News release

Velocys plc

("Velocys" or "the Company")

17 May 2021

Final audited results for the year ended 31 December 2020

Velocys, the sustainable fuels technology company, is pleased to announce its final audited results for the year ended 31 December 2020.

Financial Highlights

- Fund raise of £21m (before expenses) in July 2020
- Additional £0.5m Future Fuels for Flight and Freight grant from the UK Department for Transport secured for the Altalto waste to jet fuel project
- Revenue of £0.2m (2019: £0.3m)
- Total deferred revenue of £8.2m including £2.1m invoiced and received from commercial customers during 2020
- Administrative expenses before exceptional items reduced by 7% to £9.2m (2019: £9.9m)
- Operating loss of £8.8m (2019: £9.6m) before exceptional items
- Loss before income tax for the year of £9.6m (2019: £9.9m)
- Cash at year end of £13.1m (2019: £4.8m)

Business Highlights including post period end activities

Projects

- Granted planning permission from North East Lincolnshire Council for the Altalto Immingham site
- Ongoing discussions to secure investment by one or more strategic partners into the Mississippi Biorefinery Project, which has undergone a design review and optimisation during the second half of 2020, increasing its capacity and attractiveness to investors and Sustainable Aviation Fuel off-takers
- Successfully completed the NEDO demonstration project in Nagoya, Japan, achieving 1500 hours of integrated conversion of wood chips to Sustainable Aviation Fuel

Commercial

- We have advanced our Sustainable Aviation Fuel off-take discussions with major airlines in Europe and North America
- Abundant Feedstock supply available as evidenced by engagement with local suppliers
- Advancing additional technology licensing opportunities across three continents

Technology

- Delivered four Fischer-Tropsch reactors and completed catalyst loading for Red Rock Biofuels in Oregon, USA
- Integrated technology licensors on-boarded including TRI, Arvos, Air Liquide, Linde and Haldor Topsoe
- Appointed Worley as our engineering partner to manage delivery of our technology globally

Policy

- Invited to be a founding member of the UK Government's Jet Zero Council
- Appointed to the boards of the Renewable Transport Fuel Association and the Biotechnology Innovation Organisation

Post period end activities

- Altalto option agreement with British Airways plc extended to 31 March 2022 (Shell International Petroleum Company Limited withdrew from the agreement in January 2021)
- Collaboration agreement signed with Toyo Engineering Corporation, Japan in February 2021

Henrik Wareborn, CEO of Velocys, said:

“Velocys overcame unprecedented circumstances in 2020 due to the Covid pandemic restricting international travel and compelling all of our colleagues to work from home except those involved in reactor manufacturing, laboratory and site safety work.

“Our team demonstrated resilience and agility in adapting to the new conditions and ensured Velocys delivered all our contracted services and technology hardware to our customers.

“The successful fundraise in July 2020 enabled the Company to concentrate on client delivery from the second half of 2020 and onwards. In addition, we took the opportunity to further optimise the engineering for higher potential output and lower carbon intensity of our two reference projects in the UK and USA respectively.

“We are in a favourable position to take advantage of the growing global demand for climate change mitigation technology, specifically the decarbonisation of commercial aviation. The Company remains capital light and cost disciplined with a focus on deploying our end-to-end technology solution via partners, site owners and third-party developers worldwide.

“I thank my colleagues in Velocys and all our stakeholders for their dedication to our mission during the challenging year of 2020.”

Certain information contained in this announcement would have constituted inside information (as defined by Article 7 of Regulation (EU) No 596/2014) prior to its release as part of this announcement.

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Notes to Editors

Velocys is an international UK-based sustainable fuels technology company. Velocys designed, developed and now licenses proprietary Fischer-Tropsch technology for the generation of clean, low carbon, synthetic drop-in aviation and road transport fuel from municipal solid waste and residual woody biomass.

Velocys is at present developing two reference projects: one in Natchez, Mississippi, USA (incorporating Carbon Capture, Utilisation and Storage) and one in Immingham, UK, to produce fuels that significantly reduce both greenhouse gas emissions and key exhaust pollutants for aviation and road transport. Originally a spin-out from Oxford University, in 2008 the Company acquired a US company based on complementary reactor technology developed at the Pacific Northwest National Laboratory. Velocys is headquartered in Oxford in the United Kingdom.

www.velocys.com

Chairman's statement

Our first priority at the start of the pandemic was to ensure that we were able to provide our employees with as safe a working environment as possible, whilst maintaining their ability to work efficiently and as effectively. We closed all our offices and arranged for all employees to be able to work from home, providing additional technical support where necessary to enable them to work in a safe and secure home environment.

Four achievements during the year were of particular note and demonstrated our ongoing progress in delivering our strategy:

- The successful completion of the manufacturing of four FT reactors and catalyst and delivery to our client Red Rock Biofuels' Lakeview site in Oregon. In 2021 we look forward to working closely with Red Rock to assist with start-up and commissioning of its bioenergy plant.
- Our application for Planning Consent for the Altalto waste to jet fuel project was approved in May 2020 by North East Lincolnshire Council.
- July saw a successful and oversubscribed fund raise of £21.0 million, and further contributions from both British Airways and Shell towards the technical development of our Altalto project.
- We successfully concluded the wood chips to SAF NEDO demonstration project in Nagoya, Japan with our partner, Toyo Engineering Corporation, and look forward to delivering engineering services to the planned larger scale NEDO 2 project managed by the same consortium in Japan. We will deliver our FT reactors and catalyst in due course to NEDO 2 subject to approvals and funding by the local partners.

The year saw a significant increase of media exposure for Velocys, which was evidenced by the number of high-quality interviews with the CEO, extensive coverage by the national and international broadsheets and also in the technical press. UK Government support for our Altalto Immingham Project was validated by the mention of Velocys at the Downing Street daily briefing by the Secretary of State for Transport, Grant Shapps in June 2020 and the invitation for Velocys to be represented on the Jet Zero Council.

Strong US policy support for domestic sustainable fuel production, including SAF with negative carbon intensity has been recently reaffirmed by the new administration. This is very positive for our Bayou Fuels project in Mississippi and our other potential clients in the US.

Whilst there has been significant attention drawn to the potential use of hydrogen and electric propulsion as a means of reducing the carbon emissions of air travel, we remain convinced that the use of Sustainable Aviation Fuel provides the only near-term opportunity for the airline industry to reduce its carbon footprint at commercial scale and pace.

Management and Board
There were no changes to the Board membership during the year, however on 30 September 2021 Sandy Shaw will be standing down from the Board after 9 years of loyal service. We will be conducting a search for a replacement for Sandy during the first half of 2021, with the intention of the new NED bringing complementary skills to the Board as we enter an intensive phase of commercialisation of our technology. The Board has continued to enjoy strong and cooperative relationships with the Executive Team.

We were able to strengthen our leadership team during the year with the appointment of Helen Lillistone as Group Financial Controller. Helen has over 20 years' experience in senior finance and accounting roles within the biotech sector and has already made significant contributions to strengthening and upgrading our financial and accounting processes.

During 2021, we have further strengthened the leadership team with the appointment of David Bate as General Counsel. David is an experienced business lawyer with 26 years global energy sector experience at executive level, encompassing extensive international project experience across a wide range of countries.

The Board's Committees have continued to work constructively in supporting the Board, and I would like to thank both Sandy Shaw and Darran Messem for their efforts in chairing the Remuneration and Audit & Risk Committees respectively. I would like to particularly thank Sandy Shaw for her efforts in realising a further year of LTIP's for the broader leadership team, ensuring the alignment of the leaders of the business with the shareholders. We do not envisage increasing the size of the Board this year but will do so at a later time commensurate with the growth of our business.

Corporate governance
The Board has maintained its emphasis on good governance following the ten principles of the Quoted Companies Alliance Code. With the anticipated appointment of a new Non-Executive Director in Q3 2021, and following the standing down of Sandy Shaw, there will be a change in the Chairs of the Audit & Risk and Remuneration Committees to accommodate the skills and experience of the new Non-Executive Director to the Board.

Fund raise
The Company successfully raised £21 million before expenses through a Placing, Retail Offer and Open Offer. This enabled a variety of UK investors to participate in an oversubscribed offer. We were extremely pleased with the support shown by existing investors and to see new high-quality institutional investors join our shareholder register and thank all those who participated in the fund raise. The fund raise has enabled our team to concentrate on delivery and strategy execution, building shareholder value during this time.

Outlook
We look forward to completing the post-planning consent and final phase of technical pre-development work of our Altalto Immingham Project in Q2 2021. In addition, we are taking advantage of the learnings we have gained working closely with our engineering partner, Worley, and accelerating the technical development of our Bayou Fuels Mississippi Biorefinery Project. This will make both projects highly standardised and modular, ready for the final FEED work and future projects.

With the successful fund raise in 2020, the Company is focused on delivering its reference projects as well as seeking new commercial opportunities to deploy our technology and support current and prospective customers.

The recent announcement of a collaboration agreement with Toyo Engineering Corporation demonstrates that we are delivering and creating opportunities for enhancing revenues from third-party developers, whilst opening up a new market for Velocys in Japan and the Far East.

We are now highly focused on accelerating the customer adoption of our technology. This requires us, as mentioned in our 2020 fundraise, to expand our current manufacturing capability, ensuring it has the capacity to achieve quality and on time delivery of our reactors at the scale required by multiple clients at various locations over the next number of years.

The Executive Team will continue to engage with respective host Governments and other stakeholders during 2021 to secure the necessary policy support to unlock the economic delivery of Sustainable Aviation Fuels to the airline industry at the scale and pace required to meet their aggressive Net Zero obligations.

CEO's report

Our global opportunity
Velocys is in a good position to take advantage of the growing demand for climate change mitigation, specifically the decarbonisation of commercial aviation. The aviation sector is staking its post COVID-19 recovery on Net Zero commitments to win back its passengers and licence to operate by host governments. For medium and

long-haul flights, the only realistic prospect for the industry to decarbonise is to use fuel with a chemical composition similar to its current fossil fuel but with net zero or negative carbon intensity over the full life cycle. To avoid the need to replace or modify billions of dollars' worth of aircraft turbines and airport refuelling systems, and for aviation safety reasons, the net zero fuel must be ASTM approved and safe to blend seamlessly into the current fuel systems.

Synthetic Paraffinic Kerosene ("SPK") using the Fischer-Tropsch pathway (our enabling technology) is already ASTM approved for use at up to 50% with fossil based kerosene in commercial aviation globally. When SPK is made from sustainable feedstocks such as municipal, agricultural or forestry waste, it qualifies as Sustainable Aviation Fuel. The World Economic Forum estimates that these resources are sufficient to supply up to 95% of the world's jet fuel demand. This pathway is also the key to e-fuels (using CO2 as the carbon source, with renewable energy) which unlock an even greater additional supply.

Velocys provides the central processing technology which allows full commercial scale production of SAF using this pathway. We have integrated our technology into an end-to- end solution for site owners and developers to deploy on any site with more than 500,000 tonnes of available solid waste per year. Beyond the sharp reduction of CO2 emissions, our technology provides additional societal value through the diversion of this waste from landfills or incineration, as well as a final jet fuel with far superior air-quality properties than the fossil fuel it replaces.

The year in focus

Our Chairman has highlighted our main accomplishments for 2020, of which I am extremely proud. Our whole team demonstrated resilience and agility in adopting to the new work conditions imposed by the COVID-19 restrictions globally and managed to accelerate delivery of our engineering solutions to our clients as well as delivering hardware in the form of reactors and catalyst. I am pleased to say we did not need to furlough any employee in the US nor in the UK. I am also particularly pleased with our zero lost time incidents in the workplace at both our own sites and equally at our client sites where we have had Velocys engineers deployed during the year.

We have continued to tightly manage our overhead costs throughout 2020 by continuing the trend of effective cost management initiated at the end of 2018. My vision for Velocys is to remain capital light and low on fixed overhead costs while accessing a global capability to deliver our technology in its broadest sense via partners and third-party developers.

Our Financial review details our progress towards positive cashflow, which is our main strategic goal at this point. This enables us to unlock the full potential of future revenue generation from our technology, to meet the needs of all our stakeholders. We value our shareholder support in this final, but most important stage, from R&D to full scale commercialisation. I am very grateful for how that support was demonstrated by our early and new shareholders' engaged participation in our oversubscribed fund raise in July 2020.

Our commitment to sustainability

Velocys manages its own direct energy and resource consumption carefully. However, our overarching environmental impact is that our technology enables our clients to reduce net life cycle greenhouse gas emissions radically for their end-users. For example, 5 commercial scale Velocys enabled biorefineries each producing over 100 million litres of sustainable synthetic fuels would reduce net CO2 emissions by up to 3 million tonnes per year. This is equivalent to removing over 1 million average size petrol driven cars from the roads in the UK – but with the added benefit that the savings are in a much more difficult sector. Hence for investors, there are few other equally focused and near-time opportunities to contribute to a massive reduction of high impact CO2 emissions alongside improving air quality at altitude and around our airports.

Outlook

I am thankful for the reliable policy support we have received from both the US and UK governments during 2020 and recognise that continuing policy support is essential for the acceleration of the supply of SAF globally. It is wholly unrealistic to expect new process technologies, using sustainable feedstocks, to be able to compete on price with a mature technology such as fossil oil without a significant penalty for combusting fossil oil and a corresponding reward for producing net zero carbon fuels. Such policy support is already available and mature in parts of the US and is under development in the UK and across the EU. In addition, global aviation rules for decarbonisation under the Carbon Offsetting and Reduction Scheme for International Aviation ("CORSIA") also become mandatory from 2026.

During 2021, Velocys will continue to be an active participant in consultations with governments and regulators on this topic, for example as a member of the Jet Zero Council in the UK.

In conclusion, I want to thank my Board, Velocys colleagues, shareholders and broader stakeholders for unfailing support during such a dramatic and transformational year as 2020, putting us in a position to accelerate the adoption of our climate change mitigation technology globally over the next few years.

Financial review

Revenues
The Company recognised revenue of £0.2m (2019: £0.3m). The 2020 revenue was primarily the result of professional services for, and the delivery of reactor components to, Toyo and professional services related to ongoing reference projects. Gross profit decreased to £0.1m (2019: £0.2m).

The Company has a total of £8.2m of deferred revenue as at 31 December 2020 (2019: £6.0m) from licensing, reactor and catalyst sales which will be recognised when the project performance obligations have been met. Providing an integrated package of goods and services typically means our revenues and corresponding costs can only be recognised once a customer’s project reaches a specific performance milestone.

Expenses and income
Administrative expenses before exceptional items reduced by 7% to £9.2m (2019: £9.9m). The reduction before exceptional items is principally the result of reduced corporate overheads including a reduction in travel costs of 71% due to the COVID-19 pandemic.

The exceptional items credit of £0.1m recorded in 2019 was for part-recovery of a loan made to an associate ENVIA totalling £0.5m, offset by an impairment of £0.4m to the value of land held as an asset.

Other income totalling £0.4m mainly consisted of £0.3m from the first tranche of the F4C grant awarded by the UK Department for Transport. In 2019 other income of £0.1m was recognised from the sale of assets associated with the final closing of the ENVIA plant.

Operating losses
Operating losses were £8.8m (2019: £9.6m before exceptional items credit of £0.1m). The reduction of the operating loss is principally the result of a decrease in administrative expenses. After exceptional items, the Company recorded an operating loss of £8.8m (2019: £9.5m operating loss).

Assets and cash
The net assets of the Company were £13.1m, which is an increase of £10.7m compared to 2019. This increase was principally the result of an increase in cash, and trade and other receivables offset by a decrease in inventories and an increase in deferred revenue and other liabilities.

The cash inflow to the Company in 2020 was £9.2m (2019: £1.4m cash outflow) principally being cash generated from financing activities of £19.6m, attributed to £19.6m received net of expenses from the fund raise that was successfully completed in July, less £0.8m used in investing activities and £9.6m used in operating activities.

The Company continues to carefully manage its underlying cost base and spends prudently on strategy implementation. The Company incurs much of its expenses in US dollars and has exposure to the US dollar exchange rate. This is hedged to the extent possible by holding cash reserves in US dollars. In addition, the majority of the Company’s income is currently invoiced in dollars.

Impairment assessment
The Board has assessed the long-term potential of the Company’s in-process technology assets as at 31 December 2020, and concluded that whilst there has been a positive change in the market capitalisation value (£108.0m at 31 December 2020 compared to £11.5m at the previous year end), it is not recommending the reversal of historical impairments at this stage given the wider economic recovery considerations and relatively early phase of the COVID-19 vaccination roll-out programmes globally.

The recoverable value is determined by comparing the higher of the value in use and the fair value less costs of disposal. Previously, given the early stage of the Company’s commercialisation plans, the share price of the parent Company was deemed the most accurate indicator of value. Alongside the share price of the parent Company, the Board also considered the following factors and changes:

- The Company successfully completed the manufacture and sale of reactors and catalyst for commercial use during 2020;
- The present value of estimated future net cash flows, using the Company's internal forecasts, exceeded the market capitalisation value;
- Global demand forecasts for sustainable aviation fuel far outweigh the available supply expected to be available from new plants for many years;
- Government policy support has strengthened as countries look to meet targets and commitments for carbon reduction;
- Potential competing technologies, such as hydrogen, require changes to infrastructure whilst the Velocys technology does not face these additional barriers to market entry; and
- Company revenues have not grown versus the prior year and remain modest, and there have not been any significant new customer arrangements signed during 2020.

Therefore, taking all of the above factors into account, the Board considers that the Company's current commercial position, without any new customer contracts or additional investors into the reference projects, outweighs the other positive aspects but is confident that no impairment is required and at the same time does not recommend reversing previous impairments at this time. The Company remains confident that the internal progress made during 2020 combined with an improvement in the economic environment, will enable the Company to reassess the recoverable value in due course, which could lead to the reversal of impairments of approximately £20m less accumulated amortisation at the date of reversal.

Ventech Trustees claim

In December 2020, the Company announced that it had signed a full and final *de minimis* settlement agreement with no material effect on the financial statements and global mutual release of all current and potential future claims between the bankruptcy trustees of Ventech Engineers LLC, a former commercial partner, and the Company.

Fund raise

In July 2020 Velocys raised a total of £21.0m (before expenses) via a Placing, Retail Offer and Open Offer. Net proceeds of the capital raising are being used to:

- Complete the process engineering phase of FEED for the Altalto Immingham Project;
- Complete the fund raising for the FEED stage of the Mississippi Biorefinery Project;
- Further strengthen the Company's intellectual property portfolio and trade secrets protection;
- Provide working capital for operating costs
- Evaluate and design a de-bottlenecking of the reactor core manufacturing line in the United States to reach a production capacity of more than 12 Fischer-Tropsch reactors per year (twice the current capacity); and
- Implement learnings from a post-operative analysis of demonstration reactors for the benefit of clients via updated operating manuals and training.

Future funding

With the successful fundraise in July 2020 of £21.0m (before expenses), the financial statements have been prepared on the going concern basis, which assumes the Company will have sufficient funds available to enable it to continue to trade for the foreseeable future. The cash forecast includes the following assumptions: (i) the completion of the current stage of the FEED for the Altalto Immingham Project and the Mississippi Biorefinery Project prior to securing funding for the next stage of FEED to financial close; (ii) the completion of the new design of the upgraded manufacturing facility; (iii) the continued process of on-boarding one or more strategic investors to provide the final stages of development funding for either or both the Altalto Immingham Project and the Mississippi Biorefinery Project; (iv) revenue from the ongoing pre-FEED engineering work from the February 2021 announcement of the collaboration agreement with our customer Toyo Engineering in Japan for the development of their first commercial plant in Japan; (v) the current overhead cost run rate.

The Company's plan is to continue working with our investment partner British Airways in the Altalto Immingham Project, having secured £1.0m additional non-dilutive investment in May 2020 and securing further investment partners into the project along with completing all the engineering design and commercial arrangements required to reach financial close on the project.

At the same time in the US we are also working to secure investment by one or more strategic partners into the Mississippi Biorefinery Project, which has undergone a design review and optimisation during the last half of 2020, increasing its capacity and attractiveness to investors and SAF off-takers. We are also working with several other interested parties in Europe, the US and the Middle East developing their own projects potentially using our FT technology within an integrated technology package into a complete plant. Whilst the Board is confident that one or more of these future plans will be achieved, nothing is contracted as at the date of signing these financial statements.

Going Concern

The Company will assess its cash requirements from these activities and determine at what stage it needs to raise additional funding. This funding may be achieved from one or a combination of a capital raising (including the possibility of a placement of ordinary shares within the next 12 months) or the realisation of certain assets; selling additional technology licences; performing Pre-FEED engineering work for customers (such as the technical services agreement made with Toyo Engineering recently for their commercial plant in Japan); UK or US Government loans or grants; and selling non-core intellectual property.

Following financial close of one or both reference projects in late 2022 or early 2023, the Company's funding requirements will depend on the final structure of each of the biorefinery project consortia and on additional third party projects requiring our FT technology or the integrated technology packages, including our FT technology, we have developed over the last few years.

Based on the Company's latest forecast and cash flow projections approved by the Board, additional funding will be required within twelve months of the date of signing these financial statements. Consequently, these conditions indicate the existence of a material uncertainty that may cast doubt on the Company and Velocys plc's ability to continue as a going concern.

The financial statements do not include the adjustments that would arise if the Company and Velocys plc were unable to continue as a going concern.

The Board will be proposing a Special Resolution at the forthcoming Annual General Meeting to approve the disapplication of the pre-emption rights. This may be used by the Company in securing additional working capital in the year to come.

Consolidated income statement
for the year ended 31 December 2020

	Note	2020 £'000 Before exceptional items	2020 £'000 Exceptional items (note 2)	2020 £'000 Total	2019 £'000 Before exceptional items	2019 £'000 Exceptional items (note 2)	2019 £'000 Total
Revenue	3	178	–	178	332	–	332
Cost of sales		(101)	–	(101)	(132)	–	(132)
Gross profit		77	–	77	200	–	200
Administrative expenses		(9,238)	–	(9,238)	(9,898)	94	(9,804)
Other income	6	400	–	400	79	–	79
Operating loss		(8,761)	–	(8,761)	(9,619)	94	(9,525)
Loss before net finance costs		(8,761)	–	(8,761)	(9,619)	94	(9,525)
Finance income	4	6	–	6	48	–	48
Finance costs	5	(850)	–	(850)	(429)	–	(429)
Net finance costs		(844)	–	(844)	(381)	–	(381)
Loss before income tax		(9,605)	–	(9,605)	(10,000)	94	(9,906)
Income tax credit		810	–	810	291	–	291
Loss for the financial year attributable to the owners of Velocys plc		(8,795)	–	(8,795)	(9,709)	94	(9,615)
Loss per share attributable to the owners of Velocys plc							
Basic and diluted loss per share (pence)	8	(1.05)	–	(1.05)	(1.91)	0.1	(1.90)

Consolidated statement of comprehensive income
for the year ended 31 December 2020

	2020 £'000 Before exceptional items	2020 £'000 Exceptional items (note 2)	2020 £'000 Total	2019 £'000 Before exceptional items	2019 £'000 Exceptional items (note 2)	2019 £'000 Total
Loss for the year	(8,795)	–	(8,795)	(9,709)	94	(9,615)
Other comprehensive expense items that may be reclassified to the income statement in subsequent periods:						
Foreign currency translation differences	(251)	–	(251)	(262)	–	(262)
Total comprehensive expense for the year attributable to the owners of Velocys plc	(9,046)	–	(9,046)	(9,971)	94	(9,877)

Consolidated statement of financial position
as at 31 December 2020

	Note	**2020 £'000**	2019 £'000
Assets			
Non-current assets			
Intangible assets	9	740	444
Property, plant and equipment	10	1,479	1,734
Right-of-use asset	11	653	836
		2,872	3,014
Current assets			
Inventories	12	970	3,332
Trade and other receivables	13	6,182	1,637
Current income tax asset		810	648
Cash and cash equivalents	14	13,051	4,797
		21,013	10,414
Total assets		23,885	13,428
Liabilities			
Current liabilities			
Trade and other payables	15	(932)	(1,331)
Lease liability	11	(470)	(581)
Borrowings		(152)	–
Other liabilities		(474)	(2,804)
Deferred revenue	16	(7,774)	(5,562)
		(9,802)	(10,278)
Non-current liabilities			
Lease lability	11	(270)	(343)
Borrowings		(371)	–
Deferred revenue	16	(382)	(470)
		(1,023)	(813)
Total liabilities		(10,825)	(11,091)
Net assets		13,060	2,337
Capital and reserves attributable to owners of Velocys plc			
Called up share capital		10,642	6,438
Share premium account		199,701	184,256
Merger reserve		369	369
Share-based payments reserve		16,345	16,225
Foreign exchange reserve		3,038	3,289
Accumulated losses		(217,035)	(208,240)
Total equity		13,060	2,337

Consolidated statement of changes in equity

for the year ended 31 December 2020

	Called up share capital £'000	Share premium account £'000	Merger reserve £'000	Share based payment reserve £'000	Foreign exchange reserve £'000	Accumu-lated losses £'000	Total equity £'000
Balance at 1 January 2019	4,105	180,016	369	16,143	3,551	(198,625)	5,559
Loss for the year	–	–	–	–	–	(9,615)	(9,615)
Other comprehensive expense							
Foreign currency translation differences	–	–	–	–	(262)	–	(262)
Total comprehensive expense	–	–	–	–	(262)	(9,615)	(9,877)
Transactions with owners							
Share-based payments – value of employee services	–	–	–	82	–	–	82
Proceeds from share issues	2,333	4,240	–	–	–	–	6,573
Total transactions with owners	2,333	4,240	–	82	–	–	6,655
Balance at 31 December 2019	6,438	184,256	369	16,225	3,289	(208,240)	2,337
Balance at 1 January 2020	6,438	184,256	369	16,225	3,289	(208,240)	2,337
Loss for the year	–	–	–	–	–	(8,795)	(8,795)
Other comprehensive expense							
Foreign currency translation differences	–	–	–	–	(251)	–	(251)
Total comprehensive expense	–	–	–	–	(251)	(8,795)	(9,046)
Transactions with owners							
Share-based payments – value of employee services	–	–	–	120	–	–	120
Proceeds from share issues	4,200	15,437	–	–	–	–	19,637
Proceeds from options exercised	4	8	–	–	–	–	12
Total transactions with owners	4,204	15,445	–	120	–	–	19,769
Balance at 31 December 2020	10,642	199,701	369	16,345	3,038	(217,035)	13,060

Consolidated statement of cash flows
for the year ended 31 December 2020

	Note	**2020**	2019
		£'000	£'000
Cash flows from operating activities			
Operating loss		(8,761)	(9,525)
Depreciation and amortisation		1,099	1,094
Loss on disposal of intangible assets		72	187
Impairment of property, plant and equipment		–	439
Impairment of inventory		270	569
Share-based payments		120	82
Changes in working capital (excluding the effects of exchange differences on consolidation)			
Trade and other receivables		(4,545)	(165)
Trade and other payables		(399)	(1,687)
Other liabilities		(2,330)	712
Deferred revenue		2,124	819
Inventory		2,092	(2,473)
Cash consumed by operations		(10,258)	(9,948)
Tax credits received		648	736
Net cash used in operating activities		(9,610)	(9,212)
Cash flows from investing activities			
Purchase of property, plant and equipment		(342)	(779)
Purchase of intangible assets		(513)	(394)
Payment from associate ENVIA		–	3,432
Interest received		6	33
Net cash (used in)/generated from investing activities		(849)	2,292
Cash flows from financing activities			
Proceeds from issues of shares and exercise of options		21,000	7,000
Costs of issuing shares		(1,363)	(427)
Proceeds from issue of share options		12	–
Principal elements of lease payments		(457)	(479)
Interest paid		(142)	(201)
Proceeds from borrowings		567	–
Repayment of borrowings		–	(371)
Net cash generated from financing activities		19,617	5,522
Net increase/(decrease) in cash and cash equivalents		9,158	(1,398)
Cash and cash equivalents at beginning of year	14	4,797	6,964
Exchange movements on cash and cash equivalents		(904)	(769)
Cash and cash equivalents at end of year	14	13,051	4,797

Notes to the consolidated financial statements

1. Accounting policies

The principal accounting policies applied in the preparation of these consolidated financial statements are summarised below. The policies have been consistently applied to each year presented unless otherwise stated.

Basis of preparation

The financial information contained in this document does not constitute Group statutory financial statements as defined in Sections 435 of the Companies Act 2006. It is based on, and is consistent with, that in the Group's statutory consolidated financial statements for the year ended 31 December 2020.

The Group's auditors, PricewaterhouseCoopers LLP, have given an unqualified audit opinion on the consolidated financial statements for the year ended 31 December 2020. The auditors' report included a material uncertainty in respect of going concern to which the auditors drew attention without qualifying their report. The consolidated financial statements will be filed with the Registrar of Companies, subject to their approval by the Company's shareholders on 23 June 2021 at the Company's Annual General Meeting.

The consolidated financial statements have been prepared in accordance with international accounting standards in conformity with the requirements of the UK Companies Act 2006 ("IFRS").

The financial statements have been prepared under the historical cost convention. For the years ended 31 December 2020 and 2019, there were no applicable financial assets and liabilities requiring revaluation at fair value.

The preparation of financial statements to conform to IFRS as adopted by the UK requires the use of certain critical accounting estimates and the exercise of management's judgement in the application of the Company's accounting policies. Areas involving a higher degree of judgement or complexity, and areas where assumptions and estimates are significant to the financial statements are set out in the relevant note below.

Going concern

The nature of the Company's strategy means that the precise timing of milestones and funds generated during the early years of development projects are difficult to predict. The directors have prepared financial forecasts to estimate the likely cash requirements of the Company and Velocys plc over the next twelve months from the date of approval of the financial statements. The cash forecast includes the following assumptions:

- the completion of the current stage of the Front End Engineering Design ("FEED") for the Altalto Immingham Project and the Mississippi Biorefinery Project prior to securing funding for the next stage of FEED to financial close;
- the completion of the new design of the upgraded manufacturing facility;
- the continued process of on-boarding one or more strategic investors to provide the final stages of development funding for either or both the Altalto Immingham Project and the Mississippi Biorefinery Project;
- revenue from the ongoing pre-FEED engineering work from the February 2021 announcement of the collaboration agreement with our customer Toyo Engineering Corporation for the development of their first commercial plant in Japan; and
- the current overhead cost run rate.

The forecasts show that the Company and Velocys plc require additional external funding within the 12-month forecast period to be able to continue as a going concern. This funding may be achieved from one or a combination of, a capital raising (including the possibility of a placement of ordinary shares within the next 12 months) or the realisation of certain assets; selling additional technology licences; performing Pre-FEED engineering work for customers (such as the technical services agreement made with Toyo Engineering Corporation recently for their commercial plant in Japan); UK or US government loans or grants; and selling non-core intellectual property.

The directors are confident that the funding required for the Company and Velocys plc to continue as a going concern will be secured within a period of 12 months from the date of approval of the financial statements and have therefore prepared the financial statements on a going concern basis. However, as at the date of approval of the financial statements no additional funding is committed. Should additional funding not be secured within 12 months from the date of approval of these financial statements, the Company and Velocys plc would not be a going concern. As such, these conditions indicate the existence of a material uncertainty that may cast significant doubt on the Company and Velocys plc's ability to continue as a going concern.

The financial statements do not include any adjustments that would arise if the Company and Velocys plc were unable to continue as a going concern.

Changes in accounting policies

New standards, interpretations and amendments adopted from 1 January 2020

The Company has assessed the new standards, interpretations and amendments issued that are effective from 1 January 2020 and does not consider these to be relevant to the financial statements or to have a material impact on the Company in the current or future reporting periods and on foreseeable future transactions.

New standards, interpretations and amendments not yet effective

There are a number of standards, amendments to standards, and interpretations which have been issued by the International Accounting Standards Board ("IASB") that are effective in future accounting periods that the Company has decided not to adopt early.

The following amendments are effective for the accounting period beginning 1 January 2022:

- Onerous Contracts – Cost of Fulfilling a Contract (Amendments to IAS 37);
- Property, Plant and Equipment: Proceeds before Intended Use (Amendments to IAS 16);
- Annual Improvements to IFRS Standards 2018-2020 (Amendments to IFRS1, IFRS9, IFRS16 and IAS 41); and
- References to Conceptual Framework (Amendments to IFRS 3).

In January 2020, the IASB issued amendments to IAS 1, which clarify the criteria used to determine whether liabilities are classified as current or non-current. These amendments clarify that current or non-current classification is based on whether an entity has the right at the end of the reporting period to defer settlement of the liability for at least twelve months after the reporting period. The amendments also clarify that 'settlement' includes the transfer of cash, goods, services or equity instruments unless the obligation to transfer equity instruments arises from a conversion feature classified as an equity instrument separately from the liability component of a compound financial instrument. The amendments were originally effective for annual reporting periods beginning on or after 1 January 2022. However, in May 2020, the effective date was deferred to annual reporting periods beginning on or after 1 January 2023.

The Company is currently assessing the impact of these new accounting standards and amendments. The Company does not believe that these amendments will have a material impact.

Significant accounting policies

Foreign currency translation

Functional and presentation currency

Items included in the financial statements of each of Velocys plc's subsidiaries are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated financial statements are presented in pounds sterling (£). It should be noted that the functional currency for Velocys plc is pounds sterling as Velocys plc is traded on the AIM market and is head quartered in the UK. Currently all new equity based fund raises are completed in the UK and made in £.

Transactions and balances

Foreign currency transactions are booked in the functional currency of the entity at the exchange rates ruling at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year- end exchange rates of monetary assets and liabilities denominated in foreign currencies are included in the Income statement. Foreign exchange gains and losses that relate to borrowings and cash and cash equivalents are presented in the Income statement within Finance income or Finance costs.

The net investment that Velocys plc has in its subsidiary undertakings is its interest in the net assets of that subsidiary.

Entities within Velocys
The results and financial position of all Velocys entities that have a functional currency different from the presentation currency (none of which is of a hyper-inflationary economy) are translated into the presentation currency as follows:

(i) assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
(ii) income and expenses for each income statement are translated at average exchange rates; and
(iii) all resulting exchange differences are recognised as a movement within other comprehensive income.

On consolidation, exchange differences arising from the translation of the net investment in foreign operations are taken to shareholders' equity.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

Other significant accounting policies are included in the note to which they apply.

2. Exceptional items
Items that are significant by virtue of their size or nature, which are considered non-recurring and which are excluded from the underlying profit measures used by the Board to monitor and measure the underlying performance of the Company are classified as exceptional operating items. Exceptional operating items are included within the appropriate Consolidated income statement category but are highlighted separately in the notes to the financial statements.

The following exceptional items have been included in the Consolidated income statement.

	2020	2019
	£'000	£'000
Administrative expenses:		
Property, plant and equipment impairment	–	(439)
Recovery of loan to an associate	–	533
Total	–	94

Administrative expenses
Property, plant and equipment impairment – in 2019, the Company made an impairment of £439,000 for the land associated with a subsidiary based on a current valuation appraisal by a third party expert. The value of the land either for development or for a sale of the land determined a lesser value than was held as an asset. As a result of the third party's appraisal, the Company determined that the land required an impairment.

Recovery of loan to an associate – in 2019, the Company released deferred revenue in the amount of £533,000 in final settlement of a loan receivable from ENVIA Energy, LLC ("ENVIA") representing the recovery on an impairment first recorded in 2018.

3. Revenue
The Company generates revenue through contracts in which it (i) sells Fischer-Tropsch ("FT") reactors, (ii) sells FT catalyst, (iii) provides licence agreements and (iv) performs engineering services. In general, contracts with the Company provide a licence agreement for the use of its intellectual property associated with the catalyst and reactors both of which have been specifically designed and over which the Company holds a significant number of patents. The majority of the Company's revenue is derived from a small number of significant commercial customers and development partners.

Revenue is recognised when the Company satisfies a performance obligation by transferring promised goods or services to a customer. The sales income related to sales of reactors and catalyst will be recognised as the performance obligations are satisfied. Revenue from engineering services is earned on a time and materials basis and is recognised as the work is performed provided that it does not relate to the sale of equipment and therefore is bound by the performance obligations of that sale.

If the entity is providing a single performance obligation in the form of an integrated set of activities, each contract is assessed to determine if it meets the criteria for recognition over time. This would require the contract to either transfer control of the combined output over time or for the entity to have an enforceable right of payment for the performance completed to date for activities that do not create an asset with alternative use.

One contract that was signed in 2018 with reactor and catalyst deliveries completed in 2020 is subject to a performance test run in 2021 or performance obligations which expire under the terms of the contract in 2021 if the test is not completed. This has been assessed as a combined performance obligation and it was determined that the above criteria have not been met as at the year end. As such, all consideration received has been deferred and revenue will be recognised when the project performance obligations described above have been met.

Critical estimates and judgements

Determining whether the goods or services provided are considered distinct performance obligations from the supply of equipment can require significant judgment. The Company's agreements, in some instances, could have a single performance obligation, which would result in the deferral of revenue until the performance obligation is satisfied. This is the case when the entity promises an integrated package of goods and services and where the customer is receiving a combined output (for example, an engineering service that results in operational technology at a particular site). In other instances, there will be no integration service and each good or service will be considered separately.

When there are multiple performance obligations, revenue from goods or services is allocated to the respective performance obligations based on relative stand alone selling prices and is recognised as the performance obligations are satisfied. Revenue from goods or services is measured as the amount of consideration expected to be received in exchange for the goods and services delivered.

	2020	2019
	£'000	£'000
FT reactor, catalyst and licence	63	273
Engineering services	115	59
Total	178	332

FT reactor, catalyst and licence revenue in the amount of £63,000 for the year ended 31 December 2020 consisted principally of the sale of catalyst to a customer in Japan, and in the previous year consisted principally of the sale of substacks to the same customer This revenue was recognised at a specific point in time upon delivery and title transfer of the catalyst (and in 2019, substacks) for the customer's demonstration plant. Revenue from engineering services was recognised on a time and materials basis during the period in which the services were delivered.

4. Finance income

	2020	2019
	£'000	£'000
Interest income on bank deposits	6	48
Total	6	48

5. Finance costs

	2020	2019
	£'000	£'000
Interest on lease liabilities	142	196
Interest on borrowings	–	4
Foreign exchange losses	708	229
Total	850	429

6. Other income

Other income consists of items such as government grants, sales of fixed assets and any other operating income recognised outside of commercial activities.
Income from government grants is recognised only when there is reasonable assurance that (a) the Company has complied with any conditions attached to the grant and (b) the grant will be received. Further details relating to the £290,000 included below can be found in note 17.

	2020	2019
	£'000	£'000
Income from government grants	290	–
Release of aged deposit received	80	–
Profit on sale of fixed assets	30	79
Total	400	79

7. Employee benefit expense

Short-term employee benefits
Accruals are included to reflect the cost of short-term compensation to employees for absences such as paid leave.

Pensions
The Company operates various defined contribution pension schemes for its employees. The Company has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefit derived from the current and prior periods.

The amount charged to the Consolidated income statement in respect of pension costs and other post-retirement benefits represents the contributions payable in the year. Differences between contributions payable and contributions actually paid are accrued. The Company has no further payment obligations once the contributions have been paid.

The average monthly number of Company employees (including Executive Directors) was as follows.

	2020	2019
	number	number
Research, design and development	17	15
Administration	16	18
Total average headcount	33	33

Their aggregate remuneration comprised the following items.

	2020	2019
	£'000	£'000
Wages and salaries	4,813	3,817
Short-term non-monetary benefits	560	543
Social security contributions and similar taxes	393	286
Defined contribution pension costs	228	188
Severance expense	43	138
Share-based payments granted to directors and employees (note 15)	120	82
Total remuneration before capitalisation of wages and salaries	6,157	5,054
Capitalisation of wages and salaries	(1,627)	(1,722)
Total remuneration	4,530	3,332

Wages and salaries include discretionary bonus payments made to Executive Directors and employees totalling £983,000 during the year ended 31 December 2020 in respect of 2019 performance. In 2019, £545,000 was credited to Wages and salaries in respect of bonuses, as the total amount paid out to Executive Directors and employees was lower than the amount accrued at 31 December 2018. The Company has not recorded a bonus accrual as at 31 December 2020 in respect of 2020 performance.

Short term non-monetary benefits are in respect of health insurance benefits provided to employees and the amounts paid for workers compensation policies in respect of US based employees.
The capitalisation of wages and salaries relates to employees who manufacture the reactors associated with one of the Company's sales contracts, where the costs are deferred until revenue and cost recognition is allowed in accordance with the performance obligations of the contract. In addition, capitalisation of wages and salaries includes those costs related to the Altalto project which are offset against Other liabilities.

Severance in the amount of £43,000 was paid to one employee who was made redundant in the year. No redundancies were made during 2019, however severance in the amount of £138,000 in 2019 was paid to a former director, who resigned in December 2018.

8. Basic and diluted loss per share

The basic loss per share is calculated by dividing the loss attributable to owners of the parent company by the weighted average number of ordinary shares in issue during the year.

	2020	2019
Loss attributable to owners of Velocys plc (£'000s)	(8,795)	(9,615)
Weighted average number of ordinary shares in issue	836,710,315	507,218,656
Basic and diluted loss per share (pence)	(1.05)	(1.90)

Diluted loss per share is calculated by adjusting the weighted average number of shares in issue to assume conversion of all potential dilutive shares. Share options have not been included in the number of shares used for the purpose of calculating diluted loss per share since these would be anti-dilutive for the period presented. At the end of 2020 and 2019 there were no other potentially dilutive instruments.

9. Intangible assets

Significant accounting policies
Cost or valuation and amortisation

Goodwill

Goodwill is stated at cost less impairments. Goodwill is deemed to have an indefinite life and is tested for impairment at least annually.

In-process technology

Development costs, where the related expenditure is separately identifiable and measurable, and management are satisfied as to the ultimate technical and commercial viability of the project and that the asset will generate future economic benefit based on all relevant available information, are recognised as an intangible asset. Capitalised development costs are carried at cost less accumulated amortisation and impairment losses. Amortisation is charged over periods expected to benefit, typically up to 20 years, commencing with launch of the product. Development costs not meeting the criteria for capitalisation are expensed as incurred.

Patents, licences and trademarks

Patents and trademarks are recorded at cost less accumulated amortisation and impairment losses. Amortisation is charged on a straight-line basis over a period of 20 years, which is their estimated useful economic life. Residual values and useful lives are reviewed annually and adjusted if appropriate. The Company decided to abandon certain non-core patents in 2020 and 2019. This resulted in a loss on disposal of patents of £72,000 (2019: loss of £187,000).

Software

Purchased software is recorded at cost less accumulated amortisation and impairment losses. Amortisation is charged on a straight- line basis over its estimated useful life or its license period, whichever is the shorter.

Amortisation
The Company amortises intangible assets with a limited useful life, using a straight-line method, over the following periods:

- In-process technology: up to 20 years
- Patents, licences and trademarks: 20 years
- Software: 2-5 years

Amortisation charges of £137,000 for patents, licences and trademarks are included in administrative expenses (2019: £112,000). There were no amortisation charges recorded in respect of other classes of intangible assets during the year as the net book value was £nil (2019: £nil).

Impairment
Intangible assets are reviewed for impairment annually and whenever events or changes in circumstances indicate their carrying value may not be recoverable. To the extent carrying value exceeds recoverable amount, the difference is recognised as an expense in the income statement. The recoverable amount used for impairment testing is the higher of value in use and fair value less costs of disposal. For the purpose of impairment testing, assets are generally tested individually or at a Cash Generating Unit ("CGU") level which represents the lowest level for which there are separately identifiable cash inflows that are largely independent of cash inflows from other assets or groups of assets. The Company has one CGU on the basis that the key end use market is that of synthetic fuels production. At this stage, the synthetic fuels segment represents 100% of the business and therefore represents the only material segment. Based on management's judgement, all products and services offered within the operating segment have similar economic characteristics.

An impairment loss in respect of Goodwill is not reversed. An impairment loss in respect of other intangible assets is reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the loss was recognised, or if there has been a change in the estimate used to determine the recoverable amount. A loss is reversed only to the extent that the asset's carrying amount does not exceed that which would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

In 2017, the Company recorded an impairment of intangible assets totalling £28.8m, which comprised £7.4m of Goodwill, £20.6m of In-process technology and £0.8m of Patents, licence and trademarks. The majority of the intangible assets arose on the Company's acquisition of Velocys, Inc. in November 2008 and relates to the acquired microchannel process technology which forms an integral part of the Company's patented Fischer-Tropsch ("FT") reactors. Over the last few years, the FT reactors have been used successfully in demonstration plants in both the US and Japan, and have also been manufactured and supplied to a commercial customer for which the Company has received £7.8m of revenue including licence fees, reactor sales and catalyst sales (see note 16).

For the impairment assessment performed in 2017, the recoverable amount was determined by comparing the carrying amount of the Company's total net assets with the fair value of the business, by reference to the value of Velocys plc's market capitalisation. This approach has been followed in subsequent years including for the assessment performed at 31 December 2020, to test whether further impairments or a reversal of previous impairments is required.

The analysis performed at 31 December 2020 compared the carrying amount of £0.7m with the value of Velocys plc's equity based on the AIM-listed shares at 31 December 2020.

This assessment also considered the operating performance of the Company during 2020 which included delivery of reactors and catalyst to an existing commercial customer, progress being made on our reference projects and new external funding obtained. Whilst there was clear evidence of the Company's progress during 2020, Management also considered the wider economic environment and increased risks posed by the COVID-19 pandemic.

Critical estimates and judgements
In assessing whether there is any indication that an asset may be impaired or whether a reversal of prior year impairments is required, the Company considers, as a minimum, a number of indicators. In 2020, the Company considered:

- At 31 December 2020, whether the carrying amount of the Company's net assets was above or below Velocys plc's market capitalisation;

- Whether significant increases or decreases in the market price of the assets had occurred;
- Whether there were significant favourable or adverse changes in the extent or manner in which the assets are being used; and
- Whether there were significant favourable or adverse changes in the global market for sustainable aviation fuel and global economic factors more generally.

Based on the 2020 analysis, the Company concluded that no further impairment was required.
As detailed in the accounting policy set out above, the Company is considered to operate as a single CGU. Whilst the Company's strategy and biorefinery development plans are clearly defined, Management considers that it is still too early to rely upon its revenue forecasts for long-term discounted cash flow analysis. Consequently, the CGU's recoverable amount has been determined based on its fair value less costs of disposal (fair value), by reference to the total value of the parent company's equity based on the AIM-listed shares of the parent company, consistent with the impairment assessment performed in previous years.

The Company also decided not to reverse prior year impairments as at 31 December 2020, despite the market capitalisation exceeding the carrying amount of the Company's net assets, as the Board concluded that the Company's current commercial position, without any significant new customer contracts or additional investors into the reference projects outweighed the other positive aspects considered.

2020	Goodwill £'000	In-process technology £'000	Patents, licence and trademarks £'000	Software £'000	Total £'000
Cost					
At 1 January 2020	7,398	23,681	1,598	96	32,773
Additions	–	–	513	–	513
Disposals	–	–	(103)	–	(103)
Foreign exchange movement	–	–	(37)	–	(37)
At 31 December 2020	7,398	23,681	1,971	96	33,146
Accumulated amortisation and impairment					
At 1 January 2020	7,398	23,681	1,154	96	32,329
Charge for the year	–	–	137	–	137
Disposals	–	–	(31)	–	(31)
Foreign exchange movement	–	–	(29)	–	(29)
At 31 December 2020	7,398	23,681	1,231	96	32,406
Net book amount					
At 31 December 2020	–	–	740	–	740

2019	Goodwill £'000	In-process technology £'000	Patents, licence and trademarks £'000	Software £'000	Total £'000
Cost					
At 1 January 2019	7,398	23,681	1,580	96	32,755
Additions	–	–	394	–	394
Disposals	–	–	(291)	–	(291)
Foreign exchange movement	–	–	(85)	–	(85)
At 31 December 2019	7,398	23,681	1,598	96	32,773
Accumulated amortisation and impairment					
At 1 January 2019	7,398	23,681	1,223	96	32,398
Charge for the year	–	–	112	–	112
Disposals	–	–	(104)	–	(104)
Foreign exchange movement	–	–	(77)	–	(77)
At 31 December 2019	7,398	23,681	1,154	96	32,329
Net book amount					
At 31 December 2019	–	–	444	–	444

10. Property, plant and equipment

Property, plant and equipment is stated at historical cost, net of depreciation and any provision for impairment. Cost includes the original purchase price of the asset and the costs attributable to bringing the asset to working condition for its intended use. Depreciation is provided on all property, plant and equipment at rates calculated to write off the cost, less estimated residual value, of each asset on a straight-line basis over its expected useful life, which for plant and machinery is three to ten years. No depreciation is provided on land or assets under construction.

Residual values and useful lives are reviewed annually. Values are estimated using benchmark prices at the balance sheet date; useful lives are estimated based on management expectations of future project requirements and operational assessment of the state of assets.

Assets are reviewed for impairment annually and also whenever events or changes in circumstances indicate their carrying value may not be recoverable. To the extent the carrying value exceeds the recoverable amount, the difference is recorded as an expense in the Income statement. The recoverable amount used for impairment testing is the higher of the value in use and fair value less costs of disposal. For the purpose of impairment testing, assets are generally tested individually or at a CGU level, which represents the lowest level for which there are separately identifiable cash inflows, which are largely independent of cash inflows from other assets or groups of assets. Property, plant and equipment were included in the list of items to which an impairment was considered but nothing applied subsequent to the impairment review.

An impairment loss in respect of property, plant and equipment would be reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the loss was recognised, or if there has been a change in the estimate used to determine the recoverable amount. A loss is reversed only to the extent that the assets carrying amount does not exceed that which would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

Expenditure funded by research partners is only capitalised where there are no significant rights acquired by the third party over the asset and the asset has a clear enduring use beyond the specific funding project, these are regularly reviewed.

2020	Assets under construction £'000	Land £'000	Plant and machinery £'000	Total £'000
Cost				
At 1 January 2020	982	1,299	8,281	10,562
Additions	–	–	342	342
Transfers to plant and machinery	(982)	–	982	–
Foreign exchange	–	(78)	(298)	(376)
At 31 December 2020	–	1,221	9,307	10,528
Accumulated depreciation and impairment				
At 1 January 2020	–	1,142	7,686	8,828
Charge for the year	–	–	500	500
Impairment	–	–	–	–
Disposals	–	–	–	–
Foreign exchange	–	(68)	(211)	(279)
At 31 December 2020	–	1,074	7,975	9,049
Net book amount				
At 31 December 2020	–	147	1,332	1,479

2019	Assets under construction £'000	Land £'000	Plant and machinery £'000	Total £'000
Cost				
At 1 January 2019	532	1,285	7,841	9,658
Additions	621	–	158	779
Transfers to plant and machinery	(171)	–	171	–
Foreign exchange	–	14	111	125
At 31 December 2019	982	1,299	8,281	10,562
Accumulated depreciation and impairment				
At 1 January 2019	33	706	7,100	7,839
Charge for the year	–	–	568	568
Impairment	–	439	–	439
Transfer to plant and machinery	(33)	–	33	–
Foreign exchange	–	(3)	(15)	(18)
At 31 December 2019	–	1,142	7,686	8,828
Net book amount				
At 31 December 2019	982	157	595	1,734

As at 31 December 2020, the Company had not entered into any contractual commitments for the material acquisition of property, plant and equipment (2019: none).

As at 31 December 2020, the gross carrying amount of fully depreciated property, plant and equipment still in use was £3,827,000.

11. Leases

The Company leases certain building and equipment under non-cancellable leases with varying lease terms. Until the 2018 financial year, leases of property, plant and equipment were classified as either finance leases or operating leases under the principles of IAS 17 Leases. As a result of the adoption of IFRS 16 on 1 January 2019, the company recognised a right-of-use asset and a lease liability on the Balance Sheet. These liabilities were measured at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rate as of 1 January 2019. The weighted average lessee's incremental borrowing rate applied to the lease liabilities on 1 January 2019 was approximately 21%.

The Company is exposed to potential future increases in variable lease payments based on an index or rate, which are not included in the lease liability until they take effect. When adjustments to lease payments based on an index or rate take effect, the lease liability is reassessed and adjusted against the right-of-use asset.

Lease terms are negotiated on an individual basis and contain a wide range of different terms and conditions. The lease agreements do not impose any covenants other than the security interests in the leased assets that are held by the lessor. Leased assets may not be used as security for borrowing purposes. Building leases are typically for a fixed period of time but may have extension options. Lease payments to be made under reasonably certain extension options are also included in the measurement of the liability.

Lease payments are allocated between principal and finance cost. The finance cost is charged to profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period.

The associated right-of-use assets for property leases were measured on a retrospective basis as if the new rules had always been applied. Other right-of-use assets were measured at the amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognised in the balance sheet as at 31 December 2018. There were no onerous lease contracts that would have required an adjustment to the right-of-use assets at the date of initial application.

To determine the incremental borrowing rate, the Company uses a build-up approach that starts with a risk-free interest rate adjusted for credit risk for leases, which does not have recent third party financing, and makes adjustments specific to the lease, e.g. term, country, currency and security. The Company is exposed to potential future increases in variable lease payments based on an index or rate, which are not included in the lease liability until they take effect. When adjustments to lease payments based on an index or rate take effect, the lease liability is reassessed and adjusted against the right-of-use asset. Interest expense (included in finance costs) was £142,000 (2019: £196,000).

Right-of-use assets are generally depreciated over the shorter of the asset's useful life and the lease term on a straight-line basis. Impairment of right-of-use assets is accounted for under IAS 36.

Payments associated with short-term leases and all leases of low-value assets are recognised on a straight-line basis as an expense in profit or loss. Short-term leases are leases with a lease term of 12 months or less. Expense related to short term leases and lease of low-value was £2,000 (2019: £2,000) and were included in administrative expenses.

Critical estimates and judgements

Leases - Estimating the incremental borrowing rate

The Company cannot readily determine the interest rate implicit in the lease, therefore, it uses its incremental borrowing rate ("IBR") to measure lease liabilities. The IBR is the rate of interest that the Company would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment. The IBR therefore reflects what the Company 'would have to pay', which requires estimation when no observable rates are available (such as for subsidiaries that do not enter into financing transactions) or when they need to be adjusted to reflect the terms and conditions of the lease (for example, when leases are not in the subsidiary's functional currency). The Company estimates the IBR using a build-up approach as stated above. The incremental borrowing rate is not sensitive to changes as a 10% movement in the IBR does not have a material impact on the lease liability.

Leases - Determining the lease term of contracts with renewal and termination options

The Company determines the lease term as the non-cancellable term of the lease, together with any periods covered by an option to extend the lease if it is reasonably certain to be exercised, or any periods covered by an option to terminate the lease, if it is reasonably certain not to be exercised.

The Group has several lease contracts that include extension and termination options. The Group applies judgement in evaluating whether it is reasonably certain whether or not to exercise the option to renew or terminate the lease. That is, it considers all relevant factors that create an economic incentive for it to exercise either the renewal or termination. After the commencement date, the Company reassesses the lease term if there is a significant event or change in circumstances that is within its control and affects its ability to exercise or not to exercise the option to renew or to terminate.

The balance sheet presents the following amounts relating to its right-to-use assets:

	Equipment	Buildings	Total
Cost	£'000	£'000	£'000
At 1 January 2020	168	1,096	1,264
Transfers to Buildings	(35)	35	–
Additions	85	211	296
Foreign exchange	(8)	(28)	(36)
At 31 December 2020	210	1,314	1,524
Accumulated depreciation			
At 1 January 2020	63	365	428
Charge for the year	63	399	462
Foreign exchange	(4)	(15)	(19)
At 31 December 2020	122	749	871
Net book amount			
At 31 December 2020	88	565	653

Cost	Equipment £'000	Buildings £'000	Total £'000
At 1 January 2019	168	870	1,038
Additions	–	208	208
Foreign exchange	–	18	18
At 31 December 2019	168	1,096	1,264
Accumulated depreciation			
At 1 January 2019	–	–	–
Charge for the year	63	351	414
Foreign exchange	–	14	14
At 31 December 2019	63	365	428
Net book amount			
At 31 December 2019	105	731	836

Additions to right-to-use assets during 2020 of £296,000 (2019: £208,000) mainly related to the expansion of the Company's office space within the Oxford Science Park, UK.

Lease liability	**2020 £'000**	2019 £'000
Current	470	581
Non-Current	270	343
	740	924

12. Inventories

Inventories are stated at the lower of cost or net realisable value less provision for impairment. Cost is determined on a first-in, first- out basis and includes transport and handling costs. In the case of manufactured products, cost includes all direct expenditure including production overheads. Where necessary, provision is made for obsolete, slow-moving and defective inventories. Items purchased for use in externally funded research and development projects are expensed to that contract immediately. Items held for the Company's own development are also expensed when acquired. Items purchased for ongoing commercial sale are held in inventory and expensed when used or sold.

	2020 £'000	2019 £'000
Raw materials and consumables	336	1,782
Work in progress	45	1,550
Finished goods	589	–
Total	970	3,332

Raw material and consumables consist of material that will be consumed in the manufacturing of reactors and catalyst. Work in progress consists of labour associated with the manufacturing of reactors. In 2020, the Company recognised £23,000 (2019: £73,000) of inventory in Cost of sales in the Consolidated income statement. The majority of the inventory delivered to customers during 2020 is recorded as a deferred cost within Trade and other receivables (see note 13).

As at 31 December 2020, the Company had a total inventory provision of £653,000 (£383,000). The Company recorded a provision of £270,000 (2019: -£191,000) related to slow moving inventory in the Administrative expenses line of the Consolidated income statement.

In 2019, the Company recognised a provision of £38,000 related to two cores manufactured for use in its reactors which did not meet the Company's specifications, and impaired test reactors totalling £123,000. The Company also reversed an impairment of £352,000 made in 2017 for a reactor that was delivered to a customer during 2019. The cost of this reactor is included in deferred costs as at 31 December 2020 and 2019 as it relates to the Red Rock Biofuels customer contract.

13. Trade and other receivables

	2020	2019
	£'000	£'000
Trade receivables	110	37
Deferred costs	4,947	1,054
Prepaid costs	531	447
Grants receivable	290	–
Other receivables	304	99
Total	6,182	1,637

Trade receivables represent assets that are held for collection of contractual cash flows and those cash flows represent solely payments of principal and interest. Trade receivables, in general, are collected within 45 days of invoice date.

Deferred costs are in respect of the Red Rock Biofuels customer contract, for which the Company has deferred revenue as shown in note 16.

Trade receivables and deferred costs (contract assets) are written off where there is no reasonable expectation of recovery. Indicators that there is no reasonable expectation of recovery include, amongst others, the failure of a debtor to engage in a repayment plan with the Company, and a failure to make contractual payments for a period of greater than 90 days past due.

Impairment losses on trade receivables and contract assets are presented as net impairment losses within administrative expenses in the income statement. Subsequent recoveries of amounts previously written off are credited against the same line item.

Grants receivable relate to the Stage Two grant funding for the Altalto waste-to-jet fuels project from the UK Department for Transport ("DfT"), under the Future Fuels for Flight and Freight Competition ("F4C"). The DfT has made £500,000 of the Stage Two grant available to the Company. As at 31 December 2020 the Company had completed the project milestones to qualify for the first tranche of £290,000 to be paid, which was received in January 2021.

As at 31 December 2020 other receivables consist of vendor deposits and sales taxes recoverable. As at 31 December 2019 other receivables mainly consisted of vendor deposits.

Critical estimates and judgements

The Company applies the IFRS 9 simplified approach to measuring Expected Credit Loss ("ECL"), which uses a lifetime expected loss allowance for trade receivables. To measure the ECL, trade receivables have been grouped based on shared credit risk characteristics and the days past due. The Company will adjust its analysis based on the historical credit loss. The Company's historical credit loss experience may also not be representative of customer's actual default in the future. As part of the ECL analysis, it was noted that trade receivables are considered to be both short term and low credit risk and as such any provision would be trivial.

14. Cash and cash equivalents

Cash and cash equivalents includes cash in hand, deposits held at call with banks and other short-term highly liquid investments with original maturities of three months or less.

	2020	2019
	£'000	£'000
Cash and cash equivalents	13,051	4,797
Total	13,051	4,797

Cash and cash equivalents is denominated in UK sterling, Euros and US dollars as follows.

	2020	2019
	£'000	£'000
Cash and cash equivalents UK sterling denominated	6,584	3,783
US dollar denominated	6,465	927
Euro denominated	2	87
Total	13,051	4,797

15. Trade and other payables

	2020	2019
	£'000	£'000
Trade payables	360	333
Other taxation and social security	31	45
Accruals	541	953
Total	932	1,331

Due to their short maturity, the fair value of trade and other payables is not considered to be materially different to their carrying values, based on discounted cash flows.

All trade payables are due in 60 days or less (2019: 60 days or less).

16. Deferred revenue

Deferred revenue consists of contract liabilities as a result of instances in which the Company receives payments prior to the satisfaction of the performance obligation, as defined in IFRS 15. Deferred revenue is allocated to the respective performance obligations based on relative transaction prices and is recognised as the performance obligation is satisfied. Determining the performance obligations associated with the Company's contracts can require significant judgment.

The Company recognised the following liabilities associated with contracts with customers:

£'000	Catalyst	Reactor	License	Total
At 1 January 2019	2,065	1,949	1,199	5,213
Contract liabilities incurred	499	853	–	1,352
Released deferred revenue	(533)	–	–	(533)
At 31 December 2019	2,031	2,802	1,199	6,032
Contract liabilities incurred	1,155	969	–	2,124
At 31 December 2020	3,186	3,771	1,199	8,156

In 2019 the Company released deferred revenue in the amount of £533,000 in final settlement of the ENVIA loan receivable balance representing a recovery on the impairment recorded in 2018 (see note 2).

Management expects that approximately 95% of the deferred revenue as at 31 December 2020 could be recognised as revenue in 2021 if the related performance obligations are met.

17. Post position financial events

The following events took place after 31 December 2020.

F4C grant from the Department for Transport

In January 2021, the Company received £290,000 of grant funding for the Altalto waste-to-fuels project from the UK Department for Transport ("DfT"), under the Future Fuels for Flight and Freight Competition ("F4C"). The DfT made a total of £0.5m available to Velocys under Phase Two of the scheme and the Company expects to receive the remaining £210,000 in the first half of 2021 subject to completion of project milestones.

US SBA loan forgiveness application
In April 2020, the Company received a $709,000 (£567,000) loan from the Pay-check Protection Program awarded by the Small Business Administration ("SBA"), a US Federal Agency. The SBA program is part of the Federal stimulus package known as the CARES (Coronavirus Aid, Relief and Economic Security) Act to offer help to small businesses in the USA during the COVID-19 crisis. This unsecured loan was awarded to support Velocys' US payroll costs in the short-term. It is an unsecured loan with a 2-year maturity and 0.98% interest. No interest or principal payments are due in the first six months. The loan is however eligible for "forgiveness", becoming non-repayable upon application by Velocys after 60 days from receipt if used for retaining US employees and maintaining US payroll costs of at least this amount in the period until the end of June 2020. Velocys met the forgiveness criteria and submitted its application to the SBA in January 2021.

Altalto Joint Development Agreement
In January 2021, by mutual consent of the parties to the Altalto Joint Development Agreement, Shell International Petroleum Company Limited ("Shell") withdrew from the agreement. Velocys and British Airways plc ("British Airways") will continue to work together in order to secure finance for the Altalto Immingham plant. Shell will no longer have an option over shares in Altalto Limited (a subsidiary of the Company), nor any rights or obligations in relation to the Altalto project. The Altalto project has no immediate funding calls and will continue according to its existing development plan. There is no direct financial impact on Altalto or Velocys as a result of these changes.

Collaboration Agreement with Toyo Engineering Corporation
In February 2021, the Company announced the signing of a collaboration agreement with Toyo Engineering Corporation ("Toyo") to start the development of their commercial projects to produce sustainable aviation fuel and other renewable fuels in Japan. The agreement follows on from the successful work already conducted in 2020 between Velocys and Toyo at the biomass-to-jet-fuel demonstration facility in Japan. The Company will grant an exclusive right for Toyo to secure and use the licence and technical services of the Velocys Fischer-Tropsch technology for a commercial plant in Japan. An advance deposit of $4.0m (£3.0m) was received in 2019 of which $3.5m (£2.6m) remains in escrow, which will be offset against future revenues.

Grant of share options to Executives and employees
In February 2021, the Company granted options under the 2012 Share Option Scheme totalling 14,088,205 to Executives and senior management in respect of 2020 performance and options totalling 500,000 to new employees who joined the Company during 2020. The exercise price was set at the time of grant at 7.86 pence being the highest of the share price at the last fund raising, the share price on the date of grant and the weighted average share price for the month prior to grant. The Executive Directors, Mr. Wareborn and Mr. Morris received a total of 3,264,503 and 2,938,053 options respectively, allocated equally between time-based and performance-based options.

Extension of the Altalto option agreement
In March 2021, the Company announced that it has agreed with British Airways to extend the Altalto option agreement to 31 March 2022. Exercise of the option would give both parties, Velocys and British Airways, equal equity ownership (50/50) of Altalto Ltd and the right to appoint a director. There is no impact on the financial results for the year ended 31 December 2020.

18. Statutory information
Copies of the 2020 Annual Report and Accounts will be posted or emailed to shareholders at least 21 days before the Company's Annual General Meeting and may be obtained, free of charge for one month from the date of posting, from the registered office of Velocys plc, Magdalen Centre, Robert Robinson Avenue, The Oxford Science Park, Oxford, OX4 4GA, UK, as well as from the Company's website www.velocys.com.

19. Annual General Meeting
The Annual General Meeting ("AGM") is to be held on 23 June 2021. Notice of the AGM will be dispatched to shareholders with the Company's Annual Report and Accounts.