Annual Report 2018

**Defenx PLC**

## Strategic report



## Governance



## Financial statements



## Other information

# Chairman's statement

Whilst 2018 was a challenging year for the Company and one of great change, we have emerged more appropriately positioned for the future. Given that Defenx is an IT company, perhaps the best way to describe 2018 was as a 'reboot' year.

**Strategic partnership with BV Tech**

Our relationship with BV Tech continues to develop, with them as both a supportive, and now majority, shareholder and as our key strategic partner.

The €950,000 loan announced in October 2018 was subsequently switched into a convertible loan. That amount was drawn (and converted into shares) in three stages in October 2018 and in January and March 2019. As a consequence, BV Tech now owns 67.1% of Defenx.

In April 2019, we signed a sales and distribution agreement with BV Tech with two main elements. The first gives them sole rights to sell our products to certain organisations within the Italian defence, space, national security and critical infrastructures sectors until December 2023. In return, Defenx has received €1.0 million and going forward will receive 50% of any sales in excess of €5.0 million across that period. The second made BV Tech a (non-exclusive) distributor of our products through to the end of 2021, and they have committed to purchase products to a minimum value of €150,000 per quarter (total €1.2 million) in the period to December 2020. In addition, we entered into a software services agreement with BV Tech which defines our product development roadmap with a cap of €1.2 million for 2019 development spend with BV Tech.

**Product Development**

As has been reported previously, we terminated our relationship with our product developers in Romania in Q1 2018; moving that responsibility to BV Tech. In April 2019 we cemented further that relationship with a software services agreement with BV Tech until at least December 2020, working to an agreed product route-map.

Our next generation data security products for personal computers and mobile devices provide three pillars of protection, securing devices, data and messaging. We are particularly excited by some of the innovations in the new product portfolio.

The English language version of our Security Suite (antivirus for Windows devices) was released in January 2019, followed by the Italian language version in June 2019 and further languages are expected to follow. Next generation versions for mobile are expected to be available shortly, with the Mobile Parental Control modules for Apple and Android having already been released in February and April 2019 respectively. Secure Mail is currently in final testing for imminent release with Mobile Communications expected shortly thereafter. Finally, we are upgrading the infrastructure for Cloud backup; migration is scheduled for completion in Q4 2019. We will work with BV Tech to develop our secure messaging for delivery in 2020.

**Management**

A significant element of the reboot has been in the changed composition of the Board and senior management. In April 2018, the Company's founder Andrea Stecconi resigned from the Board, followed by Alessandro Poerio a month later. Andrea has continued with the Group in a customer relations role, whereas Alessandro left to pursue other interests. As a consequence of those departures, I became interim Executive Chairman on 1 June 2018.

In July 2018, both Chief Financial Officer Philipp Prince and Non-executive Director Leonard Seelig also resigned, whilst Raffaele Boccardo, the President of BV Tech, assumed the additional role of interim Deputy

Executive Chairman. Philipp was replaced by Clive Eplett as interim-CFO, but given the interim nature of his appointment, he did not join the Board.

In August 2018, Nic Hellyer and Giorgio Beretta were appointed as Non-executive Directors, and chairs of the remuneration and audit committees respectively.

Our search for the right person to become CEO continues, with our preference being to make that appointment first, then recruit a permanent CFO to work alongside the new CEO.

**Current trading, outlook and funding**

As expected, and inevitably in the circumstances, 2018 revenues were again lower than past years, whilst we prepared our next generation products for launch readiness.

Offsetting that, we have reduced costs wherever possible. In particular, we eradicated marketing contributions to distributors that, in practice, were not generating a worthwhile return on spend. Headcount costs have also been reduced, both during the year and subsequently. Other operating costs have also been cut where possible without jeopardising the Group's future.

Our biggest charge to the profit and loss account was a further €1.9 million amortisation against development intangible assets. This non-cash charge represents 95% of cost of sales and 32% of all costs (excluding interest).

The consequence of these changes is a reduction in the operating loss to €3.5 million from €11.9 million in 2017.

The first quarter of 2019 continued in very similar vein to 2018, but the second quarter benefited from the sales agreements with BV Tech reported above. Marketing of our next generation products is expected to commence in during the second half of 2019, restarting the business after our 'reboot'.

As at 24 July 2019, the Group had cash resources of approximately €120,000, which is sufficient through to the end of August 2019, and, therefore, the Company remains reliant on the continued financial support of its major shareholder, BV Tech, going forward.

After a difficult period, we therefore look forward to the future with renewed optimism, with the release of our next generation products supporting our three pillars strategy and a further strengthened relationship with our largest shareholder, BV Tech.

**Anthony Reeves**

Interim Executive Chairman
26 July 2019

# Products and technology

Defenx is a cyber security company that offers a range of products for the mobile, PC and network security markets.

## Broad product portfolio

The Defenx proposition is to solve our end-user's data security needs on all their connected devices.

Our new generation products provide consumers, corporates and public-sector organisations with three pillars of data security on personal computers and mobile devices, securing devices, data and messaging.

Our current portfolio comprises the following products:

| Product | Key features |
|---|---|
| **Defenx Mobile Security Suite** | Defenx Mobile Security Suite includes antivirus, anti-phishing, webcam protection, microphone anti-capture, and anti-theft protection as well as SIM protection and safe browsing. The next generation product in this regard should be available shortly.<br>Available in 12 languages for Android and iOS. |
| **Defenx PC Antivirus & Security Suite** | Defenx Security Suite includes antivirus, anti-spam, firewall, identity protection, safe browsing, privacy and parental controls.<br>Available in five languages for Windows 10, 8, 7, Vista and XP desktop and laptop PCs. There is also a network version. |
| **Defenx Parental Control** | Defenx Parental Control protects under-age smartphone and tablet users from inappropriate content and enables parents to manage their children's online activity.<br>Parents can view call and messaging history, photos and be alerted when their child arrives or leaves specific locations. The app also includes some Defenx SOS features.<br>Available for Android and iOS (the latter in beta version). |
| **Defenx Privacy Advisor** | Defenx Privacy Advisor is a free app that allows users to monitor access to their personal data by installed apps.<br>A growing number of seemingly useful apps for smartphones can, in fact, invade your privacy, putting your personal information at risk.<br>Available for free on Android. |
| **Defenx SOS Help Me** | Defenx SOS keeps loved ones safe by alerting a designated parent or guardian by email, SMS or via a call centre in an emergency such as an unexpected fall or attack.<br>The panic function, triggered by a Bluetooth- connected button or simply by dropping the smartphone, triggers the alert.<br>Available in two languages for Android. |
| **Defenx Cloud Backup** | Defenx Cloud Backup (Memopal) protects files by securely saving a copy to the cloud. Because it keeps all file changes forever, users always have a clean version to restore, for example, following a ransomware attack. It also provides a sync folder allowing the latest version of saved files to be accessed from any computer, device and online.<br>Available in 16 languages for Windows, Apple, Linux, Android, iOS and one NAS platform. |
| **Defenx Secure Messaging (ECS/ECM)** | Defenx ECS/ECM, built on the software acquired from BV Tech, employs standard protocols, encryption algorithms and open-source software components to provide secure telephone conversations and encrypted messages and attachments.<br>Scheduled to be available in three languages for Android, iOS and Blackberry smartphones in 2020. |

# Our market and opportunity

## Global and regional drivers

Our target markets are extensive, comprising consumer, corporate and public-sector users of digital devices. Our opportunity lies in the increasing number of connected devices, the volume and sophistication of cyber-attacks and the growth in users' willingness to use online services and regulation.

*More connected devices*

- According to the GSMA[1], at the end of 2018, two-thirds of the world's population had a mobile subscription – a total of 5.1 billion unique subscribers. By 2025, GSMA forecast this to rise to nearly 5.8 billion. Smartphone penetration also continues to grow with an estimated 3.1 billion mobile internet users in 2018 increasing to 4.0 billion by 2025.
- It is not just mobile devices, but the internet of things ("IoT") too. GSMA forecasts that the IoT market will grow from an installed base of 9.1 billion devices[2] in 2018 to 25.2 billion devices by 2025, the implications of which are only just beginning to be felt.

*Industrialisation of cyber-crime*

Computer fraud is becoming industrialised.

- Some concentrate on developing new methods of attack and seeking to stay ahead of the legitimate software industry and cyber-security providers, who then franchise their methodologies to operators who can use them in a variety of ways.
- Those franchisees then operate the bought-in technologies and exploit them for criminal gain.

*More attacks and data breaches*

- Form-jacking became the new 'get-rich-quick' scheme for cyber-criminals[3], with a monthly average of 4,800 websites being compromise and consumer credit card details harvested.
- Ransomware continues to plague businesses and consumers, though lower returns to criminals resulted in lower activity.
- Android remains the key target for hackers because so many devices are not regularly updated to the latest software. Android's dominant market share makes it our key focus.
- Adoption of IoT technology continues with many devices having poor security; once connected to home or corporate networks, they offer an easy way in for hackers.
- Following the plunge in Bitcoin values, Symantec identified a decline in 'coin mining' in 2018, although it remained popular due to low barriers to entry and minimal overhead for the attacker.

*More data/online digital services*

- Migration to smartphones that operate on highspeed mobile networks, coupled with increasing consumer propensity to engage in the digital world, is driving mobile data traffic up in all regions. According to Ericsson[3], global mobile data traffic for all devices will increase eight-fold between 2017 and 2023, reaching 110 exabytes per month. Smartphones will account for close to 95% of total mobile data traffic by 2023.

*More regulation*

- Regulatory compliance has been stimulating spending on security, notably in Europe with the GDPR that came into effect 25 May 2018.
- The Facebook-Cambridge Analytica scandal is just one example where data privacy concerns may well see further regulation likely to affect security costs on corporates and public sector organisations.

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1 GSMA The Mobile Economy 2019
2 IoT connections include cellular and non-cellular connections. The term IoT connections refers to devices capable of two-way data transmission (excluding passive sensors and RFID tags). It includes connections using multiple communication methods such as cellular, short-range and others. Excludes PCs, desktops, tablets, laptops, e-readers and smartphones.
3 Symantec Internet Security Report 2019, volume 24
3 Ericsson Mobility Report, November 2017

# Financial review

2018 was a challenging year for Defenx and, as a consequence, the financial key performance indicators shifted from operational measures to cash management and funding. With new sales effectively stalling, it became imperative to control costs and ensure cash was and continues to be sufficient to bridge the business until sales revenue from our next generation of products can provide positive cashflow for the Group.

**Revenue**

Reported revenue in the year was €1.42 million (2017:€2.93 million), of which 59% (€0.84 million) of this comes from the release of previously deferred income. Further, new invoicing in the second half of 2018 was only €0.31 million.

Sales via distributors were suspended during 2018 when it became clear that, after accounting for our marketing cost contributions to distributors and difficulties in cash collection, this channel was not proving profitable.

**Gross margin**

On those new sales that were made in 2018, there were no significant marginal (additional) costs on each sale. Therefore, cost of sales comprises primarily fixed costs of hosting (for the Defenx backup products), interim updates of security suite products and amortisation of the development costs. Hence, as a KPI, gross margin becomes a largely academic measure for the year.

**Operating costs**

The Board has focused more therefore on reducing overheads wherever possible. Headcount, excluding the Board, has been reduced significantly, to 6 at the year-end compared to an average of 15 in 2017. Discretionary costs have been minimised wherever possible, though the AIM quote makes a certain level of cost unavoidable, €289,000 (2017:€234,000).

There were no performance-related bonuses during this or the preceding year.

**Impairments**

We took the precaution to write down a further €1.35 million (being 100% of the unimpaired balance) against debtors in dispute, where collection against a legal settlement agreement is proving more troublesome than anticipated.

Having reviewed the development cost intangible asset, we determined that, after the year's amortisation charge of €1.9 million, no further impairment provision was warranted.

During the year, the Company converted €2.9 million of intercompany debt owed by Defenx Italia SRL into shares, recapitalising that business to make good historical losses. That amount was immediately impaired in full in the books of the Company.

**Operating loss**

The pre-tax Group loss for the year consequently was only 32% of that reported in 2017, at €3.8 million (2017: €11.8 million)

**Taxation**

There is no current tax charge in the year and a small release of deferred taxation arising for the treatment of interest on the convertible bond. Deferred tax assets have not been recognised on temporary timing differences or accumulated losses as it is not sufficiently certain that the Group will be able to utilise them in the near future.

**Net loss and loss per share**

The loss after tax attributable to ordinary shareholders of Defenx was €3.73 million (2017: €11.64 million). This equates to a loss per share of €0.154 (2017: €1.030) undiluted and €0.150 (2017: €0.796) diluted.

In light of the Group's loss for the year and substantial profit and loss reserves deficit, the Board cannot propose a dividend. Future dividend policy will be kept under review.

**Cash flow**

Non-cash charges to the profit and loss account resulted in the net cash outflow for the year being €1.4 million, funded by €1.4 million net proceeds of share issues. The Group also repaid €0.46 million of debt in the year, resulting in a reduction in cash holdings of €0.8 million.

Since the year-end, the Company has drawn down on the remaining €0.7 million of the convertible loan from BV Tech, which was subsequently converted in full into new ordinary shares in the Company, as well as receiving €1.0 million from the sales agreement entered into BV Tech entered into in April 2019. Following payments to BV Tech under the services agreement entered into as the same time and the payment of historic liabilities, the Group had cash of approximately €120,000 as at 24 July 2019.

**Intangible assets**

During the year, the company spent €0.9 million on its software codebase, of which €0.5 million was capitalised, with the remainder being treated as of a maintenance nature, so charged to cost of sales. The development cost intangible asset of €3.5 million will be written off over three years.

**Financing**

In October 2018 the Company entered into a €0.95 million convertible, unsecured loan arrangement with BV Tech. The loan was drawn in three instalments, in October 2018 and January and March 2019, with the cash being used for general corporate purposes. In each case, the loan was converted to new ordinary shares in the Company immediately following drawdown, at the price agreed at the outset, being £0.08 per share.

There were no other new borrowings in the year across the Group.

Gross debt at the year-end was €1.79 million (2017: €2.20 million) and net debt was €1.69 million (2017: €1.24 million). This equates to a debt-equity ratio of 107.8% (2017: 30.9%) compared to the Board's target of 25%. The substantial change reflects the significant reduction in net assets caused by the posted losses, which exceeded the reduction in the cash value of the Company's debt.

**Going concern**

As noted above, at 24 July 2019, the Group had cash resources of approximately €120,000, which is sufficient through to the end of August 2019, and, therefore, the Company remains reliant on the continued financial support of its major shareholder, BV Tech, going forward.

The sales and distribution agreements signed with BV Tech in April 2019 also provide a baseline cash revenue stream for 2019 and 2020. Those and any other sales in Italy bring an additional cash benefit; rather than having to pay over Italian output VAT to the exchequer, it can be offset against the R&D tax credit claimed in 2017, boosting the Group cash flow by a further 22% (the current VAT rate in Italy).

On the basis of the above, with the general release of next generation Defenx products and the continuing support of BV Tech, satisfy the Board that Defenx remains a going concern.

# Principal risks and uncertainties

The Board is responsible for developing a comprehensive risk framework and a system of internal controls.

| Principal risk | Mitigation |
|---|---|
| **Technology**<br>The industry in which Defenx operates is in the process of continual change, reflecting technical developments as industry and government standards and practices change and emerge.<br>The markets in which Defenx operates are competitive and rapidly evolving. The Group's next generation of products may become less competitive or even obsolete as competitors introduce new products and customer behaviour changes. | New products and features are assessed against their target markets and in response to customer feedback prior to development.<br>Defenx works with expert development support from BV Tech, which has a track record of assessing and integrating software to meet customer demand. |
| **Building sales**<br>The Group's historical B2B2C sales model proved to involve greater sales and cash collection risk than was anticipated at the time.<br>In future, the Group will seek to achieve a sales mix of Software-as-a-Service (SaaS) and direct corporate and public sector sales. There is a risk this alternative route to market proves difficult to implement. | Under our new marketing approach, reliance on this channel is likely to be reduced dramatically, with more stringent credit control on any remainder.<br>BV Tech's sales and marketing resources and existing trading relationships enable access that would otherwise be difficult for the Group to obtain. The distribution agreements signed with BV Tech have provided an immediate and substantial sales boost. |
| **Competition**<br>The markets in which Defenx operates are competitive and rapidly evolving. The Group will continue to need to invest in its next generation of products to ensure they compete with market alternatives .<br>Many of the Group's competitors have greater scale with significant financial, technical, sales and marketing resource and may therefore be better able to generate sales. | Defenx's next generation of products will be optimised for mobile devices, the fastest growing product and highest volume category.<br>The relationship with BV Tech effectively provides resource scale and access to markets that Defenx does not itself have. |
| **Recruitment and retention of staff and contractors**<br>The success of Defenx depends upon high-quality staff and contractors with the relevant expertise and experience to broaden and sell the Group's products and solutions. Failure to attract and retain high calibre skills into key roles will adversely affect the Group's performance and profitability. | The Board, including the new Non-executive Directors, are highly experienced. The recruitment process, particularly the recruitment of a CEO and a permanent CFO, remains a key area of Board focus.<br>The agreements signed with BV Tech both secures continuity regarding product development and provides access to sales channels not otherwise available to the Group. |

| Principal risk | Mitigation |
| --- | --- |
| **Working capital and funding**<br><br>Even with the latest sales agreements with BV Tech, the Company only has sufficient funds through to the end of August 2019 and is reliant on the continued financial support of BV Tech.<br><br>If building new third party sales takes longer than anticipated, further funding may also be needed. | Costs and cash resources are being managed closely.<br><br>Continuing to work closely with BV Tech to develop the Group's products and sales pipeline. |
| **Cyber security and data protection**<br><br>As a provider of security solutions, Defenx may become a high-profile target and the Group's networks and products may have vulnerabilities that have from time to time been, and may in future be, targeted by attacks designed to disrupt the Group's business and harm its reputation.<br><br>As a custodian of end-user data, the Group is exposed to data loss and breaches of data protection regulations in the markets in which it operates.<br><br>Such attacks and/or data loss could adversely affect the Group's reputation, performance and operations. | The Group and BV Tech's development team actively monitor Defenx's cyber exposure and its preparedness against a range of types of threat.<br><br>The Group's IT team:<br>• monitors suspicious activities;<br>• investigates and reports on any actual or suspected incidents; and<br>• regularly implements improvements in the Group's security infrastructure.<br><br>Staff are trained to mitigate cyber risks by adopting appropriate best-practice. |
| **Operations overseas**<br><br>A significant proportion of Defenx's revenues has historically and is expected to continue to be generated outside the UK, where the Brexit process remain unresolved. The Group may be adversely affected by changes in local and regional economic, political and social conditions such as changes in law and regulation, taxation, currency restrictions.<br><br>In addition, fluctuating exchange rates and the costs of conversion and exchange controls may have an unfavourable impact on profitability, particularly if reported in Sterling. | The Group has operating subsidiaries in the UK, Italy and Switzerland, providing operating options within and outside the EU.<br><br>Selling into different national markets mitigates the risk of adverse changes in one.<br><br>The Group incurs the majority of its costs, generates most of its revenues and prepares its financial reports in Euros. This natural hedging reduces the impact of fluctuations in foreign currencies. |

# Board of Directors

**Anthony (Tony) Reeves**

Interim Executive Chairman

Appointed to the Board: 1 October 2015

Committee Membership: None

Tony has over 45 years' experience in the recruitment sector and was the executive chairman of Kellan Group plc, the AIM quoted recruitment business. Prior to this, he was chairman and chief executive officer of the Hotgroup plc from 2001 until its acquisition by Trinity Mirror Group plc in 2005. In 1986 Tony formed Lifetime Corporation, an overseas recruitment agency operating primarily in the Middle East, which was reversed into a business listed on the American Stock Exchange and sold to Olsten for US$660 million with US$1 billion sales. He is also a private investor in various early stage companies and vice president of Chelsea Football Club.

**Raffaele Boccardo**

Interim Executive Deputy Chairman

Appointed to the Board: 7 August 2017

Committee Membership: None

Raffaele graduated from the Faculty of Electronic Engineering of the University of Genoa, has a Master's in Management and International Studies from Enrico Mattei School of Milan and a Phd in Electronic Engineering, also from the University of Genoa. In the past 25 years he has been participating with leading major national and international ICT technology and innovation projects, working at the side of leading players like Finmeccanica, Olivetti, Telecom Italia. Raffaele is President and founder of BV Tech Group, one of the main players in the Italian ICT market. He is currently working with main national and international Institutions and Corporations for the continuous improvement of Cyber Security in Critical Infrastructures in the picture of existing and continuously developing International, European and National Legislations.

**Giorgio Beretta**

Non-executive Director

Appointed to the Board: 1 August 2018

Committee Membership: Audit (chairman), Remuneration

**Giorgio** is a qualified accountant with over 30 years' experience as Auditor where he has been involved in the assistance of various important private and public companies and, since 2007, has joined the Corporate Finance department as partner at BDO Italia SpA. He has a breadth of listed company and advisory experience, having advised on numerous IPOs, M&A transactions and fund raisings, as well as sitting as Chairman of VR Way SA, the first AIM Milan listed company.

**Nicholos (Nic) Hellyer**

Non-executive Director

Appointed to the Board: 1 August 2018

Committee Membership: Audit, Remuneration (Chairman)

Nic is a Fellow of the Institute of Chartered Accountants in England and Wales and has significant experience with Official List and AIM companies, both as an adviser and from current board positions. He has extensive contacts in the City and wide experience of dealing with shareholders, both private and institutional. In addition, he has considerable experience of M&A, again both from an advisory and corporate board perspective.

He is currently Finance Director of AIM quoted Pelatro Plc, a global precision marketing software specialist as well as Byotrol Plc, a consumer products company.

As set out in the Directors' report on page 26, Philipp Prince, Chief Financial Officer, and Leonard Seelig, Non-executive Director, resigned from the Board on 11 July 2018.

# Chairman's statement on governance

### Dear shareholder

As Chairman of the Board of Directors of Defenx Plc (Defenx, or the Company/Group as the context requires), it is my responsibility to ensure that Defenx has both sound corporate governance and an effective Board. As Chairman of the Company, my responsibilities include leading the Board effectively, overseeing the Company's corporate governance model, communicating with shareholders, and ensuring that good information flows freely between the Executive and Non-executives Directors in a timely manner. My leadership of the Board is undertaken in a manner which ensures that the Board retains integrity and effectiveness and includes creating the right Board dynamic and ensuring that all important matters, in particular strategic decisions, receive adequate time and attention at Board meetings.

It is the Board's job to ensure that Defenx is managed for the long-term benefit of all shareholders, with effective and efficient decision-making. Corporate governance is an important part of that role, reducing risk and adding value to our business.

The Directors recognise the value of good corporate governance in every part of its business. As Defenx is an AIM quoted company, it is required to adopt a recognised corporate governance code and disclose how it complies with that code and, to the extent Defenx departs from the corporate governance provisions outlined by that code, it must explain its reasons for doing so. The Directors have adopted the requirements of the Quoted Companies Alliance's Corporate Governance Code for Small and Mid-Size Quoted Companies (the "QCA Code"), to the extent that they consider it appropriate having regard to the Company's size, board structure, stage of development and resources. The Directors considers that compliance with the QCA Code will enable them to serve the interests of all our key stakeholders, including the Company's shareholders, and will promote the maintenance and creation of long-term value in the Company. This report describes our approach to governance, including information on relevant policies, practices and the operation of the Board and its Committees. A statement detailing how the Company has applied and complies with the QCA code, and areas of any non-compliance, is provided in the corporate governance section of our website https://investors.defenx.com/corporate-governance.

The reports from the Committees' Chairmen are set out from page 18 and explain how Defenx is seeking to develop its governance framework following the strategic partnership with BV Tech. We see the evolution of good governance going hand-in-hand with renewed growth of the Group. We believe that high standards of governance make an important contribution to shareholder value now and in the future.

Key governance related matters that have occurred during the financial year include the following:

- On 24 May 2018, Alessandro Poerio tendered his resignation as Director of the Company in order to pursue other interests and left the Company on 31 May 2018. As set out in the circular sent to shareholders on 6 April 2018, it was envisaged that Philipp Prince, Chief Financial Officer, and Leonard Seelig, independent Non-executive Director, would step down from the Board. As announced on 11 July 2018, Philipp Prince completed the handover of his responsibilities to our interim Chief Financial Officer, Clive Eplett, and resigned from the Board. Leonard Seelig resigned from the Board at the same time.

On 1 August 2018, Giorgio Beretta and Nic Hellyer were appointed to the Board as Non-executive Directors.

**Anthony Reeves**
Interim Executive Chairman
26 July 2019

## The Board

The Board comprises a balanced mix of Executive and Non-executive Directors with a combination of relevant skills and experience, designed to ensure there is effective leadership of the Group. Directors' biographies appear on page 11.

Anthony Reeves (formerly a Non-executive Director), Giorgio Beretta and Nic Hellyer are considered by the Board to be independent. In determining that they are independent the Board considered the individual's interests in the Company's shares and the share options granted to them. The Board determined that these interests aligned the Directors' interests with those of the Group and bearing in mind the small percentages held, that they remained independent. Raffaele Boccardo is not considered to be independent by virtue of his employment as CEO of BV Tech and his majority ownership stake in BV Tech, the Company's majority shareholder.

The Board is responsible for setting strategy, performance and for the stewardship of the Group, within the framework of effective controls which enable risk to be assessed and managed. Importance is placed on maintaining a robust control environment.

Anthony Reeves as interim Executive Chairman is responsible for the leadership of the Board, ensuring its effective operation and setting the agenda.

## Advisers

The Board has regular contact with its advisers to ensure that it is aware of changes to generally accepted corporate governance procedures and requirements and that the Group remains, at all times, compliant with applicable rules and regulations. The Company holds appropriate insurance cover in respect of possible legal action against its Directors. The Company's Nomad supports the Board's development, specifically providing guidance on corporate governance and other regulatory matters, as required.

All Directors may receive independent professional advice at Defenx's expense, if necessary, for the performance of their duties.

The Directors have access to the services of a Company Secretary through Liam O'Donoghue, who provides advice on company secretarial and corporate governance matters. In addition, the Directors are able to take independent legal advice at the Company's expense if so required.

The Executive Directors work full time for the Company. The Non-executive Directors are each contracted to spend a minimum of 12 days per annum on Defenx business.

In order to keep Director skillsets up to date, the Board uses third parties to advise the Directors of their responsibilities including receiving advice from the Company's external lawyers, including upon the Convertible Loan Agreement signed in October2018 and the agreements signed with BV Tech in April 2019. The Board proposes to introduce a facility for Directors to receive training on relevant developments on a more regular basis. The Board reviews the appropriateness and opportunity for continuing professional development in order to keep each Director's skillset up-to-date. In addition to their general Board responsibilities, Non-executive Directors are encouraged to be involved in specific workshops or meetings, in line with their individual areas of expertise. The Board shall review annually the appropriateness and opportunity for continuing professional development, whether formal or informal.

The Board will seek to take into account any Board imbalances for future nominations. The Company is committed to a culture of equal opportunities for all employees regardless of gender. The Board aims to be diverse in terms of its range of culture, nationality and international experience. It is the Board's intention as the size and complexity of the Company grows, to set and aim to achieve gender diversity objectives pursuant to a defined diversity policy.

### Board meeting attendance

The Board normally meets on a monthly basis. During the year, the Board met on sixteen scheduled occasions.

| Director | Position | Board meetings attended in 2018 | Remun-eration committee meetings attended | Audit committee meetings attended |
|---|---|---|---|---|
| Anthony Reeves | Non-Executive Chairman (until 31 May 2018)<br>Interim Executive Chairman (from 1 June 2018) | 16/16 | 3/3 | 3/3 |
| Raffaele Boccardo | Deputy Chairman & Non-Executive Director (until 11 July 2018)<br>Interim Executive Deputy Chairman (from 11 July 2018) | 12/16 | 3/3 | 3/3 |
| Alessandro Poerio (appointed 20 November 2017; resigned 24 May 2018) | Chief Executive Officer | 10/10* | n/a | n/a |
| Andrea Stecconi (resigned on 24 April 2018) | Chief Executive Officer (until 20 November 2017)<br>Executive Director (from 20 November 2017) | 8/8* | n/a | n/a |
| Philipp Prince (resigned 11 July 2018) | Chief Financial Officer | 11/11* | n/a | n/a |
| Leonard Seelig (resigned 11 July 2018) | Non-executive Director | 11/11* | 2/2* | 2/2* |
| Nicholos Hellyer | Non-executive Director | 3/3* | 1/1* | 1/1* |
| Giorgio Beretta | Non-executive Director | 3/3* | 1/1* | 1/1* |

** figures based on number of meetings held whilst the Director was in-post, being only part of the year.*

There were also four *ad-hoc* Board meetings convened in relation to items of special business in April, July, August and October 2019, which were attended by all Directors in post at the time the meeting was held.

### Board performance evaluation

The Board is committed to undertaking reviews of Board and Committee performance and of individual Board members every year. The first review will be conducted once new executive directors have been appointed and in post for a reasonable period.

### Risk management and internal control

The structure of the Board is subject to continual review to ensure that it is appropriate for the Company. Over the next 12 months the Company intends to review the performance of the Board as a whole to ensure that its members collectively function in an efficient manner, focusing more closely on defined objectives and targets for improving performance, as well as reviewing the effectiveness of each Committee. The Directors consider that the Company and Board are not yet of a sufficient size for a full

Board performance evaluation to make commercial and practical sense, although the Board currently runs a self-evaluation process whereby the Chairman annually assesses the individual contributions of each of the members of the team to ensure that:

- Their contribution is relevant and effective;
- That they are committed; and
- Where relevant, they have maintained their independence.

Therefore, the Board accepts that the Company does not comply with this aspect of the QCA Code, although in frequent Board meetings/calls, the Directors discuss areas where they feel a change would be beneficial for the Company, and the Company Secretary remains on hand to provide advice. As the Company grows, it intends to expand the Board and, with expansion, re-consider the need for a formal Board evaluation.

The Company has not yet adopted a policy on succession planning. The Company will consider succession planning in respect of the Board and other members of senior management as appropriate, as part of its review of Board effectiveness over the next 12 months.

### Corporate Culture

The Board recognises that its decisions regarding strategy and risk may impact the corporate culture of the Company as a whole and that this will impact the performance of the Group. It is aware that the tone set by the Board and by its decisions regarding strategy and risk may impact the corporate culture of the Company as a whole and on the way that employees and other stakeholders behave.

The Group operates in a manner that encourages an open and respectful dialogue with employees, customers and other stakeholders and the Board considers that sound ethical values and behaviours are crucial to the ability of the Company to achieve its corporate objectives. The Group is committed to the highest standards of personal and professional ethical behaviour, and this must be reflected in every aspect of the way in which the Company operates. The Board places great importance on this aspect of corporate life and seeks to ensure that this flows through all that the Company does.

The Directors consider that at present the Group has an open culture facilitating comprehensive dialogue and feedback and enabling positive and constructive challenge. The Executive Directors regularly meet with senior management and discuss staff well-being, development and staff feedback. Employees are encouraged to engage directly with Directors, and the Group seeks to promote Group values and behaviour through a top-down approach.

### Strategy, Risk management and internal control

A description of the Group's business model and strategy can be found on pages 3-10 of the Strategic Report.

The Board is responsible for determining the nature and extent of major risks facing the Group and for establishing and maintaining a risk management framework and system of internal financial controls. The Executive Directors report any new or changed risks, and any changes in risk management/control to the Board. The Board discusses all business matters having regard to the risks for the Group and to the extent that risks inherent in a particular activity are considered significant, appropriate action is taken and steps taken to mitigate the issue. The overall objective of the Board is to set policies that seek to reduce risk as far as possible without unduly affecting the Company's competitiveness and flexibility.

The Board is satisfied that the procedures in place meet the particular needs of the Group in managing the risks to which it is exposed. The Board is satisfied with the effectiveness of the system of internal controls, but by their very nature, these procedures can provide reasonable, not absolute, assurance against material misstatement or loss. The Board has delegated responsibility to the Audit Committee for ensuring that the Company's management reviews, monitors and reports on the integrity of the consolidated financial statements of the Company and related financial information. The Audit Committee will maintain effective working relationships with the Board of Directors, executive management and the external auditors and will monitor the independence and effectiveness of the auditors and the audit. The Company has strict segregation of duties and authority controls which are reviewed annually by the auditors whom report their findings to the Audit Committee.

The Board has reviewed the need for an internal audit function and has decided that, given the nature of the Group's business and assets and the overall size of the Group, the systems and procedures currently employed provide sufficient assurance that a sound system of internal controls are in place, which safeguards the shareholders' investment and the Group's assets. An internal audit function is therefore considered unnecessary. However, the Board will continue to monitor the need for this function.

A summary of the principal risks identified by the Group and how these are mitigated is set out on page 9. The key elements of the Group's risk framework and internal control systems are:

- A schedule of matters reserved for decision by the Board;
- Defined responsibilities and authority limits;
- Close involvement of the Executive Directors and other members of senior management in day-to-day operations;
- Monthly management reporting; and
- Comprehensive annual budgeting process and monitoring of performance against budget.

### Going concern

As at 24 July 2019, the Group had cash resources of approximately €120,000, which is sufficient through to the end of August 2019, and, therefore, the Company remains reliant on the continued financial support of its major shareholder, BV Tech, going forward.

In considering the Group's going concern position, the Directors have taken into account BV Tech's support for the Group to date, that has included the provision of a loan facility of €0.95 million in October 2018, now fully drawn and converted to equity, bring its aggregate investment in the Company's equity to €4.6 million, the sales agreements signed in April 2019 and receipt of a non-binding letter of support from BV Tech for €350,000 in July 2019.

Taking into account the above, the Directors are satisfied that the Group has adequate resources to continue in operational existence for the foreseeable future and, accordingly, continue to adopt the going concern basis in preparing the Group and Company financial statements.

### Relations with shareholders

The Directors are committed to regular engagement with shareholders and prospective investors and will make themselves available as appropriate.

In accordance with good governance, the Company entered into a relationship agreement with its major shareholder, BV Tech, to ensure that the Company is capable at all times of carrying on its business independently of BV Tech and its associates and for the benefit of the shareholders as a whole.

BV Tech is the Company majority shareholder and is currently interested in 25,964,850 ordinary shares representing approximately 67.1% of the Company's issued share capital.

In October 2018 BV Tech agreed to provide the Company with an unsecured loan of €0.95 million with repayment due by 1 January 2020. That loan was drawn in three instalments in October 2018, December 2018 and March 2019 and in each instance the loan was converted immediately to ordinary shares at the agreed issue price of 8 pence per share.

### Information received by the Board

The Board receives information on at least a monthly basis enabling it to review operational and financial performance (including sales activity, software development progress and working capital management); forecasts (including comparison with market expectations); potentially significant transactions; and strategy.

### Website

Our corporate website at *investors.defenx.com* provides access to Company information, announcements, published financial reports and contact details.

### AGM

The forthcoming AGM will be held on 2 September 2019, providing an opportunity for the shareholders to meet and raise questions of the Chairman, other Directors and senior management.

# Audit committee report

## Dear shareholder

I present my Audit Committee Report for the year ended 31 December 2018, which has been prepared by the Committee and approved by the Board.

The Committee is responsible for reviewing and reporting to the Board on financial reporting, internal control and risk management, and for reviewing the performance, independence and effectiveness of the external auditors in carrying out the statutory audit. The Committee advises the Board on the statement by the Directors that the Annual Report when read 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.

During the year, the Committee's primary activity involved meeting with the external auditors, considering material issues and areas of judgement, and reviewing and approving the interim and year end results and accounts.

In addition, the Committee reviewed the audit and tax services provided by Haysmacintyre LLP, the Group's external auditors. The Committee concluded that Haysmacintyre LLP are delivering the necessary audit scrutiny and that the tax services provided did not pose a threat to their objectivity and independence. Accordingly, the Committee recommended to the Board that Haysmacintyre LLP be re-appointed for the next financial year.

In the coming year, in addition to the Committee's ongoing duties, the Committee will:

- consider significant issues and areas of judgement with the potential to have a material impact on the financial statements, including impairments of the Company's debtors, investments and technologies; and
- keep the need for an internal audit function under review, having regard to the Company's strategy and resources.

**Giorgio Beretta**
Chairman of the Audit Committee
26 July 2019

### Audit committee and attendance

The Audit Committee currently comprises Giorgio Beretta (Chair) and Nic Hellyer. On 1 August 2018, Anthony Reeves and Raffaele Boccardo stepped down from the Audit Committee pending the appointment of full time Executive Directors.

Prior to his resignation on 11 July 2018, Leonard Seelig chaired the Committee. Giorgio Beretta was appointed as chairman on 1 August 2018. The Board considers that Giorgio Beretta has sufficient relevant financial experience to chair the Audit Committee given that he is a qualified accountant with over 30 years' experience and is a partner at BDO Italia.

The Committee is required by its terms of reference to meet at least twice a year.

### Objectives and responsibilities

The Committee is responsible for monitoring the integrity of the Group's financial statements, including its Annual and Interim Reports, preliminary results announcements and any other formal announcements relating to its financial performance prior to release.

The Committee's main responsibilities can be summarised as follows:

- to review the Company's internal financial controls and risk management systems;
- to monitor the integrity of the financial statements and any formal announcements relating to the Group's financial performance, reviewing significant judgements contained in them;
- to make recommendations to the Board in relation to the appointment of the external auditors and to recommend to the Board the approval of the remuneration and terms of engagement of the external auditors;
- to review and monitor the external auditors' independence and objectivity, taking into consideration relevant UK professional and regulatory requirements;
- to develop and implement policy on the engagement of the external auditors to supply non-audit services, taking into account relevant ethical guidance regarding the provision of non-audit services by the external auditors; and
- to report to the Board, identifying any matters in respect of which it considers that action or improvement is needed, and to make recommendations as to steps to be taken.

The terms of reference are reviewed annually and are available on the Company's website at investors.defenx.com.

### Significant issues considered during the year ending 31 December 2018

During 2018, the Committee:

- met with the external auditors to review and approve the annual audit plan and receive their findings and report on the annual audit;
- considered significant issues and areas of judgement with the potential to have a material impact on the financial statements, including impairments of the Group's investments and technologies;
- considered the integrity of the published financial information and whether the Annual Report and Accounts taken as a whole are fair, balanced and understandable and provide the information necessary to assess the Group's position and performance, business model and strategy;
- Agreed the change of auditors of Defenx Italia SRL from RSM to Mazars; and
- reviewed and approved the interim and year end results and accounts.

The significant accounting areas and judgements considered by the Committee were:

*Revenue recognition*

The Committee again discussed the limited information available on the activation of licences sold to B2B2C customers. The Committee also considered the change in policy wording to state explicitly that deferred revenues would not be released if the related trade receivable had not been collected. On this basis and under the Group's current revenue recognition policy, the Committee continued to be satisfied that the consequential judgement taken on licences sold and not activated and the timing of release of deferred revenue in the accounts was appropriate.

The Committee also appraised the implications on revenue recognition of IFRS 15, concluding that the existing policy applied equally to the principles of IFRS 15.

### *Recoverability of debtors*

The Committee continued to review the track record of receipts from slow-paying debtors and deterioration following the announcement of performance and integration issues in October 2017. The Committee sought regular updates from management as to the status of trade receivables (and related customer claims) and negotiations with customers to reach commercially acceptable settlements. In light of this, the Committee reviewed and accepted management proposals for a further exceptional impairment of trade receivables and was satisfied that net trade receivables were fairly stated.

### *Valuation of intangible assets*

The Committee reviewed the basis of capitalisation and considered the intangible value attributed to its intangible software development costs.

It considered the asset impairment calculations prepared by management in light of the current and projected trading levels and is satisfied that the full year impairments and resultant net book values were prepared appropriately and on a reasonable basis.

### *Going concern*

The Committee reviewed the cash flow forecasts for the Group and discussed the key assumptions and risks relevant to their achievement. The Committee was satisfied that the basis for adopting the going concern basis in preparing the Group and Company financial statements, set out in note 1 on page 40, was reasonable.

### *Risk review process*

The Audit Committee is responsible for reviewing the financial risks and the internal controls relating thereto but the Board as a whole has responsibility for reviewing the overall business risks and risk management framework. The Group's principal risks and uncertainties are set out in the Strategic Report together with mitigating actions and the internal controls and risk management procedures are summarised in the Corporate Governance Report.

### *External auditor*

The Committee reviewed the effectiveness of the audit process in respect of the year ended 31 December 2017 and immediately prior to publishing this report in respect of the year ended 31 December 2018. In doing so, the Committee considered the reports produced by Haysmacintyre LLP, met the audit engagement partner and discussed the audit with the Chief Financial Officer. The Committee continues to be satisfied that the external auditors are delivering the necessary scrutiny and robust challenge in their work. Accordingly, the Committee recommended to the Board that it is appropriate to re-appoint Haysmacintyre LLP as the Group's external auditors for the next financial year.

### *External audit and non-audit services*

During the year, Haysmacintyre LLP provided tax advisory services. An analysis of the audit and non-audit fees is provided in note 0 to the financial statements. The Committee considered the independence and objectivity of Haysmacintyre LLP in carrying out both tax and audit services. The Committee was satisfied with the written assurances received that the non-audit work undertaken by Haysmacintyre LLP did not pose a threat to their objectivity and independence.

# Remuneration committee report

## Dear shareholder

As Chairman of Defenx's Remuneration Committee, I present the Remuneration Committee Report for the year ended 31 December 2018, which has been prepared by the Committee and approved by the Board.

The Remuneration Committee is responsible for determining the remuneration policy for the executive Directors and other members of senior management, and for overseeing the Company's long-term incentive plans. The Board as a whole is responsible for determining Non-executive Directors' remuneration.

As an AIM quoted company, the Directors' Remuneration Report Regulations do not apply to Defenx and so the report that follows is disclosed voluntarily and has not been subject to audit. The Annual Report on remuneration will again be subject to an advisory vote by shareholders at our forthcoming AGM and we hope to receive your support.

The Committee will continue to monitor market trends and developments in order to assess those relevant for the Group's future remuneration policy.

## Remuneration decisions for 2018

In light of the financial performance of the Group, no annual bonuses are payable for the year ended 31 December 2018.

There were no long-term incentive awards during the year.

In recognition of his switch from Non-executive to interim Executive Chairman, and his additional time commitment in the management of Defenx, Anthony Reeves' remuneration was increased commensurately from £30,000 per year to £90,000 per year.

## Remuneration policy for 2019 and future years

Future salary awards and increases will be set in line with relevant market levels and to retain and attract high quality executives. Performance elements of remuneration will have clearly defined and challenging targets that link rewards to business performance in the short and medium-term. All variable elements of remuneration are subject to clawback or repayment in the event of serious financial misstatement or misconduct.

There have been no long-term incentive awards since admission to AIM. It remains our intention to make performance-based awards once the Board has been rebuilt.

**Nic Hellyer**
Chairman of the Remuneration Committee
26 July 2019

### Committee members and attendance

In the first part of the year, the members of the Committee were Anthony Reeves (Chairman), Leonard Seelig and Raffaele Boccardo. The Committee were aware that the Company Chairman should not chair the Remuneration Committee. Following Leonard Seelig's resignation on 11 July 2018, Nic Hellyer and Giorgio Beretta were appointed on 1 August 2018 both joined the Remuneration Committee and the former took over the role of Chairman. Anthony Reeves and Raffaele Boccardo then stepped down from the Committee pending the appointment of full time Executive Directors.

The terms of reference are reviewed annually and are available on the Company's website at investors.defenx.com.

### Single total figure of remuneration for the Directors

The table below sets out the total single figure remuneration received by each Director who served during the year ended 31 December 2018.

| € | Salary or fees | Benefits | Pension | Annual bonus | Cash total | Long-term incentive | Total |
|---|---|---|---|---|---|---|---|
| **Executive** | | | | | | | |
| Anthony Reeves | 65,000 | - | - | - | 65,000 | - | 65,000 |
| Raffaele Boccardo | | | | | | | |
| Alessandro Poerio (appointed 20 November 2017, resigned 24 May 2018) | 27,271 | - | - | - | 27,271 | - | 27,271 |
| Andrea Stecconi (resigned 24 April 2018) | 9,008 | - | - | - | 9,008 | - | 9,008 |
| Philipp Prince (resigned 11 July 2018) | 81,871 | 6,380 | 5,258 | - | 93,509 | - | 93,509 |
| **Sub-total** | 183,150 | 6,380 | 5,258 | - | 194,788 | - | 194,788 |
| **Non-executive** | | | | | | | |
| Nicholos Hellyer (appointed 1 August 2018) | 14,133 | - | - | - | 14,133 | - | 14,133 |
| Giorgio Berretta (appointed 1 August 2018) | 14,133 | - | - | - | 14,133 | - | 14,133 |
| Leonard Seelig (resigned 11 July 2018) | 18,555 | - | - | - | 18,555 | - | 18,555 |
| **Sub-total** | 46,821 | - | - | - | 46,821 | - | 46,821 |
| **Total** | 229,971 | 6,380 | 5,258 | - | 241,609 | - | 241,609 |

Alessandro Poerio was appointed to the Board as Chief Executive Officer on 20 November 2017 replacing Andrea Stecconi, who remained on the Board as an Executive Director during the year but resigned from the Board on 24 April 2018. There were no termination payments during the year. Subsequent to the year end, Alessandro Poerio and Philipp Prince received termination payments of €40,000 and €29,000 respectively.

The table below sets out the total single figure remuneration received by each Director who served during the year ended 31 December 2017.

| € | Salary or fees | Benefits | Pension | Annual bonus | Cash total | Long-term incentive | Total |
|---|---|---|---|---|---|---|---|
| **Executive** | | | | | | | |
| Alessandro Poerio (appointed 20 November 2017, resigned 24 May 2018) | 20,465 | - | - | - | 20,465 | - | 20,465 |
| Andrea Stecconi (resigned 24 April 2018) | 122,264 | - | 5,240 | - | 127,504 | - | 127,504 |
| Philipp Prince (resigned 11 July 2018) | 120,405 | 2,062 | 9,354 | - | 131,821 | 33,309 | 165,130 |
| **Sub-total** | 263,134 | 2062 | 14,594 | - | 279,790 | 33,309 | 313,099 |
| **Non-Executive** | | | | | | | |
| Anthony Reeves | 62,029 | - | - | - | 62,029 | 3,517 | 65,546 |
| Leonard Seelig (resigned 11 July 2018) | 59,707 | - | - | - | 59,707 | 2,824 | 62,531 |
| **Sub-total** | 121,736 | - | - | - | 121,736 | 6,341 | 128,077 |
| **Total** | 384,870 | 2,062 | 14,594 | - | 401,526 | 39,650 | 441,176 |

## Base salary

The Executive Directors’ service agreements are as follows:

| | with Defenx PLC | | with Defenx SA | | with Defenx Italia SRL | |
|---|---|---|---|---|---|---|
| | 2018 | **2019** | 2018 | **2019** | 2018 | **2019** |
| Alessandro Poerio | £25,000 | - | - | - | €100,000 | - |
| Andrea Stecconi | £15,000 | - | CHF130,000 | - | - | - |
| Philipp Prince | £105,000 | - | - | - | - | - |

Andrea Stecconi resigned from the Board on 24 April 2018. Alessandro Poerio resigned from the Board on 24 May 2018. Philipp Prince resigned from the Board on 11 July 2018.

### Benefits and pension

Alessandro Poerio and Andrea Stecconi received customary benefits by way of social contributions to relevant authorities in Italy and Switzerland respectively. Philipp Prince received medical and life insurance cover and was entitled to pension contributions of 5% of salary plus up to a further 5% of salary on a matched basis consistent with other UK staff.

### Annual bonus

#### *For the year ended 31 December 2018*

The financial performance targets, primarily based on revenue growth and free cash flow, have not been met. Accordingly, no annual bonuses are payable for the year ended 31 December 2018.

### Remuneration policy for Non-executive Directors

The current annual fees together with the dates of the letters of appointment are:

| | Date of letter | 2018 | 2017 |
|---|---|---|---|
| Anthony Reeves | 7 October 2015 | £90,000 | £30,000 |
| Raffaele Boccardo | 4 August 2017 | - | - |
| Nicholos Hellyer | 1 August 2018 | £42,000 | - |
| Giorgio Beretta | 1 August 2018 | £42,000 | - |

Following the resignation of Alessandro Poerio, from 1 June 2018, Anthony Reeves became Interim Executive Chairman, involving a greater time commitment. In recompense, his base remuneration was increased from £2,500 per month to £7,500 per month with effect from that date. With effect from 11 July 2018, when Raffaele Boccardo become Interim Executive Chairman, it was agreed that the Company would pay BV Tech £7,500 per month for his services, subject to a maximum of £70,000 in any 12 month period.

### Long-term incentives for Executive and Non-executive Directors

#### *Option Schemes*

The Company established an EMI Option Scheme to provide incentives to employees, including Directors, to achieve the longer-term objectives of the Group, to give suitable recognition to the ability and industry of the individuals concerned and to attract and retain suitably experienced and able people, by providing them with the opportunity to acquire ownership interests in the Company.

The vesting of the existing options is not conditional on performance conditions; the only condition being that the individual remains an employee of the Group. Future awards will vest solely on performance.

The following share option awards have been granted to Executive Directors under the EMI Option Scheme:

| | Date of grant | Number | Price | Vesting period | Expiry date |
|---|---|---|---|---|---|
| Philipp Prince | 22 July 2015 | 42,000 | £0.80 | Over 36 months | 22 July 2025 |
| Philipp Prince | 3 December 2015 | 125,000 | £1.48 | One third on first anniversary; balance over following 24 months from grant | 2 December 2025 |

The EMI status of the EMI Option Scheme ceased upon the approval of the subscription and open offer at an EGM on 23 April 2018 as a result of BV Tech’s resultant shareholding exceeding 50%.

The Company established an Unapproved Share Option Scheme and the following options have been granted under this scheme:

| | Date of grant | Number | Price | Vesting period | Expiry date |
|---|---|---|---|---|---|
| Anthony Reeves | 3 December 2015 | 15,625 | £1.48 | One third on first anniversary; balance over following 24 months from grant | 2 December 2025 |
| Leonard Seelig | 3 December 2015 | 12,500 | £1.48 | One third on first anniversary; balance over following 24 months from grant | 2 December 2025 |

As a result of their resignation, any options (in either scheme) held by Philipp Prince and Leonard Seelig had lapsed without exercise by 31 December 2018.

### Directors' interests in shares and share scheme interests

The Directors' beneficial interests in shares, together with their respective families, as at 31 December 2018 are shown below together with their interests in share schemes.

| | Long-term incentives | | | | | |
|---|---|---|---|---|---|---|
| | Subject to continued employment | Vested but not yet exercised | Beneficially owned | Total interest | Required holding (% salary) | Current holding (% salary) |
| Anthony Reeves | 5,208 | 10,417 | 31,250 | 46,875 | - | 0.24% |
| Raffaele Boccardo* | - | - | 25,964,850 | 25,964,850 | - | 28.08% |

*Raffaele Boccardo is President and CEO of BV Tech and is deemed to be beneficially interested in the shares in the company held by BV Tech on account of his 86% interest in BV Tech.

BV Tech have acquired a total of 25,964,850 ordinary shares, representing 67.1% of the Company's issued share capital, between 31 December 2016 and 18 March 2019. Save for this, there have been no changes to the Directors' shareholdings between 31 December 2016 and 30 June 2019.

None of the Directors had an interest in the shares of any subsidiary undertaking of the Company or in any significant contracts of the Group save as set out in note 25 to the financial statements.

### Terms of office for Executive and Non-executive Directors

Alessandro Poerio's and Andrea Stecconi's service agreements were subject to termination by either party on six-months' notice. Philipp Prince's service agreement was subject to termination by either party on three-months' notice. Anthony Reeves and Leonard Seelig, whilst acting as Non-executive Directors provided their services under letters of appointment, which were terminable on three-months' notice by either party. On becoming Interim Executive Directors, Anthony Reeves' and Raffaele Boccardo's revised service contracts provide for an initial notice period of three months followed by a rolling one-month period thereafter (and their Non-executive Director terms of appointment, should their roles revert as such, are terminable on three months' and one months' notice, respectively). Giorgio Beretta and Nic Hellyer's contracts are terminable on three months' notice.

# Directors' report

The Directors present their report together with the audited financial statements for the year ended 31 December 2018.

## Principal activity

Defenx PLC is a public limited company incorporated in England and Wales, registered number 08993398, with its registered office at 201 Temple Chambers, 3-7 Temple Avenue, London, EC4Y 0DT. Defenx PLC is quoted on the AIM market of the London Stock Exchange.

Its principal activity is to provide security solutions with a range of products for mobile devices and PCs, protecting them against hackers and data loss. Management and control is exercised from the UK and Defenx's main countries of operation are Italy and Switzerland.

## Review of business

The Strategic Report on pages 3 to 10 provides a review of the business, the Group's trading for the year ended 31 December 2018, key performance indicators and an indication of research and future developments, as well as the principal risks and uncertainties facing the business.

## Future developments

Working with BV Tech, Defenx will continue to develop its next generation products, releasing in 2019 first the security suite, then backup, before moving onto secure messaging in 2020. Sales and marketing efforts will focus on direct sales to the public sector, corporate and retail sectors.

## Results and dividend

The results for the year ended 31 December 2018 are set out in the consolidated statement of comprehensive income on page 33. As the Company has no distributable reserves, the Directors are not able to recommend the payment of a dividend. Further, the Board believes it is in the Company's interests to retain future earnings to fund working capital needs and achieve capital growth.

## Directors

The Directors who served during the year ended 31 December 2018 and up to the date of signing the financial statements were as follows:

| |
|---|
| A Poerio (resigned 24 May 2018) |
| A Stecconi (resigned 24 April 2018) |
| P Prince (resigned 11 July 2018) |
| A Reeves |
| R Boccardo |
| L Seelig (resigned 11 July 2018) |
| G Beretta (appointed 1 August 2018) |
| N Hellyer (appointed 1 August 2018) |

In accordance with the Articles of Association, each Director must retire from office at the third AGM after the AGM or general meeting, as the case may be, at which he was appointed or last re-appointed.

Accordingly, Anthony Reeves will retire at the forthcoming AGM and, being eligible, will offer himself for re-election.

### Directors' interests

Details of the Directors' interests in the shares of the Company and details of options granted under the Group's share scheme are set out in the Remuneration Report from page 21. No Director has any beneficial interest in the share capital of any subsidiary undertaking.

### Qualifying indemnity provision

The officers of the Company are indemnified in respect of proceedings which might be brought by a third party. No cover is provided in respect of fraudulent or dishonest transactions.

### Financial risk management policies and objectives

A summary of the Group's key operating risks is set out from page 9. The Group's risk management policies and objectives including exposure to price risk, credit risk, liquidity and cash flow risk are contained in note 20 to the financial statements.

### Share capital

Full details of changes in the Company's share capital during the year and after the year end are set out in notes 21 and 27 to the financial statements respectively. Details of employee share options and warrants are set out in note 21 .

### Substantial shareholdings

At 30 June 2019, the Company's significant shareholders were:

| | Number of shares | Holding |
|---|---|---|
| BV Tech SpA | 25,964,850 | 67.1% |

### Political donations

During the year ended 31 December 2018 the Group made no political donations.

### Events after the reporting date

Details of significant events since the balance sheet date are contained in note 27 to the financial statements.

### Provision of information to the auditors

Each of the Directors who held office at the date of approval of this Directors' Report confirms that:

- so far as he is aware, there is no relevant audit information of which the Company's and Group's auditor is unaware; and
- he has taken all the steps he ought to have taken as a Director in order to make himself aware of any information needed by the Company and the Group's auditors in connection with their report and to establish that the auditors are aware of that information.

### Auditor

Haysmacintyre LLP has expressed its willingness to continue in office as auditor to the Company. A resolution to reappoint Haysmacintyre LLP will be proposed at the forthcoming AGM.

### AGM

The AGM will be held on 2 September 2019. The notice of AGM and the ordinary and special resolutions to be put to the meeting will be notified to shareholders separately from these accounts.

### Approval

The Directors' report was approved on behalf of the Board on 26 July 2019.

**Anthony Reeves**
Interim Executive Chairman

# Statement of Directors' responsibilities

The Directors are responsible for preparing the Annual Report and the Group and Company financial statements in accordance with applicable UK law and those IFRSs as adopted by the European Union.

Under Company law the Directors must not approve the Group and Company financial statements unless they are satisfied that they present fairly the financial position, financial performance, and cash flows of the Group and Company for that period. In preparing those financial statements, the Directors are required to:

- Select suitable accounting policies;
- Present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- Provide additional disclosures when compliance with the specific requirements in IRFSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Group's financial position and financial performance;
- State that the Group and the Company have complied with IFRSs subject to any material departures disclosed and explained in the financial statements; and
- Make judgements and estimates that are reasonable and prudent.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and the Group and enable them to ensure that the financial statements comply with the Companies Act 2006 and Article 4 of the IAS regulation. They are also responsible for safeguarding the assets of the Company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the Company's website. Legislation in the UK may differ from legislation in other jurisdictions.

Each of the Directors, whose names are listed in the Strategic Report above, confirms that, to the best of his knowledge:

- The Group financial statements which have been prepared in accordance with IFRSs as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Group.
- The Strategic Report includes a fair review of the development and performance of the business and the position of the Group and the Company, together with a description of the principal risks and uncertainties that it faces.
- The Directors consider that the Annual Report and Accounts, taken as a whole is fair, balanced and understandable.

This responsibility statement was approved by the Board on 26 July 2019.

**Anthony Reeves**
Interim Executive Chairman

**Raffaele Boccardo**
Interim Deputy Executive Chairman

# Independent auditors' report to the members of Defenx PLC

**Opinion**

We have audited the financial statements of Defenx Plc (the 'parent company') and its subsidiaries (together the 'Group') for the year ended 31 December 2018 which comprise the Consolidated Statement of Comprehensive Income, Consolidated and Company Statements of Financial Position, Consolidated and Company Statements of Cash Flows, Company and Consolidated Statements of Changes in Equity and notes to the financial statements, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

In our opinion, the financial statements:

- give a true and fair view of the state of the Group's and Parent Company's affairs as at 31 December 2018 and of the Group's loss for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepare in accordance with the requirements of the Companies Act 2006

**Basis for opinion**

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the group in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applied to listed entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

**Material uncertainty related to going concern**

We draw attention to note 1 in the financial statements, which indicates that the Group and Company has prepared forecasts of its performance for the next two years and that these forecasts show a shortfall in funding under certain sales scenario sensitivities. These events or conditions, along with the other matters as set forth in note 1, indicate that a material uncertainty exists that may cast significant doubt on the parent company's ability to continue as a going concern. Our opinion is not modified in respect of this matter.

**Key audit matters**

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) we identified, including those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

*Revenue recognition*

The Group records significant revenues from business to business sales to third party distributers on a non-contingency basis with a commitment to ongoing maintenance. Our response to this presumed risk of material misstatement arising from improper revenue recognition was to consider the nature of classes of sales transactions and review methodologies for recognition and where appropriate, the deferral of income.

*Recovery of trade receivables*

The Group has continued to record slow recovery of trade receivable balances and has consequently made significant provision for those balances due at the reporting date.

Our audit work included but was not restricted to an assessment of the assumptions used in calculating bad debt provisions as well as referring to correspondence from third parties in respect to the likelihood of recoverability.

*Going concern*
The Group has recorded significantly reduced revenues, an operating loss and net cash outflow during the year which results in a risk to its ability to continue as a going concern by being unable to meet its liabilities as and when they fall due from twelve months of the approval of these financial statements.

Our audit work included but was not restricted to a review of forecasts over the forthcoming twelve months and comparison to the overall business plan; a review of the non-binding letter of support from BV Tech and their financial standing; analysis of detailed budgets and working capital forecasts; consideration of the Group's capacity to continue trading over the forthcoming twelve months; and review and confirmation of upcoming funding plans to ensure sufficient capital is available. We have noted a material uncertainty related to going concern which is highlighted in this audit report.

*Valuation of intangible assets*
The Group has significant intangible assets arising both from internal development and acquisitions of third party entities (namely Defenx Italia SRL, formerly Memopal SRL), including both goodwill and separately identifiable intangible assets. There is a risk that on consolidation the value of these assets is overstated.

Our audit work included but was not restricted to reviewing the impairment reviews prepared by management and giving scrutiny of associated calculations and forecasts used in determining expected future results. Our review was performed in conjunction with recent results and our understanding of the Group's business model.

**Our application of materiality**
The scope and focus of our audit was influenced by our assessment and application of materiality. We define materiality as the magnitude of misstatement that could reasonably be expected to influence the readers and the economic decisions of the users of the financial statements. We use materiality to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and on the financial statements as a whole.

Materiality for the Group Financial Statements as a whole was set at €90,000, determined with reference to the revenue of the Group on a consolidated basis and the loss for the year. We report to the Audit Committee any corrected or uncorrected misstatements arising exceeding €4,500.

Performance materiality was set at €67,500, being 75% of materiality.

**An overview of the scope of our audit**
Our audit scope included all components and was performed to component materiality. Our audit work therefore covered 100% of group revenue, group profit and total group assets and liabilities. It was performed to the materiality levels set out above.

The audit of Defenx Italia SRL, one of the Group's subsidiaries, was performed by a component auditor in accordance with our group audit instructions.

**Other information**
The directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

**Opinions on other matters prescribed by the Companies Act 2006**
In our opinion, based on the work undertaken in the course of the audit:

- the information given in the strategic report and the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the strategic report and the directors' report have been prepared in accordance with applicable legal requirements.

**Matters on which we are required to report by exception**
In the light of the knowledge and understanding of the group and the parent company and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or the directors' report.

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

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

**Responsibilities of directors**
As explained more fully in the directors' responsibilities statement set out on page 28, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the group's and the parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so.

**Auditor's responsibilities for the audit of the financial statements**
Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

**Use of our report**

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an Auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Ian Cliffe (Senior Statutory Auditor)
For and on behalf of Haysmacintyre LLP, Statutory Auditors
26 July 2019

10 Queen Street Place
London
EC4R 1AG

# Consolidated statement of comprehensive income

| | Note | Year ended 31 December 2018 €000 | Year ended 31 December 2017 €000 |
|---|---|---|---|
| **Revenue** | 5 | **1,420** | 2,928 |
| Cost of sales | 0 | **(1,988)** | (2,553) |
| **Gross (loss)/profit** | | **(568)** | 375 |
| Other operating income | 0 | **853** | **772** |
| Sales & marketing expenses | 0 | **(7)** | (1,975) |
| Research, development & operations expenses | 0 | **(198)** | (712) |
| Administrative expenses | 0 | **(2,250)** | (906) |
| Impairment of trade receivables | 0 | **(1,349)** | (3,020) |
| Impairment of intangible fixed assets | 0 | **-** | (6,286) |
| Operating expenses before transaction costs | | **(3,804)** | (12,899) |
| Operating loss before transaction costs | | **(3,519)** | (11,752) |
| Transaction costs | 0 | **-** | (101) |
| **Operating loss** | | **(3,519)** | (11,853) |
| Finance income | 8 | **-** | 1 |
| Finance expense | 8 | **(278)** | (184) |
| **Loss before tax** | | **(3,797)** | (12,036) |
| Income tax credit | 9 | **11** | 235 |
| **Loss and total comprehensive lost for the year** | | **(3,786)** | (11,801) |
| | | | |
| *Attributable to:* | | | |
| Equity holders of the parent | | **(3,730)** | (11,641) |
| Non-controlling interests | | **(56)** | (160) |
| **Loss and total comprehensive loss for the year** | | **(3,786)** | (11,801) |
| | | | |
| **Loss per share** – loss for the year attributable to equity holders of the parent | | | |
| Basic | 10 | **(€0.154)** | (€1.030) |
| Diluted | 10 | **(€0.150)** | (€0.976) |

The loss for the year arises from the Group's continuing operations.

There were no other items of comprehensive income.

# Consolidated statement of financial position

| | Note | 31 December 2018 €000 | 31 December 2017 €000 |
|---|---|---|---|
| **Non-current assets** | | | |
| Property, plant and equipment | 0 | **104** | 135 |
| Intangible assets | 12 | **3,513** | 4,904 |
| Research and development tax credit income | 17 | **1,149** | 1,596 |
| | | **4,766** | 6,635 |
| **Current assets** | | | |
| Trade and other receivables | 14 | **600** | 1,243 |
| Research and development tax credit income | 17 | **483** | 179 |
| Cash and short-term deposits | 15, 24 | **95** | 951 |
| | | **1,178** | 2,373 |
| **Total assets** | | **5,944** | 9,008 |
| | | | |
| **Current liabilities** | | | |
| Trade and other payables | 16 | **(2,303)** | (851) |
| Deferred revenue | 18 | **(253)** | (621) |
| Loans and borrowing | 19 | **(396)** | (663) |
| Income taxes payable | | **-** | (385) |
| | | **(2,952)** | (2,520) |
| **Non-current liabilities** | | | |
| Deferred revenue | 18 | **-** | (887) |
| Loans and borrowing | 19 | **(1,392)** | (1,533) |
| Deferred tax liabilities | 9 | **(30)** | (42) |
| | | **(1,422)** | (2,462) |
| **Total liabilities** | | **(4,374)** | (4982) |
| | | | |
| **Net assets** | | **1,570** | 4,026 |
| | | | |
| **Capital and reserves** | | | |
| Called up share capital | 21 | **635** | 287 |
| Share premium | 21 | **12,446** | 11,370 |
| Merger reserve | 22 | **1,641** | 1,641 |
| Shares to be issued reserve | 22 | **-** | 37 |
| Convertible bond option reserve | 19, 22 | **164** | 164 |
| Share based payment reserve | 22 | **153** | 210 |
| (Deficit in) retained earnings | | **(13,278)** | (9,548) |
| **Equity attributable to equity holders of the parent** | | **1,761** | 4,161 |
| Non-controlling interests | | **(191)** | (135) |
| **Total equity** | | **1,570** | 4,026 |

**Anthony Reeves**
Executive Chairman

**Raffaele Boccardo**
Deputy Executive Chairman

# Company statement of financial position

Company registration number: 08993398

| | Note | **31 December 2018 €000** | 31 December 2017 €000 |
|---|---|---|---|
| **Non-current assets** | | | |
| Intangible assets | 12 | **-** | - |
| Investments in subsidiary undertakings | 13 | **1,859** | 1,779 |
| | | **1,859** | 1,779 |
| **Current assets** | | | |
| Trade and other receivables | 14 | **93** | 79 |
| Loans to subsidiary undertakings | | **239** | 3,135 |
| Cash and short-term deposits | 15, 24 | **16** | 860 |
| | | **348** | 4,074 |
| **Total assets** | | **2,207** | 5,853 |
| | | | |
| **Current liabilities** | | | |
| Trade and other payables | 16 | **(630)** | (296) |
| Deferred revenue | 18 | **(2)** | (221) |
| Loans and borrowing | 19 | **-** | (154) |
| | | **(632)** | (671) |
| **Non-current liabilities** | | | |
| Loans and borrowing | 19 | **(1,154)** | (1,062) |
| Deferred consideration | | **-** | - |
| Deferred tax liabilities | 9 | **(30)** | (42) |
| | | **(1,184)** | (1,104) |
| **Total liabilities** | | **(1,816)** | (1,775) |
| | | | |
| **Net assets** | | **391** | 4,078 |
| | | | |
| **Capital and reserves** | | | |
| Called up share capital | 21 | **635** | 287 |
| Share premium | 21 | **12,446** | 11,370 |
| Merger reserve | 22 | **946** | 946 |
| Shares to be issued reserve | 22 | **-** | 37 |
| Convertible bond option reserve | 19, 22 | **164** | 164 |
| Share based payment reserve | 22 | **153** | 210 |
| Deficit in retained earnings | | **(13,953)** | (8,936) |
| **Equity attributable to equity holders** | | **391** | 4,078 |

The Company's loss for the year ended 31 December 2018 was €5,017,000 (2017: €7,694,000).

**Anthony Reeves**
Executive Chairman

**Raffaele Boccardo**
Deputy Executive Chairman

# Consolidated statement of cash flows

| | Note | **Year ended 31 December 2018 €000** | Year ended 31 December 2017 €000 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Loss for the year | | **(3,786)** | (11,801) |
| Income tax credit | | **(11)** | (235) |
| Loss before tax | | **(3,797)** | (12,036) |
| *Adjustments to reconcile loss before tax to net cash flows:* | | | |
| Net interest expense | 8 | **278** | 184 |
| Depreciation of property, plant and equipment | 0 | **43** | 48 |
| Amortisation of intangible assets | 12 | **1,881** | 1,292 |
| Impairment of intangible assets | 12 | **-** | 6,286 |
| Impairment of trade receivables | 14 | **1,349** | 3,021 |
| Share based payments (credit)/expense | 21 | **(94)** | 52 |
| **Operating cash flows before movements in working capital** | | **(340)** | (1,153) |
| (Increase)/decrease in trade and other receivables | | **(706)** | 1,011 |
| Increase/(decrease) in trade and other payables | | **1,452** | (1,738) |
| Decrease in provisions | | **(1,255)** | (86) |
| | | **(509)** | (813) |
| Interest paid | | **(278)** | (146) |
| Tax paid | | **(243)** | (215) |
| **Net cash flow from operating activities** | | **(1,370)** | (2,327) |
| ***Investing activities*** | | | |
| Purchase of property, plant and equipment | 0 | **(12)** | (51) |
| Development costs – internally and contractor developed | 12 | **(490)** | (1,828) |
| **Net cash used in investing activities** | | **(502)** | (1,879) |
| ***Financing activities*** | | | |
| Net proceeds from issue of share capital | 21 | **1,424** | 3,440 |
| Proceeds from borrowings | 19, 23 | **72** | 1,750 |
| Repayment of borrowings | 19, 23 | **(458)** | (1,070) |
| **Net cash from financing activities** | | **1,038** | 4,120 |
| **Net decrease in cash and cash equivalents** | | **(834)** | (86) |
| Cash and cash equivalents at 1 January | | **929** | 1,015 |
| **Cash and net cash equivalents at 31 December** | 15 | **95** | 929 |

# Company statement of cash flows

| | Note | **Year ended 31 December 2018 €000** | Year ended 31 December 2017 €000 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Loss for the year | | **(5,017)** | (7,695) |
| Income tax credit | | **(12)** | (5) |
| Loss before tax | | **(5,029)** | (7,700) |
| *Adjustments to reconcile loss before tax to net cash flows:* | | | |
| Net interest income | | **72** | (92) |
| Amortisation of intangible assets | 12 | **-** | 101 |
| Impairment of investments | 13 | **-** | 65 |
| Impairment of loans to subsidiary | | **2,897** | 6,404 |
| Share based payments expense | 22 | **(94)** | 54 |
| **Operating cash flows before movements in working capital** | | **(2,154)** | (1,168) |
| (Increase)/decrease in trade and other receivables | | **(14)** | 262 |
| Increase/(decrease) in trade and other payables | | **334** | (867) |
| Increase/(decrease) in provisions | | **(219)** | 17 |
| | | **101** | (588) |
| Interest received | | **-** | - |
| Interest paid | | **(72)** | (108) |
| Tax paid | | **-** | - |
| **Net cash flow from operating activities** | | **(2,125)** | (1,864) |
| ***Investing activities*** | | | |
| Development costs – internally and contractor developed | 12 | **-** | (1,869) |
| Investment in subsidiary | 13 | **(80)** | - |
| Loans to subsidiary | | **-** | (533) |
| **Net cash used in investing activities** | | **(80)** | (2,402) |
| ***Financing activities*** | | | |
| Net proceeds from issue of share capital | 21 | **1,424** | 3,440 |
| Proceeds from borrowings | 19, 24 | **-** | 1,358 |
| Repayment of borrowings | 19, 24 | **(63)** | (716) |
| **Net cash from financing activities** | | **1,361** | 4,082 |
| **Net increase in cash and cash equivalents** | | **(844)** | (184) |
| Cash and cash equivalents at 1 January | | **860** | 1,043 |
| **Cash and net cash equivalents at 31 December** | 15 | **16** | 859 |

# Consolidated statement of changes in equity

| | Share capital €000 | Share premium account €000 | Merger reserve €000 | Shares to be issued reserve €000 | Convertible bond option reserve €000 | Share based payment reserve €000 | Retained earnings €000 | Total €000 | Non Controlling Interests €000 | Total equity €000 |
|---|---|---|---|---|---|---|---|---|---|---|
| **As at 1 January 2017** | **197** | **5,542** | **1,641** | **-** | **0** | **156** | **2,093** | **9,629** | **21** | **9,650** |
| Profit / (loss) for the year | - | - | - | - | - | - | (11,641) | (11,641) | (160) | (11,801) |
| Shares issued | 90 | 5,828 | - | - | - | - | - | 5,918 | 4 | 5,922 |
| Shares to be issued | - | - | - | 37 | - | - | - | 37 | - | 37 |
| Convertible bond issue | - | - | - | - | 164 | - | - | 164 | - | 164 |
| Share based payments | - | - | - | - | - | 54 | - | 54 | - | 54 |
| **As at 31 December 2017** | **287** | **11,370** | **1,641** | **37** | **164** | **210** | **(9,548)** | **4,161** | **(135)** | **4,026** |
| Loss for the year | **-** | **-** | **-** | **-** | **-** | **-** | **(3,730)** | **(3,730)** | **(56)** | **(3,786)** |
| Shares issued | **348** | **1,076** | **-** | | **-** | **-** | **-** | **1,424** | **-** | **1,424** |
| Shares to be issued | - | - | - | **(37)** | - | - | - | **(37)** | - | **(37)** |
| Share based payments | **-** | **-** | **-** | **-** | **-** | **(57)** | **-** | **(57)** | **-** | **(57)** |
| **As at 31 December 2018** | **635** | **12,446** | **1,641** | **-** | **164** | **153** | **(13,278)** | **1,761** | **(191)** | **1,570** |

# Company statement of changes in equity

| | Share capital €000 | Share premium account €000 | Merger reserve €000 | Shares to be issued reserve €000 | Convertible bond option reserve €000 | Share based payment reserve €000 | Retained earnings €000 | Total €000 |
|---|---|---|---|---|---|---|---|---|
| **As at 1 January 2017** | **197** | **5,542** | **946** | **-** | **-** | **156** | **(1,242)** | **5,599** |
| Loss for the year | - | - | - | - | - | - | (7,694) | (7,694) |
| Shares issued | 90 | 5,828 | - | - | - | - | - | 5,918 |
| Shares to be issued | - | - | - | 37 | - | - | - | 37 |
| Convertible bond issue | - | - | - | - | 164 | - | - | 164 |
| Share based payments | - | - | - | - | - | 54 | - | 54 |
| **As at 31 December 2017** | **287** | **11,370** | **946** | **37** | **164** | **210** | **(8,936)** | **4,078** |
| Loss for the year | **-** | **-** | **-** | **-** | **-** | **-** | **(5,017)** | **(5,017)** |
| Shares issued | **348** | **1,076** | **-** | **-** | **-** | **-** | **-** | **1,424** |
| Shares to be issued | - | - | - | **(37)** | - | - | - | **(37)** |
| Share based payments | **-** | **-** | **-** | **-** | **-** | **(57)** | **-** | **(57)** |
| **As at 31 December 2018** | **635** | **12,446** | **946** | **-** | **164** | **153** | **(13,953)** | **391** |

# Notes to the consolidated financial statements

Defenx PLC is a public limited company incorporated in the UK on 11 April 2014, trading from 105 Victoria Street, London, SW1E 6QT. The Company's ordinary shares are traded on AIM. The consolidated financial statements comprise Defenx PLC and its subsidiaries, Defenx SA, a company incorporated in Switzerland, and Defenx Italia SRL (formerly Memopal SRL), a company incorporated in Italy (together referred to as the "Group"), for the year ended 31 December 2018.

The Company has taken advantage of the exemption available under section 408 of the Companies Act 2006 and has not presented the parent's own income statement. The parent's loss for the period ended 31 December 2018 amounted to €5,017,000 (2017: €7,694,000).

## 1. Basis of preparation

These financial statements have been prepared in accordance with International Financial Reporting Standards and Interpretations (collectively IFRSs) issued by the International Accounting Standards Board (IASB) as adopted by the European Union (adopted IFRSs).

The preparation of the financial statements in compliance with adopted IFRSs requires the use of certain critical accounting estimates. It also requires management to exercise judgement in applying the accounting policies. The areas where significant judgements and estimates have been made in preparing the financial statements and their effect are disclosed in note 3.

### *Basis of measurement*

These financial statements have been prepared on a historical cost basis, except for the following items (refer to individual accounting policies for details):

- Financial instruments – fair value through profit or loss
- Financial instruments – available for sale
- Contingent consideration
- Net defined benefit liability
- Cash-settled share-based payment liabilities.

### *Basis of consolidation: business combinations and merger accounting*

The financial statements have been prepared on a consolidated basis in line with the principles laid out in IFRS 3: *Business Combinations*. The Group's accounting policy on business combinations is set out in note 2a) below.

The standard states that in instances where group reconstructions have taken place, such as in the case of a share for share exchange, guidance should be taken from the appropriate national GAAP in preparing the financial statements. The Directors have therefore considered the implications of UK FRS 6: *Acquisitions and Mergers* and considered it appropriate to adopt merger accounting in respect of the acquisition of Defenx SA by the parent company in 2014. This resulted in a merger reserve in the consolidated statement of financial position, being the difference between the nominal value of new shares issued by the parent company for the acquisition of the shares and the subsidiary's own issued share capital.

The merger reserve is also used where more than 90% of the shares in a subsidiary are acquired and the consideration includes the issue of new shares by the parent company, thereby attracting merger relief under the Companies Act 2006.

### *Going concern*

The strategic report outlines the activities of the Group along with factors which may affect its future development and performance. The Group's financial position is discussed in the Financial Review along with details of its cash flow and liquidity.

As at 31 December 2018 the Group had net assets of €1.57 million (31 December 2017: €4.03 million) as set out in the consolidated statement of financial position. The Directors have prepared detailed forecasts of the Group's performance for the two years commencing 1 January 2019. The forecasts contain certain assumptions about the level of future sales, margins and the level of cash recovery from trading, taking a more conservative view than the forecasts considered in determining the impairment of intangible fixed assets.

As at 24 July 2019, the Group had cash resources of approximately €120,000, which is sufficient through to the end of August 2019, and, therefore, the Company remains reliant on the continued financial support of its major shareholder, BV Tech, going forward. BV Tech has provided a non binding letter of support for €350,000 in this regard.

During 2017, BV Tech subscribed for an aggregate €1.43 million in ordinary shares in the Company. In April 2018, by way of a subscription and underwritten open offer, BV Tech invested a further €1.08 million in the Company. On 1 October 2018 a loan agreement was entered into with BV Tech, whereby BV Tech provided an unsecured loan of €0.95 million with repayment due by 1 January 2020. The loan was then amended such that it became a convertible loan of the same quantum and on the same material terms.

In April 2019, Defenx Italia SRL signed a sales and distribution agreement with BV Tech with two main elements. The first gives sole rights to sell Defenx products to certain organisations within the Italian defence, space, national security and critical infrastructures sectors until December 2023. The second appointed BV Tech as a (non-exclusive) distributor of Defenx products generally. The contractual value of the former is €1m plus 50% of any sales in excess of €5m and under the latter, a commitment to purchase products to a minimum value of €150,000 per quarter (total €1.2m) up to December 2020. Together, these agreements give a substantial minimum sales revenue and cash inflow.

After considering the forecasts and the risks, the Directors recognise the uncertainty over future performance, consider it attainable and are satisfied that the Group has adequate resources to continue in operational existence for the foreseeable future with the continued support of its major shareholder, BV Tech, and, accordingly, continue to adopt the going concern basis in preparing the Group and Company financial statements.

## 2. Principal accounting policies

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies are consistent with those applied in the prior financial year and are applied by all Group entities unless otherwise stated.

### *a) Business combinations and goodwill*

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred, which is measured at acquisition date fair value, and the amount of any non-controlling interests in the acquiree. For each business combination, the Group elects whether to measure the non-controlling interests in the acquiree at fair value or at the proportionate share of the acquiree's identifiable net assets. Acquisition related costs are expensed as incurred and included in administrative expenses.

When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date.

Any contingent consideration to be transferred by the acquirer will be recognised at fair value at the acquisition date. Contingent consideration classified as an asset or liability that is a financial instrument and within the scope of IAS39 *Financial Instruments: Recognition and Measurement*, is measured at fair value with the changes in fair value recognised in the statement of income.

Goodwill is initially measured at cost (being the excess of the aggregate of the consideration transferred and the amount recognised for non-controlling interests and any previous interest held over the net identifiable assets acquired and liabilities assumed). If the fair value of the net assets acquired is in excess of the aggregate consideration transferred, the Group re-assesses whether it has correctly identified all of the assets acquired and all of the liabilities assumed and reviews the procedures used to measure the amounts to be recognised at the acquisition date. If the reassessment still results in an excess of the fair value of net assets acquired over the aggregate consideration transferred, then the gain is recognised in profit or loss.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash generating units (CGU) that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units.

Where goodwill has been allocated to a CGU and part of the operation within that unit is disposed of, the goodwill associated with the disposed operation is included in the carrying amount of the operation when determining the gain or loss on disposal. Goodwill disposed in these circumstances is measured based on the relative values of the disposed operation and the portion of the cash-generating unit retained.

### *b) Revenue recognition*

Revenue is recognised to the extent that it is probable that economic benefits will flow to the Group and the revenue can be reliably measured in accordance with IFRS 15 *Revenue from Contracts with Customers*. Revenue is measured at the fair value of the consideration received or receivable for the sale of goods or services provided in the normal course of business, net of all related discounts and sales taxes.

The Group's revenues to date comprise sales of software licences, the majority of which are for 12 months with a limited number for two, three and five years. These term-based agreements include free upgrades and enhancements on a when-and-if-available basis. The Group recognises the software licence portion of revenue at the time of delivery while the portion attributable to upgrades and enhancements is deferred and recognised in the statement of comprehensive income on a straight-line basis over the period of the relevant agreement.

To the extent that the related trade receivable has not been settled in cash, deferred revenue is not recognised in the statement of comprehensive income but transferred and offset against the trade receivables balance in the statement of financial position.

Customers have no right of return; once sold, licences are neither refundable nor returnable. However, where it is in the commercial interests of the Group, management may negotiate the return or exchange of unsold licences.

### *c) Foreign currency*

The Group's and the Company's functional and presentation currency is the Euro.

Transactions in foreign currencies are initially recorded at the respective functional currency rates ruling when the transactions occurred. Foreign currency monetary assets and liabilities are translated at the rates ruling on the reporting date. Differences arising on settlement or translation are recognised in profit or loss. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions.

### *d) Trade and other receivables*

Trade receivables are stated at fair value, being the lower of their original invoiced value and recoverable amount. A provision for impairment is made where there is objective evidence that the Group will not be able to recover balances in full. Indications of impairment include customers in financial difficulty or seriously in default against agreed payment terms. There is no material variance between carrying and fair values.

### *e) Property, plant and equipment*

Property, plant and equipment are recognised initially at cost. After initial recognition, these assets are carried at cost less any accumulated depreciation and impairment losses. Cost comprises the aggregate amount paid, and the fair value of any other consideration given to acquire the asset.

Depreciation is calculated on a straight-line basis over the estimated useful lives of the assets, and is applied separately to each identifiable component, as follows:

- Cloud equipment 3 to 7 years
- Office equipment 5 to 10 years

An item of property, plant and equipment and any significant part initially recognised is de-recognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on de-recognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the statement of profit or loss when the asset is de-recognised.

The residual values, useful lives and methods of depreciation of property, plant and equipment are reviewed at each financial year end and adjusted prospectively, if appropriate.

### *f) Intangible assets*

Identifiable intangible assets are recognised when the Group controls the asset, it is probable that future economic benefits attributable to the asset will flow to the Group and the cost of the asset can be reliably measured. Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is their fair value at the date of acquisition.

Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and accumulated impairment losses. Internally generated intangibles, excluding capitalised development costs, are not capitalised and the related expenditure is reflected in profit or loss in the period in which the expenditure is incurred.

Research costs are expensed as incurred. Development expenditures on an individual project are recognised as an intangible asset when the Group can demonstrate:

- The technical feasibility of completing the intangible asset so that the asset will be available for use or sale
- Its intention to complete and its ability and intention to use or sell the asset
- How the asset will generate future economic benefits
- The availability of resources to complete the asset
- The ability to measure reliably the expenditure during development

Following initial recognition of the development expenditure as an asset, the asset is carried at cost less any accumulated amortisation and accumulated impairment losses. Amortisation of the asset begins when development is complete, and the asset is available for use. It is amortised over the period of expected future benefit. Amortisation is recorded in cost of sales. During the period of development, the asset is tested for impairment annually.

Amortisation is calculated on a straight-line basis over the estimated useful lives of the assets, and is applied separately to each identifiable component, as follows:

- Development costs 3 to 5 years
- Customer relationships 3 years

### g) *Impairment of assets*

At each balance sheet date, the Directors review the carrying amounts of property, plant, equipment and intangible assets to determine whether there is any indication that those assets have suffered an impairment. If any such indication exists, the recoverable amount of the asset, which is the higher of its fair value less costs to sell and its value in use, is estimated in order to determine the extent of the impairment loss. Where the asset does not generate cash flows that are independent of other assets, the Directors estimate the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amounts are based on a calculation of expected future cash flows discounted to their present value using pre-tax discount rates that reflect market assessments of the time value of money and risks specific to the asset for which the expected future cash flows have not been adjusted.

Any impairment charge is recognised in the statement of income in the period in which it occurs for assets carried at cost if the recoverable amount is less than the carrying value. Where an impairment loss subsequently reverses due to a change in the original estimate, the carrying amount of the asset is increased to the lower of the initial costs and the revised estimate of its recoverable amount.

### h) *Research and development tax credits*

Defenx Italia SRL received R&D tax credits in Italy in the year. On the basis that these are not calculated as a function of profits and the benefit can also be offset against tax liabilities other than taxes on profits, the most appropriate basis for accounting is under IAS20 relating to government grants.

Accordingly, the recoverable amount is disclosed as a current or non-current asset as appropriate.

The tax credit also forms a subsidy against the cost of the underlying intangible asset. This element is shown separately within Deferred Revenue (rather than netted off against the carrying value of the asset) and is released to the consolidated statement of comprehensive income to offset the part of the amortisation charge relating to the subsidised element of the asset cost.

### i) *Pension costs*

The Group makes defined contributions to its employees' pension plans according to the laws of the country of employment. The pension costs charged in the financial statements represent the contributions payable by the Group and Company during the year.

### j) *Share-based payments*

In accordance with IFRS 2 Share-based payments reflects the economic cost of awarding shares and share options to employees and Directors by recording an expense in the statement of income equal to the fair value of the benefit awarded. The expense is recognised in the statement of income over the vesting period of the award with a corresponding increase in equity via the share-based payment reserve.

Fair value is measured by the use of a Black-Scholes model, which takes into account conditions attached to the vesting and exercise of the options. The expected life used in the model is adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions and behavioural considerations.

Where awards are granted to employees of the subsidiary, the fair value of the award at grant is recorded in the parent company's financial statements as an increase in the value of the investment with a corresponding increase in equity via the share-based payment reserve.

The dilutive effect of outstanding options is reflected as additional share dilution in the computation of diluted earnings per share.

### k) *Leased assets and obligations*

Leases are classified as finance leases when the terms of the lease transfer substantially all the risks and rewards of ownership to the Group. All other leases are classified as operating leases.

### *l) Operating leases*

Assets leased under operating leases are not recorded on the statement of financial position. Rental payments are charged directly to the statement of income on a straight-line basis over the lease term.

### *m) Current and deferred taxation*

Current tax is the expected tax payable on taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustments to tax payable in respect of previous years.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profits ('temporary differences') and is accounted for using the balance sheet liability method.

Deferred tax liabilities are generally recognised for all taxable temporary differences.

Deferred tax assets are generally recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Where there are deductible temporary differences arising in subsidiaries, deferred tax assets are recognised only where it is probable that they will reverse in the foreseeable future and taxable profits will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled, or the asset is realised. Deferred tax is charged or credited to the statement of income.

### *n) Cash and cash equivalents*

Cash and cash equivalents includes cash in hand, deposits held with banks, other short-term highly liquid investments with original maturities of three months or less and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities in the statement of financial position.

### *o) Trade and other payables*

Trade payables are recognised at fair value. There is no material variance between book and fair values.

### *p) Borrowings*

Bank loans and overdrafts are recorded initially at their fair value, net of direct transaction costs and finance charges and are recognised in the statement of income over the term of the instrument. There is no material variance between book and fair values.

### *q) Convertible debt*

The proceeds received on issue of the Group's convertible debt are allocated into their liability and equity components. The amount initially attributed to the debt component equals the discounted cash flows using a market rate of interest that would be payable on a similar debt instrument that does not include an option to convert. Subsequently, the debt component is accounted for as a financial liability measured at amortised cost until extinguished on conversion or maturity of the bond. The balance of the proceeds is allocated to the equity conversion option and is recognised in the 'Convertible debt option reserve' within shareholders' equity, net of income tax effects. Issue costs incurred are allocated between liability and equity in proportion to the value of each component.

## 3. Judgements and estimates

The Board makes judgements and assumptions concerning the future that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. The resulting accounting estimates calculated using these judgements and assumptions will, by definition, seldom equal the related actual results but are based on historical experience and expectations of future events. Actual results may differ from these estimates.

The judgements and key sources of estimation uncertainty that may have a significant effect on the amounts recognised in the financial statements are discussed below:

### *Revenue recognition (note 2b)*

Judgement is required in the assessment of licence activation timing and the resultant period over which deferred revenue is released to the statement of income. Licences can be activated immediately upon sale (e.g. for online sales), sometime after sale (e.g. through our B2B2C customers) or not at all (e.g. typically where our licences are sold as a bundle). Management has estimated the average period from which deferred revenues start to be released. The share of revenue attributable to upgrades and enhancements that is deferred represents a small proportion of total revenue. Therefore, although the period over which deferred revenue is released is uncertain, the impact on the financial statements is not materially dependent on this judgement.

### *Recovery of trade receivables*

In July 2018 compromise agreements were reached with four major customers, including a write down of the amount payable to Defenx by those customers. An impairment provision was made in 2017 to reduce the carrying value of these trade debtors to reflect the amount collectable under the agreements. In 2018, the remaining balance has been impaired to nil, because payments scheduled in 2019 have not been received.

### *Impairment of assets (note 12)*

Judgement is required in the impairment assessment of assets, notably intangible software development costs. Recoverable amounts are based on a calculation of expected future cash flows, which require assumptions and estimates of future performance to be made. Cash flows are discounted to their present value using pre-tax discount rates based on the Directors market assessment of risks specific to the asset.

## 4. Changes in accounting policies and disclosures

### *New standards adopted during the year*

There were two new standards or interpretations effective for the first time for periods beginning on or after 1 January 2018 that apply to the Group's financial statements although neither has a significant impact.

#### *IFRS 9 Financial Instruments*

IFRS 9 replaced IAS 39 for accounting periods commencing on or after 1 January 2018. It impacts the classification and measurement of financial instruments and requires certain additional disclosures. The changes to recognition and measurement of financial instruments and changes to hedge accounting rules do not have major impact on the Group's current accounting treatment or hedging activities due to the simple nature of our financial instruments. The standard also requires entities to use an expected credit loss model for impairment of financial assets instead of an incurred credit loss model.

The Directors anticipate that IFRS 9 will not have a material impact on the financial statements due to the significant impairment against trade receivables in 2017 and 2018. Future provisioning policy will reflect improved customer credit assessment and acceptance procedures as the Group shifts towards a mix of retail and direct corporate customer bases.

*IFRS 15 Revenue from Contracts with Customers*

IFRS 15 replaced IAS 18 *Revenue*, IAS 11 *Construction Contracts* and related interpretations. The standard introduced a single, five-step revenue recognition model that is based upon the principle that revenue is recognised at the point that control of goods or services is transferred to the customer. The standard also updates revenue disclosure requirements.

Defenx currently sells products as conventional term licences or on a renewing subscription basis. The software licence portion of term licence sales is recognised at the time of delivery to third party distributors who assume the risks and rewards associated with the onward sale of these licenses to end users, with the portion attributable to upgrades and enhancements deferred and recognised on a straight-line basis over the activated licence term. Subscription sales and related direct costs are wholly recognised over the subscription term once all recognition criteria are met.

The Directors specifically considered the application of IFRS 15 to the revenue recognition of the Group's term licence contracts. Having assessed the commercial arrangements with customers in the context of IFRS 15, the Board concluded that the earlier accounting policy and methodology continued to be equally appropriate under the new accounting standard. Accordingly, no change in accounting treatment arose or was been applied as a consequence of IFRS 15 and no adjustment made to either sales or deferred revenue.

***New standards, interpretations and amendments not yet effective***

There are a number of standards and interpretations which have been issued by the International Accounting Standards Board that are effective in future accounting periods that the Group has decided not to adopt early. The most significant of these is IFRS 16 Leases (mandatorily effective for periods beginning on or after 1 January 2019).
Their likely impact is as follows:

*IFRS 16 Leases*

IFRS 16 will replace IAS 17 for accounting periods commencing on or after 1 January 2019 and will require all leases to be recognised on the balance sheet. The new standard brings most leases on-balance sheet for lessees under a single model, eliminating the distinction between operating and finance leases. Instead of recognising an operating expense for its operating lease payments, the Group will instead recognise interest on its lease liabilities and amortisation on its right-of-use assets.

During the year, the Group had only one operating lease within the scope of IFRS 16 covering two vehicle leases. For the year ended 31 December 2018, reported EBITDA would have increased by the amount of its current operating lease cost, which was approximately €10,000 (2017: €nil). Therefore, the Directors anticipate that IFRS 16 will not have a material impact on the financial statements.

*Other*

None of the following other standards issued by the IASB have had, or are expected to have, a material impact on the Group:

- IFRIC 22 Foreign Currency Translations and Advance Consideration (effective 1 January 2018)
- Amendments to IFRS 2 classification and Measurement of Share-based payment Transactions (effective 1 January 2018)
- Amendments to IFRS 4: Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts (effective 1 January 2018)
- Amendments to IAS 40: Transfers of Investment Property (effective 1 January 2018)
- Annual Improvements to IFRS Standards 2014-2016 cycle dealing with matters in IFRS 1 First-time Adoption and IAS 28 Investments in Associates and Joint Ventures (effective1 January 2018)
- IFRIC 23 Uncertainty over Income Tax Positions (effective 1 January 2019)
- Amendments to IFRS 9 Prepayment Features with Negative Compensation (effective 1 January 2019)
- Amendments to IAS 28: Long-term Interests in Associates and Joint Ventures (effective 1 January 2019)
- IFRS 17 Insurance Contracts (effective 1 January 2021)

## 5. Segmental analysis

The Group operates as a single division selling three main categories of product:

- Security – anti-malware software protection for mobile, PC and network devices
- Protection – client, server and web-based applications to monitor, manage and secure the online activities of individuals, families and corporate employees
- Backup – Cloud-based backup and synchronisation solutions to protect data and securely share it

Accordingly, the Group has a single reportable segment. This is consistent with the internal reporting provided to the chief operating decision-maker, identified Executive Board Directors.

Revenue by product category for the Group is as follows:

| | **31 December 2018 €000** | 31 December 2017 €000 |
|---|---|---|
| **Revenue by product category** | | |
| Security | **874** | 2,293 |
| Backup | **545** | 614 |
| Other | **1** | 21 |
| | **1,420** | 2,928 |

Non-current assets (capitalised development costs) by product segment for the Group are as follows:

| | **31 December 2018 €000** | 31 December 2017 €000 |
|---|---|---|
| **Non-current assets by product category** | | |
| Security | **1,779** | 4,002 |
| Protection | **26** | 44 |
| Backup | **331** | 993 |
| | **2,136** | 5,039 |

Impairment losses by segment are disclosed in note 12. The Group does not analyse costs or assets other than intangible assets by product platform.

### *Geographical segments*

The Group is managed centrally and accordingly the Group does not analyse costs or assets by geographical region. Revenue by customer location is as follows:

| | **31 December 2018 €000** | 31 December 2017 €000 |
|---|---|---|
| **Revenue by geographic market (customer location)** | | |
| Europe (EU including the UK) | **1,030** | 2,203 |
| Europe (Non-EU) | **336** | 725 |
| Other | **54** | - |
| | **1,420** | 2,928 |

## 6. Operating profit

| The operating loss is stated after charging: | **31 December 2018 €000** | 31 December 2017 €000 |
|---|---|---|
| **Cost of sales** | | |
| External Development costs | **107** | 791 |
| Amortisation of intangible assets (note 12) | **1,881** | 1,292 |
| | | |
| **Other operating income** | | |
| Research & development tax credit income | **(838)** | (772) |
| | | |
| **Operating expenses before transaction costs** | | |
| Marketing contributions | **-** | 1,550 |
| Impairment of trade receivables (note 14) | **1,349** | 3,020 |
| Depreciation of property, plant and equipment (note 11) | **43** | 48 |
| Impairment of intangible assets (note 12) | **-** | 6,286 |
| Staff costs (note 7) | **677** | 1,278 |
| Lease payments – land and buildings | **103** | 116 |
| Lease payments – plant and machinery | **10** | 139 |
| AIM listing and related costs | **289** | 234 |
| Net foreign exchange losses/(gains) | **4** | (61) |
| Share based payment expense (Note 21) | **(153)** | 54 |
| | | |
| **Transaction costs** | | |
| Costs in respect of the strategic partnership with BV Tech | **-** | 101 |
| | | |
| **Auditors' remuneration (included within administrative expenses)** | | |
| *Audit services* | | |
| Parent company and group audit | **35** | 26 |
| Audit of the parent company's subsidiary | **-** | 23 |
| *Non-audit services* | | |
| Tax compliance and other fees | **4** | 9 |
| Total auditors' remuneration | **58** | 58 |

In 2018, €156,000 (2017:€234,000) of share issuance costs in respect of the Open Offer in April 2018 and subscriptions by BV Tech and placing in April and August 2017 were charged to the share premium account.

## 7. Staff Costs

Staff costs (including Directors' emoluments) incurred in the year were as follows:

| | **31 December 2018 €000** | 31 December 2017 €000 |
|---|---|---|
| Wages and salaries | **620** | 1,057 |
| Social security costs | **82** | 142 |
| Pension costs | **32** | 25 |
| Share based payments expense | **(57)** | 54 |
| | **677** | 1,278 |

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

| | **31 December 2018 Number** | 31 December 2017 Number |
|---|---|---|
| Executive Directors* | **1** | 2 |
| Sales & marketing* | **3** | 4 |
| Research, development & operations | **3** | 7 |
| Administration* | **2** | 2 |
| | **9** | 15 |
| * of which employed by the Company | 2 | 4 |

| | **€000** | €000 |
|---|---|---|
| **Directors' emoluments** | | |
| Emoluments (including non-executive Directors' fees) | **241** | 402 |

| | **€** | € |
|---|---|---|
| **Highest paid Director** | | |
| Emoluments | **94** | 132 |

Included in directors' emoluments is €5,000 (2017: €15,000) in respect of payments to defined contribution pension schemes.

## 8. Finance income and expenses

| | **31 December 2018 €000** | 31 December 2017 €000 |
|---|---|---|
| **Finance income** | | |
| Interest income | **-** | 1 |
| **Finance expense** | | |
| Bank overdrafts, loans, invoice discounting and other | **4** | 18 |
| Supply chain finance | **20** | 49 |
| Vendor loans | **2** | 39 |
| Convertible bond | **252** | 78 |
| | **278** | 184 |

## 9. Taxation

No liability to UK, Swiss or Italian income tax arose on ordinary activities for the year ended 31 December 2018. The tax (credit)/charge for 2017 was as follows:

| | **31 December 2018 €000** | 31 December 2017 €000 |
|---|---|---|
| **Current tax** | | |
| Current tax on loss for the year | **-** | - |
| Adjustment for over provision in prior periods | **-** | (224) |
| | **-** | (224) |
| **Deferred tax** | | |
| Origination and reversal of temporary differences | **(11)** | (11) |
| **Total income tax expense** | **(11)** | (235) |

The reasons for the difference between the actual income tax charge for the year and the standard rate of corporation tax in the UK applied to the profit for the year are as follows:

| | **31 December 2018 €000** | 31 December 2017 €000 |
|---|---|---|
| Loss for the year | **(3,786)** | (11,801) |
| Tax credit | **(11)** | (235) |
| Loss before tax | **(3,797)** | (12,036) |
| | | |
| **Tax using Defenx PLC's domestic tax rate of 19% (2017: 19.25%)** | **(721)** | (2,317) |
| Expenses not deductible for tax purposes | **(14)** | 217 |
| Research & development tax credits | **(159)** | (185) |
| Adjustment for over provision in prior periods | **-** | (200) |
| Temporary timing differences | **(57)** | 1,509 |
| Effect of higher tax rates in Italy and Switzerland | **-** | (85) |
| Losses carried forward for future offset | **951** | 837 |
| **At the effective income tax rate** | **-** | (224) |

The aggregate tax rate in Switzerland was 20% during the year (2017: 20.0%). The corporation tax rate in the UK was reduced from 20% to 19% effective 1 April 2017 and 17% effective 1 April 2020.

The accumulated tax losses available to the Group at 31 December 2018 were €9.3 million (2017: €4.2 million). These losses relate to activities and are available indefinitely for offsetting against future taxable profits, of Defenx PLC in the UK, Defenx SA in Switzerland and Defenx Italia SRL in Italy. Losses have, where permitted, been carried back for offset against prior year tax payable. Loss carry back is not permitted in Switzerland.

Deferred tax is calculated in full on temporary differences under the liability method using tax rates of 19%, (2017: 19.25%, 24% (2017: 24.0%) and 20% (2017: 20.0%) being the respective effective rates of tax applicable in UK, Italy and Switzerland where the deferred tax arises. There were no deferred tax liabilities arising from these calculations at the year end.

No deferred tax asset is recognised in respect of either temporary timing differences or accumulated tax losses as it is not sufficiently certain that the Group will be able to utilise them in the near future. Accordingly, the deferred tax credit for the financial year relates to the release of the brought forward deferred tax liability as follows:

| | Consolidated statement of financial position | | Consolidated statement of income | |
|---|---|---|---|---|
| | **31 December 2018 €000** | 31 December 2017 €000 | **31 December 2018 €000** | 31 December 2017 €000 |
| Accelerated amortisation for accounts purposes | **-** | - | **-** | (80) |
| Disallowed bad debt provision | **-** | - | **-** | (59) |
| Other timing differences | **(30)** | (42) | **(11)** | 49 |
| Arising on acquisition of Defenx Italia SRL | **-** | - | **-** | 79 |
| Deferred tax (income)/expense | | | **(11)** | (11) |
| Net deferred tax (liability) | **(30)** | (42) | | |

If the Group were able to recognise all unrecognised deferred tax assets, the deficit in retained earnings would decrease by €1.1 million (2017: €0.76 million).

## 10. Earnings per share (EPS)

Basic EPS amounts are calculated by dividing the (loss)/profit for the year attributable to ordinary equity holders of the parent company, Defenx, by the weighted average number of ordinary shares outstanding during the year.

Diluted EPS amounts are calculated by dividing the (loss)/profit attributable to ordinary equity holders by the weighted average number of ordinary shares outstanding during the year plus the number of shares that the convertible bond would convert into plus the weighted average number of ordinary shares that would be issued on the exercise of dilutive options (note 21).

The following reflects the income and share data used in the basic and diluted EPS computations:

| | **31 December 2018 €000** | 31 December 2017 €000 |
|---|---|---|
| Loss attributable to equity holders of the parent for basic EPS | **(3,730)** | (11,641) |
| Effect of: | | |
| - interest on convertible bond | **77** | 77 |
| - tax effect of above items | **(15)** | (15) |
| | **(3,668)** | (11,579) |
| | | |
| Weighted average number of ordinary shares for basic EPS | **23,812** | 11,237 |
| Effect of: | | |
| - dilution from convertible bond | **625** | 625 |
| - dilution from deferred shares | **-** | - |
| - dilution from share options and warrants | **-** | - |
| - contingent shares on acquisition of Defenx Italia SRL | **-** | - |
| Weighted average number of ordinary shares for diluted EPS | **24,437** | 11,862 |

Relevant transactions involving ordinary shares or potential ordinary shares since 31 December 2018 are set out in note 27.

## 11. Property, plant and equipment

| | Cloud equipment €000 | Office equipment €000 | Total €000 |
|---|---|---|---|
| **Cost** | | | |
| At 1 January 2017 | 193 | 275 | 468 |
| Additions | 41 | 10 | 51 |
| At 31 December 2017 | 234 | 285 | 519 |
| Additions | 12 | - | 12 |
| **At 31 December 2018** | **246** | **285** | **531** |
| | | | |
| **Accumulated depreciation** | | | |
| At 1 January 2017 | 115 | 221 | 336 |
| Depreciation charge | 23 | 25 | 48 |
| At 31 December 2017 | 138 | 246 | 384 |
| Depreciation charge | 40 | 3 | 43 |
| **At 31 December 2018** | **178** | **249** | **427** |
| | | | |
| **Net book value** | | | |
| At 31 December 2017 | 96 | 39 | 135 |
| **At 31 December 2018** | **68** | **36** | **104** |

There was no property, plant and equipment held under finance leases. There was no property, plant and equipment in the statement of financial position of the Company.

## 12. Intangible assets

*Group*

| | Goodwill €000 | Development costs €000 | Customer relationships €000 | Total €000 |
|---|---|---|---|---|
| **Cost** | | | | |
| At 1 January 2017 | 1,139 | 8,133 | 354 | 9,626 |
| Additions – internally and contractor developed | - | 1,828 | - | 1,828 |
| Additions – purchased for shares | - | 2,674 | - | 2,674 |
| At 31 December 2017 | 1,139 | 12,635 | 354 | 14,128 |
| Additions – internally and contractor developed | - | 490 | - | 490 |
| **At 31 December 2018** | **1,139** | **13,125** | **354** | **14,618** |
| **Accumulated amortisation** | | | | |
| At 1 January 2017 | - | 1,597 | 49 | 1,646 |
| Amortisation charge | - | 1,174 | 118 | 1,292 |
| Impairment charge | 1,139 | 4,960 | 187 | 6,286 |
| At 31 December 2017 | 1,139 | 7,731 | 354 | 9,224 |
| Amortisation charge | - | 1,881 | - | 1,881 |
| **At 31 December 2018** | **1,139** | **9,612** | **354** | **11,105** |
| **Net book value** | | | | |
| At 31 December 2017 | - | 4,904 | - | 4,904 |
| **At 31 December 2018** | **-** | **3,513** | **-** | **3,513** |

Development costs represent qualifying expenditure on the development of software products for resale less accumulated amortisation and impairment costs. The amortisation period of development costs is three years from the time the asset is brought into use. The additions made in 2018 were not brought into use until 2019.

Development costs of €0.5 million (2017: €6.9 million) for products under development at the year-end have not yet been launched or amortised. The Group has no contractual commitments for development costs at 31 December 2018 (2017: €nil) but in April 2019 committed to development spend with BV Tech during 2019 of €1.2 million.

### *Impairment*

The Group is required to test, on an annual basis, whether goodwill and intangibles have suffered any impairment or when there are indications that the value of the assets might be impaired. The recoverable amount is determined based on value in use calculations. The use of this method requires the estimation of future cash flows and the determination of a discount rate in order to calculate the present value of the cash flows.

If the recoverable amount is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is recognised as an expense immediately in the statement of income. Goodwill is considered impaired if the carrying value of the cash-generating unit to which it relates is greater than the higher of fair value less costs of disposal and the value in use. Goodwill is allocated to the Group's Backup segment cash-generating unit.

The Group has assessed the net present value of individual products held as development costs against forecasts of future sales of the related products, unit sales prices and costs over a five-year period. No sales beyond five years have been included in the calculations.

In October 2017, the Group announced that the delivery of product updates to address certain recently-identified performance issues and back-end integration was taking longer than expected and that previously anticipated sales orders were unlikely to be recognised in 2017, with a corresponding adverse impact on the Group's financial performance for the year to 31 December 2017. This had an adverse impact on the value in use of certain products in that year resulting in the following impairments:

| | *Group* | | *Company* | |
|---|---|---|---|---|
| | **31 December 2018 €000** | 31 December 2017 €000 | **31 December 2018 €000** | 31 December 2017 €000 |
| **Development costs** | | | | |
| Security | - | 3,292 | - | - |
| Protection | - | 1,668 | - | - |
| Backup | - | 1,326 | - | - |
| | **-** | **6,286** | **-** | **-** |

The key assumptions in the value in use calculations are:

| | **31 December 2018** | 31 December 2017 |
|---|---|---|
| Gross margin | **60-85%** | 60-85% |
| Future marketing contributions | **0%** | 0% |
| Discount rate | **25%** | 25% |

Gross margins have been based on past experience and future expectations in the light of anticipated economic and market conditions. Discount rates are based on the Group's WACC adjusted to reflect the Directors' assessment of specific risks related to the cash generating unit. Growth rates beyond the first two years are based on economic data pertaining to the region concerned.

Future events may cause these assumptions to change, which could have an adverse effect on the future results of the Group.

### *Company*

The Company's intangible assets all relate to capitalised software development costs.

| | Development costs €000 | Total €000 |
|---|---|---|
| **Cost** | | |
| At 1 January 2017 | 1,830 | 1,830 |
| Additions – internally developed | 1,869 | 1,869 |
| Additions – purchased | 2,674 | 2,674 |
| Transferred to Defenx Italia SRL | (6,373) | (6,373) |
| At 31 December 2017 and 31 December 2018 | - | - |
| **Accumulated amortisation** | | |
| At 1 January 2017 | - | - |
| Amortisation charge | 101 | 101 |
| Transferred to Defenx Italia SRL | (101) | (101) |
| At 31 December 2017 and 31 December 2018 | - | - |
| **Net book value** | | |
| At 31 December 2017 | - | - |
| **At 31 December 2018** | - | - |

## 13. Investment in subsidiaries

The following subsidiary undertakings have been included in the financial statements:

| *Name* | *Country of incorporation and principal place of business* | *Ownership* | *Non-controlling interests* |
|---|---|---|---|
| Defenx SA | Via Obino 14, Castel San Pietro 6874, Switzerland | 100.0% | - |
| Defenx Italia SRL (formerly Memopal SRL) | Via Larga 7, 20122 Milan, Italy | 95.2% | 4.8% |

Both subsidiaries have only one class of ordinary share.

Both subsidiaries' principal activity is that of the parent, namely the development, provision and distribution of software solutions.

The movement in investments in the Company's statement of financial position is:

| | **31 December 2018 €000** | 31 December 2017 €000 |
|---|---|---|
| Opening balance 1 January | **1,779** | 1,844 |
| Additions | **80** | - |
| Impairment charge | **-** | (65) |
| Closing balance at 31 December | **1,859** | 1,779 |

In December 2018, the ordinary share capital of Defenx Italia SRL was increased by €80,059 with the Company's contribution settled in cash. There was no change in the Group's ownership interest.

Due to a procedural oversight, the 2017 accounts for Defenx SA have not yet been filed with the Swiss authorities. This omission is in the process of being rectified.

Subsidiaries profit/(loss) and capital and reserves

| | *Profit/(loss)* | | *Capital and reserves* | |
|---|---|---|---|---|
| | **31 December 2018 €000** | 31 December 2017 €000 | **31 December 2018 €000** | 31 December 2017 €000 |
| Defenx SA | **(1,800)** | (6,525) | **(3,465)** | (1,665) |
| Defenx Italia SRL | **(1,164)** | (3,277) | **643** | 1,807 |

## 14. Trade and other receivables

| | *Group* | | *Company* | |
|---|---|---|---|---|
| | **31 December 2018 €000** | 31 December 2017 €000 | **31 December 2018 €000** | 31 December 2017 €000 |
| Gross trade receivables | **5,013** | 4,833 | **-** | - |
| Offset deferred revenue | **(194)** | (619) | **-** | - |
| Provision for impairment | **(4,566)** | (3,217) | **-** | - |
| **Net trade receivables** | **253** | 997 | **-** | - |
| Other receivables | **347** | 246 | **93** | 79 |
| **Total trade and other receivables** | **600** | 1,243 | **93** | 79 |
| | | | | |
| **Provisions for impairment** | | | | |
| Opening balance at 1 January | **3,217** | 196 | **-** | - |
| Utilised during the year | **-** | - | **-** | - |
| Net increase during the year | **1,349** | 3,021 | **-** | - |
| Closing balance at 31 December | **4,566** | 3,217 | **-** | - |

Gross trade receivables of €4.41 million (2017: €4.41 million) relate to customers with whom the Group is in dispute. Deferred revenues of €194,000 (2017: €619,000) due to be recognised in the statement of comprehensive income relating to these customers have been transferred from the deferred revenue balance (note 18) and offset against gross trade receivables. The provision for impairment relating to these customers has been thereby reduced correspondingly.

The movement in the impairment provision for trade receivables has been included in operating expenses in the statement of income. Other classes of financial assets included within trade and other receivables do not contain impaired assets.

At 31 December 2018, €187,000 (2017: €76,000) of trade receivables had been sold to providers of invoice discounting services. The Group is committed to underwrite any of the debts transferred and therefore continues to recognise the debts sold within trade receivables until the debtors repay or default. The proceeds from transferring the debts are included in loans and borrowing until the debts are collected or the Group makes good any losses incurred by the lender.

At the year end, all amounts shown under receivables, except offset deferred revenue, are due within one year.

The carrying value of trade and other receivables classified as financial assets approximates to fair value.

Standard business to business trade credit terms are 30 days. No credit is given for online sales.

## 15. Cash and cash equivalents

Cash and cash equivalents comprise balances on bank accounts, cash in transit and cash floats held in the business. Finance charges are accounted for on an accruals basis and charged to the statement of income when the liability is recognised.

Cash and cash equivalents are held in Euro, Sterling, Swiss Francs and US Dollars and placed on deposit in the UK, Italy and Switzerland. The carrying value of cash and cash equivalents classified as financial assets equals fair value.

## 16. Trade and other payables

| | *Group* | | *Company* | |
|---|---|---|---|---|
| | **31 December 2018 €000** | 31 December 2017 €000 | **31 December 2018 €000** | 31 December 2017 €000 |
| Trade payables | **1,592** | 424 | **623** | 149 |
| Other payables and accruals | **711** | 427 | **7** | 147 |
| **Total trade and other payables** | **2,303** | 851 | **630** | 296 |

Trade and other payables shown above are payable within one year. The carrying value of trade and other payables classified as financial liabilities measured at amortised cost approximates to fair value.

Trade payables include €880,000 payable to BV Tech, primarily for product development work, this balance being settled in full by April 2019.

## 17. Research and development tax credits

| | *Group* | | *Company* | |
|---|---|---|---|---|
| | **31 December 2018 €000** | 31 December 2017 €000 | **31 December 2018 €000** | 31 December 2017 €000 |
| At 1 January | **1,775** | - | **-** | - |
| Received during the year | **-** | 1,775 | **-** | - |
| Offset against taxes payable | **(143)** | - | **-** | - |
| At 31 December | **1,632** | 1,775 | **-** | - |
| Current | **483** | 179 | **-** | - |
| Non-current | **1,149** | 1,596 | **-** | - |

In 2017, research and development tax credits were received in Defenx Italia SRL for amounts invested in developing the Defenx software product portfolio. The tax credit can be used to offset various Italian tax liabilities such as VAT, social security and income tax. No claim has been made for 2018.

## 18. Deferred revenue

| | Group | | Company | |
|---|---|---|---|---|
| | **31 December 2018 €000** | 31 December 2017 €000 | **31 December 2018 €000** | 31 December 2017 €000 |
| At 1 January | **1,508** | 590 | **221** | - |
| Billings deferred during the year | **(93)** | 918 | **-** | 221 |
| Billings released to the statement of income | **(130)** | (384) | **(219)** | - |
| Offset against trade receivables | **(194)** | (619) | **-** | - |
| Research and development tax credit deferred during the year | **-** | 1,775 | **-** | - |
| Research and development tax credit released to the statement of income | **(838)** | (772) | **-** | - |
| At 31 December | **253** | 1,508 | **2** | 221 |
| Current | **253** | 621 | **2** | 221 |
| Non-current | **-** | 887 | **-** | - |

Deferred revenue of €194,000 (2017: €619,000) relating to certain customers has been transferred and offset against gross trade receivables (see note 14).

## 19. Loans and borrowing

The book and fair value of interest bearing loans and borrowings was:

| | | Group | | Company | |
|---|---|---|---|---|---|
| | Ultimate maturity | **31 December 2018 €000** | 31 December 2017 €000 | **31 December 2018 €000** | 31 December 2017 €000 |
| ***Current*** | | | | | |
| Overdrafts | On demand | **-** | 22 | **-** | - |
| Invoice discounting facility | Up to 120 days | **149** | 77 | **-** | - |
| Bank loans – unsecured | 30/06/2019 | **102** | 200 | **-** | - |
| Bank loans – unsecured | 22/11/2021 | **130** | 122 | **-** | - |
| Vendor loans from business combinations | 31/07/2018 | **15** | 242 | **-** | 154 |
| | | **396** | 663 | **-** | 154 |

| | | Group | | Company | |
|---|---|---|---|---|---|
| | Ultimate maturity | **31 December 2018 €000** | 31 December 2017 €000 | **31 December 2018 €000** | 31 December 2017 €000 |
| ***Non-current*** | | | | | |
| Bank loans – unsecured | 30/06/2019 | **-** | 103 | **-** | - |
| Bank loans – unsecured | 22/11/2021 | **238** | 368 | **-** | - |
| Vendor loans from business combinations | 31/07/2018 | **-** | - | **-** | - |
| Convertible bonds | 31/08/2020 | **1,154** | 1,062 | **1,154** | 1,062 |
| | | **1,392** | 1,533 | **1,154** | 1,062 |
| **Total loans and borrowing** | | **1,788** | 2,196 | **1,154** | 1,216 |

Overdrafts and other short facilities attract variable interest at between 3% and 6% per annum. The bank and vendor loans, both denominated in Euros, attract interest at 3% over 3-month EURIBOR and at 8% fixed per annum respectively. The convertible bonds (see below) carry a 10% per annum coupon. The average effective interest rate for the year ended 31 December 2018 was 7.9% (2017: 8.4%).

The currency profile of the Group's loans and borrowings was:

| | *Group* | | *Company* | |
|---|---|---|---|---|
| | **31 December 2018 €000** | 31 December 2017 €000 | **31 December 2018 €000** | 31 December 2017 €000 |
| Euro | **634** | 1,134 | **-** | 154 |
| Sterling | **1,154** | 1,062 | **1,154** | 1,062 |
| Swiss franc | **-** | - | **-** | - |
| | **1,788** | 2,196 | **1,154** | 1,216 |

At 31 December 2018, the Group had available €70,000 (2017: €720,000) of undrawn committed borrowing facilities. During the year a supply chain facility of £450,000, relating to the Company, was withdrawn.

### *UK Bond Network secured convertible bonds*

On 31 August 2017, the Company issued 1,250,000 secured convertible bonds of 10% at a face value of £1 each. Interest is paid quarterly.

The bonds are repayable three years from their issue date at a total face value of £1.25 million, can be converted at any time into shares at the rate of one share per £2 of loan ("Conversion Price") at the holder's option and can be repaid by the Company at any time on or after 31 August 2019, subject to the share price being at least 130% of the Conversion Price for 20 consecutive dealing days. During the year, the Conversion Price was adjusted to £1.808 following the issue of new ordinary shares on 23 April 2018 and £1.5118 following the convertible loan agreement made with BV Tech on 1 October 2018, as further set out in note 21 below.

The Company, Defenx SA and Defenx Italia SRL each entered into an all assets debenture and guarantee and a security trust deed (each in customary form) to provide security in respect of the convertible bonds.

Under IAS 32, the convertible bonds are accounted for as a compound financial instrument. The value of the liability component and the equity conversion component were determined at the date the instrument was issued. The fair value of the liability component, included in non-current borrowings, was calculated using a market interest rate for an equivalent instrument without conversion option with the balance recorded as a convertible debt reserve.

The issue fees of €167,000 have been allocated between liability and equity in proportion to the value of each component. The value of the liability and its associated fees is held on the balance sheet at amortised cost. This value will increase to its principal value of £1.25 million over the life of the instrument, with interest costs being taken to the Income Statement on a monthly basis.

The fair value movement on the convertible bonds was as follows:

| | **31 December 2018 €000** | 31 December 2017 €000 |
|---|---|---|
| Fair value of convertible bonds brought forward/at inception (31 August 2017) | **1,062** | 981 |
| Accrued interest not yet due for payment | **10** | 38 |
| Change in fair value of convertible bonds | **82** | 43 |
| Closing balance at 31 December | **1,154** | 1,062 |
| Current element of convertible bond liability | **-** | - |
| Non-current element of convertible bond liability | **1,154** | 1,062 |

## 20. Financial instruments and risk management

The Group is exposed through its operations to the following financial risks:

- credit risk
- fair value or cash flow interest rate risk
- foreign exchange risk
- liquidity risk

In common with all other businesses, the Group is exposed to risks that arise from its use of financial instruments. This note describes the Group's objectives, policies and processes for managing those risks and the methods used to measure them. Further quantitative information in respect of these risks is presented throughout these financial statements.

There have been no substantive changes in the Group's exposure to financial instrument risks, its objectives, policies and processes for managing those risks or the methods used to measure them from previous periods unless otherwise stated in this note.

### *General objectives, policies and processes*

The overall objective of the Board is to set policies that seek to reduce risk as far as possible without unduly affecting the Group's competitiveness and flexibility.

The Group does not use derivative financial instruments such as forward currency contracts, interest rate swaps or similar instruments. The Group does not issue or use financial instruments of a speculative nature.

### *Principal financial instruments*

The principal financial instruments used by the Group, from which financial instrument risk arises, are as follows:

- trade receivables
- cash and cash equivalents
- trade and other payables
- bank overdrafts
- floating rate bank loans

A summary of the financial instruments held by category is provided below:

| | Group | | Company | |
|---|---|---|---|---|
| | **31 December** | 31 December | **31 December** | 31 December |
| | **2018** | 2017 | **2018** | 2017 |
| ***Financial assets*** | **€000** | €000 | **€000** | €000 |
| Net trade receivables | **253** | 997 | **-** | 1 |
| Other receivables | **347** | 246 | **93** | 78 |
| Net receivables | **600** | 1,243 | **93** | 79 |
| Cash and cash equivalents | **95** | 951 | **16** | 860 |

Trade receivables principally comprise amounts outstanding for sales to customers and are typically payable between 90 and 120 days. The year-end average age of trade debtors was 151 days (2017: 183 days). An impairment review of outstanding trade receivables is carried out at each period end and, if appropriate, a specific amount provided for. A general provision is also maintained reflecting the fact that some customers are small and do not have strong credit histories.

| | Group | | Company | |
|---|---|---|---|---|
| | **Year ended** | Year ended | **Year ended** | Year ended |
| | **31 December** | 31 December | **31 December** | 31 December |
| | **2018** | 2017 | **2018** | 2017 |
| ***Financial liabilities*** | **€000** | €000 | **€000** | € |
| Trade payables | **1,592** | 424 | **623** | 149 |
| Other payables and accruals | **711** | 427 | **7** | 147 |
| Loans and borrowing | **1,788** | 2,196 | **1,154** | 1,216 |
| **Total payables** | **4,091** | 3,047 | **1,784** | 1,512 |

Trade and other payables and accruals comprise amounts outstanding for trade purchases and ongoing costs and are typically payable within 90 days. The year-end average age of trade creditors was 194 days (2017: 66 days). Where there is a contractual right of set-off with a customer that is also a supplier, notably in relation to marketing contributions payable to customers, relevant receivable and payable balances are set against one another.

### *Financial instruments not measured at fair value*

Financial instruments not measured at fair value include cash and cash equivalents, trade and other receivables, trade and other payables, and loans and borrowings.

Due to their short-term nature, the carrying value of cash and cash equivalents, trade and other receivables, trade and other payables approximates their fair value. Book values and expected cash flows are reviewed by the Board and any impairment charged to the statement of income in the relevant period.

There were no changes to the valuation techniques during the period.

### *Cash and cash equivalents*

Cash and cash equivalents comprise balances on bank accounts, cash in transit and cash floats held in the business. Finance charges are accounted for on an accruals basis and charged to the statement of income when payable. Cash and cash equivalents are held in Euro, Swiss Francs, Sterling and US Dollars and placed on deposit in UK banks.

### *Credit risk*

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations. The Group is mainly exposed to credit risk from credit sales.

The Group is exposed to credit risk in respect of these balances such that, if one or more customers encounter financial difficulties, this could materially and adversely affect the Group's financial results. The Group attempts to mitigate credit risk by assessing the credit rating of new customers prior to entering into contracts and by entering contracts with customers with agreed credit terms. The analysis below shows the ageing of trade and other receivables and the movement in bad debt provision in the year:

| | *Group* | | *Company* | |
|---|---|---|---|---|
| | **31 December 2018** | 31 December 2017 | **31 December 2018** | 31 December 2017 |
| ***Ageing of trade & other receivables*** | **€000** | €000 | **€000** | €000 |
| Not due at reporting date | **29** | 1,728 | **-** | - |
| Up to 3 months | **201** | 931 | **-** | - |
| 3 to 6 months | **225** | 71 | **-** | - |
| Above 6 months | **4,558** | 2,103 | **-** | - |
| **Gross receivables** | **5,013** | 4,833 | **-** | - |
| Offset deferred revenue | **(194)** | (619) | **-** | - |
| Less: provision against receivables | **(4,566)** | (3,217) | **-** | - |
| **Net receivables** | **253** | 997 | **-** | - |

Sales to one customer based in Turkey amounted to approximately 60% (2017: 11%) of Group billings. No other individual customer accounted for more than 5% of Group billings.

Customer credit risk is managed in accordance with the Group's established policy and procedures which did not change in the year. Customer credit quality is assessed and periodically reviewed based on available information and individual credit limits defined based on this assessment. Outstanding customer receivables are actively monitored and reviewed at least quarterly. At 31 December 2018, the Group had four customers (2017: four) that owed more than €500,000, accounting for 73% (2017: 92%) of trade receivables outstanding.

As at 31 December 2018, trade receivables of €418,000 (2017: €733,000) were past due but not impaired.

The recoverability of trade receivables is assessed on a case by case basis.

### *Fair value and cash flow interest rate risk*

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Group's exposure to the risk of changes in market interest rates relates primarily to the Group's debt obligations with floating interest rates.

The Group manages its interest rate risk while balancing the fixed and variable rates available as its loans and borrowings are renewed. The Group does not enter into interest rate swaps. At 31 December 2018, approximately 91% of the Group's borrowings are at a fixed rate of interest (2017: 59%).

The following table demonstrates the sensitivity to a reasonably possible change in interest rates on that portion of loans and borrowings affected. With all other variables held constant, the Group's profit before tax is affected by the impact on floating rate borrowings, as follows:

| | **Increase/decrease in basis points** | | **Effect on loss before tax** | |
|---|---|---|---|---|
| | **31 December 2018** | 31 December 2017 | **31 December 2018 €000** | 31 December 2017 €000 |
| Increase in Euro rates | **+100** | +100 | **-** | 9 |
| Decrease in Euro rates | **-50** | -50 | **-** | (4) |

The assumed movement in basis points for the interest rate sensitivity analysis is based on the currently observable market environment.

### *Foreign exchange risk*

Foreign exchange risk arises when Group entities enter into transactions denominated in a currency other than their functional currency. The Group's policy is, where possible, to allow customers to settle liabilities denominated in the customer's functional currency, primarily the Euro and Swiss franc.

The Group is predominantly exposed to currency risk on sales and purchases made from customers and suppliers based in the Eurozone. Sales and purchases from customers and suppliers are made on a central basis and the risk is monitored centrally, but not hedged utilising any forward exchange contracts. Apart from these particular cash flows the Group aims to fund expenses in the respective currency and to manage foreign exchange risk at a local level by matching the currency in which revenue is generated and expenses are incurred. As at 31 December 2018, the Group's net exposure to foreign exchange risk was as follows for those entities with Euro presentational currencies.

| | **Euro €000** | **Sterling €000** | **Swiss Franc €000** | **US Dollar €000** | **Total €000** |
|---|---|---|---|---|---|
| ***As at 31 December 2018*** | | | | | |
| Trade and other receivables | **506** | **94** | **-** | **-** | **600** |
| Cash and cash equivalents | **77** | **16** | **2** | **-** | **95** |
| Trade and other payables | **(1,207)** | **(630)** | **(466)** | **-** | **(2,303)** |
| Loans and borrowings | **(626)** | **(1,154)** | **(8)** | **-** | **(1,788)** |
| **Net current assets/(liabilities)** | **(1,250)** | **(1,674)** | **(472)** | | **(3,396)** |
| *As at 31 December 2017* | | | | | |
| Trade and other receivables | 1,172 | 71 | - | - | 1,243 |
| Cash and cash equivalents | 187 | 754 | 10 | - | 951 |
| Trade and other payables | (683) | (140) | (28) | - | (851) |
| Loans and borrowings | (1,134) | (1,062) | - | - | (2,196) |
| Net current assets/(liabilities) | (458) | (377) | (18) | - | (853) |

The following tables demonstrate the sensitivity to a reasonably possible change in Euro exchange rates, with all other variables held constant. The Group's exposure to foreign currency changes for all other currencies is not material.

| | **Increase/decrease in basis points** | | **Effect on profit before tax** | |
|---|---|---|---|---|
| | **31 December 2018** | 31 December 2017 | **31 December 2018 €000** | 31 December 2017 €000 |
| Sterling | **+20** | +20 | **(356)** | 75 |
| | **-10** | -10 | **178** | (38) |
| Swiss franc | **+10** | +10 | **86** | 2 |
| | **-10** | -10 | **(86)** | (2) |
| US Dollar | **+20** | +20 | **-** | - |
| | **-20** | -20 | **-** | - |

### *Liquidity risk*

Liquidity risk arises from the Group's management of working capital. The risk is that the Group will encounter difficulty in meeting its financial obligations as they fall due. The Group's policy is to ensure that it will always have sufficient cash to allow it to meet its liabilities when they become due. To achieve this aim, it seeks to maintain cash balances to meet expected requirements for a period of at least 90 days.

The Board receives rolling 12-month cash flow projections on a quarterly basis as well as information regarding cash balances. At the end of the financial year, these projections indicated that the Group expected to have sufficient liquid resources to meet its obligations under all reasonably expected circumstances.

The liquidity risk of each group entity is managed centrally. Budgets are set locally and agreed by the Board in advance, enabling the Group's cash requirements to be anticipated. Where facilities of group entities need to be increased, approval must be sought from the Chief Finance Officer. Where the amount of the facility is above a certain level, agreement of the Board is needed.

The table below analyses financial liabilities by contractual maturities. Amounts disclosed in the table are the contractual undiscounted cash flows.

| | *Group* | | *Company* | |
|---|---|---|---|---|
| | **31 December 2018 €000** | 31 December 2017 €000 | **31 December 2018 €000** | 31 December 2017 €000 |
| ***Ageing of trade & other payables*** | | | | |
| Up to three months | **1,024** | 851 | **377** | 296 |
| Three to six months | **418** | - | **46** | - |
| Above six months | **861** | - | **207** | - |
| | **2,303** | 851 | **630** | 296 |
| ***Ageing of loans and borrowing*** | | | | |
| Up to three months | **425** | 306 | **-** | 57 |
| Between three to 12 months | **159** | 357 | **-** | 97 |
| Between one and two years | **1,204** | 226 | **1,154** | - |
| Between two and five years | **-** | 1,307 | **-** | 1,062 |
| Over five years | **-** | - | **-** | - |
| | **1,788** | 2,196 | **1,154** | 1,216 |

### *Capital management*

The Group's capital is made up of share capital, share premium, merger reserve, non-controlling interests and retained profits totalling €1.57 million at 31 December 2018 (2017: €4.03 million) as set out in the statement of changes in equity.

The Group's objectives when maintaining capital are:

- to safeguard the ability to continue as a going concern, so that the Group can continue to provide returns for shareholders and benefits for other stakeholders; and
- to provide an adequate return to shareholders by pricing products and services commensurately with the level of risk.

The Group sets the amount of capital it requires in proportion to risk. The Group manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying assets. The Group's strategy is to finance working capital requirements from existing cash resources and debt facilities while investment activity is finance wherever possible with surplus cash resources or through the issue of new shares where an acceptable return can be generated.

The Group monitors capital on the basis of its debt-to-equity ratio. This ratio is calculated as net debt to total equity as defined above. Net debt is calculated as total debt (as shown in the consolidated statement of financial position) less cash and cash equivalents. The Group's strategy is to limit the debt-to-equity ratio to 25% to balance leverage with the availability of low cost debt, notably working capital facilities in Italy. Any increase over this limit requires Board approval. The debt-to-equity ratio at 31 December 2018 was 107.8% (2017: 30.9%) as set out below:

| | **31 December 2018 €000** | 31 December 2017 €000 |
|---|---|---|
| Loans and borrowing | **1,788** | 2,196 |
| Less: cash and cash equivalents | **(95)** | (951) |
| Net debt | **1,693** | 1,245 |
| Total equity | **1,570** | 4,026 |
| Debt-to-equity ratio | **107.8%** | 30.9% |

The increase in the debt-to-equity ratio during 2018 resulted from the 84% reduction in total equity caused by the loss and the 24% increase in net debt for the financial year, notably the issue of convertible bonds by the UK.

The composition of the Group's loans and borrowings is analysed in note 19, as is the movement on its convertible bond issued during the year. Other loans and borrowings consist entirely of bank and short term financing which were subject only to negligible non-cash changes during the year. All cash movements arising from financing activities are analysed in the consolidated statement of cash flows.

## 21. Share capital

| | Number of shares | Share capital | Share premium |
|---|---|---|---|
| | 000 | €000 | € |
| **As at 1 January 2017** | **8,618** | **197** | **5,542** |
| Issue of new ordinary shares – BV Tech subscription | 862 | 18 | 1,134 |
| Issue of new ordinary shares – BV Tech asset consideration | 1,982 | 42 | 2,632 |
| Conversion of deferred shares | 300 | 6 | 275 |
| Conversion of adviser warrants | 79 | 2 | 78 |
| MBooster SRL fee shares | 22 | 1 | 37 |
| Issue of new ordinary shares – placing | 933 | 18 | 1,633 |
| Issue of new ordinary shares – BV Tech subscription | 156 | 3 | 273 |
| Equity issue costs | - | - | (234) |
| **As at 31 December 2017** | **12,952** | **287** | **11,370** |
| MBooster SRL fee shares | 243 | 5 | 51 |
| Subscription and open offer | 14,963 | 310 | 1,067 |
| Equity issue costs | - | - | (156) |
| BV Tech loan conversion | 1,652 | 33 | 114 |
| **As at 31 December 2018** | **29,810** | **635** | **12,446** |

### *Ordinary share capital*

The ordinary shares of £0.018 carry the right to one vote per share at general meetings of the Company and the rights to share in any distribution of profits or returns of capital and to share in any residual assets available for distribution in the event of a winding up. The shares are denominated in Sterling.

On 24 January and 5 April 2018, 77,936 and 164,381 shares respectively were issued to strategic adviser MBooster SRL at 1.8 pence per share in settlement of fees.

On 6 April 2018 14,962,899 shares were issued under a subscription and open offer at 8 pence per share.

On 2 October 2018 1,652,232 shares were issued at 8 pence per share following the conversion of the first draw down against the convertible loan from BV Tech.

The Company has not issued any partly paid shares nor any convertible securities or exchangeable securities. The Company does not hold any treasury shares.

## Share based payments

Defenx has established EMI and Unapproved Option Schemes as part of the Group's incentive and retention strategy. Following the change of control in April 2018, the EMI status no longer applied.

Under the option schemes, the Group, at its discretion, may grant share options over the ordinary shares of Defenx to employees and Directors. The share options generally vest over 36 months, either from inception or from the first anniversary of grant, provided the holder remains in employment. There are no performance conditions. The exercise price of the share options is equal to the market price of the underlying shares on the date of grant. The contractual term of the share options is 10 years and there are no cash settlement alternatives.

The fair value of the options and warrants is estimated at the grant date using a Black-Scholes pricing model, taking into account the terms and conditions upon which the options were granted, and the estimated share price volatility of the Company relative to that of its competitors.

The fair value of options and warrants issued was estimated on the date of grant using the following assumptions:

| | **31 December 2018** | 31 December 2017 |
|---|---|---|
| Weighted average share price | **£1.140** | £1.202 |
| Weighted average exercise price | **£1.160** | £1.215 |
| Expected volatility | **40%** | 40% |
| Risk free rate of return | **1.5%** | 1.5% |
| Expected life (years) | **5** | 5 |
| Expected dividend yield | **0%** | 0% |

The expected life of the share options is based on current expectations and is not necessarily indicative of exercise patterns that may occur. The full contractual life of options is ten years and warrants is five years. The expected volatility reflects the assumption that the historical volatility over a period similar to the life of the options is indicative of future trends, which may not necessarily be the actual outcome. Expected volatility was determined by referring to the share prices of a selection of comparable AIM quoted companies.

| | **Year ended 31 December 2018** | | Year ended 31 December 2017 | |
|---|---|---|---|---|
| | **Number** | **WAEP*** | Number | WAEP* |
| Outstanding at 1 January | **444,614** | **£1.274** | 523,364 | £1.215 |
| Granted during the year | **-** | **-** | - | - |
| Forfeited during the year | **(179,500)** | **£1.321** | - | - |
| Exercised during the year | **-** | **-** | (78,750) | £0.886 |
| Expired during the year | **-** | **-** | - | - |
| Outstanding at 31 December | **264,114** | **£1.242** | 444,614 | £1.274 |
| Vested at 31 December | **264,114** | **£1.242** | 364,572 | £1.244 |
| Exercisable at 31 December | **264,114** | **£1.242** | 364,572 | £1.244 |

** Weighted average exercise price*

The weighted average remaining contractual life for the share options outstanding as at 31 December 2018 was 3.9 years (2017: 6.1 years).

The range of exercise prices for options and warrants outstanding at the end of the year was £0.80 to £2.00 (2017: £0.80 to £2.00).

No options were granted during the year. The total equity-settled share-based payment movement recognised in the year was a reduction of €(57,000) (2017: increase, €54,000).

National Insurance is payable on gains made by employees on exercise of share options granted to them. The Company has entered into a reciprocal arrangement with employees such that the employees will reimburse any National Insurance liability.

## 22. Reserves

The following describes the nature and purpose of each reserve within equity:

| | |
|---|---|
| Share premium | The amount of capital contributed in excess of the nominal value of each Ordinary £0.018 Share. |
| Merger reserve | The amount arising from the use of merger accounting (as set out in note 1) being the difference between the parent's cost of investment in Defenx SA and the issued share capital of Defenx SA.<br><br>The merger reserve is also used where more than 90% of the shares in a subsidiary are acquired and the consideration includes the issue of new shares by the parent, thereby attracting merger relief under the Companies Act 2006. |
| Shares to be issued reserve | Shares for which consideration has been received but which are not issued yet. |
| Convertible debt option reserve | Amount of proceeds on issue of convertible debt relating to the equity component (i.e. option to convert the debt into share capital). |
| Share based payment reserve | Aggregate fair value of vested share based payments awarded |
| Retained earnings | All other net gains and losses and transactions with owners (e.g. dividends) not recognised elsewhere. |

## 23. Controlling party

Defenx PLC is controlled by BV Tech, a company registered in Italy. At 31 December 2018 it held 57.2% of the Company's ordinary shares. Following subsequent full drawdown and conversion of the convertible loan agreed in October 2018, BV Tech's holding currently stands at 67.1%.

## 24. Notes supporting statements of cash flows

For the purpose of the statement of cash flows, cash and cash equivalents comprise the following at 31 December:

| | *Group* | | *Company* | |
|---|---|---|---|---|
| | **31 December 2018 €000** | 31 December 2017 €000 | **31 December 2018 €000** | 31 December 2017 €000 |
| Cash at bank | **95** | 953 | **16** | 860 |
| Bank overdrafts | **-** | (2) | **-** | - |
| | **95** | 951 | **16** | 860 |

Non-cash transactions from financing activities are shown in the reconciliation of liabilities from financing transactions below:

| | *Non-current loans and borrowings* €000 | *Current loans and borrowings* €000 | *Convertible bond* €000 | *Total* €000 |
|---|---|---|---|---|
| At 1 January 2018 | 471 | 663 | 1,062 | 2,196 |
| Cash flows | - | (500) | - | (500) |
| Fair value changes | - | - | 82 | 82 |
| Loans and borrowings becoming current | (233) | 233 | - | - |
| Interest accruing in period | - | - | 10 | 10 |
| At 31 December 2018 | 238 | 396 | 1,062 | 1,788 |

## 25. Related party transactions

### *BV Tech strategic partnership*

In 2017, the Company entered into a long-term strategic partnership with BV Tech, a leading independent Italian corporate IT and cyber security solutions provider, comprising, in part, a software acquisition by the Company and cash subscription by BV Tech, with the intention to enhance Defenx's product portfolio and enable the Group to penetrate the European corporate market to generate high-quality, recurring revenues in the medium term.

In October 2018, the Company entered into a convertible loan agreement with BV Tech for €950,000, convertible to ordinary shares at a price of 8 pence per share. The loan has been fully drawn in three stages in October 2018 and January and March 2019. In each case the loan was immediately converted to shares.

As set-out in note 27 below, in April 2019, the Company entered into enhanced sales and distribution agreements with BV Tech.

The balance outstanding to BV Tech at the year-end was €830,000 (2017: €nil). All transactions were on arm's length terms.

### *Key management personnel – Group*

In the opinion of the Board, only the Executive Directors of the Company are regarded as key management personnel.

Key management personnel compensation, including social security, comprised the following:

| | **31 December 2018 €000** | 31 December 2017 €000 |
|---|---|---|
| Wages and salaries | **183** | 263 |
| Pension | **5** | 15 |
| Benefits | **6** | 2 |
| Share based payments expense | **-** | 33 |
| | **194** | 313 |

The remuneration of key management personnel is determined by the remuneration committee having regard to the performance of individuals and market trends.

### *Other related party transactions – Company*

| | **31 December 2018 €000** | 31 December 2017 €000 |
|---|---|---|
| ***Transactions between Defenx PLC and Defenx SA*** | | |
| Income – invoiced by Defenx PLC | **200** | 160 |
| Expenses – invoiced by Defenx SA | **-** | (69) |
| Interest receivable – invoiced by Defenx PLC | **327** | 238 |
| Long-term loans from Defenx PLC to Defenx SA | **3,151** | 3,268 |
| Impairment of loans to subsidiary | **(3,268)** | (3,268) |
| Net long-term loans from Defenx PLC to Defenx SA | **(117)** | - |
| ***Transactions between Defenx PLC and Defenx Italia SRL*** | | |
| Transfer of intangible fixed assets – contract with Defenx PLC | **-** | 6,272 |
| Long-term loans from Defenx PLC to Defenx Italia SRL | **583** | 6,272 |
| Impairment of loans to subsidiary | **(3,136)** | (3,136) |
| Net long-term loans from Defenx PLC to Defenx Italia SRL | **(2,554)** | 3,136 |
| ***Transactions between Defenx SA and Defenx Italia SRL*** | | |
| Income – invoiced by Defenx SA | **-** | 385 |
| Expenses – invoiced by Defenx Italia SRL | **-** | (583) |
| Net trade receivables in Defenx SA with Defenx Italia SRL | **478** | 580 |
| Impairment of net trade receivables | **-** | (580) |
| Net trade receivables in Defenx SA with Defenx Italia SRL after impairment | **(478)** | - |

## 26. Commitments and contingencies

### *Operating lease commitments – Group as lessee*

The Group has operating leases on office premises in London (UK), Balerna (Switzerland) and Rome (Italy) on three, six and three months' notice respectively, and for its primary data centre in Rome. Future minimum rentals payable under non-cancellable operating leases as at 31 December 2018 are €37,000 (2017: €35,000) within one year.

### *Finance lease and hire purchase commitments*

The Group has no finance lease or hire purchase commitments.

### *Commitments*

At 31 December 2018, the Group had no commitments relating to software development (2017: €nil).

### *Contingent liabilities*

The Directors are not aware of any contingent liabilities at 31 December 2018.

## 27. Events after the reporting date

In January 2019 and March 2019, the Company drew down €500,000 and €300,000 respectively against the convertible loan facility from BV Tech. In each case, the loan was converted immediately into ordinary shares, issued at 8 pence each, resulting in the issue of 5,631,259 and 3,267,842 shares respectively to BV Tech.

In April 2019, the Group signed agreements whereby BV Tech:

- will have the sole rights to sell Defenx products to certain bodies within the Italian defence, space, national security or critical infrastructures sectors, through to the end of December 2023 for which BV Tech will pay Defenx a total consideration of €1.0 million, which has been received in three instalments before the end of June 2019. In addition, Defenx will receive a royalty fee equal to 50% of any revenues from the sale of its products (during the period to 31 December 2023) to such clients in excess of €5.0 million;
- has committed to purchase Defenx's products, with a minimal value of €1.2 million, over a two year period, effective from 1 January 2019. Accordingly, Defenx will receive a minimum of €1.2 million in a number of instalments over the two year period from BV Tech for such products. The previous restrictions regarding the distribution of Defenx's products have also been removed, such that BV Tech is now able to distribute, on a non-exclusive basis, all of Defenx's products through any direct and indirect channel of distribution or sales through to 31 December 2021. The value of any Defenx products sold by BV Tech pursuant to this distribution agreement will, unless agreed otherwise by the parties, be based on the prices set out in the 2017 Distribution Agreement; and
- will undertake to provide services to Defenx in respect of its range of new and existing products over the course of 2019 pursuant to a software services agreement between the Group and BV Tech. The aggregate fee payable by the Group to BV Tech for the services under this services agreement is calculated and payable monthly on a 'time spent' basis, capped at €1.2 million.

  The services agreement contains warranties in favour of Defenx Italia SRL in respect of the intellectual property created pursuant to the services. BV Tech has the right of first refusal to extend the services agreement for a further year on the same terms, subject to its fees and/or timing for delivery of its services at least matching terms proposed by third party suppliers, all other criteria being at least equal. The services agreement contains a number of termination rights of each party, for cause, rather than for convenience.

  The services agreement does not form part of the master services agreement previously entered into with BV Tech, as announced on 27 September 2017.

# Company information

## Directors

Anthony Reeves
Raffaele Boccardo
Giorgio Beretta
Nicholos Hellyer

## Secretary

Liam O'Donoghue

## Registrars

SLC Registrars
42–50 Hersham Road
Walton-on-Thames
Surrey KT12 1RZ

## Registered office

201 Temple Chambers
3-7 Temple Avenue
London EC4Y 0DT

## Registered number

08993398

## Share capital

The ordinary share capital of Defenx PLC is admitted to trading on AIM, a market operated by London Stock Exchange Group plc. The shares are listed under the trading ticker DFX.

The ISIN number is GB00BYNF4J61 and the SEDOL number is BYNF4J6.

## Auditors

Haysmacintyre LLP
10 Queen Street Place
London EC4R 1AG

## Nominated adviser

Strand Hanson Limited
26 Mount Row
London W1K 3SQ

## Broker

WH Ireland Limited
11 St James's Square
Manchester M2 6WH

## Solicitors

Trowers & Hamlins LLP
3 Bunhill Row
London
EC1Y 8YZ

## Bankers

National Westminster Bank
135 Bishopsgate
London EC2M 3UR

Credit Suisse AG
SGCT 1, Viale Stazione 19
6501 Bellinzona, Switzerland

Banca UniCredit SpA
Piazza San Benedetto da Norcia, 29
00040 Pomezia (RM), Italy

Banca Sella SpA
Via Alessio Baldovinetti, 132
00142 Roma, Italy

## Website

investors.defenx.com

# Five-year track record

| | | 2018 | 2017 | 2016 | 2015 | 2014 |
|---|---|---|---|---|---|---|
| **As at 31 December** | | | | | | |
| Revenue | €000s | **1,420** | 2,928 | 7,088 | 4,490 | 2,382 |
| Revenue growth | % | **-52%** | -59% | +58% | +88% | +15% |
| Gross (loss)/profit | €000s | **(568)** | 375 | 5,847 | 3,977 | 2,034 |
| Gross margin | % | **(40.0)%** | 12.8% | 82.5% | 88.6% | 85.4% |
| Operating (loss)/profit (before transaction costs) | €000s | **(3,519)** | (11,752) | 1,840 | 979 | 805 |
| Operating margin (before transaction costs) | % | **(247.8)%** | -401.4% | 26.0% | 21.8% | 33.8% |
| (Loss)/profit before tax | €000s | **(3,797)** | (12,036) | 1,590 | 362 | 761 |
| Earnings per share | | | | | | |
| Basic | | **(€0.15)** | (€1.03) | €0.19 | €0.04 | €0.17 |
| Diluted | | **(€0.15)** | (€0.98) | €0.17 | €0.04 | €0.16 |
| | | | | | | |
| Net cash flow from operating activities | €000s | **(1,370)** | (2,327) | 2,322 | (1,022) | 388 |
| Free cash flow (after capitalised development costs) | €000s | **(1,860)** | (4,155) | (1,667) | (2,372) | (823) |
| Net cash used in investing activities | €000s | **(502)** | (1,879) | (4,558) | (1,351) | (1,211) |
| Net cash from financing activities | €000s | **1,038** | 4,120 | 1,916 | 3,512 | 1,026 |
| Net increase in cash and cash equivalents | €000s | **(856)** | (86) | (319) | 1,139 | 203 |
| Cash and cash equivalents at year end | €000s | **95** | 929 | 1,015 | 1,334 | 206 |
| | | | | | | |
| Net assets | €000s | **1,570** | 4,027 | 9,651 | 5,812 | 2,048 |
| Net assets per share | | **€0.05** | €0.31 | €1.12 | €0.95 | €0.51 |

# Notice of AGM

**DEFENX PLC**
**(the Company)**

**(Company number 08993398)**

Notice is given that the Annual General Meeting (AGM) of the members of the Company will be held at the offices of Strand Hanson, 26 Mount Row, London, W1K 3SQ on 2 September 2019 at 12:00 p.m. to consider and, if thought fit, pass the following resolutions, of which resolutions 1 to 6 (inclusive) will be proposed as ordinary resolutions and resolution 7 will be proposed as special resolutions:

### Ordinary resolutions:

***Report and accounts***

1. To receive the audited Accounts and Reports of the Directors and auditors for the year ended 31 December 2018.

***Remuneration report***

2. To approve the report on Directors' remuneration for the year ended 31 December 2018.

***Re-election of Director***

3. To re-elect as a Director Mr. Anthony Reeves, who is retiring in accordance with Article 25.1 of the Company's Articles of Association and, being eligible, is offering himself for re-election.

***Re-appointment of auditor***

4. To re-appoint haysmacintyre as auditor until the conclusion of the next AGM of the Company at which accounts are laid.

***Auditor's remuneration***

5. To authorise the Directors to determine the remuneration of the auditor.

***Directors' authority to allot shares***

6. That in substitution for all existing authorities, the Directors be generally and unconditionally authorised in accordance with section 551 of the Companies Act 2006 (the Act) to exercise all the powers of the Company to allot shares in the Company or to grant rights to subscribe for or convert any security into shares in the Company up to an aggregate nominal amount of £696,760.09 during the period from the date of the passing of this resolution. The authority hereby conferred shall expire at the conclusion of the next AGM of the Company in 2020, except that the Company may before such expiry make any offer or agreement which would or might require shares to be allotted or such rights to be granted after such expiry and the Directors may allot shares or grant such rights in pursuance of such offer or agreement as if the authority conferred by this resolution had not expired.

### Special resolution:

***Authority to dis-apply pre-emption rights***

7. That, subject to resolution 6 above being passed and Section 551 of the Act, the Directors be empowered, pursuant to Section 570 of the Act, to allot equity securities (as defined in Section 560 of the Act) as if Section 561(1) of the Act did not apply to any such allotment, provided that this power shall be limited to the allotment of equity securities:

(a) during the period expiring on the date of the next AGM of the Company or but so that this power shall enable the Company to make offers or agreements which would or might require equity securities to be allotted after the expiry of this power;

(b) up to an aggregate nominal amount of £696,760.09; and

(c) shall include the power to sell treasury shares under Section 727 of the Act.

26 July 2019

**Registered office:**

201 Temple Chambers
3-7 Temple Avenue
London EC4Y 0DT

**By order of the Board**

Liam O'Donoghue
Company Secretary

**Notes:**

1. A member entitled to attend and vote at the above meeting has the right to appoint a proxy or proxies to attend and vote in his place. A proxy need not be a member of the Company.
2. The form of proxy and the power of attorney or other authority, if any, under which it is signed, or a copy of such power or authority certified by a notary, must be completed and returned to the offices of the Company's registrars, SLC Registrars, Elder House, St Georges Business Park, 207 Brooklands Road, Weybridge, Surrey KT13 0TS, to arrive not later than 12:00 p.m. on Thursday 29th August.
3. In accordance with regulation 41 of the Uncertificated Securities Regulations 2001, (as amended) only those persons entered in the register of members of the Company as the holders of Ordinary Shares at 6:30 p.m. on Thursday 29th August 2019 are entitled to attend and vote at the meeting in respect of the Shares held by them at the relevant time. Any changes made to the register of members of the Company after that time will be disregarded in determining the right of any person to attend or vote at the meeting.
4. Resolution 3 – Under Article 25.1 of the Company's Articles of Association, each Director must retire from office at the third annual general meeting after the annual general meeting or general meeting (as the case may be) at which he was appointed or last re-appointed.
5. Resolutions 4 and 5 – The auditors are required to be re-appointed at each AGM at which accounts are presented. The Board on the recommendation of the Audit Committee, which has evaluated the effectiveness and independence of the external auditors, is proposing the re-appointment of haysmacintyre pursuant to Resolution 4. Resolution 5 is proposed to authorise the Board to fix the remuneration of the auditors.
6. Resolution 6 – This resolution is to renew the authority given to the Directors to allot Shares or rights to subscribe for or convert security into Shares in the capital of the Company subject to the conditions of the Act. The authority to be given by this resolution is limited to the allotment of 38,708,894 Ordinary Shares representing 100% of issued Share capital at the date of this notice and shall be in substitution for all existing authorities but shall be without prejudice to any allotment of Shares or grant of rights to subscribe for or convert security into Shares already made or offered or agreed to be made pursuant to such authorities. The authority hereby conferred shall expire at the conclusion of the next AGM of the Company in 2020.
7. Resolution 7 - When Shares are to be allotted for cash, section 561(1) of the Companies Act 2006 provides that existing shareholders have pre-emption rights and that any new Shares are offered first to such shareholders in proportion to their existing shareholdings. This resolution is seeking to authorise the Directors to allot Shares of up to an aggregate nominal amount of £696,760.09 otherwise than on a pro-rata basis. This represents 100% of the Company's issued Share capital on the date of this document. This authority shall expire at the next AGM of the Company in 2020. Whilst the Directors have no intention at the present time of issuing relevant securities, other than pursuant to existing rights under employee share schemes, they are seeking annual renewal of this authority in accordance with best practice and to ensure the Company has maximum flexibility in managing capital resources.

**Documents**

8. The following documents, which are available for inspection during normal business hours at the registered office of the Company on any business day, will also be available for inspection on the day of the meeting until the Company's normal close of business:

   (a) copies of Executive Directors' service contracts with the Company;

(b) copies of Non-executive Directors’ letters of appointment; and

(c) a copy of the Company’s current Articles of Association.