 years	5.8 years
Weighted average risk-free rate	2.64%	4.90%
Expected dividend yield	-	-

Expected volatility was estimated by considering comparable companies and historical volatility of the group's share price over the previous 5 years.

The group recognised total expenses of £146k related to equity-settled share-based payment transactions in the year ended 30 June 2010 (2009 - £232k).

KOBALT MUSIC GROUP LIMITED

NOTES TO THE FINANCIAL STATEMENTS

Year ended 30 June 2010

9. PROFIT ATTRIBUTABLE TO THE COMPANY

The profit for the financial year dealt with in the financial statements of the parent company was £546k (2009 - £1,248k) As permitted by Section 408 of the Companies Act 2006, no separate profit and loss account is presented in respect of the parent company

10. TANGIBLE FIXED ASSETS

GROUP

	Office equipment and fixtures £'000	Software £'000	Computer equipment £'000	Total £'000
Cost				
At 1 July 2009	405	1,506	291	2,202
Additions	27	286	213	526
Disposals	(3)	-	(55)	(58)
At 30 June 2010	429	1,792	449	2,670
Depreciation				
At 1 July 2009	173	859	206	1,238
Provided during the year	69	237	86	392
Disposals	(2)	-	(55)	(57)
At 30 June 2010	240	1,096	237	1,573
Net book value				
At 30 June 2010	189	696	212	1,097
At 30 June 2009	232	647	85	964

Included in tangible fixed assets are leased assets with a net book value of £nil (2009 - £6k)

KOBALT MUSIC GROUP LIMITED

NOTES TO THE FINANCIAL STATEMENTS

Year ended 30 June 2010

10. TANGIBLE FIXED ASSETS (continued)

COMPANY	Office equipment and fixtures £'000	Computer equipment £'000	Software £'000	Total £'000
Cost				
At 1 July 2009	186	230	1,505	1,921
Additions	4	152	286	442
Disposals	-	(55)	-	(55)
At 30 June 2010	<u>190</u>	<u>327</u>	<u>1,791</u>	<u>2,308</u>
Depreciation				
At 1 July 2009	83	172	859	1,114
Provided during the year	28	48	238	314
Disposals	-	(55)	-	(55)
At 30 June 2010	<u>111</u>	<u>165</u>	<u>1,097</u>	<u>1,373</u>
Net book value				
At 30 June 2010	<u>79</u>	<u>162</u>	<u>694</u>	<u>935</u>
At 30 June 2009	<u>103</u>	<u>58</u>	<u>646</u>	<u>807</u>

Included above are leased assets with a net book value of £nil (2009 - £6k)

11. INVESTMENTS

COMPANY	Investment in subsidiary undertakings £'000
Cost	
At 1 July 2009 and at 30 June 2010	<u>119</u>

KOBALT MUSIC GROUP LIMITED

NOTES TO THE FINANCIAL STATEMENTS

Year ended 30 June 2010

11. INVESTMENTS (continued)

The company's wholly owned subsidiaries are as follows

Company	Class of shares	Proportion of voting rights and shares held	Country of registration or incorporation (if not England and Wales)
<i>Subsidiary undertakings</i>			
Kobalt Music Scandinavia AB	Ordinary	100%	Sweden
Kobalt Music Publishing Limited	Ordinary	100%	
Kobalt Music Services Limited	Ordinary	100%	
Kojam Music Limited	Ordinary	100%	
Kobalt Music Administration Limited	Ordinary	100%	
Kollector Limited	Ordinary	100%	
Kobalt Music Publishing (Italia) Limited	Ordinary	100%	
Kobalt Music Publishing America Inc	Ordinary	100%	USA
Kobalt Music Services America Inc	Ordinary	100%	USA
KMG Germany GmbH	Ordinary	100%	Germany
Kobalt Digital Services Limited	Ordinary	100%	
Kobalt Digital Licensing Limited	Ordinary	100%	
Kobalt Digital Services America Inc	Ordinary	100%	USA
Kobalt Digital Licensing America Inc	Ordinary	100%	USA

The principal activity of all subsidiary undertakings, other than the Kobalt Digital entities, is music publishing. The principal activity of the Kobalt Digital companies is the distribution and licensing of music recordings.

12. DEBTORS

	GROUP		COMPANY	
	2010 £'000	2009 £'000	2010 £'000	2009 £'000
Amounts owed by group undertakings	-	-	19,767	11,122
Other debtors	344	471	180	80
Prepayments and accrued income	14,137	12,245	189	131
	<u>14,481</u>	<u>12,716</u>	<u>20,136</u>	<u>11,333</u>

Other than £152k (2009 - £152k), which relates to rent deposits on leases that are due to expire after more than one year from the balance sheet date, all debtors are due within one year.

KOBALT MUSIC GROUP LIMITED

NOTES TO THE FINANCIAL STATEMENTS

Year ended 30 June 2010

13. CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR

	GROUP		COMPANY	
	2010 £'000	2009 £'000	2010 £'000	2009 £'000
Bank overdraft	-	80	-	-
Obligations under finance leases and hire purchase contracts (note 15)	-	6	-	6
Amounts owed to group undertakings	-	-	7,721	3,934
Trade creditors	282	730	100	95
Accruals and deferred income	22,771	18,353	176	240
Other taxes and social security costs	111	170	98	145
Other creditors	164	41	16	26
	<u>23,328</u>	<u>19,380</u>	<u>8,111</u>	<u>4,446</u>

14. CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR

	GROUP		COMPANY	
	2010 £'000	2009 £'000	2010 £'000	2009 £'000
Convertible loan	4,056	-	4,056	-

The convertible loan is secured by a charge over the group's assets

As detailed in note 18, the convertible loan was converted into ordinary shares on 31 December 2010

15. OBLIGATIONS UNDER FINANCE LEASES AND HIRE PURCHASE CONTRACTS

Amounts due under finance leases and hire purchase contracts

GROUP AND COMPANY	2010 £'000	2009 £'000
Amounts payable		
Within one year	-	7
Less finance charges allocated to future periods	-	(1)
	<u>-</u>	<u>6</u>

The group has annual commitments under non-cancellable operating leases are as follows

	Plant and machinery		Land and building	
	2010 £'000	2009 £'000	2010 £'000	2009 £'000
Operating leases which expire				
Within one year	-	-	69	66
Between one and five years	11	11	152	104
After more than five years	-	-	81	81
	<u>-</u>	<u>-</u>	<u>202</u>	<u>151</u>

KOBALT MUSIC GROUP LIMITED

NOTES TO THE FINANCIAL STATEMENTS Year ended 30 June 2010

16. CALLED UP SHARE CAPITAL

	2010 £'000	2009 £'000
Called up, allotted and fully paid		
4,902,315 (2009 - 4,852,315) ordinary shares of £0.05 each	245	242
1,030,274 (2009 - Nil) BA ordinary shares of £0.005 each	5	-
	<u>250</u>	<u>242</u>

On 9 July 2009, 200,000 ordinary shares of £0.05 each in the authorised but unissued capital of the company were divided into 2,000,000 ordinary shares of £0.005 each. Of these shares, 1,400,000 were designated BA ordinary shares of £0.005 each, 300,000 were designated as BB ordinary shares of £0.005 each with the remaining 300,000 shares being designated as BC ordinary shares of £0.005 each.

On 3 September 2009, the group issued 1,030,274 of the BA ordinary shares at par.

On 27 January 2010, 50,000 ordinary shares of £0.05 each were issued for consideration of £296k as a result of the exercise of share options.

On 31 December 2010, 684,986 ordinary shares of £0.05 each were issued for consideration of £4,062k as a result of the conversion of the loan.

17. RECONCILIATION OF MOVEMENT IN SHAREHOLDERS' FUNDS AND STATEMENT OF MOVEMENT ON RESERVES

GROUP

	Called up share capital £'000	Share premium account £'000	Share option reserve £'000	Profit and loss account £'000	Sharehol- ders' deficit 2010 Total £'000	Sharehol- ders' deficit 2009 Total £'000
At 1 July	242	10,768	728	(13,531)	(1,793)	247
Loss for the year	-	-	-	(1,889)	(1,889)	(2,363)
New equity share capital subscribed	8	294	-	-	302	91
Costs of issuing shares	-	(16)	-	-	(16)	-
Equity settled share based payment charge	-	-	146	-	146	232
At 30 June	<u>250</u>	<u>11,046</u>	<u>874</u>	<u>(15,420)</u>	<u>(3,250)</u>	<u>(1,793)</u>

KOBALT MUSIC GROUP LIMITED

NOTES TO THE FINANCIAL STATEMENTS

Year ended 30 June 2010

17. RECONCILIATION OF MOVEMENT IN SHAREHOLDERS' FUNDS AND STATEMENT OF MOVEMENT ON RESERVES (continued)

COMPANY	Called up share capital £'000	Share premium account £'000	Share option reserve £'000	Profit and loss account £'000	Sharehol- ders' funds 2010 Total £'000	Sharehol- ders' funds 2009 Total £'000
At 1 July	242	10,768	728	(2,843)	8,895	7,324
Profit for the year	-	-	-	546	546	1,248
New equity share capital subscribed	8	294	-	-	302	91
Costs of issuing shares	-	(16)	-	-	(16)	-
Equity settled share based payment charge	-	-	146	-	146	232
At 30 June	<u>250</u>	<u>11,046</u>	<u>874</u>	<u>(2,297)</u>	<u>9,873</u>	<u>8,895</u>

Share option reserve

The group has issued equity-settled share-based payments to certain employees and suppliers. Equity-settled share-based payments are measured at fair value at the date of grant. The fair value determined at the grant date of the equity-settled share-based payments is expensed on a straight-line basis over the vesting period, based on the group's estimate of shares that will eventually vest and adjusted for the effect of non market-based vesting conditions. A corresponding entry is recognised in the share option reserve.

18. POST BALANCE SHEET EVENTS

Convertible loan stock totalling £4,056k as at the balance sheet date was converted into ordinary shares on 31 December 2010.