# the Local Shopping REIT plc

**Annual Report**

for the year ended 30 September 2013

Stock Code: LSR

# What we do . . .

## The Local Shopping REIT plc ("LSR") is a Real Estate Investment Trust ("REIT") that owns a diversified portfolio principally comprising local shopping assets in urban and suburban centres throughout the UK.

Typical of the portfolio are shops in local shopping parades and neighbourhood venues for convenience or "top-up" shopping. As at 30 September 2013 the Company's directly owned portfolio comprised 640 properties, with over 2,000 letting units.

The Company's strategy is to maximise shareholder value through (inter alia):

- disposing of its assets progressively in accordance with prevailing market conditions with a view to repaying the Company's existing debt facilities (where consistent with the protection of value) and ultimately returning value to shareholders;
- exploiting the potential of the portfolio through active asset management.

### What is a REIT?

Real Estate Investment Trusts are listed property investment companies or groups not liable to corporation tax on their rental income or capital gains from their qualifying activities.

For more information see **LSR at a Glance** on pages **2** and **3**

See further information online:
**www.localshoppingreit.co.uk**

# Introduction to the 2013 Annual Report

Welcome to the Annual Report of the Local Shopping REIT plc for the year ended 30 September 2013. Besides fulfilling the legal obligations for reporting to shareholders, this document aims to meet the recently introduced requirements for the provision of a Strategic Report.

As shareholders will be aware, the most significant event for the Company during the year was the Strategy Review undertaken by the Company's non-executive directors. Consequential to this was the adoption by the Company of a new investment policy (which is set out in the Strategic Report) and the decision to outsource the executive management of the business to INTERNOS Global Investors LIMITED ("INTERNOS"). These changes are reflected in the contents of this report.

Following the Strategy Review, the Company's Joint Chief Executives, Mike Riley and Nick Gregory, and its Finance Director, Victoria Whitehouse, left the business during July 2013. All three made vital contributions in maintaining the operational performance of the business during a difficult period in the retail property market and we are grateful to them. Other members of the team transferred to INTERNOS where they continue their work on the portfolio, in line with the new investment policy, and we thank them for their assistance in ensuring an effective transition. We also welcomed as a director of the Company Steve Faber who, as Head of UK Investment Management at INTERNOS, holds primary responsibility for executing the revised investment strategy.

The directors consider that, in accordance with the UK Corporate Governance Code 2012, the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's performance, business model and strategy. We hope you will find this report informative and helpful.

**Grahame Whateley**
Chairman

## Contents


### Overview

02 LSR at a Glance
04 Highlights

### Strategic Report

05 Investment Policy
06 Business Review
10 Finance Review
14 Principal Risks
16 Corporate Responsibility

### Our Governance

18 Directors' Report
19 Board of Directors
20 Governance
29 Audit Committee Report
30 Remuneration Report

### Our Financials

36 Independent Auditors' Report to the Members of The Local Shopping REIT plc
38 Consolidated Income Statement
38 Consolidated Statement of Comprehensive Income
39 Consolidated Balance Sheet
40 Consolidated Statement of Cash Flows
41 Consolidated Statement of Changes in Equity
42 Notes to the Financial Statements
67 Company Balance Sheet

### Supplementary Information

73 Glossary of Terms
74 Shareholder Contacts

# LSR at a Glance

**Our directly owned portfolio was revalued at 30 September 2013 at £168.9m, reflecting an equivalent yield (excluding the residential element) of 9.48%. The portfolio comprised 640 properties, with 2,037 letting units, producing an annual rental income of £15.45m.**

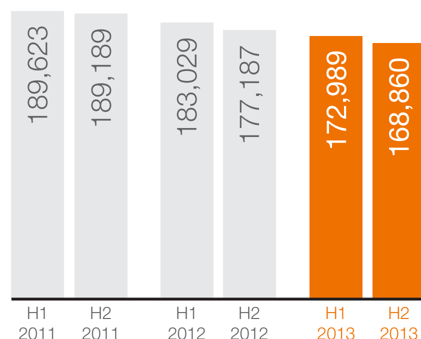
Over the year as a whole, the portfolio Market Rent fell on a like-for-like basis by 1.44%.

On a like-for-like basis, the portfolio value decreased by 4.06% over the period.

## **Portfolio Value** (£000)

-4.70%

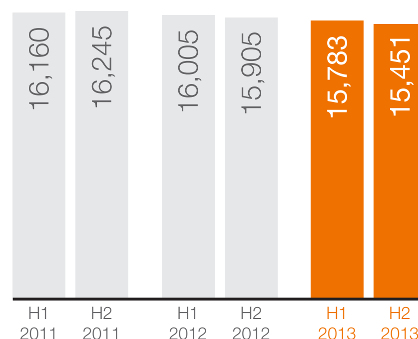
2012: £177,187




## **Portfolio Rent** (£000)

-2.85%

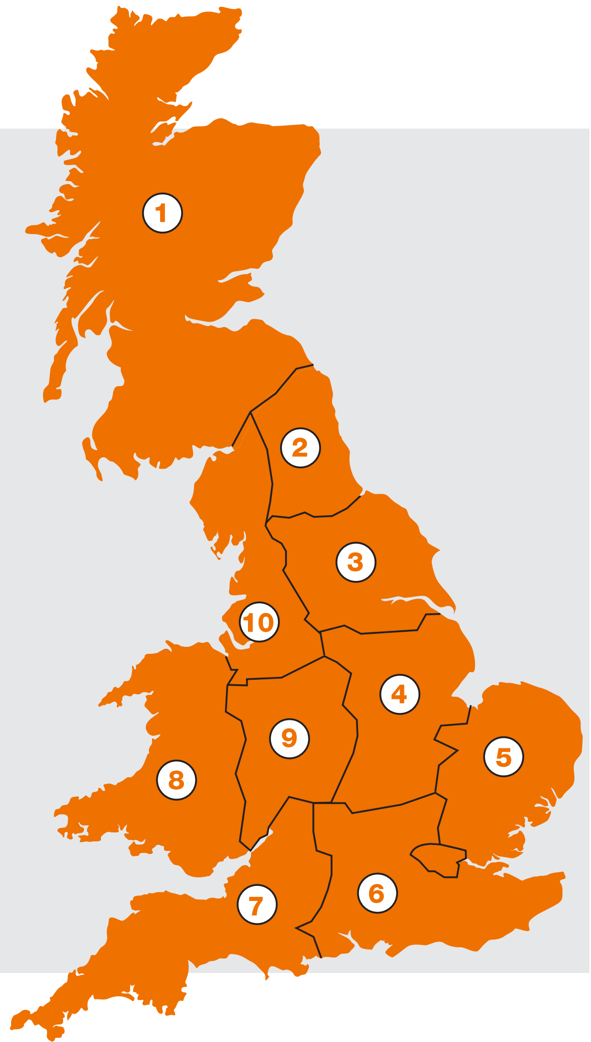
2012: £15,905



# Exploiting the potential of our property portfolio through active asset management

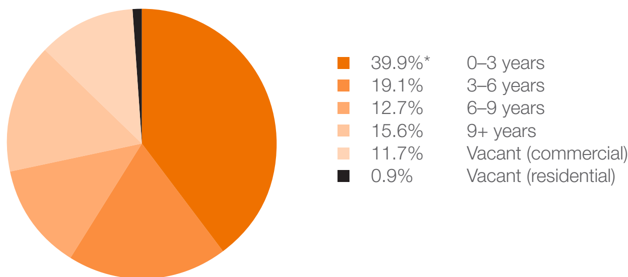
% of portfolio

| | Market Rent | Value |
|---|---|---|
| 1 Scotland | 11.9% | 11.5% |
| 2 North East | 2.6% | 2.7% |
| 3 Yorkshire & Humberside | 8.5% | 8.0% |
| 4 East Midlands | 4.00% | 4.3% |
| 5 East Anglia | 4.8% | 5.1% |
| 6 London and South East | 25.9% | 28.4% |
| 7 South West | 13.4% | 13.8% |
| 8 Wales | 5.2% | 4.7% |
| 9 West Midlands | 7.8% | 6.7% |
| 10 North West | 15.8% | 14.7% |




## Lease Expiry Profile

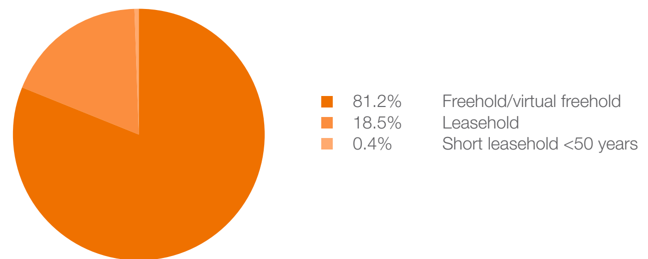
As a percentage of ERV



| | |
|---|---|
| 39.9%* | 0–3 years |
| 19.1% | 3–6 years |
| 12.7% | 6–9 years |
| 15.6% | 9+ years |
| 11.7% | Vacant (commercial) |
| 0.9% | Vacant (residential) |

## Tenure

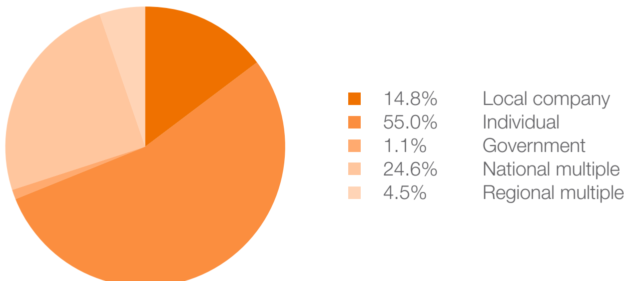
As a percentage of valuation



| | |
|---|---|
| 81.2% | Freehold/virtual freehold |
| 18.5% | Leasehold |
| 0.4% | Short leasehold <50 years |

## Tenant Grade

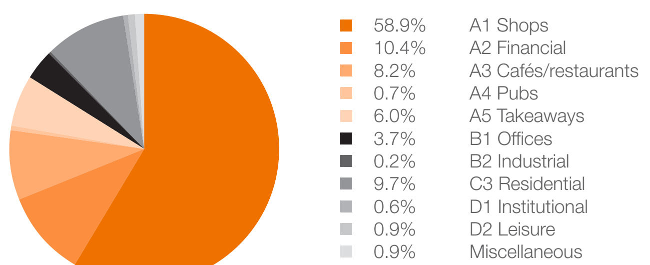
As a percentage of Market Rent



| | |
|---|---|
| 14.8% | Local company |
| 55.0% | Individual |
| 1.1% | Government |
| 24.6% | National multiple |
| 4.5% | Regional multiple |

## Planning Use

As a percentage of Market Rent



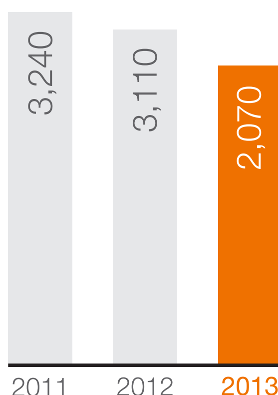
| | |
|---|---|
| 58.9% | A1 Shops |
| 10.4% | A2 Financial |
| 8.2% | A3 Cafés/restaurants |
| 0.7% | A4 Pubs |
| 6.0% | A5 Takeaways |
| 3.7% | B1 Offices |
| 0.2% | B2 Industrial |
| 9.7% | C3 Residential |
| 0.6% | D1 Institutional |
| 0.9% | D2 Leisure |
| 0.9% | Miscellaneous |

* Including residential AST leases.

# Highlights

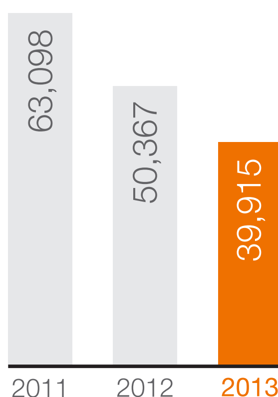
## Recurring Profit (£000)

-33.44%




## Adjusted Net Asset Value (£000)

-20.75%




## Financial Highlights

- Recurring profit £2.07m or 2.5 pence per share (2012 restated: £3.11m or 3.8 pence per share) with a loss for the financial year of £6.07m or 7.5 pence per share (2012: loss of £9.17m or 11.3p per share).
- Net Asset Value (NAV) of £33.6m or 41 pence per share (2012: £41.3m or 50 pence per share).
- Adjusted NAV of £39.9m, or 48 pence per share, excluding liabilities arising from derivative financial instruments (2012: £50.4m, or 61 pence per share).
- Total net debt of £127.7m, reflecting an LTV of 75.2%. New finance arrangements agreed extending HSBC facility to April 2018.
- Debt free properties valued at £7.9m.

## Portfolio

- Directly owned portfolio revalued at 30 September 2013 at £168.9m (2012: £177.2m), reflecting an equivalent yield (excluding the residential element) of 9.48%. The portfolio comprised 640 properties, with 2,037 letting units, producing an annual rental income of £15.45m.
- During the year three commercial units and nine flats sold at a 16.02% premium to their preceding valuation of £1,169,600.
- On a like-for-like basis, excluding the sold properties, portfolio valuation decreased by 4.06% from £176.0m to £168.9m.
- Annual rent roll of £15.45m (2012: £15.9m) with like-for-like rent down 2.3% (2012: down 1.7%).
- Over the year, portfolio Market Rent reduced by 1.94% (2012: -0.45%). On a like-for-like basis, Market Rent reduced by 1.44%.

## Operational Highlights

- Overall void rate 12.38%, equivalent to Market Rent of £2.11m (2012: 10.9% and £1.89m).
- Void rate improved from 12.43% (end-July) to 11.97% (end-October).
- 116 vacant commercial units let at an annual rental income of £1,003,840 per annum (2012: 107 units let at £986,309 per annum).
- 154 rent reviews with an average rental uplift of 5.4% (£114,833) above previous passing rent.
- 42 lease renewals secured at a net rental decrease of £29,469 (-5.4%), but at £3,456 (0.7%) above Market Rent.
- Rental deposits held of £862,000 or 22.3% of the quarterly rent roll (2012: £927,000).
- Seven flat conversions completed and leased, adding £55,440 per annum to rent roll.
- Planning consent secured for nine flats and two changes of use, including the division of one unit into two.
- Strategy Review completed, culminating in the adoption of a new investment policy and appointment of external investment manager with effect from 22 July 2013.
- As a consequence of the Strategy Review, estimated future cost savings of £0.9m per annum resulting from lower administrative costs and the recently negotiated surrender of the Company's West End office.

## Joint Ventures

Consistent with the adoption of its revised investment policy, the Company ceased further investment in joint ventures and disposed of its investment in the joint venture with Pramerica Real Estate Investors and with Schroders. The Company maintains its investment in its small joint venture with an established UK financial institution, which is expected to wind-down in due course.

Strategic Report

# Investment Policy

**On 25 July 2013 the Company adopted the new investment policy set out below. The Directors have appointed INTERNOS Global Investors Limited ("INTERNOS") to execute the new policy and to take responsibility for the operational management and performance of the Company's investment property portfolio.**

## Objectives

The Company's investment objective is to maximise value for its shareholders from its existing portfolio of local real estate assets, comprising local shops in urban and suburban areas, as well as neighbourhood and convenience properties throughout the UK.

The Company seeks to achieve this through:

- Realising its assets progressively in accordance with prevailing market conditions with a view to repaying the Company's existing debt facilities (where consistent with the protection of value) and ultimately returning value to shareholders;
- Exploiting the potential of its remaining property portfolio through active asset management; and
- Making further investments in properties only where such investment is deemed by the Board, in consultation with INTERNOS, to be significant to protect or enhance the realisable value of an existing property asset. In such circumstances the Company may seek to purchase assets intrinsically linked to existing assets in its core local retail portfolio (such as flats situated above local convenience stores in order to exploit marriage value).

The Company has the power under its Articles to borrow up to an amount equal to 75% of gross assets at the time of the drawdown. The Company intends to reduce its gearing ratio from its current level going forward.

## Strategy

The Company seeks to implement its investment policy as follows:

- All property assets will be sold as expeditiously as is consistent with the protection of value, with an initial focus on those properties already optimised for sale and those in markets where the Company has relatively few assets, so as to reduce property management costs. The Company aims to complete the disposal programme within a period of approximately four years.
- Proceeds from the sales of properties will be used to repay the Company's existing debt facilities. The amount the Company will have to pay in respect of termination fees (including crystallisation of any mark to market liability) under its derivative arrangements will be significantly increased or reduced depending on the prevailing interest rates at the time of the repayment of the debt. Accordingly, the Company has not set a prescriptive timetable for the sale of the properties, but has instructed and incentivised INTERNOS to dispose of properties at such a time during the next four years with the intention of aiming to minimise the total break costs payable and ultimately maximise the monies paid to the shareholders.

Strategic Report

# Business Review

- As the property assets of the Company are sold, the Board will use cash proceeds in excess of the amount that is required to repay allocated loan amounts and related financing costs either for further debt repayment or for return of capital to the shareholders in accordance with its assessment at that time of what will deliver the best time and risk adjusted returns to shareholders.
- The orderly phasing of property sales over a period of time is a key aspect of this proposal and the new investment policy, firstly in order to protect value and not over-supply this specialist property market at any one time, and secondly to mitigate associated friction costs, and in particular the early repayment of hedging arrangements. Balancing these two factors will be an important part of executing the new investment policy.
- New property assets will not be acquired unless such an acquisition is deemed by the Board, in consultation with INTERNOS, to be essential to protect or enhance the realisable value of an existing property asset. A corporate transaction, such as the merger or sale of the Company, will be considered, where this offers opportunity to accelerate the realisation of optimal value for shareholders.

## Business Model

Our business model continues to focus on generating profits from our portfolio of investment properties throughout the United Kingdom, which largely comprise local and convenience shopping assets. Core to the achievement of good returns is letting space to reliable tenants at affordable rents and the minimisation of tenancy voids and their associated costs.

Our model is focussed on the following principal contributors to the success of our business:

- the talent and commitment of our asset management team;
- our relationships with national and local advisers and agents; and
- the well-being of the businesses that occupy our properties and the communities in which they operate.

## Business Review 2012-13

Of greatest significance was the conclusion of the Strategy Review carried out by the non-executive directors during the year, and the subsequent adoption by shareholders of the Company's new investment policy. The principal objective of the new policy is (in summary) for the Company to sell its assets progressively in accordance with prevailing market conditions, with a view to repaying debt and ultimately returning value to shareholders.

As a result of the Strategy Review the Joint Chief Executives, Mike Riley and Nick Gregory, and the Finance Director, Victoria Whitehouse, left the business during July 2013 and INTERNOS Global Investors Limited ("INTERNOS") was appointed by the Board to execute the new strategy and manage the Company's investment property portfolio. Members of the operational team transferred to INTERNOS and Steve Faber, Head of UK Investment Management at INTERNOS, joined the Board.

As a result of the change in investment policy, the Company withdrew from fee based asset management activities for joint ventures and third parties and disposed of its interests in its joint venture with Pramerica Real Estate Investors and its investment with Schroders. The Company retains its interest in the small joint venture with an established UK institution.

On an operational level we seek to execute the revised investment policy through:

- identifying priority properties for sale – for example, those producing low cash returns as a result of high actual or potential void rates and/or high maintenance or capital expenditure;
- targeting likely purchasers – for example, potential owner-occupiers and (particularly with residential flats) local investors;
- carrying out the sales programme in a manner that does not incur unnecessary debt finance breakage costs;
- continuing to optimise the portfolio value and recurring profits through active management of the assets, minimising rental voids, arrears and costs (both operational and corporate);
- as appropriate, exploiting opportunities for adding value through re-gearing leases, planning consents and developments.

In executing the sales strategy, we recognise that:

- the residual portfolio needs to be of sufficient quality to facilitate potential refinancing;
- the level of cash held by the business must be sufficient to fund continuing operations;
- the Company will need to continue to comply with the REIT and other applicable regulatory regimes.

## Results and Net Asset Value

On an IFRS basis, the Group recorded a loss for the financial year of £6.07m (2012: IFRS loss of £9.18m). The recurring profit for the year was £2.07m (2.5p per share), compared with a restated recurring profit of £3.11m (3.8p per share) in 2012. A reconciliation of the recurring profit to the loss before tax in the Income Statement is given in the Financial Review section, below.

In addition the Group earned a non-recurring profit of £845,000 from its joint venture with Pramerica (which was divested during the year) and its now discontinued asset management activities for joint ventures and third parties (2012: loss of £294,000).

The net asset value of the Group declined over the year by £7.7m to £33.6m, primarily as a result of the fall in the valuation of the property portfolio. This equates to an NAV per share of 41 pence (30 September 2012: 50 pence). The NAV per share adjusted for the fair value of interest rate swap contracts fell to 48 pence (2012: 61 pence).

## Portfolio Performance and Asset Management

### Portfolio Summary

| | |
|---|---|
| Value | £168.9 |
| Initial Yield | 8.72% |
| Reversionary Yield | 9.70% |
| Equivalent Yield* | 9.48% |
| Rent p.a. | £15.5m |
| Market Rent | £16.9m |

Our investment property portfolio was re-valued at 30 September 2013 at £168,860,000. This reflected an equivalent yield (excluding the residential element) of 9.48%. The portfolio comprised 640 properties, with 2,037 letting units, producing an annual rental income of £15.45m.

On a like-for-like basis the portfolio valuation decreased by 4.07% from £176.0m to £168.9m.

The aggregate Market Rent for the portfolio at 30 September 2013 was £16,896,962, a fall of 1.94% (2012: -0.45%). On a like-for-like basis, the portfolio Market Rent fell by 1.44%.

Rental income and the portfolio vacancy rate continued to be affected by the challenging conditions in the retail market and the economy generally. The combined Market Rent of vacant properties at the year-end was £2,106,193m or 12.38% of aggregate portfolio Market Rent (2012: 10.94%). Of this, commercial properties accounted for £2,097,243 and residential units were £159,028. The portfolio void rate reflects our balanced policy of taking possession early where tenants are in financial difficulty, which has contributed to the reduction in bad debts in comparison with 2011-12.

The void rate improved during the final quarter and into the new financial year, moving from 12.43% (end-July) to 11.97% (end-October). We also no longer distinguish between assets deliberately held vacant and other vacant properties.

We continued our localised and pragmatic approach to leasing during the year, enabling us to let 116 vacant commercial units at a total rent of £1,003,840 per annum (2011-12: 107 lettings at £986,309). These units were let, on average, at 17.2% below Market Rent. However, of these new leases 21 are subject to stepped rents, rather than extended rent-free periods (an approach which is both conducive to the independent trader sector and helpful to our cash flow). Our average rent free period on lettings completed during the year was 67 days (2012: 69 days). At 30 September 2013 the letting pipeline comprised 34 units under offer, at rents totalling £396,610 per annum.

Rent reviews were carried out on 154 units during the year, increasing rental income by a total of £114,833 per annum, reflecting an average uplift of 5.4% over the previous passing rent and 7.6% above Market Rent.

## Range of values within the portfolio

| Value Range | No. of Properties | Value £m | Equivalent Yield* |
|---|---|---|---|
| £0 - 100k | 188 | 13.5 | 9.38% |
| £101k - £200k | 219 | 31.1 | 8.51% |
| £201k - £500k | 157 | 51.4 | 8.73% |
| £501k - £1m | 52 | 35.8 | 8.11% |
| £1m - £3m | 22 | 30.3 | 8.22% |
| £3m + | 2 | 6.7 | 7.79% |
| Total | 640 | 168.9 | 9.48% |

*Excluding residential element

The average property value is £265,503 and the median is £135,000. The residential element of the portfolio has been valued at £17,831,525, based typically on 85% of vacant possession value. The average value of the residential units is £55,724.

Strategic Report

# Business Review continued

Leases were renewed on 42 units, resulting in a net rental decrease of £29,469 (-5.4%), but at a slight increase (0.7%) over Market Rent. In addition, we undertook 11 surrender and re-grants, resulting in average increases at 9.7% above the previous passing rent, and exceeding Market Rent by 14.7%.

We continue to seek rent deposits of between three to six months on the letting of units. The total value of deposits held at 30 September 2013 was approximately £862,000 (30 September 2012: approximately £927,000) or 22.3% of our quarterly rent roll, providing a measure of protection against tenant default.

During the year we completed a number of conversion projects, resulting in the addition of seven flats to the portfolio. These were all let within a short time of project completion, adding £55,440 per annum to the portfolio rent roll. Two further conversions of redundant upper parts were underway at the year-end, one of which will provide a new stand-alone flat, whilst the other will extend an existing flat. In addition, during the year we secured planning consents for nine flats and two further changes of use, including the division of one unit into two.

Whilst the removal of empty property rates and the increasing imposition of council tax on vacant residential flats did not have a material impact during the year, in common with other landlords we anticipate that this will become an increasing factor in future years.

## Acquisitions and Sales

The new investment policy, adopted in July 2013, focuses on the orderly selling down of our property portfolio. Accordingly, we do not plan to acquire properties unless to do so contributes to the achievement of the overall sales strategy. We did not in any case acquire any new properties during 2012-13.

During the year we sold three commercial units and nine flats for a total of £1.36m, representing a 16.02% premium to valuation. Following the year-end we completed the sale of one further commercial unit. Further sales of 22 properties (16 commercial and six flats) were in solicitors' hands at the date of this report.

## Joint Ventures and Third Party Asset Management

In accordance with the new investment policy, during July 2013 we disposed of our investment in the joint venture with Pramerica Real Estate Investors ("LPI") and co-investment with Schroders ("LRF"). At the same time we relinquished our asset management contracts for those ventures and for our continuing small joint venture with a UK bank. Prior to their cessation our external asset management activities, including those associated with co-investment projects, produced profit after tax of £845,000 during the year (2012: £294,000).

## Property Investment Market

Investor demand for retail property remains highly selective over asset quality and income security, with institutional investors focussed on medium to larger investments in top tier retail locations. Private investors remain active in the market for smaller lot sizes. Some agents have reported a limited uptick in activity from opportunistic investors who are starting to move further up the risk curve, acquiring selective assets in good secondary locations where there is a clear asset management opportunity. Auction houses are reporting an increase in investment volumes and higher success rate provides evidence of an improvement in demand for high street retail.

Pricing levels in the market remain polarised and reflect the trends evident in the occupier market, with yields remaining stable for assets in top trading locations that benefit from long leases and tenants of national covenant strength. In contrast, there has been further outward pressure for the secondary and tertiary assets with investors factoring in significant costs associated with voids and refurbishment.

## Occupier Market

The traditional high street occupier market remains a challenging environment for landlords, particularly for assets located in small and medium sized towns outside of London and the South East, with some markets suffering from vacancy rates as high as 30%, compared to the national rate of 14.1% reported in June 2013 (Local Data Company).

High occupancy costs (in particular business rates), declines in real wages and continued pressure on the traditional retail model continues to impact on the viability of retailers. A number of high profile administrations over the past 12 months released significant numbers

## Like-for-like portfolio – adjusted for part sales

| | 30 September 2013 | 30 September 2012 | Change |
|---|---|---|---|
| Value | **£168.9** | £176.0 | -4.07% |
| Initial Yield* | **8.72%** | 8.62% | +10bps |
| Reversionary Yield* | **9.70%** | 9.40% | +31bps |
| Equivalent Yield* | **9.48%** | 9.31% | +18bps |
| Rent p.a. | **£15.5m** | £15.8m | -2.48% |
| Market Rent p.a. | **£16.9m** | £17.1m | -1.25% |

* Excluding residential element

of retail units on to the market. Many retailers with strong covenants are focussing primarily on the rationalisation of existing store portfolios to the top trading locations.

These trends are particularly apparent in traditional high streets in second tier towns, where the shift in shopping patterns means that national chains find it difficult to operate at target profitability levels. The velocity of this structural shift has been exacerbated by well publicised difficulties in the retail sector (for example, Blockbuster, Woolworths, Clintons, Peacocks, Bon Marché, Game, JJB, Jessops), so that poorly located shops are experiencing prolonged void periods, with many such assets now obsolete.

This negative commentary relates primarily to comparison retailing, often in moribund locations and based on declining product lines (for example, video). Against this, certain retail segments are performing robustly; some as a product of the downturn (for example, cheque cashing and charity), but mostly because the optimal delivery model is a conveniently located shop.

Examples include coffee shop, hairdresser, tattooist, restaurant and the convenience store formats of national food retailers. These uses are often well suited to premises that are located in local or neighbourhood shopping locations.

## Business Outlook

An improvement in institutional investor sentiment seems likely to translate to increasing interest in assets outside of central London, placing some downward pressure on yields for assets in good locations within affluent markets – predominantly in the South East.

Assets in poor secondary and tertiary locations are likely to remain out of favour with larger investors, as they continue to price in shorter contracted income streams and uncertainty over leasing vacant space. These markets will remain largely driven by local investors, who tend to be highly selective and often reliant on the availability of financing.

Across the sectors it has become apparent that a number of investors are willing to engage in activities associated with higher levels of risk – for example, office development. It remains to be seen if this pressure of money will engage with the more granular and geographically diffuse opportunity presented by the local shopping sector.

The outlook for the retail sector continues to be mixed. Despite the economy starting to show signs of a meaningful recovery it will take time before this filters through to real wage growth for consumers, meaning that comparison retailers will remain under pressure.

A shortage of prime high street pitches and competition between retailers to secure operational space in established retail locations may start to provide some stability for rental values. This appears to be supported in part by a number of on-line retailers, often in the fashion sector, who are looking to establish a physical presence to underpin brand identity with consumers. By so doing, they can take advantage of the economic benefits (lower delivery costs outweighing bricks, mortar and staff costs) of click-and-collect.

However, these positive trends seem likely to remain focussed on the prime high street locations. The outlook for second tier towns appears set to remain weak, with rental values under pressure as landlords compete to secure income and avoid paying rates for vacant premises.

The environment for local shopping appears more benign; insofar as it never really experienced the temporary prosperity of the last boom, but equally the segment has not suffered at an occupational level to the extent that second tier towns have.

## Values by Region

| | % of portfolio value | Valuation movement |
|---|---|---|
| Scotland | 11.5% | -7.7% |
| North East | 2.7% | -10.1% |
| Yorkshire & Humberside | 8.0% | -4.8% |
| East Midlands | 4.3% | -7.8% |
| East Anglia | 5.1% | +1.1% |
| London & South East | 28.4% | -1.8% |
| South West | 13.8% | +3.4% |
| Wales | 4.7% | -7.7% |
| West Midlands | 6.7% | -6.1% |
| North West | 14.7% | -2.8% |

Strategic Report

# Finance Review

The financial statements contained in this report have been prepared in accordance with International Reporting Standards ("IFRS"). No new accounting policies were adopted during the year.

## Results

The Group has recorded a loss for the financial year of £6.07m. This arose, in the main, from the following factors:

- the write-down of the fair value of the property portfolio, which is recorded in the Income Statement in accordance with IFRS;
- professional advisers' fees, staff termination costs and other expenses incurred in relation to the change in investment policy;
- the fall in rental income during the year as a result of the sale of a number of properties, an increase in the void rate and the granting of rent concessions to tenants;
- charges incurred and accelerated amortisation of bank finance fees as a result of the renegotiation and extension of banking facilities.

## Key Performance Indicators

The following financial key performance indicators are monitored by the directors to review the performance of the business, in addition to the specific measures described in the Business Review which are used to monitor the performance of the property portfolio.

| | 30 September 2013 | 30 September 2012 restated |
|---|---|---|
| Interest cover* | 184% | 209% |
| Loan to value (LTV) ratio† | 75.2% | 73.5% |
| Adjusted NAV per share‡ | 48p§ | 61p§ |
| Gearing (net of cash held) | 380% | 317% |
| Recurring profit per share¶ | 2.5p | 3.8p |

* Based on rental income compared to interest payable
† Net of cash held
‡ Based on 82,505,853 shares in issue at 30 September 2013 (2012: 82,505,853)
§ Adjusted to exclude the fair value of financial derivatives
¶ Based on 81,409,308 shares on which dividends were previously paid (2012: 81,409,308)

## Recurring Profit

The recurring profit for the year was £2.07m (2012 restated: £3.11m), the calculation of which remains consistent with previous years. A reconciliation of the loss before tax to the recurring profit, including the effect of discontinued operations, is as follows:

| | 30 September 2013 £000 | 30 September 2012 restated £000 |
|---|---|---|
| Loss before tax | (6,071) | (9,178) |
| Profit on discontinued operations | (345) | (294) |
| Profit (loss) before tax on continuing operations | (6,416) | (9,472) |
| Movement in fair value of the portfolio | 8,778 | 12,165 |
| Movement in the fair value of the interest rate swaps held | (2,753) | (216) |
| Profit on sale of investment properties | (114) | (84) |
| Non-recurring income | (75) | (130) |
| Non-recurring expenditure and net resolution of aged balances | 2,519 | 506 |
| Non-recurring income and expenditure incurred by joint ventures | 131 | 341 |
| Recurring profit on continuing operations | 2,070 | 3,110 |

The recurring profit per share for the year was 2.5 pence (2012 restated: 3.8 pence). Until the year under review the Group's dividend policy was to distribute 100% of recurring profits by way of dividend. Following the change in dividend distribution policy described in the Business Review, no dividend will be paid for the year (2012: 4.0p per share).

The major factor in the reduction of the recurring profit was the diminution in gross rental income of £1.16m, from £15.81m to £14.65m, resulting from an increase in the void rate during the year and the decrease in Market Rent.

Property operating costs remained broadly consistent during the period, at £2.6m. The loss of asset management income from joint ventures and third parties from July onwards (which is unlikely to be replaced) also impacted on the recurring profit.

A further contributing factor was the sale of a number of properties during the year, and the full effect of sales that occurred during 2011-12.

Non-recurring expenditure includes:

- charges incurred and accelerated amortisation of bank finance fees as a result of the renegotiation and extension of banking facilities;
- professional advisers' fees, staff termination costs and other expenses incurred in relation to the Strategy Review and the change in investment policy;
- net resolution of aged balances arising from the introduction of improved systems for estimating accruals and pre-payments following the management changes arising from the Strategy Review.

Excluding the impact of significant non-recurring items from both years, administrative expenses for the year were broadly in line with 2011-12. The level of administrative expenses is expected to reduce in future years, as the revised management arrangements and the exit of the Company's office lease commitments take full effect.

Our continuing focus throughout the year on credit control has led to a reduction in impairment losses recognised to £656,314 (2012: £684,352).

Bank interest payable remained broadly in line with 2011-12. The Group continues to hold the same total cover of interest rate swaps as in 2012 subject to the £200,000 per quarter amortisation of one of the contracts. The liability arising from these swaps has reduced compared with 2012, with a credit of £2.75m reflected in the Income Statement for the year (2012: £0.2m).

## Net Assets

The net assets of the Group fell to £33.6m at the year end (2012: £41.3m), largely as a result of the decline in the fair value of the portfolio.

During the year, further investment was made in reconfiguring properties to improve prospects for sale and letting, including the conversion of redundant upper parts to residential flats. In addition, investment was made in maintaining the condition of properties to ensure the units remain attractive to new tenants and retain existing tenants, as well as to comply with regulatory requirements.

The Group's revaluation policy remains unchanged. At the half year and year end, 25% of the portfolio, plus all properties purchased in these two six-month periods (2013: none), were valued by Allsop LLP, a firm of Chartered Surveyors, acting as external valuers, who are experienced in property types held by the Group. The remainder of the portfolio was valued on the basis of Market Value by the directors who have relevant experience and professional qualifications.

## Joint Ventures and Investments

Investments in joint ventures continue to be equity accounted for during the period of the Group's ownership. The Group continues to hold an interest in the small property joint venture with a financial institution. At the year end the Group had invested £0.71m in this joint venture. The Group's interest in the joint venture with Pramerica Real Estate Investors and its co-investment with Schroders were divested in July 2013. A loss was incurred on the disposal of the joint venture interests of £0.50m, which is included in the Discontinued Operations result in the Consolidated Income Statement.

## Banking Facilities

For much of the year the Group operated using the following facilities:

**Group debt facilities in place at 30 September 2012**

| Loan | Facility £m | Loan Outstanding £m | Undrawn Facility £m | LTV Covenant | Termination Date |
|---|---|---|---|---|---|
| Barclays Fixed Rate Loan | 69.2 | 69.2 | – | No | October 2016 |
| HSBC Term Loan 1 | 47.7 | 47.7 | – | No | April 2016 |
| HSBC Term Loan 2 | 10.5 | 10.5 | – | Yes | October 2016 |
| HSBC Revolving Credit Facility | 35.0 | 9.5 | 25.5 | Yes | October 2016 |
| | £162.4m | £136.9m | £25.5m | | |

Strategic Report

# Finance Review continued

Following the Strategy Review, the Group's debt facilities were restructured and extended as shown in the table below.

**Group debt facilities in place at 30 September 2013**

| Loan | Facility £m | Net Amount Outstanding £m | LTV Covenant | Amortisation | Termination Date |
|---|---|---|---|---|---|
| Indus (Eclipse 2007-1) plc | 69.2m | 68.6m (Note: Net of £600k held on amortisation escrow a/c) | None | £300k per quarter held in amortisation escrow account | 16 January 2017 |
| HSBC – Term Loan 1 | 46.5m | 46.5m | 91.5% – NOS 4/6 combined | 1.8% pa of outstanding loan | 30 April 2018 |
| HSBC – Term Loan 2 | 19.8m | 19.8m | 91.5% – NOS 4/6 combined | 1.8% pa of outstanding loan | 30 April 2018 |
| **Total** | **£135.5m** | **£134.9m** | | | |

At 30 September 2013 the total debt outstanding was £134.9m (2012: £136.9m), net of the Indus escrow deposit balance of £600,000.

The change in LSR's strategy to focus on a realisation programme was approved by the Group's lenders, HSBC Bank plc ("HSBC") and Indus (Eclipse 2007-1) plc ("Indus") (an affiliate of Barclays Bank plc), resulting in a number of changes to the facilities.

In the case of Indus, consent was granted on the condition that an amortisation payment of £300,000 is paid each quarter into an account over which the lender's agent has sole signing rights. As at 30 September 2013, £600,000 has been transferred to this account relating to the April and July 2013 interest payment dates. Although these amounts have not yet been used to repay the facilities, the Net Amount Outstanding figure in the table assumes that they netted off against the loan in order to provide a fair reflection of the amount outstanding.

In the case of HSBC, the lender required that the existing facilities for two subsidiaries be amended and re-stated, with the following principal amendments:

- Cross-collateralisation of the two facilities, with security being granted over each of the property owning companies and their respective portfolios to secure the debt outstanding on the other facility. Although this provides the bank with a more diversified security pool, it also allows the Group to sell assets held by either subsidiary without triggering hedge break costs. Previously only assets held by one subsidiary, whose loan was partly un-hedged, could be sold without incurring swap break costs.
- The commitments have been reduced – one subsidiary now has a term loan of £46.5m and the other has a term loan of £19.8m, both of which are fully drawn.
- The revolving facility previously available to one of the subsidiaries has been cancelled and the undrawn facility commitment of £25.6m cancelled. Whilst the loss of the revolving facility reduces the financial flexibility available to the Group, the corresponding saving in undrawn commitment fees is £154k per annum.
- The financial covenants on both facilities are now tested on a consolidated basis, with total loan to value ratios not to exceed 91.5%, and total projected and current interest cover ratios not to exceed 120%. As at the 31 July 2013 interest payment date the total loan to value ratio was 82.12% and the interest cover was 175.3%.
- The repayment date for both facilities is extended to 30 April 2018. The extension of the loans enhances the Group's ability to execute the sales strategy at best value whilst minimising hedge break costs.
- A fixed margin of 2%. now applies to both facilities. An additional margin will accrue from 1 January 2015 and become payable on repayment of the loans (this accrues at the rate of 1%. per annum from 1 January 2015, 1.5 %. from 1 January 2016 and then 2%. thereafter from 1 January 2017). The margin increases in part reflects the price paid for the loan extension.

- Amortisation instalments are to be paid on each interest payment date, calculated as being 0.45%. of the loan balances on each interest payment date.
- The transfer of properties into the relevant subsidiaries (the aggregate value of which must be a minimum of £5m) from other Group property owning vehicles.

In addition, INTERNOS also entered into duty of care agreements with both lenders pursuant to which the lender is granted certain rights in relation to the termination of the Investment Management Agreement.

All of the loans have actual and forecast interest cover tests which must be complied with under the terms of the facilities. The interest cover is tested at various times throughout the year and, at each testing date each loan was determined to be compliant. The level of the interest cover ratio ("ICR") required by each loan is listed below (each loan reporting period includes an actual and forecast ratio).

| Loan | Actual ICR Covenant | Actual ICR – Qtr ending 30/9/2013 | Forecast ICR Covenant | Forecast ICR – Qtr ending 30/9/2013 |
|---|---|---|---|---|
| Indus (Eclipse 2007-1) plc | 110% | 139.4% | 110% | 145.9% |
| HSBC – Term Loan 1 | 120% | 175.3%* | 120% | 148.8% |
| HSBC – Term Loan 2 | 120% | 175.3%* | 120% | 148.8% |

* Ratio does not reflect the impact of a full quarter of the increased interest margin. We estimated the ratio will reduce to 169.8% after allowing for a full quarter of interest and the increased rent from the additional £5m security.

At the year end the Group held properties with a total value of approximately £7.9m, with no debt drawn against them. This figure will reduce to £6.64m when transfers to provide the additional £5m of security to HSBC are completed. These assets provide the Group with a measure of flexibility and will enable the Group to meet commitments that cannot be funded from cashflow, such as capital expenditure. The Group will also benefit from the reduction in its administrative overhead costs as a result of the changes implemented following the Strategy Review.

## Taxation

The Group continued to operate as a REIT throughout the year. Accordingly, any profits and gains from the property investment business should be exempt from Corporation Tax provided certain conditions continue to be met. The asset management income earned in the year will form part of the "residual" business, profits from which are not exempt from Corporation Tax. The Group continues to have available losses to relieve any such profits arising. Therefore, no provision for Corporation Tax has been made.

## Dividend

As announced during the year, the Board reviewed the Company's dividend distribution policy in the light of the adoption of the new investment policy and decided that it should not recommend the payment of dividends for the time being. Accordingly, no dividend will be paid in respect of the year. In making this decision the Board took into account the cash flow requirements of the business alongside the decision not to extend future borrowings. The Company has received advice that, for the time being, this will not affect the Company's REIT status. The Board will continue to keep the dividend policy under review.

Strategic Report

# Principal Risks

The directors recognise that no commercial reward comes without some element of risk. In determining the principal risks to which the business is exposed, the directors recognise that a number of these, such as the condition of the UK domestic economy, are external and beyond the Company's power to influence. However, such risk areas are monitored and appropriate mitigating action, such as reviewing investment programmes, is taken in response. The Audit Committee considers the risk areas the Company is exposed to in the light of prevailing economic conditions and the risk areas set out in this section are subject to review. The Company's approach to risk management reflects its granular business model and position in the market and involves the expertise of its asset managers and third party advisers. The management team evaluates each investment, disinvestment and asset management decision on its own merits within the Company's overall investment policy. Operational progress and key investment and disposal decisions are considered in regular management team meetings as well as being subject to informal peer review. Higher level risks and financial exposures are subject to constant monitoring. Major investment and disposal decisions are subject to review by non-executive directors in accordance with a protocol set by the Board.

| Potential Risk | Impact | Mitigation |
|---|---|---|
| **Property Portfolio Performance** | | |
| Effect on tenants of downturn in macroeconomic environment | Tenant defaults<br>Reduced rental income<br>Increased void costs<br>Reduction in Net Asset Value and realisation value of assets | Rental arrears continually monitored – early discussions with tenants appearing to be in difficulties<br>Regular review of all properties for lease terminations and tenant risk, with early action to take control of units when appropriate<br>Limited requirement for tenant incentives within sub-sector<br>Close liaison with local agents enables swift decisions on individual properties<br>Tendency of small traders to take early action in response to economic conditions<br>Diverse tenant base<br>Sustainable location and property use |
| Higher than anticipated property maintenance costs | Costs not matched by income streams and/or improvement in property value | All material expenditure authorised by asset manager and director<br>Capital expenditure subject to regular review<br>Focus on sale of assets with high potential capital expenditure |
| Changes to legal environment, planning law or local planning policy | Adverse impact on portfolio<br>Loss of development opportunity<br>Reduction in realisation value of assets | Monitoring of UK property environment and regulatory proposals<br>Close liaison with agents and advisers<br>Membership of and dialogue with relevant industry bodies |

| Potential Risk | Impact | Mitigation |
|---|---|---|
| Failure to comply with regulatory requirements in connection with property portfolio, including health, safety and environmental | • Tenant and third party claims resulting in financial loss<br>• Reputational damage | • Managing agents and professional advisers provide guidance on regulatory requirements<br>• Asset managers and agents monitor individual properties<br>• Managing agents operate formal regulatory certification process for residential accommodation<br>• Ongoing programme of risk assessments for key multi-tenanted sites<br>• Insurance policies cover key risks |
| **Corporate Governance & Management** | | |
| Non-availability of information technology systems or failure of data security | • Loss of applications impacts on operations and reporting ability<br>• Financial claims arising from leak of confidential information | • INTERNOS has effective security regime with off-site data back-up |
| Financial market conditions | • Insufficient finance available at acceptable rates to fulfil business plans<br>• Financial impact of debt interest<br>• Breach of banking covenants | • Debt facilities in place<br>• Appropriate hedging in place for over 90% of borrowings<br>• Impact of interest rates on property yields monitored and investment/disposal policy adjusted accordingly |
| Capital management and liquidity | • Insufficient funds to fulfil operational plans and financial commitments<br>• Breach of banking covenants<br>• Inability to undertake asset management initiatives<br>• Inability to return cash to shareholders | • Board monitors quarterly debt reporting and forecasts against annual plan and banking covenants<br>• Management forecasts prepared and reviewed to identify capital requirements<br>• Uncharged properties and cash available to satisfy working capital requirements<br>• Revised investment policy aimed at reducing indebtedness<br>• Compliance with banking covenants reviewed quarterly with banks and reported to Board<br>• Retention of recurring profits to enhance cash position |

# Corporate Responsibility

During the year we continued to focus on the three principal contributors to the success of our business:

- the talent and commitment of our team;
- our relationships with national and local advisers, partners and clients; and
- the well-being of the businesses that occupy our properties and the communities in which they operate.

Following the Strategy Review and the appointment of INTERNOS as manager of the Company's investment portfolio and operations, the Company's asset management and accounts team transferred to INTERNOS and the Company's other employees left the business. Accordingly, the Company had no employees at the year-end. We were heartened by the manner in which the transferring team approached the necessary changes, their integration into INTERNOS and their continued focus on the Company's activities. We are satisfied that their employment terms and career development opportunities have been enhanced as a result of their transfer to INTERNOS.

## Business Integrity

Our business model is based on the maintenance and utilisation of an extended network of advisors and agents. It follows that our ability to operate successfully is largely dependent on our reputation for integrity and a straightforward and honest approach conducting business. We strive to behave and transact business in accordance with the highest professional standards, and we look to those who act on our behalf do the same. Besides complying with all relevant legislation and professional guidelines, this includes customer care and external complaint procedures. Our arrangements with INTERNOS, which is regulated by the Financial Conduct Authority, include the provision of all applicable compliance procedures. Having given due consideration to relevant human rights issues, we do not believe that the provision of detailed information in this area is relevant to the understanding of the performance and position of the business. However, we are confident that our business model and the transactions in which we engage do not contravene human rights principles or applicable legislation. Our approach to these matters is underpinned by a whistle-blowing procedure, enabling perceived irregularities to be notified to members of the Board, principally the senior independent non-executive director.

## Employees

As a result of the Strategy Review a number of employees left the business with the remainder transferring to INTERNOS. Within the Strategy Review process the non-executive directors gave careful consideration to employee-related issues. Having placed considerable emphasis on the personal development of our staff, we were pleased that a similar attitude prevails within INTERNOS. We also noted that the team members who have transferred to INTERNOS will have available to them an expanded range of personal and career development opportunities.

Prior to the changes resulting from the Strategy Review, the gender make-up of the business was as follows:

| | Male | Female |
|---|---|---|
| Non-executive directors | 3 | – |
| Executive directors | 2 | 1 |
| Staff | 5 | 7 |

Following the Strategy Review we no longer have any employees. The Company has four directors, all of whom are male.

## Health, Safety and Welfare

We have always placed the highest priority on the welfare of our employees, particularly bearing in mind the risks arising from visits to remote sites. We are pleased to note that the directors of INTERNOS place equal emphasis on this consideration.

INTERNOS continues to apply our policy of requiring our property managers and contractors to ensure that maintenance and construction activities conform to relevant regulations and that due consideration is given to the welfare of occupants and neighbours. Our managing agents undertake regular checks of gas and electrical installations within the residential elements of our portfolio in conformance with regulatory requirements, and address reported items for improvement, together with a continuing programme of risk assessments covering relevant multi-occupancy sites.

## Community and Partnerships

Notwithstanding the recent change in the Company's strategy, we continue to take seriously our responsibilities as an owner of property assets within local communities, the well-being of which remains vital to our interests during our stewardship. We anticipate that our new strategy will result in many of our assets reverting to local ownership, whilst continuing to serve their communities, and we will seek to deal constructively with all stakeholders during this process.

We remain proud of the network of national, regional and local agents and advisers that we have built up, whose goodwill and support is our mainstay. However, we wish to pay particular tribute to the members of our core asset management and finance team, many of whom have transferred to INTERNOS, for their contribution and dedication during the recent period of transition.

## Environment

Our business model and investment policy is by its nature supportive of reducing the carbon impact of retail shopping. Typically, our shops are within easy distance of their customers' homes or workplaces. Our development activity focuses on the return to profitable use of space that would otherwise remain vacant, including the conversion of redundant upper parts in shopping locations. Besides rejuvenating existing locations, we believe this is likely to reduce the development pressure on greenfield sites. Such work is carried out in accordance with applicable energy and resource saving standards and noise impact reduction requirements. Wherever possible, we use local agents and contractors. Our contractors are required to dispose of waste in accordance with best practice, and energy reduction and recycling arrangements are in place in our office.

**Grahame Whateley**
Chairman
3 January 2014

# Directors' Report

**The directors of The Local Shopping REIT plc ("the Company") present their report and the audited financial statements of the Company together with its subsidiary and associated undertakings ("the Group") for the year ended 30 September 2013.**

The Directors' Report comprises the information set out on pages 18 to 35.

The Company is a public limited company incorporated in England under registered number 05304743, with its registered office at 65 Grosvenor Street, London, W1K 3JH.

## Statement of Directors' Responsibilities in Respect of the Annual Report and the Financial Statements

The directors are responsible for preparing their annual report and the Group and parent Company financial statements in accordance with applicable law and regulations. Company law requires that the directors prepare Group and parent Company financial statements for each financial year. Under that law they are required to prepare the Group financial statements in accordance with IFRSs as adopted by the European Union and applicable law and have elected to prepare the parent Company financial statements in accordance with UK Accounting Standards (UK Generally Accepted Accounting Practice). 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 the parent Company and of their profit or loss for the relevant period.

In preparing each of the Group and parent Company financial statements, the directors are required to:

- select suitable accounting policies and apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- for the Group financial statements, state whether they have been prepared in accordance with IFRSs as adopted by the EU;
- for the parent Company financial statements, state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the parent Company financial statements; and
- prepare the financial statements on the going concern basis, unless it is inappropriate to presume that the Group and the parent Company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the parent Company's transactions and disclose with reasonable accuracy at any time the financial position of the parent Company and enable them to ensure that its financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the directors are also responsible for preparing a directors' report, a directors' remuneration report and a corporate governance statement, each of which conforms to the relevant law and regulations. The directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website.

Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions. The directors consider that the annual report and accounts, taken as a whole, is fair, balanced and understandable in accordance with the UK Corporate Governance Code 2012, and provides the information necessary for shareholders to assess the Company's performance, business model and strategy.

The Independent Auditor's Report is set out on pages 36 and 37. So far as the directors are aware, there is no information relevant to the Auditors' preparation of their report that has not been disclosed to the Company's Auditors. Each director has taken all steps required of a director to ensure that he is aware of any information relevant to the audit and to establish that all such information has been disclosed to the Auditors. The directors consider that the sections headed Business Review, Finance Review, Governance and the Remuneration Report together fulfil the requirement for an enhanced Business Review under section 417 of the Companies Act 2006.

The Governance section is a statement for the purposes of the Disclosure and Transparency Rule 7.2.1.

# Board of Directors

### Grahame Whateley

Independent Non-Executive Chairman, aged 70

Grahame Whateley has chaired the Board since January 2005, having spent his working life in the property industry, for much of that time as Chairman of the Castlemore Group. He is Chairman of the Cedar Group of companies and is a non-executive director of Arden Partners Plc. He serves on the Remuneration and Nomination Committees.

### Stephen East

Senior Independent Non-Executive Director, aged 55

Stephen East joined the Board in September 2009, having previously served as Finance Director of MEPC plc and as Finance Director of Woolworth Group plc. He holds non-executive directorships of Marwyn Management Partners plc, CQS Diversified Fund Limited and Snoozebox Holdings plc. He also serves on the board of Genesis Housing Association. He previously held non-executive appointments with Regus Group plc and Star Energy Group plc. Stephen is a Chartered Accountant and a Fellow of the Association of Corporate Treasurers. He chairs the Audit Committee and the Nomination Committee and also serves on the Remuneration Committee.

### Steve Faber

Executive Director, aged 39

As Head of UK Investment Management at INTERNOS, Steve holds primary responsibility for executing the agreement between the Company and INTERNOS for the management of LSR's investment property portfolio in accordance with the Company's investment strategy. Steve is a Chartered Surveyor with 17 years' experience gained across all UK Market sectors. Having started his career with Tesco Stores PLC where he had a UK-wide remit dealing with operational and investment properties, he later joined Land Securities Trillium where he advised the Government and the BBC on occupation strategies. Steve then became Director and Head of UK Asset Management at Deutsche Bank's alternative investment manager RREEF, responsible for real estate in excess of £2bn in a role encompassing full life cycle ownership of assets. Steve holds FCA authorisation as an Investment Manager.

### Nicholas Vetch

Independent Non-Executive Director, aged 51

Having trained as a Chartered Surveyor, Nick Vetch became Chief Executive of Edge Properties which he founded in 1989. In 1998 he founded Big Yellow Group PLC, of which he is Executive Chairman. He is also a non-executive director of Blue Self Storage SL, which operates in Spain. Nick Vetch serves on the Audit Committee and chairs the Remuneration Committee.

# Governance

The Company is subject to, and complies with, the Listing Rules and the Disclosure & Transparency Rules of the Financial Services Authority. The Company is also subject to the UK Corporate Governance Code ("the Code") promulgated by the Financial Reporting Council, the 2012 edition of which applied to the Company during the year. Subject to matters set out below, the directors consider that the Company complies with all provisions of the Code to the extent to which they apply to companies outside the FTSE 350.

## Board Responsibilities and Operation

The Company is led by the Board, which is responsible for determining the strategy of the business and its effective stewardship. All major investment decisions are taken by the Board as a whole and there is a formal schedule of items reserved for consideration by the Board. The Board meets regularly to review the Company's operations and progress with its strategy. Twelve meetings were held during the year. Each Board meeting has a formal agenda. All material aspects of the business are reviewed on a regular basis, with key items highlighted, to enable the Board to monitor well-being and progress. These include portfolio performance, acquisitions and sales, asset management, investment in joint ventures as well as finance, business development and welfare and environmental matters. Risk management and controls are reviewed in the light of advice from the Audit Committee and the external auditors. In consultation with the Board and committee Chairmen, the Company Secretary ensures that all directors receive relevant reports and papers prior to each meeting.

Additional meetings and discussions are arranged outside the Board's regular schedule as necessary. The non-executive directors took the lead in steering the Strategy Review and making recommendations to shareholders as to the Company's future direction and investment policy.

During the year the executive directors, to whom day-to-day operational management was delegated, consulted the non-executive directors on a regular basis outside normal Board meetings. Since the change in investment policy, this process now applies to executives of INTERNOS. The non-executive directors also make themselves available to provide advice to the management team. The non-executive directors hold meetings and discussions in the absence of the executive directors.

During the year the division of responsibilities between executive and the non-executive directors continued to be well-defined and recorded. During the tenure of the former Joint Chief Executives, their remit was clearly separate from that of the Chairman, with the Chairman taking responsibility for corporate governance and effective leadership of the Board, and the Joint Chief Executives being responsible to the Board for the executive management of the business. Following the appointment of INTERNOS, the remit for the executive management of the business is clearly defined by the agreement between the Company and INTERNOS, and Steve Faber, as executive director, is responsible to the Board for its implementation.

The Chairman ensures that due consideration is given to key items of business, including ensuring sufficient opportunity for preparatory work prior to formal meetings. The senior independent director provides a separate communication channel for shareholders and other interested parties, and also has a remit under the Company's "whistle-blowing" arrangements.

The responsibilities of each non-executive director are set out clearly in his letter of appointment, which is available for inspection by members at the Company's registered office during normal office hours. All directors ensure that they provide sufficient time to fulfil their duties. All directors have access to the advice and services of the Company Secretary, and there is an agreed procedure whereby directors can take independent professional advice at the Company's expense.

## Board Composition

Biographical details for each of the directors, including their membership of the Board's committees, are set out on page 19. All the directors listed, other than Steve Faber, held office throughout the year to 30 September 2013. Steve Faber was appointed as an executive director on 5 July 2013. The Company's former executive directors, Mike Riley, Nick Gregory and Victoria Whitehouse, resigned on 5 July 2013.

Prior to these changes the Board comprised an independent Chairman, two further independent non-executive directors (including the senior independent non-executive director) and three executive directors. Board membership was therefore divided equally between executive and non-executive directors. Following the changes mentioned above, the Board has three non-executive directors and one executive director.

Having considered the criteria set out in the Code and the character and attributes of each individual, the Board considers each of the non-executive directors to be independent within the spirit of the Code and that no individual or group can dominate decision-making.

The Board has noted that Grahame Whateley will enter his tenth year as Chairman of the Company during 2014. Having given this matter careful consideration the directors other than Mr Whateley concluded that Mr Whateley's length of service has no bearing on his independence.

The Company's Articles of Association require any director appointed to the Board during the year to be reappointed at the next Annual General Meeting. All directors are, as a minimum, subject to retirement and re-election at every third Annual General Meeting following their initial election. As announced in the 2012 Annual Report, the directors adopted the best-practice policy of each director resigning and offering themselves for re-election at each Annual General Meeting, even though this is not a strict requirement for companies outside the FTSE 350. This policy was applied at the 2013 Annual General Meeting, when all directors then holding office were reappointed.

## Board Committees

The Board has established Audit, Remuneration and Nomination Committees. The minutes of each committee meeting are circulated to the Board as a whole. Each committee operates within terms of reference determined by the Board having regard to independent external guidance. Terms of reference for each committee are available on the Company's website www.localshoppingreit.co.uk. The work of the committees is described below.

## Nomination Committee

The Nomination Committee comprises at least three directors, the majority of whom are independent non-executive directors. The Committee is responsible for approving all director appointments and is responsible for ensuring that the required standards of skills, experience and stewardship ability are met. In appointing new directors, the Committee and the Board consider advice from external professional consultants. It has been the Board's practice for candidates to be interviewed separately by executive and non-executive directors. The Committee has formal terms of reference approved by the Board and is chaired by the Company's senior independent non-executive director, Stephen East. The Committee met once during the year.

## Audit Committee

The Audit Committee's Chairman is Stephen East and its other member is Nick Vetch, both of whom are independent non-executive directors. The Board considers Mr East to have the requisite skills and experience to chair the Committee. The Company Secretary acts as secretary to the Committee. The report of the Audit Committee can be found on page 29.

The Committee's terms of reference were updated during the year to reflect the terms of the Code. The Committee's responsibilities include:

- monitoring the integrity of the Company's financial statements and formal announcements relating to its financial performance and reviewing significant financial reporting judgements contained in them (subject to the Board's overall responsibility for reviewing and approving the annual directors' report and financial statements);
- reviewing the adequacy and effectiveness of the Company's internal financial controls, internal control and risk management systems, fraud detection, regulatory compliance and whistle-blowing arrangements;
- making recommendations to the Board for the approval of shareholders on the appointment, re-engagement or removal of the external Auditors and approving the Auditors' terms of engagement and remuneration;
- overseeing the Company's relationship with the external Auditors, reviewing and monitoring the Auditors' independence and objectivity and the effectiveness of the audit process, taking into consideration UK professional and regulatory requirements;
- approving the annual audit plan and reviewing the Auditors' findings and the effectiveness of the audit programme;
- developing and implementing policy on the engagement of the external Auditors to supply non-audit services, taking account of relevant ethical guidance, and making recommendations to the Board in respect of any action or improvement that may be needed;
- reporting to the Board on how the Committee has discharged its activities.

# Governance continued

The Committee continues to consider that the Company's size and activities do not warrant the establishment of an internal audit function.

Other members of the Board may attend the Committee's meetings by invitation. Representatives of the Company's Auditors, KPMG Audit Plc ("KPMG"), also attend the Committee's meetings and the Committee's Chairman also holds discussions with the Auditors in the absence of executive directors and members of the management team. KPMG Audit Plc have provided the directors with written confirmation of their independence.

## Remuneration Committee

Full details of the membership of the Remuneration Committee and the Company's remuneration policy are set out in the Remuneration Report at page 30. In view of the then ongoing Strategy Review, the Committee did not meet during the year.

Each member's attendance record at Board and Committee meetings is set out in the table below:

| Director | Board | Audit | Remuneration | Nomination |
|---|---|---|---|---|
| Stephen East | 12 | 4 | – | 1 |
| Steve Faber* | 3 | – | – | – |
| Nick Gregory† | 5 | – | – | – |
| Mike Riley† | 6 | – | – | – |
| Nick Vetch | 9 | 4 | – | 1 |
| Grahame Whateley | 8 | – | – | – |
| Victoria Whitehouse† | 6 | – | – | – |

* Appointed 5 July 2013
† Resigned 5 July 2013

## Performance Evaluation of the Board and its Committees

The membership, remits and operations of the Board and its Committees are subject to annual evaluation. This process is led by the senior independent director supported by the Company Secretary.

## Directors' interests in contracts

The directors took note of potential conflicts of interest in relation to the transfer of the Group's interest in Local Parade Investments LLP, the joint venture with Pramerica, to new shareholders including the Group's former Joint Chief Executives. Similarly considerations applied to arrangements by which the Group ceased its asset management activities for joint ventures and third parties, which activities were taken over by a company in which the former Joint Chief Executives are interested. Having received advice on these matters, the directors concluded that it was in the Group's interest to authorise the potential conflict.

Subject to the foregoing, during the year:

1. No director had any material interest in any contract or arrangement with any company within the Group; and
2. Save for the contingent interests of participants in the Company's Long Term Incentive Plan in shares in the Company held by LSR Trustee Limited, no director had any beneficial interest in any subsidiaries of the Company.

The interests of the directors who held office during the year in the issued share capital of the Company as at the date of this report, all of which were beneficial, are set out below:

| Director | Ordinary 20p Shares 2013 | 2012 |
|---|---|---|
| Stephen East | **75,000** | 75,000 |
| Steve Faber* | **–** | – |
| Nicholas Gregory† | **600,000** | 600,000 |
| Mike Riley† | **500,000** | 600,000 |
| Nicholas Vetch | **2,873,563** | 2,873,563 |
| Grahame Whateley | **5,255,171** | 7,655,171 |
| Victoria Whitehouse† | **1,149** | 1,149 |

* Appointed 5 July 2013
† Resigned 5 July 2013

Directors' interests in employee share schemes are set out in the Remuneration Report on page 35.

The Company's Articles of Association provide a framework for directors to report actual or potential situational conflicts, enabling the Board to give such situational conflicts appropriate and early consideration. All directors are aware of the importance of consulting the Company Secretary regarding possible situational conflicts.

## Directors' Indemnities and Insurance Cover

To the extent permitted by law, the Company indemnifies its directors and officers against claims arising from their acts and omissions related to their office. In accordance with the Code, the Company also maintains an insurance policy in respect of claims against directors. The Company has also arranged professional indemnity insurance cover in relation to its asset management and advisory activities for joint ventures and third parties.

## Directors' Performance Appraisal

Prior to the completion of the Strategy Review and the appointment of INTERNOS the Company had a performance review process in place whereby the non-executive directors, through the Chairman, provided feedback to the executive directors on their individual performance and the executive directors were involved in the non-executive directors' appraisal of the performance of the Chairman. Following the recent changes this process is under review and performance appraisal arrangements appropriate to the changed circumstances will be put in place during 2014.

## Director Induction

Arrangements are made to provide new directors with an induction programme into the Company's activities. Non-executive directors visit the Company's offices between formal meetings and discuss the Company's activities with members of the management team on an informal basis. Asset managers are pleased to make arrangements for directors to inspect investment properties.

## Internal Governance Policies

The directors recognise that the Company's ability to operate successfully is largely dependent on the maintenance of its straightforward approach to doing business and its reputation for integrity. All those who act on the Company's behalf are therefore required to behave and transact business in accordance with the highest professional standards. This includes complying with the requirements of the Model Code, Anti-money Laundering regulations, the Data Protection Act and the Bribery Act, as well as customer care and external complaint guidelines. The Company's arrangements with INTERNOS, which is regulated by the Financial Conduct Authority, include the provision of all applicable compliance procedures. This regime is underpinned by a whistle-blowing procedure, enabling perceived irregularities to be notified to members of the Board, principally the senior independent non-executive director.

# Governance continued

## Internal Controls

The Board has overall responsibility for the Company's internal control systems and for monitoring its effectiveness. The Board's approach is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable assurance against material misstatements or loss. Having regard to the Company's size, the establishment of a separate internal audit function has not been considered appropriate. The Board's approach to internal controls covers all companies within the Group and there are no associate or joint venture entities which it does not cover. A summary of the principal risks to which the business is exposed may be found on pages 14 and 15.

The principal foundations of the Company's internal control framework are:

- statements of areas of responsibility reserved to the Board and its committees, with prescribed limits to executive directors' authority to commit to expenditure and borrowing;
- effective committee structure with terms of reference and reporting arrangements to the Board;
- clear remits for the delegation of executive direction and internal operational management functions;
- framework for independent directors to provide advice and support to executive directors on an individual basis;
- top-level risk identification, evaluation and management framework monitored by the Audit Committee;
- internal procedures covering all operational activity, limits of authority and authorisation procedures;
- effective systems for authorising capital expenditure and significant revenue items and monitoring actual cost incurred;
- regular review meetings with managing agents and other advisers, including review of agents' management and reporting systems;
- structured induction process for all joiners and ongoing staff development;
- regularly updated internal staff handbook explaining the Company's policies and procedures, including health and safety, corporate governance and professional conduct;
- regular team meetings to review operational progress and discuss future developments;
- established procedures for electronic information control and security;
- regular operational and individual performance reviews by executive management;
- regular reporting to the Board of operational results against expectations with commentary on variances;
- regular review of operational forecasts and consideration by the Board on a quarterly basis;
- regular review of the Company's funding requirements against the status of the financial markets and the continuing effectiveness of the Company's hedging arrangements; and
- quarterly reporting to the Board of health, safety and environmental matters.

The arrangements described above were amended following the Strategy Review, since which a clear definition of executive remits and authority levels has been set out in the Investment Advisory Agreement between the Company and INTERNOS. These now supersede the arrangements relating to employees and internal procedures. The Board is satisfied that the internal control arrangements established by INTERNOS (which is regulated by the Financial Conduct Authority) in respect of the Company's business are appropriate.

As part of its half-year and year-end activities, the Board reviews the effectiveness of the Company's risk management systems against the principal risks facing the business and their associated mitigating factors, taking into account the findings and recommendations of the Auditors. Following its review of the Auditors' findings during 2013 and its examination of the control framework established by INTERNOS the Board considers that the Company's approach is acceptable.

## Investor Relations

The directors place considerable emphasis on effective communications with the Company's investors. In addition to the regular dialogue regarding the Company's operation progress, the non-executive directors consulted shareholders during the Strategy Review process. Directors are happy to comply with shareholder requests for meetings as soon as practicable, subject to regulatory constraints.

The Board is provided with feedback on these meetings, as well as regular commentary from investors and the Company's bankers and advisers. The Board provides interim management reports and other announcements in accordance with regulatory requirements. Regulatory announcements and key publications can also be accessed via the Company's website.

The Company's Annual General Meeting provides a further forum for investors to discuss the Company's progress and the Board encourages shareholders to attend. The Company complies with relevant regulatory requirements and also the UK Corporate Governance Code in relation to convening the meeting, its conduct and the announcement of voting on resolutions. The Annual Report and Notice of the Annual General Meeting are sent to shareholders at least 20 working days prior to the meeting and are available on the Company's website. The results of resolutions considered at the Annual General Meeting are announced to the Stock Exchange and are also published on the website and lodged with the National Storage Mechanism. Investors may elect to receive communications from the Company in electronic form and be advised by email that communications may be accessed via the Company's website.

## Acquisitions and Disposals

During the year the Group disposed of its interest in Local Parade Investments LLP (a joint venture with Pramerica Real Estate Investors) and its co-investment with Schroders in Local Retail Fund Limited Partnership.

The Group made no material acquisitions during the year.

## Group Companies

The subsidiary undertakings of the Company are set out in note 24 to the financial statements.

## Group Result and Dividend

The loss for the Group attributable to shareholders for the year was £6.1m (2012: loss of £9.2m). The recurring profit for the year was 2.5p per share (2012 restated: 3.8p). The definition of recurring profit is set out in the glossary of terms at the end of the Report.

In view of the Strategy Review and the resultant change in the Company's investment policy, no interim dividend has been or will be distributed in respect of the financial year. The directors will keep the dividend distribution policy under review.

## Use of financial instruments

The Company's use of financial instruments to reduce its exposure to risks arising from interest rate fluctuations is described in note 20 to the financial statements.

## Share Capital

Details of the Company's issued share capital are set out in note 16 to the financial statements. All of the Company's issued shares are listed on the London Stock Exchange. The Company's share capital comprises one class of Ordinary Shares of 20p each. All issued shares are fully paid up and rank equally. Shares acquired through the Company's employee share schemes rank *pari passu* with shares in issue and no shares carry special rights regarding control of the Company. The Company's Articles impose requirements on shareholders in relation to distributions and the size of individual holdings, in order to ensure that the Company continues to conform to the UK REIT regime. Subject to this, there are no restrictions on the transfer of shares or the size of holdings. The directors are not aware of any agreements between shareholders in relation to the Company's shares. The Company's issued share capital did not alter during the year.

# Governance continued

## Transactions in the Company's shares

The Company's previous authority to purchase its own shares was extended at the Annual General Meeting in March 2013, which authorised purchases of up to 14.99% of the Company's issued Ordinary Share capital (excluding shares held in treasury). This authority expires at the 2014 Annual General Meeting, at which a resolution will be proposed for its renewal. The directors exercise their authority to purchase the Company's shares only when they consider it in the Company's best interests to do so. No share purchases were made during the year.

The directors are also authorised to offer shareholders the alternative of receiving fully paid Ordinary Shares in lieu of dividends. This authority was not used during the year.

## Substantial Interests

As at 23 January 2013, the last practicable reporting date before printing this document, the Company had been notified of the following major interests (of 3% or more) in its issued
share capital:

| Name | Ordinary Shares | % |
|---|---|---|
| New Solera Holdings | 19,855,199 | 24.07 |
| Thames River Capital | 8,840,324 | 10.71 |
| AXA Framlington | 7,650,000 | 9.27 |
| Schroders | 7,601,611 | 9.21 |
| J G Whateley | 5,255,171 | 6.37 |
| EII Capital Management | 4,335,366 | 5.25 |
| N J Vetch | 2,873,563 | 3.48 |
| Alliance Trust Savings | 2,570,891 | 3.12 |
| Mark Begg Asset Management | 2,493,113 | 3.02 |

## Effect of change of control on significant contracts

Funding agreements entered into by certain Group companies require the written approval of the relevant bank before any change can be made to the nature, constitution, management or ownership of the business. The employment contracts of directors do not contain any provisions specifically relating to a change of control. The Company's employee share schemes contain change of control provisions which are considered to be standard for such schemes. (At the year end the Company had no remaining employees and the application of the employee share schemes is expected to expire during the 2013-14 financial year in accordance with the terms of each scheme.)

## Key Contracts

During the year certain Group companies participated in joint venture and co-investment arrangements and asset management contracts with external parties. In July 2013 the Group disposed of its interest in the joint venture with Pramerica Real Estate Investors and its co-investment with Schroders. At the same time the Group ceased its external asset management activities. The Group continues to participate in the small joint venture with a UK bank.

With effect from 22 July 2013 the Group appointed INTERNOS Global Investors Limited ("INTERNOS") to execute the Group's new investment policy and to take responsibility for the management and performance of the Company's investment property portfolio. Details of the Group's Investment Advisory Agreement with INTERNOS, including remuneration arrangements, are contained in note 26 to the financial statements.

During the year the Group entered into new agreements with HSBC Bank plc and Indus (Eclipse 2007-1) plc (an affiliate of Barclays Bank plc) respecting the Group's loan and banking facilities, details of which are set out in the Banking Facilities section of the Finance Review.

## Carbon Reporting

### Scope

Bearing in mind that the Company disposed of the majority of its interests in joint ventures during the year, as well as its asset management activities for joint ventures and third parties, we will report only on data related to its activities of investing in and managing our core property portfolio.

We believe that our outsourced business model, employing some 50 firms of local agents and advisers and preferring small local contractors to national organisations, is inherently environmentally friendly. However, it is impracticable to collect energy consumption data from such businesses in relation to the Company's activities. It is also not possible to measure the energy consumed by the Company's tenants nor is this consumption within the Company's control. Accordingly, the scope of the Company's environmental reporting focuses on energy consumed by the Company and its wholly-owned subsidiaries through:

- the use of its offices;
- the activities of its staff and its recently appointed asset manager, INTERNOS, in relation to the Company's business;
- shared facilities provided by the Company within its property portfolio;
- activities within vacant properties.

### Carbon Emissions Data

In relation to Scope 1 (gas and fuel) our consumption of gas is minimal, being our share of the gas consumed in heating in the Company's former office, a multi-tenanted office block, our occupancy of which will terminate during the current year. The data supplied therefore relates almost entirely to fuel consumed on journeys between property sites. As we do not have a company car fleet, all such journeys are made in employees' private vehicles. We have assessed vehicles used against the categories given on the DEFRA website. The use of hire cars and air flights has been minimal.

Besides the energy consumed within our offices, the Scope 2 figures include consumption in our vacant properties for which we are responsible. This includes any electricity used in relation to development work in the conversion or remodelling of premises. The figures do, however, include standing charges for which the Company takes responsibility. Given the granularity of the Company's property portfolio it has not been practicable to separately identify this element.

Our direct usage and emissions of water is minimal, being largely confined to hygiene and refreshment purposes within our offices. A small element of utility supply within vacant premises will relate to water. However, this largely relates to standing charges and consumption is negligible.

The data has been compiled using the software tools available on the DEFRA website.

| | **2013 kg $CO_2$e** | **kg $CO_2$e per £1m t/o** | 2012 kg $CO_2$e | kg $CO_2$e per £1m t/o |
|---|---|---|---|---|
| Scope 1 (gas and fuel) | **8,292** | **566.05** | 8,034 | 508.19 |
| Scope 2 (electricity) | **206,734** | **14,112.50** | 273,473 | 17,298.56 |
| **Total gross emissions** | **215,026** | **14,678.55** | 281,507 | 17,806.75 |

# Governance continued

## Employee Share Schemes

The Company operates the following employee share schemes:

- The Local Shopping REIT plc Company Share Option Plan ("CSOP"); and
- The Local Shopping REIT plc Long Term Incentive Plan ("LTIP").

Details of these schemes are set out in the Remuneration Report on page 33. As the Company no longer has any employees, it is expected that each of the schemes will wind-down in accordance with their rules. The Company's Employee Benefit Trust operates to supply shares as appropriate to meet obligations arising from employee share schemes. The voting rights of shares held by the Employee Benefit Trust are identical to the remainder of the Company's issued share capital. The Employee Benefit Trust has waived its entitlement to dividends for the period.

## REIT Regime

The Company is subject to the regulatory regime for UK Real Estate Investment Trusts.

## Political Donations

During the year the Company made no donations for political purposes (2012: nil).

## Amendment of Articles

The Company has no rules in place in relation to the amendment of its Articles in addition to statutory provisions.

## Auditors

The Company's Auditors, KPMG Audit Plc, has instigated an orderly wind-down of business. The Board has decided to put KPMG LLP forward to be appointed as Auditors and a resolution concerning their appointment will be put to the forthcoming Annual General Meeting.

## Going Concern

The directors have considered whether it is appropriate to prepare the financial statements on a going concern basis. The diversity of the tenant base across retail sectors and its geographical spread around the country demonstrates no reliance on one significant tenant. The loan facilities, together with the attached covenants, are detailed in this document. All covenants have been met throughout the year. The directors have prepared profit and cashflow forecasts for the period to 30 September 2018 which include assumptions relating to the orderly sale of properties under the current investment strategy which the directors consider to be reasonable. These forecasts project the Company's funding needs will be comfortably met by its existing banking facility agreements without any breach of related covenants over the remaining life of the facilities which expire in 2017 and 2018.

On the basis of these projections the directors consider that the Group will continue to be compliant with its banking covenants and sufficient resources will be available to enable it to continue as a going concern for at least the next 12 months. The directors note that a number of other viable alternative strategies remain available to the Company and they will continue to evaluate whether to continue with its current investment policy or to change to one of these viable alternative strategies. Accordingly, the financial statements have been prepared on the going concern basis.

## Responsibilities Statement

The directors confirm that to the best of their knowledge:

- the report of the directors includes a fair review of the development and performance of the business and the position of the issuer and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face; and
- 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 undertakings included in the consolidation taken as a whole.

# Audit Committee Report

The Committee met four times during the year and each member's attendance record is set out in the table on page 22.

During the year the Committee paid particular attention to the significant areas set out below, which were discussed in detail with the Auditors.

## Valuation of Investment Properties

The Committee considered the valuation provided by Allsop LLP ("Allsop") together with the internal directors' valuation and the methodology adopted in both cases. As in previous years Allsop carried out an independent "red book" valuation on 25% of the investment property portfolio in March and a further 25% in September, and we noted that this pattern had resulted in all properties in the portfolio having been subject to a formal external valuation during the preceding 24 months. We took comfort from the consistency of approach between the Allsop valuation and the directors', noting also that Allsop had carried out an independent desktop valuation to inform and support the directors' valuation in September. In concluding that we were content with the valuation assumptions and judgements, the Committee noted the work performed by the Auditors, in particular around the review of market trends and voids, the consideration of yields and absolute value outliers and the verification of input data. This provided us with further comfort that the valuation and the key assumptions underlying it were appropriate.

## Going Concern Assumption

Consideration was given to technical implications for the Going Concern assumption arising from the Company's adoption of the new investment policy, which includes prioritising the liquidation of property assets, the repayment of debt and the return of capital to shareholders. In concluding that it was appropriate for the Going Concern assumption to apply to the Company's new investment strategy, the Committee noted the alternative strategic options available to the Company, together with management forecasts that the Company should continue to operate comfortably within its banking facilities during the lifetime of the facilities.

## Revenue Recognition and Value of Trade Receivables

The Committee discussed with the Auditors the appropriate approach to revenue recognition and the level of risk in relation to the recoverability of tenant arrears. It was noted that the Auditors had carried out a detailed assessment in this area and that management had also carried out a full review of sales ledgers, ensuring that relevant items were provided for in full.

## Fraud Risk and Management Override

The Committee reviewed the substantive work carried out by the Auditors in relation to the risk of fraud and the potential for management to override controls, noting that this had produced no indication of management override that could lead to a material misstatement.

The Committee also covered the following items:

- ensuring that the format of the financial statements and the information supplied meets the standards set by the International Accounting Standards Board;
- reviewing the accounting treatment of receivables and ensuring effective co-ordination between the Company's records and those of its managing agents;
- ensuring that the audit programme properly reflected the risk profile of the business;
- reviewing the integrity of the Company's control environment in the context of the appointment of INTERNOS and the transfer to INTERNOS of staff and systems;
- ensuring that the Committee's terms of reference continued to accord with the Code.

In accordance with the Code, as part of the Company's year-end process the Committee also assessed the effectiveness of the external audit process during the year (including the full-year audit and the Auditors' half-year review). Having reviewed a number of alternative approaches the Committee adopted an assessment framework covering ten key aspects of the audit process. The Committee had regard to the fact that KPMG have been the Company's Auditors since its stock market listing in 2007. Having carefully considered the outcome of this exercise, the Committee decided that it was appropriate to recommend that KPMG be reappointed as Auditors to the Company for a further year.

Entities related to KPMG Audit Plc provide non-audit services to the Company, in particular tax advice in connection with the Company's REIT status. In order to safeguard the objectivity of the Auditors, strict procedures are in place for the engagement of KPMG entities in non-audit work. All work undertaken by KPMG is notified to the Chairman of the Audit Committee and careful consideration is given to whether such work might give rise to a conflict of interest. The Chairman of the Audit Committee must separately authorise any item of work that could result in fees being paid in excess of 50% of the audit fee in any year.

**Stephen East**
Audit Committee Chairman

# Remuneration Report

## Committee Chairman's Statement

This is the first Remuneration Report to be issued to shareholders under the new regulations that came into effect on 1 October 2013 (and our 30 September year-end date means that we are amongst the first companies required to adopt the new framework). The fact that this change relates to a period during which all of the Company's staff members left our employment has added to the challenge of fulfilling the new reporting requirements.

As referred to above, this report should be considered in the context of the changes brought about by the Strategy Review and the Company's subsequent adoption of a new investment policy during the year. These were attended by the departure of the previous team of executive directors and other staff and the transfer of the Company's remaining employees to INTERNOS. In consequence the Company had no employees at the year-end and it is unlikely that the Company will directly recruit any employees in the foreseeable future.

The Remuneration Committee ("the Committee") continued to oversee the operation of the Company's share-related performance plans during the year. Under the terms of each plan, awards made to former employees have either lapsed at the end of 2012-13 (in the case of the Long Term Incentive Plan) or will be exercised or lapse during 2013-14 (in the case of the Company Share Option Plan).

During the year the Committee operated in accordance with formal terms of reference set by the Board, within which it has been responsible for:

- determining the broad policy for the remuneration and benefits of the Company's executive directors and senior managers;
- approving the design and performance targets for share-related performance plans for the Company; and
- determining the individual remuneration packages of each director, giving due regard to the provisions and recommendations of the Code and the Listing Rules.

The Committee comprises independent non-executive directors. The following directors served on the Committee during the year:

Nick Vetch (Committee Chairman);
Stephen East; and
Grahame Whateley.

Biographical details of the members of the Committee are set out on page 19. The Committee did not consider it appropriate to meet during the year, whilst the Strategy Review was underway.

Other than the Company Secretary, who serves as secretary to the Committee, other directors or executives attend meetings of the Committee only by invitation. The Committee has access to independent advice from New Bridge Street, remuneration consultants. New Bridge Street is part of Aon Hewitt Limited, which does not provide any other services to the Group.

## Remuneration Policy

The Company's remuneration policy has been based on the principles set out below:

- within a competitive market, enabling the recruitment and retention of individuals whose talent matches the entrepreneurial and leadership needs of the business, enabling the Company to fulfil its investment objectives for its shareholders; and
- placing emphasis on performance-related rewards and focusing on incentive targets that are closely aligned with the interests of shareholders.

### *Salary and Benefit Mix*

The Committee has aimed to reflect these principles in the mix of basic pay, benefits, annual bonus and long-term awards contained in the remuneration packages adopted for the executive directors and senior managers. The approach adopted by the Committee has been to set base pay and other fixed remuneration for executive directors at less than the median for companies in the FTSE real estate sector, with total remuneration including performance-based awards being aimed at between the median and upper quartile relative to the sector. The Company has also provided pension, healthcare and insurance benefits where appropriate in relation to market norms.

It has been the Company's policy to use share-based incentive schemes to incentivise all permanent employees to contribute to the success of the business. The Company has established two schemes, the Long Term Incentive Plan ("LTIP") and the Employee Share Option Plan ("CSOP"), described below, for this purpose. The LTIP has been used primarily to incentivise executive directors and senior staff.

As the Company no longer has any directly-engaged employees, its previous employee remuneration arrangements no longer apply. However, the directors will engage with INTERNOS with the aim of ensuring that those working on the Company's portfolio, including the Company's former employees, are appropriately incentivised.

In the event that the directors consider it to be in shareholders' interests for the Company to directly engage members of staff, including executive directors, the remuneration policy set out in this report will be applied. In applying the remuneration policy, the Committee will use its discretion, within the terms of schemes previously adopted by the Company, to provide a tailored mix of benefits that encourages individuals to maximise their efforts in the best interests of shareholders.

## *Director Appointments*

Under the Company's Articles one-third of the directors are subject to retirement at each Annual General Meeting. However, in recognition of the best practice provisions of the UK Corporate Governance Code, the Board has implemented a policy for directors to be subject to re-election at each Annual General Meeting. This policy was put into effect at the Annual General Meeting in March 2013. The Articles require that director appointments made by the Board directors are ratified at the subsequent General Meeting of the Company.

For non-executive directors, the Company's policy is for initial appointments to be for a term of 12 months, subject to extension by periods of 12 months thereafter and also subject at any time to termination on notice by the Company or the director. This policy is reflected in the terms of the formal appointment document which is in place for each non-executive director, which also sets out the expected time commitment of the non-executive directors to the Company's affairs.

For executive directors, the Company's policy is for service contracts not to be capable of termination by the Company at not more than one year's notice.

See Table 2 below.

## *Non-Executive Pay*

The Company's policy is for the level of non-executive pay to be reviewed at least every three years by the Chairman and the executive directors. In view of the changed circumstances, future reviews of non-executive remuneration will be conducted by independent consultants commissioned by the Company Secretary. The level of non-executive pay has not changed since the Company's flotation in May 2007. Consideration will be given to conducting such a review following the AGM in March 2014.

## *Payments on Loss of Office*

The Company's policy on payments to directors on loss of office, in the absence of a breach of contract or other misconduct by the director, is to seek agreement to a termination settlement based on the value of base salary and contractual entitlements that would have applied to the director during his or her contractual notice period. The Remuneration Committee will determine the extent to which it is in the Company's best interests for the director work during his or her notice period, or (to the extent permissible under his or her contract) to be required not to undertake duties or attend at the Company's premises or receive a payment in lieu of notice. The Committee may seek to require mitigation where it appears to it that it is reasonable in all the circumstances to do so. Should it appear to the Company that the director may pursue a claim against the Company in respect of a breach of employment rights in addition to his or her contractual entitlement, the Committee may authorise settlement terms with the director that it considers to be reasonable in all the circumstances and in the best interests of the Company.

# Remuneration Report continued

## *Shareholder Approval*

A resolution concerning shareholder approval of the Company's remuneration policy, as described in this report, will be put to the Company's Annual General Meeting in March 2014.

Table 1: Directors' Total Remuneration 2013-14

| Director | Salary | Short term incentives | Long term incentives | Pension contributions | Benefits in kind | Total |
|---|---|---|---|---|---|---|
| **Non-executive directors** | | | | | | |
| Stephen East | 30,000 | – | – | – | – | 30,000 |
| Nick Vetch | 30,000 | – | – | – | – | 30,000 |
| Grahame Whateley | 50,000 | – | – | – | – | 50,000 |
| **Executive directors** | | | | | | |
| Steve Faber* | – | – | – | – | – | – |
| **Total** | **110,000** | **–** | **–** | **–** | **–** | **110,000** |

Table 2: Directors' Service Contracts

| | Date of appointment as director | Date of current appointment letter | Expiry of term |
|---|---|---|---|
| **Non-executive directors** | | | |
| **Director** | | | |
| Stephen East | 10 September 2009 | 9 September 2013 | 9 September 2014 |
| Nick Vetch | 30 March 2007 | 30 March 2013 | 29 March 2014 |
| Grahame Whateley | 20 September 2004 | 30 March 2013 | 29 March 2014 |
| **Executive directors** | | | |
| **Director** | **Date of contract** | | **Notice period** |
| Steve Faber* | Not applicable | | Not applicable |
| Nick Gregory† | 30 March 2007 | | 12 months from either party |
| Mike Riley† | 30 March 2007 | | 12 months from either party |
| Victoria Whitehouse† | 30 March 2007 | | 12 months from either party |

* Appointed 5 July 2013
† Resigned 5 July 2013

## Remuneration Implementation Report

This section sets out the ways in which the Company applied its remuneration policy during 2012-13.

## *Base Pay and Benefits*

In addition to their base salary, executive directors were provided with private health insurance, death in service and disability insurance and critical illness cover. The Committee's previous policy was to review executives' base pay and benefits against comparable market groups. However, it was considered that it would not be appropriate to conduct this exercise whilst the Strategy Review was ongoing. Accordingly, the level of base pay and the mix of benefits of the former executive directors did not change during the year.

## *Directors' Pensions*

The Company maintained its Stakeholder Pension Plan and Group Personal Pension plan, which were open to all employees, including executive directors. No director was a member of the Stakeholder Pension Plan. Victoria Whitehouse was a member of the Group Personal Pension Plan and contribution details in respect of her membership during the year are set out in Table 3 below. During the year the Company made contributions to the personal pension plans of executive directors, as a percentage of base salary, as follows:

Nick Gregory: 10% per annum
Mike Riley: 10% per annum

## *Annual Executive Bonus Plan ("the Bonus Plan")*

Against the backdrop of the Strategy Review during the year the Committee did not consider it appropriate to implement the Bonus Plan operated by the Company in previous years. No payments were made during the year in respect of the operation of the Bonus Plan in previous years.

## *Long Term Incentive Plan ("the LTIP")*

The LTIP was established to enable employees, including executive directors, to be granted awards of the Company's shares in the form of a nil cost option. The LTIP has been operated by the Committee in conjunction with the Company's Employee Benefit Trust ("EBT"), which may grant awards on the Committee's recommendation. The exercise of all awards granted under the LTIP has been conditional on the achievement of objective performance targets set by the Committee at the time of grant. Performance has been measured over a minimum period of three years and awards were not able to be exercised until after the expiry of the relevant performance period and achievement of the stated performance conditions. No new awards were made under the LTIP during the year and, as the Company no longer has any employees, it is unlikely that any awards will be made in the foreseeable future. Details of awards to directors made under the LTIP which were outstanding during the year are set out in Table 4 below. These awards, made in January 2011, lapsed at 30 September 2013, owing to the non-achievement of the recurring earnings per share targets related to the awards.

## *Company Share Option Plan ("the CSOP")*

Under the terms of the CSOP, employees of the Company, including executive directors, have been eligible to be granted options over the Company's shares at the discretion of the Remuneration Committee. The exercise price of options granted under the CSOP has been equal to the market value of the Company's shares at the date of grant and the exercise of options has not been subject to a separate performance target. The CSOP has been approved by HM Revenue & Customs.

The options previously granted have been capable of exercise between the third and tenth anniversary of their grant. No awards have been made to executive directors under the CSOP. Under the rules of the CSOP the remaining awards in place must be exercised by their holders within six months of their departure, failing which they will automatically lapse.

## *Non-Executive Directors*

The level of fees paid to non-executive directors was set at the time of the Company's admission to the Official List of the London Stock Exchange having regard to market levels at that time. The level of remuneration for non-executive directors, which is set out in the table below, did not change during the year.

## *Directors' Contracts and Terms of Appointment*

Grahame Whateley has an appointment document dated 30 March 2007, subject to annual extensions. Nick Vetch has an appointment document dated 30 March 2007, subject to annual extensions. Stephen East has an appointment document dated 9 September 2009, subject to annual extensions.

The service contracts applicable to the Company's former executive directors Nick Gregory, Mike Riley and Victoria Whitehouse were all dated 30 March 2007 and provided for 12 months' notice. Steve Faber is an employee of INTERNOS and has not entered into a service contract with the Company.

Copies of the directors' service agreements are kept at the Company's registered office, where they are available for inspection by shareholders during usual business hours on weekdays.

# Remuneration Report continued

## *Director Terminations and Compensation for Loss of Office*

Following the Company's Strategy Review Nick Gregory, Mike Riley and Victoria Whitehouse left the Company, in connection with which the Company made the payments in settlement of termination claims set out in Table 3 below.

Following their departure the Company sold its interest in Local Parade Investments LLP, the joint venture with Pramerica, to investors including Mr Gregory and Mr Riley. At that time asset management activities which the Group had undertaken for Local Parade Investments LLP, Local Retail Fund LP (the Company's former co-investment with Schroders) and the Company's continuing joint venture with a financial institution, together with a number of minor asset management instructions, transferred to a company in which Mr Gregory and Mr Riley were interested.

## *Investor Commentary*

During the year the Company did not receive any communications from shareholders specifically regarding directors' pay, although the broad aim of reducing corporate overheads going forward was recognised by shareholders during the Strategy Review process.

Save as indicated below, the remainder of this report has been audited.

**Table 3: Directors' Total Remuneration**

**2012-13**

| Director | Salary | Bonus | Pension contributions | Benefits in kind | Compensation Payments | Total 2013 |
|---|---|---|---|---|---|---|
| **Non-executive directors** | | | | | | |
| Stephen East | 30,000 | – | – | – | – | **30,000** |
| Nick Vetch | 30,000 | – | – | – | – | **30,000** |
| Grahame Whateley | 50,000 | – | – | – | – | **50,000** |
| **Executive Directors** | | | | | | |
| Steve Faber* | – | – | – | – | | **–** |
| Nick Gregory† | 216,750 | – | 23,833 | 5,381 | 310,000 | **555,964** |
| Mike Riley† | 225,250 | – | 23,833 | 6,551 | 310,000 | **565,634** |
| Victoria Whitehouse† | 94,269 | – | 9,400 | 1,531 | 152,000 | **257,200** |
| **Total** | 646,269 | – | 57,066 | 13,463 | 772,000 | **1,488,798** |

**2011-12**

| Director | Salary | Bonus | Pension contributions | Benefits in kind | Compensation Payments | Total 2012 |
|---|---|---|---|---|---|---|
| **Non-executive directors** | | | | | | |
| Stephen East | 30,000 | – | – | – | – | 30,000 |
| Nick Vetch | 30,000 | – | – | – | – | 30,000 |
| Grahame Whateley | 50,000 | – | – | – | – | 50,000 |
| **Executive Directors** | | | | | | |
| Steve Faber* | – | – | – | – | | – |
| Nick Gregory† | 285,000 | – | 26,000 | 7,300 | – | 318,300 |
| Mike Riley† | 285,000 | – | 26,000 | 6,700 | – | 317,700 |
| Victoria Whitehouse† | 132,500 | 1,200 | 1,300 | 2,300 | – | 137,300 |
| **Total** | 812,500 | 1,200 | 53,300 | 16,300 | – | 883,300 |

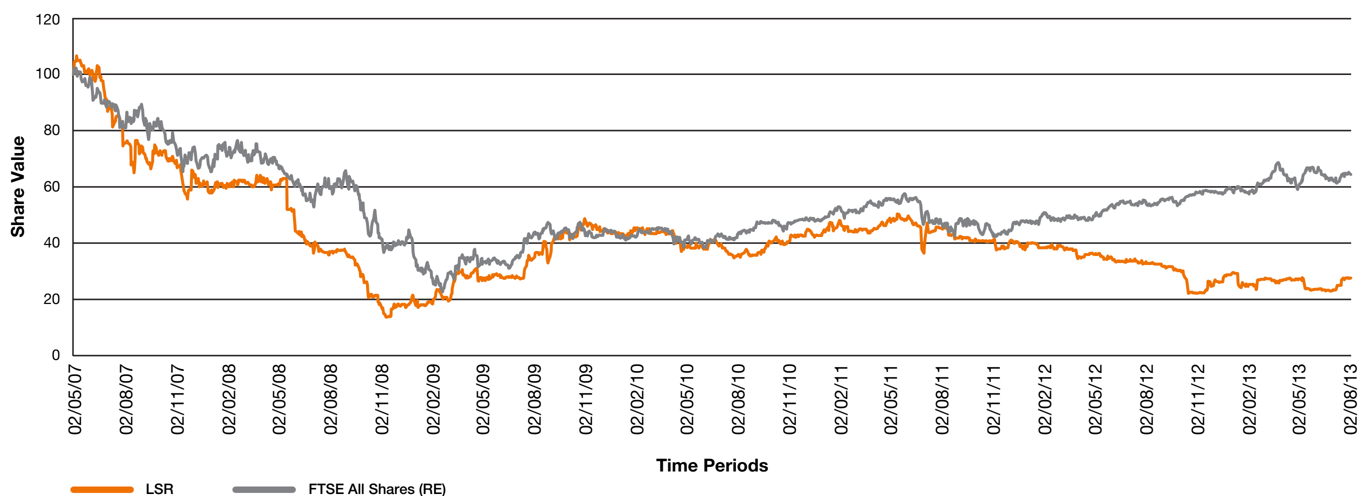
* Appointed 5 July 2013
† Resigned 5 July 2013

### Table 4: Directors' LTIP Awards

| Director | Subject to award at 1 October 2012 | Granted during year | Exercised during year | Lapsed during year | Shares subject to award at 30 September 2013 | Market value per share at award date | Exercise date from | Exercise date to |
|---|---|---|---|---|---|---|---|---|
| Nick Gregory† | 619,905 | – | – | 619,905 | – | £0.59 | 12 January 2014 | 11 January 2021 |
| Mike Riley† | 619,905 | – | – | 619,905 | – | £0.59 | 12 January 2014 | 11 January 2021 |
| Victoria Whitehouse† | 186,821 | – | – | 186,821 | – | £0.59 | 12 January 2014 | 11 January 2021 |
| **Total** | 1,426,631 | – | – | 1,426,631 | – | | | |

† Resigned 5 July 2013

## TSR Performance Graph (Not Audited)




**Nicholas Vetch**
Remuneration Committee Chairman

The foregoing reports were approved by the directors on 3 January 2014.

**William A Heaney**
Company Secretary

# Independent Auditors' Report

to the Members of The Local Shopping REIT plc

Opinions and conclusions arising from our audit

## Our opinion on the financial statements is unmodified

We have audited the financial statements of The Local Shopping REIT plc for the year ended 30 September 2013 set out on pages 38 to 72.

In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the parent Company's affairs as at 30 September 2013 and of the Group's loss for the year then ended;
- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union;
- the parent Company financial statements have been properly prepared in accordance with UK Accounting Standards; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

## Our assessment of risks of material misstatement

In arriving at our audit opinion above on the financial statements the risks of material misstatement that had the greatest effect on our group audit were as follows:

- Valuation of investment property portfolio: Investment property is the Group's single largest asset category. Its valuation requires significant judgements and estimates, from both management and the external valuers, in relation to yield rates and void levels. In this area our audit procedures included, among others, using our own specialist real estate valuers in evaluating the assumptions used by the Group and its external valuer, in particular those relating to yield rates and void levels. We compared the Group's assumptions to externally derived data as well as our own assessments in relation to yield rates on a geographic basis as well as a property type basis. Further, we compared the sales price achieved on disposals during the year and post balance sheet date to the carrying amounts of the disposed properties in the accounting records; and assessed the portfolio valuation as a whole for 'outliers' such as yields in excess of, and significantly below, the average for the portfolio and those properties resulting in the most significant valuation uplift or decrease, which we then investigated with management and the external valuers by assessing specific qualitative factors relevant to each outlier. We also assessed the adequacy of the Group's disclosures (see note 8). concerning the classification of investment properties held for sale, and also the sensitivities around the estimates and judgments used to complete the valuation.
- Going concern: The Group announced its change in investment strategy in July 2013 to one of an orderly liquidation of assets. We discussed with management the availability of other strategies, and assessed the viability of such strategies, that remain open to the Group such as potential refinancing, recommencing a programme of property purchasing or the disposal of the Group as a going concern. Our procedures were designed to assess the viability of these alternatives particularly around selling the business as a going concern. Our work involved critically assessing the cash flow forecasts prepared by management to ascertain the level of cash headroom and debt covenants headroom for the foreseeable future and challenging management's assumptions included in the forecasts particularly around property disposals, yield and void rates, and default rates, to consider whether these are realistic alternatives to ceasing trading.

## *Our application of materiality and an overview of the scope of our audit*

The materiality for the Group financial statements as a whole was set at £706,000. This has been calculated with reference to a benchmark of total assets which we consider to be one of the principal considerations for members of the Company in assessing the financial performance of the Group.

We agreed with the audit committee to report to it all corrected and uncorrected misstatements we identified through our audit with a value in excess of £47,000 in addition to other audit misstatements below that threshold that we believe warranted reporting on qualitative grounds.

Our audit of the Group, which comprised a single reporting component, was undertaken to the materiality level specified above and was all performed at the Group's head office in London.

## *Opinion on 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 Strategic Report and 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*

Under ISAs (UK and Ireland) we are required to report to you if, based on the knowledge we acquired during our audit, we have identified other information in the annual report that contains a material inconsistency with either that knowledge or the financial statements, a material misstatement of fact, or that is otherwise misleading.

In particular, we are required to report to you if:

- we have identified material inconsistencies between the knowledge we acquired during our audit and the directors' statement that they consider that the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's performance, business model and strategy; or
- the Report from the Audit Committee on pages 29 does not appropriately address matters communicated by us to the audit committee.

Under the Companies Act 2006 we are required 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 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 28, in relation to going concern;
- the part of the Corporate Governance Statement on pages 20 to 28 relating to the Company's compliance with the nine provisions of the 2010 UK Corporate Governance Code specified for our review; and
- certain elements of the report to shareholders by the Board on directors' remuneration.

We have nothing to report in respect of the above responsibilities.

## Scope of report and responsibilities

As explained more fully in the Directors' Responsibilities Statement set out on page 18, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. A description of the scope of an audit of accounts is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate. This report is made solely to the Company's members as a body and subject to important explanations and disclaimers regarding our responsibilities, published on our website at www.kpmg.com/uk/auditscopeukco2013a, which are incorporated into this report as if set out in full and should be read to provide an understanding of the purpose of this report, the work we have undertaken and the basis of our opinions.

**John Leech** (Senior Statutory Auditor)
for and on behalf of KPMG Audit Plc, Statutory Auditor
Chartered Accountants
One Snowhill
Snow Hill Queensway
Birmingham
B4 6GH
3 January 2014

# Consolidated Income Statement

for the year ended 30 September 2013

| | Note | 2013 £000 | 2012 £000 |
|---|---|---|---|
| **Gross rental income** | | **14,649** | 15,809 |
| Property operating expenses | | **(2,579)** | (2,545) |
| **Net rental income** | | **12,070** | 13,264 |
| Profit on disposal of investment properties | | **114** | 84 |
| Loss from change in fair value of investment properties | 8 | **(8,778)** | (12,165) |
| Administrative expenses including non-recurring items | 3 | **(4,520)** | (3,305) |
| Net other income | 4 | **22** | 16 |
| Share of results from jointly controlled entities | 9 | **(134)** | (11) |
| **Operating (loss)/profit before net financing costs** | | **(1,226)** | (2,117) |
| Financing income* | 5 | **4** | 3 |
| Financing expenses* | 5 | **(7,947)** | (7,574) |
| Movement in fair value of financial derivatives | 5 | **2,753** | 216 |
| **Loss before tax** | | **(6,416)** | (9,472) |
| Taxation | 6 | **–** | – |
| **Loss for the year from continuing operations** | | **(6,416)** | (9,472) |
| **Discontinued operations** | | | |
| **Profit for the year from discontinued operations** | | **345** | 294 |
| **Loss for the financial year attributable to equity holders of the Company** | | **(6,071)** | (9,178) |
| **Basic and diluted loss per share on loss for the year** | 18 | **(7.5)p** | (11.3)p |
| **Basic and diluted loss per share on continuing operations for the year** | 18 | **(7.9)p** | (11.6)p |

* Excluding movement in the fair value of financial derivatives.

Loss for the financial year attributable to equity holders of the Company is split between continuing operations (2013: £(6,416,000); 2012: £(9,472,000)) and discontinued operations (2013: profit £345,000; 2012: profit £294,000).

Comparative figures for 2012 have been restated to reclassify amounts relating to discontinued operations (see note 25).

# Consolidated Statement of Comprehensive Income

for the year ended 30 September 2013

| | 2013 £000 | 2012 £000 |
|---|---|---|
| Loss for the financial year | **(6,071)** | (9,178) |
| **Total comprehensive income for the year** | **(6,071)** | (9,178) |
| Attributable to: | | |
| **Equity holders of the parent Company** | **(6,071)** | (9,178) |

# Consolidated Balance Sheet

as at 30 September 2013

| | Note | 2013 £000 | 2012 £000 |
|---|---|---|---|
| **Non-current assets** | | | |
| Property, plant and equipment | 7 | – | 126 |
| Investment properties | 8 | 166,107 | 178,109 |
| Investments in jointly controlled entities | 9 | 507 | 4,070 |
| Other investments | 10 | – | 909 |
| | | 166,614 | 183,214 |
| **Current assets** | | | |
| Trade and other receivables | 11 | 4,784 | 4,698 |
| Investment properties held for sale | 8 | 3,675 | – |
| Cash | 12 | 6,626 | 5,496 |
| | | 15,085 | 10,194 |
| **Total assets** | | 181,699 | 193,408 |
| **Non-current liabilities** | | | |
| Interest bearing loans and borrowings | 13 | (134,363) | (136,380) |
| Finance lease liabilities | 15 | (922) | (922) |
| Derivative financial instruments | 19 | (3,872) | (6,595) |
| | | (139,157) | (143,897) |
| **Current liabilities** | | | |
| Interest bearing loans and borrowings | 13 | – | – |
| Trade and other payables | 14 | (6,499) | (5,739) |
| Derivative financial instruments | 19 | (2,417) | (2,447) |
| | | (8,916) | (8,186) |
| **Total liabilities** | | (148,073) | (152,083) |
| **Net assets** | | 33,626 | 41,325 |
| **Equity** | | | |
| Issued capital | 16 | 18,334 | 18,334 |
| Reserves | 16 | 3,773 | 3,773 |
| Capital redemption reserve | 16 | 1,764 | 1,764 |
| Retained earnings | | 9,755 | 17,454 |
| **Total attributable to equity holders of the Company** | | 33,626 | 41,325 |

The financial statements were approved by the Board on 3 January 2014. They were signed on its behalf by:

**Steven Faber**
Director

The registered number of the Company is 05304743.

# Consolidated Statement of Cash Flows

for the year ended 30 September 2013

| | Note | 2013 £000 | 2012 £000 |
|---|---|---|---|
| **Operating activities** | | | |
| Loss for the year | | (6,071) | (9,178) |
| Adjustments for: | | | |
| Loss from change in fair value of investment properties | 8 | 8,778 | 12,165 |
| Net financing costs | 5 | 5,190 | 7,355 |
| Profit on disposal of investment properties | | (114) | (84) |
| Loss on disposal of discontinued operations | 26 | 500 | – |
| Depreciation | 7 | 123 | 40 |
| Share of results of jointly controlled entities | 9 | 134 | 207 |
| | | 8,540 | 10,505 |
| (Increase)/decrease in trade and other receivables | | (86) | (925) |
| (Decrease)/increase in trade and other payables | | 788 | (80) |
| | | 9,242 | 9,500 |
| Interest paid | | (7,525) | (7,265) |
| Loan arrangement fees paid | | (481) | (21) |
| Interest received | | 4 | 3 |
| Corporation tax paid | | – | – |
| **Net cash from operating activities** | | 1,240 | 2,217 |
| **Investing activities** | | | |
| Proceeds from sale of investment properties | | 1,356 | 2,174 |
| Acquisition and improvements to investment properties | 8 | (1,693) | (2,251) |
| Proceeds of sale from property, plant and equipment | | 3 | – |
| Proceeds of sale from discontinued operations | | 2,753 | – |
| Proceeds of sale from other investments | | 725 | – |
| Acquisition of property, plant and equipment | 7 | – | (5) |
| Investment in jointly controlled entities | 9 | (317) | (2,454) |
| Repayment of investment in jointly controlled entities | | 681 | – |
| Investment in other investments | 10 | – | (909) |
| **Cash flows from investing activities** | | 3,508 | (3,445) |
| **Net cash flows from operating activities and investing activities** | | 4,748 | (1,228) |
| **Financing activities** | | | |
| Repayment of borrowings | | (68,300) | (300) |
| New borrowings | | 66,310 | 5,900 |
| Dividends paid | 17 | (1,628) | (3,337) |
| **Cash flows from financing activities** | | (3,618) | 2,263 |
| Net increase/(decrease) in cash | | 1,130 | 1,035 |
| Cash at beginning of year | | 5,496 | 4,461 |
| **Cash at end of year** | 12 | 6,626 | 5,496 |

# Consolidated Statement of Changes in Equity

for the year ended 30 September 2013

| | Share capital £000 | Reserves £000 | Capital redemption reserve £000 | Retained earnings £000 | Total £000 |
|---|---|---|---|---|---|
| Balance at 1 October 2011 | 18,334 | 3,773 | 1,764 | 29,969 | 53,840 |
| **Total comprehensive income for the year** | | | | | |
| Loss for the year | – | – | – | (9,178) | (9,178) |
| **Transactions with owners, recorded directly in equity** | | | | | |
| Dividends | – | – | – | (3,337) | (3,337) |
| **Total contributions by and distributions to owners** | – | – | – | (3,337) | (3,337) |
| **Balance at 30 September 2012** | 18,334 | 3,773 | 1,764 | 17,454 | 41,325 |
| **Total comprehensive income for the year** | | | | | |
| Loss for the year | – | – | – | (6,071) | (6,071) |
| **Transactions with owners, recorded directly in equity** | | | | | |
| Dividends | – | – | – | (1,628) | (1,628) |
| **Total contributions by and distributions to owners** | – | – | – | (1,628) | (1,628) |
| **Balance at 30 September 2013** | **18,334** | **3,773** | **1,764** | **9,755** | **33,626** |

# Notes to the Financial Statements

for the year ended 30 September 2013

## 1 Accounting Policies

### Basis of Preparation

The Local Shopping REIT plc ("the Company") is a company incorporated and domiciled in the UK. The Group's financial statements have been prepared in accordance with International Financial Reporting Standards as adopted by the EU (adopted "IFRS") and in accordance with the provisions of the Companies Act 2006.

The financial statements are prepared in pounds sterling, rounded to the nearest thousand. They have been prepared under the historical cost convention except for the following assets which are measured on the basis of fair value: investment properties, derivative financial instruments, other investments and investment properties held for sale.

The directors have considered whether it is appropriate to prepare the financial statements on a going concern basis. The diversity of the tenant base across retail sectors and its geographical spread around the country demonstrates no reliance on one significant tenant. The loan facilities, together with the attached covenants, are detailed in this document. All covenants have been met throughout the year. The directors have prepared profit and cash flow forecasts for the period to 30 September 2018 which include assumptions relating to the orderly sale of properties under the current investment strategy which the directors consider to be reasonable. These forecasts project the Company's funding needs will be comfortably met by its existing banking facility agreements without any breach of related covenants over the remaining life of the facilities which expire in 2017 and 2018.

On the basis of these projections the directors consider that the Group will continue to be compliant with its banking covenants and sufficient resources will be available to enable it to continue as a going concern for at least the next 12 months. The directors note that a number of other viable alternative strategies remain available to the Company and they will continue to evaluate whether to continue with its current investment policy or to change to one of these viable alternative strategies. Accordingly, the financial statements have been prepared on the going concern basis.

The accounting policies set out below have, unless otherwise stated, been applied consistently to all periods presented in these financial statements.

### Basis of Consolidation

The consolidated financial statements include the financial statements of the Company and all its subsidiary undertakings up to 30 September 2013. Subsidiaries are consolidated from the date on which the Group obtains control, being the power to govern the financial and operating policies of the entity so as to obtain benefit from its activities. They continue to be consolidated until the date that such control ceases. The financial statements of subsidiaries are prepared using consistent accounting policies. Inter-company transactions and balances are eliminated.

### Investment Property

Investment properties are those properties owned by the Group that are held to earn rental income or for capital appreciation or both and are not occupied by the Company or any of its subsidiaries.

The fair value of investment properties is based on market values being an estimated amount for which a property could be exchanged on the date of valuation under an arm's length transaction between a willing buyer and seller after proper marketing wherein the parties had acted knowledgeably, prudently and without compulsion. Professional external valuers have valued a sample selected by themselves of 25% of the existing portfolio at the half year and year end and all new purchases since the previous valuation to the half year and to the year end. The remainder of the portfolio has been valued on the basis of market value at the year end by the directors who have appropriate recognised professional qualifications and recent experience of the location and category of the property being valued.

Investment properties are treated as acquired at the point the Group assumes the significant risks and returns of ownership. Subsequent expenditure is charged to the asset's carrying value only when it is probable that future economic benefits associated with the expenditure will flow to the Group and the cost of each item can be reliably measured. All other repairs and maintenance costs are charged to the Income Statement during the period in which they are incurred.

Disposals of investment properties are recognised on completion; profits and losses arising are recognised through the Income Statement, the profit is determined as the difference between the sales proceeds and the carrying amount of the asset at the last valuation date plus any additional expenditure incurred since that date.

## 1 Accounting Policies continued

Interest on loans associated with acquiring investment properties is expensed on an effective interest rate basis.

Rental income from investment properties is accounted for as described below.

### Investment Properties Held for Sale

Investment properties held for sale are included in the Balance Sheet at their fair value. In determining whether assets no longer meet the investment criteria of the Group, consideration has been given to the conditions required under IFRS 5.

### Head Leases

Where a property is held under a head lease and is classified as an investment property, it is initially recognised as an asset based on the sum of the premium paid on acquisition and if the remaining life of the lease at date of acquisition is considered to be material, the net present value of the minimum ground rent payments. The corresponding rent liability to the leaseholder is included in the Balance Sheet as a finance obligation in current and non-current liabilities.

The payment of head rent reduces the gross liability and the interest element of the finance lease is charged to the Income Statement. Head leases considered not to have a material life remaining at the date of acquisition are accounted for as operating leases with the head rent paid being expensed through the Income Statement.

### Property, Plant and Equipment

All property, plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure which is directly attributable to the acquisition of the asset.

Depreciation in the previous year has been charged to the Income Statement on the following basis:

Fixtures and fittings – 15% reducing balance;
Computer equipment – straight-line basis over three years; and
Leasehold improvements – straight-line basis over the shorter of the length of lease or the useful economic life.

Since the year end the company has agreed a termination of its lease of its former offices with an effective date in June 2014. None of the leasehold improvements will be realisable, and it is anticipated that the fixtures, fittings and computer equipment assets will generate negligible funds, if any. For this reason the assets have been fully depreciated in the year.

### Joint Ventures

The Group has contractual arrangements with other parties which represent jointly controlled entities. These take the form of agreements to share control over other entities. The consolidated financial statements include the Group's share of the total recognised gains and losses of jointly controlled entities on an equity accounted basis. Under the equity method, the interests in the jointly controlled entities are carried in the Balance Sheet at cost plus post-acquisition changes in the Group's share of their net assets, less distributions received and less any impairment in value of the individual investments. The Income Statement reflects the Group's share of the jointly controlled entities' results after interest and tax.

The financial statements of the jointly controlled entities are prepared for the same reporting period as the Group. Where necessary, adjustments are made to bring the accounting policies used in line with those of the Group.

During the year one of the joint ventures was disposed of. Its results have been included up to the date of disposal.

### Other Investments

Other non-current investments are classified as available for sale financial assets and are recognised at fair value. Changes in the fair value in the year are recognised directly in the Statement of Comprehensive Income. Dividend income from investments is recognised in the Income Statement when the right to receive payment is established.

During the year the one non-current investment was disposed of. Its results have been included up to the date of disposal.

# Notes to the Financial Statements

for the year ended 30 September 2013

## 1 Accounting Policies continued

### Trade and Other Receivables

Trade and other receivables are initially recognised at fair value and subsequently held at amortised cost less impairment. Impairment is made where it is established that there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivable. The impairment is recorded in the Income Statement.

### Cash and Cash Equivalents

Cash and cash equivalents comprise cash balances and deposits held on call. Cash equivalents are short-term, highly liquid investments with original maturities of three months or less.

### Derivative Financial Instruments and Hedging

The Group uses derivative financial instruments such as interest rate swaps to economically hedge risks associated with interest rate fluctuations. The Group does not hold or issue derivatives for trading purposes.

Such instruments are initially measured at fair value on the date on which a contract is entered into and are subsequently remeasured at fair value. Financial derivatives are recognised as current and non-current based on the maturity profile of the associated cash flows.

The Group has determined that the derivative financial instruments held did not qualify as effective for hedge accounting under the criteria set out in IAS 39 and consequently any gains or losses arising from changes in their fair value are taken to the Income Statement. In the future and on an ongoing basis as new derivative financial instruments are entered into, the directors will review the derivative contracts to consider whether they qualify for hedge accounting.

### Financial Assets

Financial assets are impaired when there is objective evidence that the cash flows from the financial asset are reduced.

### Trade and Other Payables

Trade and other payables are initially recognised at fair value and subsequently held at amortised cost less impairment.

### Ordinary Share Capital

External costs directly attributable to the issue of new shares are shown in equity as a deduction from the proceeds.

Shares which have been repurchased are classified as treasury shares and shown in retained earnings. They are recognised at the trade date for the amount of consideration paid, together with directly attributable costs. This is presented as a deduction from total equity. Shares held by the Employee Benefit Trust are treated as being those of the Group.

The nominal value of shares cancelled has been taken to a capital redemption reserve.

### Rental Income

Rental income from investment properties leased out under operating leases is recognised in the Income Statement on a straight-line basis over the term of the lease. When the Group provides lease incentives to its tenants the cost of incentives are recognised over the lease term, on a straight-line basis, as a reduction to income.

### Other Income

Other income includes asset management fees which are recognised in the Income Statement as earned under the terms of each agreement.

### Taxation

Corporation tax on the profit or loss for the year comprises current and deferred tax. Corporation tax is recognised in the Income Statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

As a REIT, the Group will be exempt from corporation tax on the profits and gains from its property investment business, provided it continues to meet certain conditions. Non-qualifying profits and gains of the Group (the residual business) continue to be subject to corporation tax. Therefore, current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date and any adjustment to tax payable in respect of previous years. The REIT entry charge is expensed on the date of entry to the REIT regime.

## 1 Accounting Policies continued

Deferred tax is provided using the balance sheet liability method. Provision is made for temporary differences between the carrying amounts of assets and liabilities in the financial statements for financial reporting purposes and the amounts used for taxation purposes. Deferred income tax is calculated after taking into account any indexation allowances and capital losses on an undiscounted basis. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities using tax rates enacted or substantially enacted at the balance sheet date. Deferred tax assets are recognised only to the extent that it is probable that future profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised. Deferred tax assets and liabilities are only offset if there is a legally enforceable right of set-off.

### Pensions

The Group operates a defined contribution pension plan. Contributions payable by the Group in respect of defined contribution plans are charged to administrative expenses as incurred.

### Share-based Payments

There were no material share-based payment arrangements during the period.

### Employee Benefit Trust

The Group operates an Employee Benefit Trust in order to hedge its obligations under the CSOP and LTIP schemes. The Group either purchases own shares directly or it funds the trust to acquire shares in the Company. Transactions of the Employee Benefit Trust are treated as being those of the Company and are therefore reflected in the Group financial statements.

### Use of Estimates and Judgements

To be able to prepare accounts according to generally accepted accounting principles, management must make estimates and assumptions that affect the asset and liability items and revenue and expense amounts recorded in the financial statements. These estimates are based on historical experience and various other assumptions that management and the Board of directors believe are reasonable under the circumstances. The results of these considerations form the basis for making judgements about the carrying value of assets and liabilities that are not readily available from other sources.

The areas requiring the use of estimates and judgements that may significantly impact the Group's earnings and financial position include the estimation of: the fair value of investment properties, derivative financial instruments and trade receivables.

The valuation of the Group's investment properties is the main area of judgement exercised by the Board in respect of the Group's results. The Board has obtained an external valuation of the portfolio carried out by professionally qualified valuers in accordance with the Appraisal and Valuation Standards of the Royal Institution of Chartered Surveyors in respect of all properties purchased since 1 October 2012 and a further 25% of the portfolio at the half year and year end as selected by the valuers. The valuers were acting as independent valuers and have good information and experience of the current market prices for properties similar to those owned by the Group. Their opinion of Market Value was primarily derived using comparable recent market transactions on an arm's length basis. The tone of their valuation has been adopted by the directors to value the remainder of the portfolio. The assumptions underlying the valuation of the commercial properties within the portfolio include: future rental income, an appropriate discount rate, any planned capital expenditure and the strength of the local letting market in relation to the Market Rent of any letting voids. In addition to these assumptions, in respect of the residential element of the portfolio, a discount of 85% is typically applied to reflect vacant possession.

The valuation of derivative financial instruments and the fixed rate loan are also areas where judgement has been exercised by the Board. These assets and liabilities have been valued by the Group's bankers. These valuations have been relied upon by the Board.

The Group is required to assess whether there is sufficient objective evidence to require the impairment of individual trade receivables. It does this through a regular review of arrears with consideration given to any specific circumstances relating to the receivable.

# Notes to the Financial Statements

for the year ended 30 September 2013

## 1 Accounting Policies continued

### New Standards and Interpretations Not Yet Adopted

There are a number of amendments to standards and interpretations of standards which are not yet effective for the year ended 30 September 2013 and have not been applied in preparing these consolidated financial statements. These are as follows:

Amendments to existing standards

Amendments to IFRS 7 – Presentation of items of other comprehensive income.

- IAS 27 – Separate Financial Statements
- IAS 28 – Investments in Associates and Joint Ventures
- IAS 32 – Financial Instruments: Presentation
- IFRS 9 – Financial Instruments
- IFRS10 – Consolidated Financial Statements
- IFRS 11 – Joint arrangements
- IFRS12 – Disclosure of Interests in Other Entities
- IFRS 13 – Fair Value Measurement

All of the above amendments to existing standards are endorsed by the European Union (EU) at the date of approval of these financial statements.

At the date of approval of these financial statements, the following interpretations and amendments to standards were issued, endorsed by the EU and are mandatory for the Group for the first time for the financial year beginning on 1 October 2012:

Amendments to IAS 1 – Presentation of financial statements.

The adoption of these standards would result in no material impact to these financial statements.

## 2 Segmental Reporting

IFRS 8 requires operating segments to be identified on the basis of internal reports that are regularly reported to the chief operating decision maker to allocate resources to the segments and to assess their performance.

Since the establishment of the jointly controlled entities and other investments, the Group has identified two operating and reporting segments which are reported to the Board of directors on a quarterly basis. The Board of directors is considered to be the chief operating decision maker.

The financial information presented quarterly to the Board is the recurring profit achieved by each segment. The segments identified are: properties owned directly by the Group and the asset management income earned, together with the share of results due to the Group from the joint ventures.

Following the Strategy Review, the Board consider there to be only one reportable segment. As the results for 2012 have been restated for discontinued activities, segmental analysis for 2012 is not considered to be material.

## 3 Administrative Expenses

a) The following fees have been paid to the Group's Auditors:

| | 2013 £000 | 2012 £000 |
|---|---|---|
| Auditors' remuneration for audit services: | | |
| Audit of parent Company | 34 | 34 |
| Audit related assurance services | 16 | 16 |
| Statutory audit of subsidiaries | 52 | 52 |
| Auditors' remuneration for non-audit services: | | |
| Tax services | 37 | 37 |
| Other services supplied | 10 | 50 |

The other services supplied in 2013 relate to professional advice received in connection with the strategic review and restructure, and in 2012 with the exploration of a potential transaction which was considered by the Company.

b) Included in administrative expenses are staff costs and directors' remuneration.

The average number of persons employed by the Group was as follows:

| | 2013 Number of employees | 2012 Number of employees |
|---|---|---|
| Administration | 11 | 14 |

The average shown above for 2013 is for the full year. For the period from October 2012 to June 2013, when all the existing employees either left or were transferred to Internos Global Investors Limited, the average was 15. From July 2013 onwards the average has been nil.

The aggregate payroll costs of these people were as follows:

| | 2013 £000 | 2012 £000 |
|---|---|---|
| Wages and salaries | 1,024 | 1,489 |
| Payments under compromise agreements | 965 | – |
| Social security costs | 157 | 180 |
| Other pension costs | 79 | 89 |
| Equity settled share-based payments | – | 5 |
| | 2,225 | 1,763 |

Directors' emoluments are disclosed separately in the Remuneration Report.

c) Share Awards

There were no material share-based payment arrangements during the period.

# Notes to the Financial Statements

for the year ended 30 September 2013

## 3 Administrative Expenses continued

d) Non-recurring items

IAS 1 (Revised) – "Presentation of financial statements" requires material items of income and expenditure to be disclosed separately. The amounts are items which, in management's opinion, need to be disclosed by virtue of their size or incidence in order for the user to obtain a proper understanding of the financial information.

Included in the administration costs are charges arising from the reconstruction following the strategic review, and are non-recurring:

In administration costs:

| | 2013 £000 | 2012 £000 |
|---|---|---|
| Paid to directors under compromise agreements | 772 | – |
| Employer's NI on the above payments | 15 | – |
| Paid to employees under compromise agreements | 193 | – |
| Employer's NI on the above payments | 6 | – |
| Legal, professional and advisory fees | 912 | – |
| Dilapidations provision on termination of company's office lease | 39 | – |
| Professional fees | – | 506 |
| | 1,937 | 506 |
| Included within financial costs: | | |
| Accelerated amortisation of loan fees | 312 | – |
| | 2,249 | 506 |

During the preceding year the Company incurred costs of £506,000 principally in connection with professional advice received regarding the exploration of a potential transaction which was considered by the Company.

## 4 Net Other Income

| | 2013 £000 | 2012 restated £000 |
|---|---|---|
| Other income | 22 | 22 |
| Other expenses | – | (6) |
| | 22 | 16 |

2012 balances have been restated to exclude asset management income and costs relating to discontinued operations (note 25).

## 5 Net Financing Costs

| | 2013 £000 | 2012 £000 |
|---|---|---|
| Interest receivable | 4 | 3 |
| Interest receivable excluding fair value movements | 4 | 3 |
| Fair value gains on derivative financial instruments (note 19) | 2,753 | 216 |
| Financing income | 2,757 | 219 |
| | | |
| Bank loan interest | (7,436) | (7,338) |
| Amortisation of loan arrangement fees | (143) | (181) |
| Write off of loan arrangement fees | (313) | – |
| Head rents treated as finance leases | (55) | (55) |
| Financing expenses excluding fair value movements | (7,947) | (7,574) |
| Fair value losses on derivative financial instruments (note 19) | – | – |
| Financing expenses | (7,947) | (7,574) |
| | | |
| Net financing costs | (5,190) | (7,355) |

## 6 Taxation

| | 2013 £000 | 2012 £000 |
|---|---|---|
| **Current tax** | | |
| Corporation tax charged at 23.5% (2012: 25%) | – | – |
| Total current tax | – | – |
| **Deferred tax** | | |
| Origination and reversal of temporary differences | – | – |
| Total tax charge in the Income Statement | – | – |

### Reconciliation of Effective Tax Rate

| | 2013 £000 | 2012 £000 |
|---|---|---|
| Loss before tax | (6,071) | (9,178) |
| Corporation tax in the UK of 23.5% (2012: 25%) | (1,427) | (2,294) |
| Tax relief available from REIT status | (1,199) | (1,560) |
| Effects of: | | |
| Revaluation deficit and other non-deductible items | 2,004 | 3,308 |
| Deferred tax asset not recognised | 622 | 546 |
| | – | – |

### Factors that may affect future current and total tax charges

The March 2013 UK Budget announced that the UK corporation tax rate will reduce to 20% by 2015. A reduction in the rate from 24% to 23% (effective from 1 April 2013) was substantively enacted on 3 July 2012, and further reductions to 21% (effective from 1 April 2014) and 20% (effective from 1 April 2015) were substantively enacted on 2 July 2013. This would reduce the Company's future tax charge accordingly.

From 11 May 2007, the Group elected to join the UK REIT regime. As a result, the Group will be exempt from corporation tax on the profits and gains from its property investment business from this date, provided it continues to meet certain conditions. Non-qualifying profits and gains of the Group (the residual business) continue to be subject to corporation tax. The directors consider that all the rental income post-11 May 2007 originates from the Group's tax exempt business.

On entering the UK REIT regime, a conversion charge equal to 2% of the gross market value of properties involved in the property rental business, at that date, became due which has now been paid in full.

Due to the availability of losses no provision for corporation tax has been made in these accounts. The deferred tax asset not recognised relating to these losses can be carried forward indefinitely. It is not anticipated that sufficient profits from the residual business will be generated in the foreseeable future to utilise the losses carried forward as the current year losses will be adequate to cover foreseeable profits. The unprovided deferred tax asset at 30 September 2013 was £2,648,000 (2012: £2,003,000).

# Notes to the Financial Statements

for the year ended 30 September 2013

## 7 Property, Plant and Equipment

| | Leasehold Improvements £000 | Fixtures and Fittings £000 | Computer Equipment £000 | Total £000 |
|---|---|---|---|---|
| **Cost** | | | | |
| At 1 October 2011 | 166 | 38 | 71 | 275 |
| Additions | 1 | 3 | 1 | 5 |
| At 30 September 2012 | **167** | **41** | **72** | **280** |
| Additions | – | – | – | – |
| Disposals | – | – | (7) | (7) |
| **At 30 September 2013** | **167** | **41** | **65** | **273** |
| **Depreciation** | | | | |
| At 1 October 2011 | 59 | 19 | 36 | 114 |
| Charge for year | 17 | 3 | 20 | 40 |
| At 30 September 2012 | **76** | **22** | **56** | **154** |
| Charge for year | 91 | 19 | 13 | 123 |
| Written back on disposals | – | – | (4) | (4) |
| **At 30 September 2013** | **167** | **41** | **65** | **273** |
| **Net book value** | | | | |
| **At 30 September 2013** | **–** | **–** | **–** | **–** |
| At 30 September 2012 | 91 | 19 | 16 | 126 |
| At 30 September 2011 | 107 | 19 | 35 | 161 |

Since the year end the company has agreed a termination of its lease of its former offices with an effective date in June 2014. None of the leasehold improvements will be realisable, and it is anticipated that the fixtures, fittings and computer equipment assets will generate negligible funds, if any. For this reason the assets have been fully depreciated in the year.

## 8 Investment Properties

| | Freehold Investment Properties £000 | Leasehold Investment Properties £000 | Total £000 |
|---|---|---|---|
| At 30 September 2011 | 155,039 | 35,072 | 190,111 |
| Additions | 1,971 | 280 | 2,251 |
| Disposals | (1,953) | (135) | (2,088) |
| Fair value adjustments | (10,213) | (1,952) | (12,165) |
| At 30 September 2012 | 144,844 | 33,265 | 178,109 |
| Property improvements | 1,434 | 259 | 1,693 |
| Disposals | (1,159) | (83) | (1,242) |
| Fair value adjustments | (7,473) | (1,305) | (8,778) |
| Investment properties held for sale | (2,857) | (818) | (3,675) |
| **At 30 September 2013** | **134,789** | **31,318** | **166,107** |

## 8 Investment Properties continued

The investment properties have all been revalued to their fair value at 30 September 2013.

At the half year and year end, all properties acquired in those six months, together with a sample selected by the valuers of 25% of the portfolio, at the half year and at the year end have been valued by Allsop LLP, a firm of independent Chartered Surveyors. The valuations were undertaken in accordance with the Royal Institution of Chartered Surveyors Appraisal and Valuation Standards on the basis of market value. Market value is defined as the estimated amount for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm's length transaction, after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion.

The remainder of the portfolio has been valued on the basis of market value by the directors who have an appropriate recognised professional qualification and recent experience in the location and category of the property being valued.

All rental income recognised in the Income Statement is generated by the investment properties held and all direct operating expenses incurred resulted from investment properties that generated rental income.

A reconciliation of the portfolio valuation to the total value given in the Balance Sheet for investment properties is as follows:

| | 2013 £000 | 2012 £000 |
|---|---|---|
| Portfolio valuation | 168,860 | 177,187 |
| Investment properties held for sale | (3,675) | – |
| Head leases treated as investment properties held under finance leases per IAS 17 | 922 | 922 |
| Total per Balance Sheet | 166,107 | 178,109 |

## 9 Investments in jointly controlled entities

The Group has the following investments in jointly controlled entities:

| | 2013 | | 2012 | |
|---|---|---|---|---|
| | Country | Ownership | Country | Ownership |
| Local Parade Investments LLP | United Kingdom | nil | United Kingdom | 20% |
| Gracechurch Commercial Investments Limited | United Kingdom | 50% | United Kingdom | 50% |

On 26 November 2010 an agreement was entered into with Local Parade Investments LLP ("LPI"), a newly incorporated entity. The initial investment made was £20. The principal activity of the entity is the acquisition and management of retail parades. This investment was disposed of as part of the reconstruction following the strategic review, in July 2013. This is now reflected in discontinued operations (note 25).

On 28 September 2011 an agreement was entered into with Gracechurch Commercial Investments Limited ("Gracechurch"), a newly incorporated entity. The initial investment made was £500,000. The principal activity of the entity is to manage properties for investment purposes.

# Notes to the Financial Statements

for the year ended 30 September 2013

## 9 Investments in jointly controlled entities continued

| | Gracechurch £000 | LPI £000 | Total £000 |
|---|---|---|---|
| Cost | | | |
| At 1 October 2011 | 652 | 1,171 | 1,823 |
| Equity investments | – | 2,454 | 2,454 |
| Loan advances | – | – | – |
| Share of results, net of tax | (11) | (196) | (207) |
| Distributions received | – | – | – |
| At 30 September 2012 | 641 | 3,429 | 4,070 |
| Equity investments | – | – | – |
| Loan advances | – | 317 | 317 |
| Share of results, net of tax | (134) | 187 | 53 |
| Distributions received | | (681) | (681) |
| Investment disposed of | – | (3,252) | (3,252) |
| **At 30 September 2013** | **507** | **–** | **507** |

The summarised financial information in respect of the Group's share of the jointly controlled entities is shown below.

Year ended 30 September 2012

| | Gracechurch £000 | LPI £000 | Total £000 |
|---|---|---|---|
| Non-current assets | 1,158 | 7,064 | 8,222 |
| Current assets | 731 | 408 | 1,139 |
| Non-current liabilities | (1,147) | (3,659) | (4,806) |
| Current liabilities | (101) | (384) | (485) |
| | 641 | 3,429 | 4,070 |
| Represented by: | | | |
| Capital | 500 | – | 500 |
| Loans | 210 | 3,622 | 3,832 |
| Brought forward share of results | (58) | 3 | (55) |
| Share of results, net of tax | (11) | (196) | (207) |
| Group's share of net assets | 641 | 3,429 | 4,070 |

| | Gracechurch £000 | LPI £000 | Total £000 |
|---|---|---|---|
| Net rental income | 141 | 360 | 501 |
| Property expenses | (46) | (71) | (117) |
| Administrative expenses | (2) | (53) | (55) |
| Change in fair value of investment properties | (75) | (271) | (346) |
| Net interest payable | (57) | (166) | (223) |
| Movement in fair value of financial derivatives | (17) | (35) | (52) |
| Profit/(Loss) on disposal of investment properties | 72 | 40 | 112 |
| Tax | (27) | – | (27) |
| | (11) | (196) | (207) |

## 9 Investments in jointly controlled entities continued

**Year ended 30 September 2013**

| | Gracechurch £000 | LPI £000 | Total £000 |
|---|---|---|---|
| Non-current assets | 1,019 | – | 1,019 |
| Current assets | 44 | – | 44 |
| Non-current liabilities | (491) | – | (491) |
| Current liabilities | (65) | – | (65) |
| | 507 | – | 507 |
| Represented by: | | | |
| Capital | 500 | – | 500 |
| Loans | 210 | – | 210 |
| Brought forward share of results | (68) | – | (68) |
| Share of results, net of tax | (135) | – | (135) |
| Group's share of net assets | 507 | – | 507 |

| | Gracechurch £000 | LPI £000 | Total £000 |
|---|---|---|---|
| Net rental income | 91 | 544 | 635 |
| Property expenses | (26) | (101) | (127) |
| Administrative expenses | (14) | (24) | (38) |
| Change in fair value of investment properties | (139) | 22 | (117) |
| Net interest payable | (54) | (252) | (306) |
| Movement in fair value of financial derivatives | 8 | (7) | 1 |
| Profit on disposal of investment properties | – | 5 | 5 |
| Tax | – | – | – |
| | (134) | 187 | 53 |

# Notes to the Financial Statements

for the year ended 30 September 2013

## 10 Other investments

On 8 March 2012, the Group entered into a partnership and property advisory agreement with Local Retail Fund GP Limited, a newly incorporated entity. The initial investment made was £45. The principal activity of the entity is the acquisition and management of a diversified portfolio of local retail property in the UK. As part of the restructuring following strategic review, this investment was disposed of in July 2013.

| | Total £000 |
|---|---|
| **Fair value** | |
| At 1 October 2011 | – |
| Additions | 909 |
| At 30 September 2012 | 909 |
| Disposals | (909) |
| **At 30 September 2013** | **–** |
| | |
| **Impairment losses** | |
| At 1 October 2011 | – |
| Charge for the year | – |
| At 30 September 2012 | – |
| Charge for the year | 184 |
| Disposals | (184) |
| **At 30 September 2013** | **–** |
| | |
| **Net book value** | |
| **At 30 September 2013** | **–** |
| At 30 September 2012 | 909 |
| At 30 September 2011 | – |

## 11 Trade and Other Receivables

| | **2013 £000** | 2012 £000 |
|---|---|---|
| Trade receivables | **2,822** | 2,915 |
| Other receivables | **711** | 662 |
| Prepayments | **1,251** | 1,121 |
| | **4,784** | 4,698 |

## 12 Cash

| | **2013 £000** | 2012 £000 |
|---|---|---|
| Cash in the Statement of Cash Flows | **6,626** | 5,496 |

Included in bank balances are amounts held pending the next interest payment due in October 2013. Until the interest payment has been deducted from these balances the cash is not available for use by the Group. At the year end the amount held on such account was £1,905,672 (2012: £2,319,327) with accruals for interest due of £1,493,409 (2012: £1,385,714).

## 13 Interest Bearing Loans and Borrowings

| | 2013 £000 | 2012 £000 |
|---|---|---|
| **Non-current liabilities** | | |
| Secured bank loans | **134,939** | 136,929 |
| Loan arrangement fees | **(576)** | (549) |
| | **134,363** | 136,380 |
| **Current liabilities** | | |
| Current portion of secured bank loans | **–** | – |

All bank borrowings are secured by fixed charges over certain of the Group's property assets and floating charges over the companies which own the assets charged.

Cash flow forecasts in respect of the loans have been prepared. In respect of the Barclays loan they did not differ significantly from the projections prepared before the restructuring, and this loan was not deemed to be an extinguishment. Bank and legal fees of £52,000 incurred in relation to this loan were added to the loan arrangements fees to be amortised over the remaining period of the loan. The secured bank loans above are net of £600,000 which is held in an escrow account. This escrow account is an interest-bearing account, for which the lender has sole signing rights, where all funds deposited shall be applied towards repayment of the loan on 16 January 2017.

The HSBC forecasts did differ significantly and the loan was considered to be extinguished and replaced by a new loan. Loan arrangement fees brought forward of £313,000 were written off to the income statement as non-recurring charges. New bank and legal fees of £429,000 in respect of this loan will be amortised over the period of this loan.

For more information about the Group's exposure to interest rate risk, see note 20.

## 14 Trade and Other Payables

| | 2013 £000 | 2012 £000 |
|---|---|---|
| Trade payables | **929** | 527 |
| Other taxation and social security | **444** | 522 |
| Other payables | **1,005** | 1,004 |
| Accruals and deferred income | **4,121** | 3,686 |
| | **6,499** | 5,739 |

Other payables include rent deposits held in respect of commercial tenants of £862,000 (2012: £834,000).

## 15 Leasing

**Obligations Under Finance leases**

Finance lease liabilities on head rents are payable as follows:

| | Minimum Lease Payment £000 | Interest £000 | Principal £000 |
|---|---|---|---|
| At 30 September 2011 | 6,919 | (5,997) | 922 |
| (Payments)/charge | (55) | 55 | – |
| At 30 September 2012 | 6,864 | (5,942) | 922 |
| (Payments)/charge | (55) | 55 | – |
| **At 30 September 2013** | **6,809** | **(5,887)** | **922** |

In the above table, interest represents the difference between the carrying amount and the contractual liability/cash flow.

All leases expire in more than five years.

# Notes to the Financial Statements

for the year ended 30 September 2013

## 16 Capital and Reserves

### Share Capital

| | 2013 Ordinary 20p Shares | | 2012 Ordinary 20p Shares | |
|---|---|---|---|---|
| | Number 000 | Amount £000 | Number 000 | Amount £000 |
| Allotted, called up and fully paid | 91,670 | 18,334 | 91,670 | 18,334 |

### Investment in Own Shares

At the year end, 9,164,017 shares were held in treasury (2012: 9,164,017).

The number of shares held by the Company's Employee Benefit Trust, LSR Trustee Limited at the year end was 1,096,545 (2012: 1,096,545). During the year the EBT transferred no shares (2012: Nil) to employees on the vesting of awards under the Long Term Incentive Plan. During the year the EBT transferred no shares (2012: 17,544) to employees on the exercise of awards under the Company's Share Option Scheme.

### Reserves

The value of shares issued to purchase Gilfin Property Holdings Limited in excess of their nominal value has been shown as a separate reserve in accordance with the Companies Act 2006.

### Capital Redemption Reserve

The capital redemption reserve arose in prior years on the cancellation of 8,822,920 Ordinary 20p Shares.

### Calculation of Net Asset Value Per Share (NAV)

| | 2013 £000 | 2012 £000 |
|---|---|---|
| Net assets | 33,626 | 41,325 |
| Fair value of derivative financial instruments (see note 19) | 6,289 | 9,042 |
| Adjusted net assets | 39,915 | 50,367 |

| | 2013 Number 000 | 2012 Number 000 |
|---|---|---|
| Allotted, called up and fully paid shares | 91,670 | 91,670 |
| Treasury shares | (9,164) | (9,164) |
| Number of shares | 82,506 | 82,506 |
| NAV per share | 41p | 50p |
| Adjusted NAV per share | 48p | 61p |

## 17 Dividends

The following dividends were paid during the current and previous years.

| Date paid | Dividend per share | Total payment £000 | Classification of dividend |
|---|---|---|---|
| 31 December 2012 | 2.0 pence | 1,628 | PID |
| 30 June 2012 | 2.0 pence | 1,628 | PID |
| 30 December 2011 | 2.1 pence | 1,709 | non–PID |
| 30 June 2011 | 1.9 pence | 1,546 | PID |
| 31 December 2010 | 1.9 pence | 1,546 | PID |
| 30 June 2010 | 1.7 pence | 1,384 | PID |

Under the REIT legislation, the Company's dividends are divided into two components, known as Property Income Distributions ("PID") and non-Property Income Distributions ("non-PID").

## 18 Earnings Per Share

### Basic Earnings Per Share

The calculation of basic earnings per share was based on the loss attributable to Ordinary Shareholders and a weighted average number of Ordinary Shares outstanding, calculated as follows:

### Loss Attributable to Ordinary Shares

| | 2013 £000 | 2012 £000 |
|---|---|---|
| Loss for the year | (6,071) | (9,178) |
| Profit for the year from discontinued operations | 345 | 294 |
| Loss on continuing operations for the year | (6,416) | (9,472) |

### Weighted Average Number of Ordinary Shares

| | 2013 Number 000 | 2012 Number 000 |
|---|---|---|
| Issued Ordinary Shares at 1 October 2012 | 91,670 | 91,670 |
| Shares held by EBT | (1,096) | (1,103) |
| Treasury shares | (9,164) | (9,164) |
| Weighted average number of Ordinary Shares at 30 September 2013 | 81,410 | 81,403 |

### Diluted Earnings Per Share

There is no difference between basic and diluted earnings per share in the prior year and no difference in the current year.

# Notes to the Financial Statements

for the year ended 30 September 2013

## 19 Derivative Financial Instruments

Derivative financial instruments held by the Group are interest rate swaps used to manage the Group's interest rate exposure. These are shown in the Balance Sheet as follows:

| | Fair Value 2011 £000 | Movements in Income Statement £000 | Fair Value 2012 £000 | Movements in Income Statement £000 | Fair Value 2013 £000 |
|---|---|---|---|---|---|
| Non-current liabilities | (7,264) | 669 | (6,595) | 2,723 | (3,872) |
| Current liabilities | (1,994) | (453) | (2,447) | 30 | (2,417) |
| Fair value | (9,258) | **216** | (9,042) | **2,753** | (6,289) |

At 30 September 2013 and 30 September 2012 these derivative financial instruments did not qualify as effective swaps for hedge accounting under the criteria set out in IAS 39.

A summary of the swaps and their maturity dates are as follows:

| Notional value of swap £000 | Effective date | Maturity date | Rate payable on fixed leg % | Fair value 2012 £000 | Movement in Income Statement £000 | Fair value 2013 £000 |
|---|---|---|---|---|---|---|
| 21,779 | 16 July 2007 | 31 January 2017 | 4.34 | (3,622) | 1,104 | (2,518) |
| 3,000 | 22 November 2006 | 30 April 2013 | 5.15 | (80) | 80 | – |
| 12,000 | 06 September 2006 | 30 April 2013 | 5.06 | (315) | 315 | – |
| 6,000 | 08 December 2006 | 30 April 2013 | 5.13 | (160) | 160 | – |
| 1,500 | 09 August 2006 | 30 April 2013 | 5.20 | (41) | 41 | – |
| 22,500 | 30 April 2013 | 20 July 2016 | 5.05 | (3,093) | 522 | (2,571) |
| 6,000 | 25 October 2006 | 30 April 2013 | 5.29 | (165) | 165 | – |
| 1,500 | 30 April 2010 | 30 April 2013 | 5.20 | (40) | 40 | – |
| 3,000 | 11 October 2006 | 30 April 2013 | 5.21 | (83) | 83 | – |
| 10,500 | 30 April 2013 | 29 July 2016 | 5.05 | (1,443) | 243 | (1,200) |
| | | | | (9,042) | 2,753 | (6,289) |

The interest rate receivable on each swap is LIBOR. The notional value of the £21,779,000 swap amortises at a rate of £200,000 per quarter.

The derivative financial instruments included in the above tables are stated at their fair value based on quotations from the Group's bank.

More details of the Group's policy regarding the management of interest rate risk are given in note 20.

## 20 Financial Instruments and Risk Management

The Board of directors has overall responsibility for the establishment and oversight of the Group's risk management framework. As described in the Corporate Governance report, this responsibility has been assigned to the executive directors with support and feedback from the Audit Committee. The Audit Committee oversees how management monitors compliance with the Group's risk management policies and procedures and reviews the adequacy of the risk management framework in relation to the risks faced by the Group.

The Group has identified exposure to the following financial risks from its use of financial instruments: capital management risk, market risk, credit risk and liquidity risk.

## 20 Financial Instruments and Risk Management continued

### Capital Management Risk

The Group's capital consists of long-term borrowings, cash and equity attributable to the shareholders. The Board's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain the future development of the business. The Board regularly reviews the Group's capital structure, cost of capital, gearing levels and other specific measures. From time to time, the Company purchases its own shares when the Board considers that this course of action would enhance the value of the Group for shareholders. The Group has had a policy of paying 100% of recurring profits as a dividend each year. Following the restructuring in July 2103 dividend policy will be reviewed half-yearly by the Board. There were no other changes in the Group's approach to capital management during the year.

### Market Risk

Market risk is the risk that changes in market conditions, such as interest rates, foreign exchange rates and equity prices, will affect the Group's profit or loss and cash flows. The Group's exposure to market risks is restricted to interest rate risk only. The Group borrows at fixed and floating rates of interest and uses financial instruments to fix the floating rates of interest in accordance with its policy.

The Group and its jointly controlled entities do not speculate in financial instruments. They are only used to limit their exposure to interest rate fluctuations. The Group's policy is to hedge between 60% and 100% of its interest rate exposure. At 30 September 2013, 92% (2012: 91%) of the Group's debt was fixed or protected, as shown below.

| | At 30 September 2013 | | | | At 30 September 2012 | | | |
|---|---|---|---|---|---|---|---|---|
| | Interest bearing loans £000 | Fixed rate loans £000 | Notional value of swaps £000 | Loans not protected by swaps £000 | Interest bearing loans £000 | Fixed rate loans £000 | Notional value of swaps £000 | Loans not protected by swaps £000 |
| Fixed rate loan* | 69,229 | 69,229 | – | – | 69,229 | 69,229 | – | – |
| Variable rate loan | 65,710 | – | 54,778 | 10,932 | 67,700 | – | 55,978 | 11,722 |
| | 134,939 | 69,229 | 54,778 | 10,932 | 136,929 | 69,229 | 55,978 | 11,722 |

* The fixed rate interest bearing loan is shown gross of £600,000 held in an escrow account at 30 September 2013 (2012: £nil). This escrow account is an interest-bearing account, for which the lender has sole signing rights, where all funds deposited shall be applied towards repayment of the loan on 16 January 2017.

The variable rate loan is protected by interest rate swaps which are carried at fair value. These have been identified as Level 2 in the fair value hierarchy. Level 2 is defined as inputs other than quoted prices included within Level 1 that are observable for the liability either directly (i.e. as prices) or indirectly (as derived from prices).

### Sensitivity Analysis

IFRS 7 requires an illustration of the impact on the Group's financial performance of changes in interest rates. The following sensitivity analysis has been prepared in accordance with the Group's existing accounting policies and considers the impact on the Income Statement and on equity of an increase of 100 basis points (1%) in interest rates. As interest rates were below 1% in the current and previous year, it has not been possible to consider the impact of a decrease of 100 basis points on interest income and expense as it would result in a negative rate of interest. Therefore, the impact of a fall in interest rates has been restricted to 0%. It has been possible to consider the impact of a 1% change in rates on the fair value of derivatives as the contracted rates are greater than 1%. All other variables remain the same and any consequential tax impact is excluded. The analysis assumes that changes in market interest rates affect the interest income and interest expense of derivative financial instruments. Changes in the fair value of derivative financial instruments have been estimated by discounting future cash flows at appropriate market rates prevailing at each year end.

# Notes to the Financial Statements

for the year ended 30 September 2013

## 20 Financial Instruments and Risk Management continued

Actual results in the future may differ materially from these assumptions and as such, these tables should not be considered as a projection of likely future gains and losses.

| | 2013 | | | | 2012 | | | |
|---|---|---|---|---|---|---|---|---|
| | Impact on income | | Impact on equity | | Impact on income | | Impact on equity | |
| | + £000 | - £000 | + £000 | - £000 | + £000 | - £000 | + £000 | - £000 |
| Impact on interest income and expense | 62 | 53 | 62 | 53 | 72 | 85 | 72 | 85 |
| Impact on fair value of derivatives | 1,692 | 1,699 | 1,692 | 1,699 | 2,129 | 1,500 | 2,129 | 1,500 |

## Credit Risk

Credit risk is the risk of financial loss to the Group if a tenant, bank or counterparty to a financial instrument fails to meet its contractual obligations and arises principally from the Group's receivables from tenants, cash and cash equivalents held by the Group's banks and derivative financial instruments entered into with the Group's banks.

### Trade and Other Receivables

The Group's exposure to credit risk is influenced mainly by the individual characteristics of each tenant. The Group has over 2,000 tenants in 640 properties. There is no significant concentration of credit risk due to the large number of small balances owed by a wide range of tenants who operate across all retail sectors. Geographically there is no concentration of credit risk in any one area of the UK. An analysis of the business by region, user type and tenant grade is given on page 3. The level of arrears is monitored monthly by the Group and more frequently on a tenant by tenant basis by the asset managers.

### Cash, Cash Equivalents and Derivative Financial Instruments

Three major UK banks provide the majority of the banking services used by the Group. Financial derivatives are only entered into with these core banks.

The Group's financial assets which are exposed to credit risk are classified as follows and are shown with their fair value:

**30 September 2013**

| | At fair value £000 | Available for sale £000 | At amortised cost £000 | Total carrying amount £000 | Fair value £000 |
|---|---|---|---|---|---|
| Investments in jointly controlled entities | – | – | 507 | 507 | 507 |
| Other Investments | – | – | – | – | – |
| Cash and cash equivalents | – | 6,626 | – | 6,626 | 6,626 |
| Trade receivables | – | – | 2,822 | 2,822 | 2,822 |
| Other receivables | – | – | 711 | 711 | 711 |
| | – | 6,626 | 4,040 | 10,666 | 10,666 |

**30 September 2012**

| | At fair value £000 | Available for sale £000 | At amortised cost £000 | Total carrying amount £000 | Fair value £000 |
|---|---|---|---|---|---|
| Investments in jointly controlled entities | – | – | 4,070 | 4,070 | 4,070 |
| Other Investments | – | 909 | – | 909 | 909 |
| Cash and cash equivalents | – | 5,496 | – | 5,496 | 5,496 |
| Trade receivables | – | – | 2,915 | 2,915 | 2,915 |
| Other receivables | – | – | 662 | 662 | 662 |
| | – | 6,405 | 7,647 | 14,052 | 14,052 |

## 20 Financial Instruments and Risk Management continued

For all classes of financial assets, the carrying amount is a reasonable approximation of fair value.

The ageing of trade receivables is as follows:

| | Total £000 | Impairment £000 | 2013 After Impairment £000 | Total £000 | Impairment £000 | 2012 After Impairment £000 |
|---|---|---|---|---|---|---|
| Not yet due | 782 | – | 782 | 811 | – | 811 |
| Past due by one to 30 days | 1,107 | (4) | 1,103 | 1,320 | (4) | 1,316 |
| Past due by 30–60 days | 166 | (11) | 155 | 214 | (8) | 206 |
| Past due by 60–90 days | 262 | (15) | 247 | 235 | (10) | 225 |
| Past due by 90 days | 769 | (234) | 535 | 877 | (520) | 357 |
| | 3,086 | (264) | 2,822 | 3,457 | (542) | 2,915 |

Trade receivables that are not impaired are expected to be recovered.

Other receivables at 30 September 2013 and 30 September 2012 were not past due.

The movement in the trade receivables' impairment allowance during the year was as follows:

| | 2013 £000 | 2012 £000 |
|---|---|---|
| Balance at beginning of year | 542 | 542 |
| Impairment loss recognised | 656 | 684 |
| Trade receivables written off | (934) | (684) |
| Balance at end of year | 264 | 542 |

The impairment loss recognised relates to the movement in the Group's assessment of the recoverability of outstanding trade receivables.

**Liquidity Risk**

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity risk is to ensure, as far as possible, that it will always have adequate resources to meet its liabilities when they fall due for both the operational needs of the business and to meet planned future investments. This position is formally reviewed on a quarterly basis or more frequently should events require it.

The Group's financial liabilities are classified and are shown with their fair value as follows:

**30 September 2013**

| | At Fair Value £000 | At Amortised Cost £000 | Total Carrying Amount £000 | Fair Value £000 |
|---|---|---|---|---|
| Interest bearing loans and liabilities | – | 134,363 | 134,363 | 143,356 |
| Finance lease liabilities | – | 922 | 922 | 922 |
| Derivative financial instruments | 6,289 | – | 6,289 | 6,289 |
| Trade payables | – | 929 | 929 | 929 |
| Other payables | – | 889 | 889 | 889 |
| Accruals | – | 1,863 | 1,863 | 1,863 |
| | 6,289 | 138,966 | 145,255 | 154,248 |

# Notes to the Financial Statements

for the year ended 30 September 2013

## 20 Financial Instruments and Risk Management continued

**30 September 2012**

| | At Fair Value £000 | At Amortised Cost £000 | Total Carrying Amount £000 | Fair Value £000 |
|---|---|---|---|---|
| Interest bearing loans and liabilities | – | 136,380 | 136,380 | 148,439 |
| Finance lease liabilities | – | 922 | 922 | 922 |
| Derivative financial instruments | 9,048 | – | 9,048 | 9,048 |
| Trade payables | – | 527 | 527 | 527 |
| Other payables | – | 862 | 862 | 862 |
| Accruals | – | 2,084 | 2,084 | 2,084 |
| | 9,048 | 140,775 | 149,823 | 161,882 |

For all classes of financial liabilities, other than the fixed rate loan, the carrying amount is a reasonable approximation of fair value.

The fair value of the fixed rate element of the interest bearing loan disclosed above has been valued by the Group's bankers.

The Group has undrawn committed borrowing facilities available at 30 September as follows:

| | 2013 £000 | 2012 £000 |
|---|---|---|
| Expiring in two to five years | | |
| Bank loans – revolving credit facility | – | 25,500 |
| | – | 25,500 |
| Expiring after more than five years | | |
| Bank loans – term loan facility | – | – |
| Bank loans – revolving credit facility | – | – |
| | – | – |

The maturity profiles of the Group's financial liabilities are as follows:

**30 September 2013**

| | Carrying Value £000 | Contractual Cash Flows £000 | Within One Year £000 | One to Two Years £000 | Two to Three Years £000 | Three to Four Years £000 | Four to Five Years £000 | Over Five Years £000 |
|---|---|---|---|---|---|---|---|---|
| Interest bearing loans and borrowings | 134,363 | 158,547 | 8,072 | 8,408 | 8,747 | 69,949 | 63,371 | – |
| Finance lease liabilities | 922 | 6,863 | 55 | 55 | 55 | 55 | 55 | 6,588 |
| Derivative financial instruments | 6,289 | 6,789 | 2,417 | 2,233 | 1,858 | 281 | – | – |
| Trade payables | 929 | 929 | 929 | – | – | – | – | – |
| Other payables | 889 | 889 | 889 | – | – | – | – | – |
| Accruals | 1,863 | 1,863 | 1,863 | – | – | – | – | – |
| | 145,255 | 175,880 | 14,225 | 10,696 | 10,660 | 70,285 | 63,426 | 6,588 |

## 20 Financial Instruments and Risk Management continued

**30 September 2012**

| | Carrying Value £000 | Contractual Cash Flows £000 | Within One Year £000 | One to Two Years £000 | Two to Three Years £000 | Three to Four Years £000 | Four to Five Years £000 | Over Five Years £000 |
|---|---|---|---|---|---|---|---|---|
| Interest bearing loans and borrowings | 136,380 | 165,332 | 7,431 | 7,431 | 7,431 | 73,640 | 69,399 | – |
| Finance lease liabilities | 922 | 6,863 | 55 | 55 | 55 | 55 | 55 | 6,588 |
| Derivative financial instruments | 9,048 | 9,048 | 2,447 | 2,392 | 2,246 | 1,818 | 145 | – |
| Trade payables | 527 | 527 | 527 | – | – | – | – | – |
| Other payables | 862 | 862 | 862 | – | – | – | – | – |
| Accruals | 2,084 | 2,084 | 2,084 | – | – | – | – | |
| | 149,823 | 184,716 | 13,406 | 9,878 | 9,732 | 75,513 | 69,599 | 6,588 |

Contractual cash flows include the undiscounted committed interest cash flows and, where the amount payable is not fixed, the amount disclosed is determined by reference to the conditions existing at the year end.

## 21 Operating Lease Arrangements

a) Leases as Lessee

Future minimum lease payments payable by the Group under non-cancellable operating leases are payable as follows:

| | Land and Buildings | |
|---|---|---|
| | **2013 £000** | 2012 £000 |
| The next year | **72** | 96 |
| Years two to five | **–** | 384 |
| Beyond five years | **–** | 24 |
| | **72** | 504 |

During the year ended 30 September 2013 £96,000 was recognised as an expense in the Income Statement in respect of operating leases (2012: £96,000). The lease on the company's previous office has been terminated with an effective termination date in June 2014.

b) Leases as Lessor

The investment properties are let under operating leases. Future minimum lease payments receivable by the Group under non-cancellable operating leases are receivable as follows:

| | **2013 £000** | 2012 £000 |
|---|---|---|
| Less than one year | **3,883** | 3,861 |
| Between one and five years | **5,505** | 5,602 |
| More than five years | **6,187** | 6,567 |
| | **15,575** | 16,030 |

# Notes to the Financial Statements

for the year ended 30 September 2013

## 22 Capital Commitments

At 30 September 2013 the Group had contracted capital expenditure for which no provision has been made in these financial statements of £28,000 (2012: £292,000).

At 30 September 2013, the jointly controlled entities had contracted capital expenditure for which no provision has been made in these financial statements of £Nil (2012: £64,000).

## 23 Related Parties

**Transactions with Key Management Personnel**

The only transactions with key management personnel relate to remuneration which is set out in the Remuneration Report.

The key management personnel of the Group for the purposes of related party disclosures under IAS 24 comprise all executive and non-executive directors.

Following the Company's Strategy Review Nick Gregory, Mike Riley and Victoria Whitehouse left the Company, in connection with which the Company made the payments in settlement of termination claims set out in the Remuneration Report.

Following their departure the Company sold its interest in Local Parade Investments LLP, the joint venture with Pramerica, to investors including Mr Gregory and Mr Riley. At that time asset management activities which the Group had undertaken for Local Parade Investments LLP, Local Retail Fund LP (the Company's former co-investment with Schroders) and the Company's continuing joint venture with a financial institution, together with a number of minor asset management instructions, transferred to a company in which Mr Gregory and Mr Riley were interested.

## 24 Group Entities

**Subsidiaries**

| | Country of Incorporation | Ownership Interest* 2013 | 2012 |
|---|---|---|---|
| NOS Limited | United Kingdom | 100% | 100% |
| NOS 2 Limited | United Kingdom | 100% | 100% |
| NOS 3 Limited | United Kingdom | 100% | 100% |
| NOS 4 Limited | United Kingdom | 100% | 100% |
| NOS 5 Limited | United Kingdom | 100% | 100% |
| NOS 6 Limited | United Kingdom | 100% | 100% |
| Palladium Investments Limited | United Kingdom | 100% | 100% |
| NOS 8 Limited | United Kingdom | 100% | 100% |
| Gilfin Property Holdings Limited | United Kingdom | 100% | 100% |
| LSR Asset Management Limited | United Kingdom | 100% | 100% |
| NOS Residential Limited | United Kingdom | 100% | 100% |
| LSR Asset Services Limited | United Kingdom | Nil% | 100% |
| LSR Investment Services Limited | United Kingdom | 100% | 100% |
| LSR Gresham Asset Advisers Limited | United Kingdom | 100% | 100% |
| LSR Gresham Investments Limited | United Kingdom | 100% | 100% |
| **Jointly controlled entities** | | | |
| Local Parade Investments LLP | United Kingdom | Nil% | 20% |
| Gracechurch Commercial Investments Limited | United Kingdom | 50% | 50% |

* All interests are in Ordinary Shares except for Local Parade Investments LLP where the investment is in partnership capital.

## 25 Discontinued operations

In July 2013 as part of the reconstruction following the strategic review, the company disposed of its interests in Local Parade Investments LLP and LSR Asset Services Limited. In addition it ceased its asset management activities being carried on by LSR Asset Management Limited and LSR Gresham Asset Advisors Limited.

The results of the discontinued operations, which have been included in the consolidated income statement, were as follows:

| | 2013 £000 | 2012 £000 |
|---|---|---|
| **Joint venture in Local Parade Investments LLP** | | |
| Share of revenue | 544 | 360 |
| Share of expenses | (357) | (556) |
| Share of profit/(loss) | 187 | (196) |
| **Asset management** | | |
| Revenue | 702 | 550 |
| Expenses | (44) | (60) |
| Profit | 658 | 490 |
| Profit before tax | 845 | 294 |
| Taxation | – | – |
| | 845 | 294 |
| Loss on disposal of discontinued operations | (500) | – |
| Net profit attributable to discontinued operations (attributable to equity holders of the company) | 345 | 294 |
| Basic and diluted earnings per share | 0.4p | 0.3p |

| | 2013 £000 | 2012 £000 |
|---|---|---|
| Cash flows from (used in) discontinued operation | | |
| Net cash from (used in) operating activities | 960 | (166) |
| Net cash used in investing activities | 364 | (2,454) |
| Net cash from financing activities | (1,239) | 2,664 |
| Net cash flows for the year | 85 | 44 |

| | 2013 £000 |
|---|---|
| **Effect of disposals on the financial position of the group** | |
| Investment in subsidiaries | 3,290 |
| Cash | 37 |
| Trade payables | (37) |
| **Net assets and liabilities** | 3,290 |
| Consideration received, satisfied in cash | 2,790 |
| Cash and cash equivalents disposed of | (37) |
| **Net cash inflow** | 2,753 |

# Notes to the Financial Statements

for the year ended 30 September 2013

## 26 Significant contracts

With effect from 22 July 2013 the Company entered into a management agreement with Internos Global Investors Limited("Internos"). Under this agreement the Company pays to Internos:

1. An annual management fee of 0.70% of the gross asset value of the portfolio, subject to a minimum fee of £1m in each of the first two years, £0.95m for the third year and £0.9m for the fourth year.

2. An annual performance fee of 20% of the recurring operating profits above a pre-agreed target recurring profit.

3. Fees for property sales as follows:

| | |
|---|---|
| Up to £50m | nil |
| £50m - £150m | 0.5% of sales |
| Over £150m | 1.5% of sales |

4. A terminal fee of 5.7% of cash returned to the Company's shareholders in excess of 36.1 pence per share per annum from the Effective Date outside of dividend payments (the "Terminal Fee Hurdle"). The Terminal Fee Hurdle rises by 8% per annum after the first year but reduces on a pro-rata daily basis each time equity is returned to shareholders outside of dividend payments from recurring operating profits.

Under the terms of the agreement Internos received a fee of £291,967 during the year. In addition Internos received a one off fee of £50,000 for work carried out in renegotiating the HSBC loan facilities.

# Company Balance Sheet

at at 30 September 13

| | Note | 2013 £000 | 2013 £000 | 2012 £000 | 2012 £000 |
|---|---|---|---|---|---|
| **Fixed assets** | | | | | |
| Property, plant and equipment | C5 | | – | | 126 |
| Investments | C6 | | 84,334 | | 130,327 |
| | | | 84,334 | | 130,453 |
| **Current assets** | | | | | |
| Debtors | C7 | 2,927 | | 7,936 | |
| Cash | | 1,764 | | 149 | |
| | | 4,691 | | 8,085 | |
| Creditors: Amounts falling due within one year | C8 | (49,284) | | (47,158) | |
| Net current liabilities | | | (44,593) | | (39,073) |
| Total assets less current liabilities | | | 39,741 | | 91,380 |
| Creditors: Amounts falling due after one year | | | – | | – |
| Net assets | | | 39,741 | | 91,380 |
| **Capital and reserves** | | | | | |
| Share capital | C9 | | 18,334 | | 18,334 |
| Reserves | C9 | | 3,742 | | 3,742 |
| Capital redemption reserve | C9 | | 1,764 | | 1,764 |
| Profit and loss account | C9 | | 15,901 | | 67,540 |
| Shareholders' funds | | | 39,741 | | 91,380 |

These financial statements were approved by the Board of directors on 3 January 2014 and were signed on its behalf by:

**Steven Faber**
Director

The registered number of the Company is 05304743.

# Notes to the Company's Financial Statements

for the year ended 30 September 2013

## C1 Accounting Policies

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the Company's financial statements.

### Basis of Preparation

The financial statements have been prepared in accordance with applicable UK Accounting Standards and under the historical cost accounting rules.

### Cash Flow Statement

Under FRS 1, the Company is exempt from the requirement to prepare a cash flow statement on the grounds that the Company is included in its own published consolidated financial statements.

### Related Party Transactions

The Company has taken advantage of the exemption in FRS 8 – Related Party Transactions and has not disclosed transactions or balances with entities which form part of the Group as these consolidated financial statements include the results of these entities.

### Financial Instruments

The Company has adopted the requirements of FRS 29 – Financial Instruments Disclosures and has taken the exemption under that standard from disclosure on the grounds that the Group financial statements contain disclosures in compliance with IFRS 7.

### Investments

Investments in subsidiary undertakings are stated at historic cost less provisions for impairment.

### Tangible Fixed Assets

All fixed assets are stated at historical cost less depreciation. Historical cost includes expenditure which is directly attributable to the acquisition of the asset.

Depreciation is charged to the profit and loss account on the following bases:

Fixtures and fittings – 15% reducing balance;
Computer equipment – straight-line basis over three years; and
Leasehold improvements – straight-line basis over the life of the lease.

Since the year end the company has agreed a termination of its lease of its former offices with an effective date in June 2014. None of the leasehold improvements will be realisable, and it is anticipated that the fixtures, fittings and computer equipment assets will generate negligible funds, if any. For this reason the assets have been fully depreciated in the year.

### Taxation

The charge for taxation is based on the result for the period and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes. Deferred tax is recognised, without discounting, in respect of all timing differences between the treatment of certain items for taxation and accounting purposes, which have arisen, but not reversed by the balance sheet date, except as otherwise required by FRS 19.

### Pensions

The Company operates a defined contribution pension plan. Contributions payable by the Company in respect of defined contribution pension plans are charged to administrative expenses as incurred.

### Share-Based Payments

There were no material share-based payment arrangements during the period.

### Employee Benefit Trust

The Company operates an Employee Benefit Trust in order to hedge its obligations under the CSOP and LTIP schemes. The Company either purchases own shares directly or it funds the trust to acquire shares in the Company. Transactions of the Employee Benefit Trust are treated as being those of the Company and are reflected in the Company's financial statements.

## C1 Accounting Policies continued

### Ordinary Share Capital

External costs directly attributable to the issue of new shares are shown in equity as a deduction from the proceeds.

Shares which have been repurchased are classified as treasury shares and shown in retained earnings. They are recognised at the trade date for the amount of consideration paid, together with directly attributable costs. This is presented as a deduction from total equity. Shares held by the Employee Benefit Trust are treated as being those of the Company.

The nominal value of shares cancelled has been taken to a capital redemption reserve.

### Loss for the Financial Year

The Company has taken advantage of Section 408 of the Companies Act 2006 and has not included its own profit and loss account in these financial statements. The Company's loss for the year was £50,011,000 (2012: £2,764,000).

## C2 Remuneration of Directors

The detailed information concerning directors' emoluments, shareholdings and share options is shown in the Remuneration Report.

All directors of the Company are directors of the Group.

## C3 Remuneration of Auditors

The detailed information concerning Auditors' remuneration is shown in note 3 to the Group financial statements.

## C4 Staff Numbers, Costs and Share Option Schemes

The detailed information concerning staff numbers, costs and share option schemes is shown in note 3 to the Group financial statements.

## C5 Tangible Fixed Assets

| | Leasehold Improvements £000 | Fixtures and Fittings £000 | Computer Equipment £000 | Total £000 |
|---|---|---|---|---|
| **Cost** | | | | |
| At 30 September 2012 | 167 | 41 | 72 | 280 |
| Additions | – | – | – | – |
| **Disposals** | | | (7) | (7) |
| **At 30 September 2013** | **167** | **41** | **65** | **273** |
| **Accumulated depreciation** | | | | |
| At 30 September 2012 | 76 | 22 | 56 | 154 |
| Charge for year | 91 | 19 | 13 | 123 |
| Disposals | | | (4) | (4) |
| **At 30 September 2013** | **167** | **41** | **65** | **273** |
| **Net book value** | | | | |
| **At 30 September 2013** | **–** | **–** | **–** | **–** |
| At 30 September 2012 | 91 | 19 | 16 | 126 |

Since the year end the company has agreed a termination of its lease of its former offices with an effective date in June 2014. None of the leasehold improvements will be realisable, and it is anticipated that the fixtures, fittings and computer equipment assets will generate negligible funds, if any. For this reason the assets have been fully depreciated in the year.

# Notes to the Company's Financial Statements

for the year ended 30 September 2013

## C6 Fixed Asset Investments

| | Shares in Group Undertakings £000 | Total £000 |
|---|---|---|
| **Cost** | | |
| At 30 September 2012 | 155,355 | 155,355 |
| Additions | – | – |
| **At 30 September 2013** | 155,355 | 155,355 |
| **Provisions** | | |
| At 30 September 2012 | 25,028 | 25,028 |
| Impairment charge for year | 45,993 | 45,993 |
| **At 30 September 2013** | 71,021 | 71,021 |
| **Net book value** | | |
| **At 30 September 2013** | 84,334 | 84,334 |
| At 30 September 2012 | 130,327 | 130,327 |

An impairment review of the carrying value of the Company's investments in its subsidiary undertakings has been performed. In carrying out this review, the directors had due regard to the nature of the property investments held, which is commensurate with the funding arrangements in place. On the basis of this review which included a review of the underlying assets of the individual subsidiaries the directors have written down the value of investments in subsidiary undertakings to their estimated realisable value.

The companies in which the Company's interests at the year end are more than 20% are as follows:

| Subsidiary undertaking | Nature of Business | Ownership Interest* |
|---|---|---|
| NOS Limited | Dormant | 100% |
| NOS 2 Limited | Property investment | 100% |
| NOS 3 Limited | Property investment | 100% |
| NOS 4 Limited | Property investment | 100% |
| NOS 5 Limited | Property investment | 100% |
| NOS 6 Limited | Property investment | 100% |
| Palladium Investments Limited | Property investment | 100% |
| NOS 8 Limited | Property investment | 100% |
| Gilfin Property Holdings Limited | Property investment | 100% |
| LSR Asset Management Limited | Property management | 100% |
| NOS Residential Limited | Property investment | 100% |
| LSR Investment Services Limited | Dormant | 100% |
| LSR Gresham Asset Advisers Limited | Property management | 100% |
| LSR Gresham Investments Limited | Property investment | 100% |

* All interests are in Ordinary Shares.

All of the above companies are incorporated in Great Britain.

## C7 Debtors

| | 2013 £000 | 2012 £000 |
|---|---|---|
| Amounts owed by Group undertakings | 2,722 | 7,820 |
| Other debtors | – | 14 |
| Other taxation and social security | 125 | – |
| Prepayments | 80 | 102 |
| | 2,927 | 7,936 |

## C8 Creditors

| | 2013 £000 | 2012 £000 |
|---|---|---|
| Trade creditors | 93 | 108 |
| Amounts owed to Group undertakings | 48,721 | 46,548 |
| Other taxation and social security | 130 | 36 |
| Accruals | 340 | 466 |
| | 49,284 | 47,158 |

## C9 Reconciliation of Shareholders' Funds

**Share Capital**

| | 2013 Ordinary 20p Shares | | 2012 Ordinary 20p Shares | |
|---|---|---|---|---|
| | Number 000 | Amount £000 | Number 000 | Amount £000 |
| Allotted, called up and fully paid | 91,670 | 18,334 | 91,670 | 18,334 |

**Reserves**

| | Reserves £000 | Capital Redemption Reserve £000 | Profit and Loss Account £000 | Total £000 |
|---|---|---|---|---|
| At 1 October 2011 | 3,742 | 1,764 | 73,634 | 79,140 |
| Dividend | – | – | (3,337) | (3,337) |
| Share-based payments | – | – | 7 | 7 |
| Loss for the financial year | – | – | (2,764) | (2,764) |
| At 30 September 2012 | 3,742 | 1,764 | 67,540 | 73,046 |
| Dividend | – | – | (1,628) | (1,628) |
| Loss for the financial year | – | – | (50,011) | (50,011) |
| **At 30 September 2013** | **3,742** | **1,764** | **15,901** | **21,407** |

**Investment in Own Shares**

At 30 September 2013, 9,164,017 shares were held in treasury (2012: 9,164,017).

**Reserves**

The value of shares issued to purchase Gilfin Property Holdings Limited in excess of their nominal value has been shown as a separate reserve in accordance with the Companies Act 2006.

**Capital Redemption Reserve**

The capital redemption reserve arose in prior years on the cancellation of 8,822,920 Ordinary 20p Shares.

# Notes to the Company's Financial Statements

for the year ended 30 September 2013

## C9 Reconciliation of Shareholders' Funds continued

### Dividends

The following dividends were paid during the current and previous years.

| Date paid | Dividend per share | Total payment £000 | Classification of dividend |
|---|---|---|---|
| 31 December 2012 | 2.0 pence | 1,628 | PID |
| 30 June 2012 | 2.0 pence | 1,628 | PID |
| 30 December 2011 | 2.1 pence | 1,709 | non–PID |
| 30 June 2011 | 1.9 pence | 1,546 | PID |

Under the REIT legislation, the Company's dividends are divided into two components, known as Property Income Distributions ("PID") and non-Property Income Distributions ("non-PID").

# Glossary

## Adjusted Net Asset Value ("Adjusted NAV") per share

Adjusted NAV is calculated as shareholders' funds, adjusted by the fair value of the derivative financial instruments held on the Balance Sheet, divided by the number of shares in issue at the year end, excluding treasury shares.

## Earnings Per Share ("EPS")

EPS is calculated as profit attributable to shareholders divided by the weighted average number of shares in issue in the year.

## Equivalent Yield

Equivalent yield is a weighted average of the initial yield and reversionary yield and represents the return a property will produce based upon the timing of the income received. In accordance with usual practice, the equivalent yields (as determined by the Group's external valuers) assume rent received annually in arrears and on gross values including prospective purchasers' costs (including stamp duty, and agents' and legal fees).

## Funds From Operations ("FFO")

FFO is a term adopted by the National Association of Real Estate Investment Trusts. It is calculated as net income adjusted for depreciation of investment properties and gains/losses on sales of investment properties.

## Head Lease

A head lease is a lease under which the Group holds an investment property.

## Initial Yield

Initial yield is the annualised net rent generated by a property expressed as a percentage of the property valuation. In accordance with usual practice the property value is grossed up to include prospective purchasers' costs.

## Interest Cover

Interest cover can be calculated in a number of ways. The Group interest cover given in the Finance Review is based on the percentage of times gross rental income covers financing expenses.

## Actual and Forecast Interest Cover Test (ICR)

The ICRs given in the Finance Review are calculated in different ways by each bank, as defined in the loan facility agreements. Each bank has a charge on a specific pool of property their loan relates to and the ICRs are calculated based on the gross rental income, less an adjustment for unrecoverable costs compared to the interest charged on that loan for that particular pool of assets.

## Interest Rate Swap

An interest rate swap is a financial instrument where two parties agree to exchange an interest rate obligation for a predetermined amount of time. These are used by the Group to convert floating rate debt to fixed rates.

## Investment Property Databank Ltd ("IPD")

IPD produces an independent benchmark of property returns.

## Initial Public Offering ("IPO")

An IPO is the first sale of shares by a privately owned company on a Stock Exchange. LSR issued its shares for sale on 2 May 2007.

## London Interbank Offered Rate ("LIBOR")

LIBOR is the interest rate charged by one bank to another bank for lending money.

## Loan-to-value ("LTV")

Loan-to-value is the ratio of debt, excluding any mark-to-market adjustments, to the value of investment properties.

## Market Value

Market value is the estimated amount for which a property should exchange on the date of valuation between a willing buyer and willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion.

## Market Rent

Market rent is the estimated amount for which a property should lease on the date of valuation between a willing lessor and a willing lessee on appropriate lease terms, in an arm's length transaction, after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion.

## Net Asset Value ("NAV") per share

NAV per share is calculated as shareholders' funds divided by the number of shares in issue at the year end excluding treasury shares.

## Real Estate Investment Trust ("REIT")

A REIT is a listed property company which qualifies for and has elected into a tax regime, which exempts qualifying UK property rental income and gains on investment property disposals from corporation tax. LSR converted to REIT status on 11 May 2007.

## Recurring Profit

Recurring profit is calculated by adjusting the statutory IFRS reported result for: the movement in the fair value of the property portfolio; the movement in the fair value of financial derivatives held; any profit or loss realised on the sale of properties or other fixed assets; and other one-off, non-recurring income or costs incurred which are not considered to be sustainable or of a recurring nature.

## Rent Roll

Rent roll is the total contractual annualised rent receivable from the portfolio net of any head rent payments.

## Reversionary Yield

Reversionary yield is the annualised net rent that would be generated by a property if it were fully let at market rent expressed as a percentage of the property valuation. In accordance with usual practice the property value is grossed up to include prospective purchasers' costs.

# Shareholder Information

## Registered Office

**The Local Shopping REIT plc**
**INTERNOS GLOBAL INVESTORS**
65 Grosvenor Street
London, W1K 3JH

Telephone: +44 (0)20 7355 8800
Registration number: 05304743
Website: www.localshoppingreit.co.uk

## Directors

Stephen East
Steven Faber
Nicholas Vetch
Grahame Whateley

## Company Secretary

William Heaney

## Finance Advisers

**JP Morgan Cazenove**
25 Bank Street
London, E14 5JP

## Solicitors

**Eversheds LLP**
One Wood Street
London, EC2V 7WS

**Olswang LLP**
90 High Holborn
London, WC1V 6XX

**DWF Biggart Baillie LLP**
No. 2 Lochrin Square
96 Fountainbridge
Edinburgh, EH3 9QA

## Auditors

**KPMG Audit Plc**
One Snowhill
Snow Hill Queensway
Birmingham, B4 6GH

## Valuers

**Allsop LLP**
33 Wigmore Street
London, W1U 1BZ

## Registrar

**Equiniti Limited**
Aspect House
Spencer Road
Lancing, BN99 6QQ

## Principal Bankers

**Barclays Bank PLC**
5 The North Colonnade
Canary Wharf
London, E14 4BB

**HSBC Bank plc**
8 Canada Square
London, E14 5HQ

**The Royal Bank of Scotland plc**
Level 8
280 Bishopsgate
London, EC2M 4RB

Key dates and other important information are available on our website: www.localshoppingreit.co.uk

Created by
Jonesandpalmer
www.jonesandpalmer.co.uk
empowering corporate communications

**The Local Shopping REIT plc**
65 Grosvenor Street
London
W1K 3JH

Telephone: +44 (0)20 7355 8800
Registration number: 05304743
Website: www.localshoppingreit.co.uk