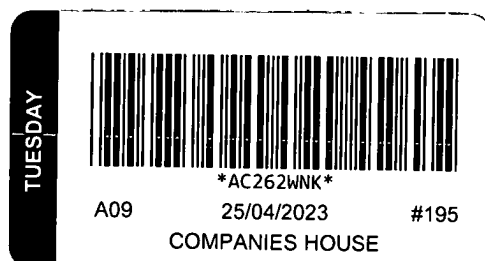


Company registration number 06652152 (England and Wales)

SMARTKEM LIMITED
UNAUDITED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2022
PAGES FOR FILING WITH REGISTRAR



SMARTKEM LIMITED

CONTENTS

	Page
Balance sheet	1 - 2
Statement of changes in equity	3
Notes to the financial statements	4 - 11

SMARTKEM LIMITED**BALANCE SHEET****AS AT 31 DECEMBER 2022**

	Notes	2022		2021	
		£	£	£	£
Fixed assets					
Tangible assets	4		500,212		594,755
Current assets					
Debtors	5	3,745,758		2,109,330	
Cash at bank and in hand		654,617		6,501,699	
		<u>4,400,375</u>		<u>8,611,029</u>	
Creditors: amounts falling due within one year	6	<u>(2,658,814)</u>		<u>(1,696,866)</u>	
Net current assets			<u>1,741,561</u>		<u>6,914,163</u>
Total assets less current liabilities			<u>2,241,773</u>		<u>7,508,918</u>
Creditors: amounts falling due after more than one year	7		<u>(15,494,702)</u>		<u>(12,739,080)</u>
Net liabilities			<u>(13,252,929)</u>		<u>(5,230,162)</u>
Capital and reserves					
Called up share capital	9		13,322		13,322
Share premium account			29,044,365		29,044,365
Profit and loss reserves			<u>(42,310,616)</u>		<u>(34,287,849)</u>
Total equity			<u>(13,252,929)</u>		<u>(5,230,162)</u>

The directors of the company have elected not to include a copy of the profit and loss account within the financial statements.

For the financial year ended 31 December 2022 the company was entitled to exemption from audit under section 477 of the Companies Act 2006 relating to small companies.

The directors acknowledge their responsibilities for complying with the requirements of the Companies Act 2006 with respect to accounting records and the preparation of financial statements.

The members have not required the company to obtain an audit of its financial statements for the year in question in accordance with section 476.

These financial statements have been prepared and delivered in accordance with the provisions applicable to companies subject to the small companies regime.


SMARTKEM LIMITED

BALANCE SHEET (CONTINUED)

AS AT 31 DECEMBER 2022

20/4/2023

The financial statements were approved by the board of directors and authorised for issue on and are signed on its behalf by:

DocuSigned by:


415A4F5BD0AE4CF...
B Keck
Director

Company Registration No. 06652152

SMARTKEM LIMITED**STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2022**

	Notes	Share capital £	Share premium account £	Profit and loss reserves £	Total £
Balance at 1 January 2021		12,077	29,031,753	(27,659,636)	1,384,194
Year ended 31 December 2021:					
Loss and total comprehensive income for the year		-	-	(10,468,450)	(10,468,450)
Issue of share capital	9	1,245	12,612	-	13,857
Credit to equity for equity settled share-based payments	8	-	-	3,840,237	3,840,237
Balance at 31 December 2021		13,322	29,044,365	(34,287,849)	(5,230,162)
Year ended 31 December 2022:					
Loss and total comprehensive income for the year		-	-	(8,022,767)	(8,022,767)
Balance at 31 December 2022		13,322	29,044,365	(42,310,616)	(13,252,929)

SMARTKEM LIMITED

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2022

1 Accounting policies

Company information

Smartkem Limited is a private company limited by shares incorporated in England and Wales. The registered office is Manchester Technology Center, Hexagon Tower, Delaunays Road, Blackley, Manchester, M9 8GQ.

1.1 Accounting convention

These financial statements have been prepared in accordance with FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland" ("FRS 102") and the requirements of the Companies Act 2006 as applicable to companies subject to the small companies regime. The disclosure requirements of section 1A of FRS 102 have been applied other than where additional disclosure is required to show a true and fair view.

The financial statements are prepared in sterling, which is the functional currency of the company. Monetary amounts in these financial statements are rounded to the nearest £.

The financial statements have been prepared under the historical cost convention. The principal accounting policies adopted are set out below.

1.2 Going concern

The company meets its day to day working capital requirements through long-term funding provided in February 2021 by its parent company, SmartKem, Inc. (Note 8 and Note 13).

After making enquiries, the directors have a reasonable expectation that the company has adequate resources to continue in operational existence for the foreseeable future. The company therefore continues to adopt the going concern basis in preparing its financial statements.

1.3 Turnover

Turnover from the sale of organic semiconductor materials is recognised upon raising an invoice following dispatch of materials to the customer.

Turnover from Joint Development Agreements is recognised in the accounting period in which agreed research, development and technology transfers deliverables under each phase of such agreements are completed.

1.4 Tangible fixed assets

Tangible fixed assets are initially measured at cost and subsequently measured at cost, net of depreciation and any impairment losses.

Depreciation is recognised so as to write off the cost of assets less their residual values over their useful lives on the following bases:

Plant and equipment	25% on net book value
Fixtures and fittings	25% on net book value
Computers	25% on net book value

The gain or loss arising on the disposal of an asset is determined as the difference between the sale proceeds and the carrying value of the asset, and is credited or charged to profit or loss.

1.5 Impairment of fixed assets

At each reporting period end date, the company reviews the carrying amounts of its tangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the company estimates the recoverable amount of the cash-generating unit to which the asset belongs.

SMARTKEM LIMITED

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2022

1 Accounting policies

(Continued)

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately in profit or loss.

Recognised impairment losses are reversed if, and only if, the reasons for the impairment loss have ceased to apply. Where an impairment loss subsequently reverses, the carrying amount of the asset (or cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (or cash-generating unit) in prior years. A reversal of an impairment loss is recognised immediately in profit or loss.

1.6 Cash and cash equivalents

Cash and cash equivalents are basic financial assets and include cash in hand, deposits held at call with banks, other short-term liquid investments with original maturities of three months or less, and bank overdrafts.

1.7 Financial instruments

The company has elected to apply the provisions of Section 11 'Basic Financial Instruments' of FRS 102 to all of its financial instruments.

Financial instruments are recognised in the company's balance sheet when the company becomes party to the contractual provisions of the instrument.

Financial assets and liabilities are offset, with the net amounts presented in the financial statements, when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis or to realise the asset and settle the liability simultaneously.

Basic financial assets

Basic financial assets, which include debtors and cash and bank balances, are initially measured at transaction price including transaction costs and are subsequently carried at amortised cost using the effective interest method unless the arrangement constitutes a financing transaction, where the transaction is measured at the present value of the future receipts discounted at a market rate of interest. Financial assets classified as receivable within one year are not amortised.

Impairment of financial assets

Financial assets, other than those held at fair value through profit and loss, are assessed for indicators of impairment at each reporting end date.

Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows have been affected. If an asset is impaired, the impairment loss is the difference between the carrying amount and the present value of the estimated cash flows discounted at the asset's original effective interest rate. The impairment loss is recognised in profit or loss.

If there is a decrease in the impairment loss arising from an event occurring after the impairment was recognised, the impairment is reversed. The reversal is such that the current carrying amount does not exceed what the carrying amount would have been, had the impairment not previously been recognised. The impairment reversal is recognised in profit or loss.

SMARTKEM LIMITED

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2022

1 Accounting policies

(Continued)

Derecognition of financial assets

Financial assets are derecognised only when the contractual rights to the cash flows from the asset expire or are settled, or when the company transfers the financial asset and substantially all the risks and rewards of ownership to another entity, or if some significant risks and rewards of ownership are retained but control of the asset has transferred to another party that is able to sell the asset in its entirety to an unrelated third party.

Classification of financial liabilities

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the company after deducting all of its liabilities.

Basic financial liabilities

Basic financial liabilities, including creditors, and loans from group companies, are initially recognised at transaction price unless the arrangement constitutes a financing transaction, where the debt instrument is measured at the present value of the future payments discounted at a market rate of interest. Financial liabilities classified as payable within one year are not amortised.

Debt instruments are subsequently carried at amortised cost, using the effective interest rate method.

Trade creditors are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Amounts payable are classified as current liabilities if payment is due within one year or less. If not, they are presented as non-current liabilities. Trade creditors are recognised initially at transaction price and subsequently measured at amortised cost using the effective interest method.

Derecognition of financial liabilities

Financial liabilities are derecognised when the company's contractual obligations expire or are discharged or cancelled.

1.8 Equity instruments

Equity instruments issued by the company are recorded at the proceeds received, net of transaction costs. Dividends payable on equity instruments are recognised as liabilities once they are no longer at the discretion of the company.

1.9 Taxation

The tax expense represents the sum of the tax currently payable and deferred tax.

Current tax

The tax currently payable is based on taxable profit for the year. Taxable profit differs from net profit as reported in the profit and loss account because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The company's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the reporting end date.

SMARTKEM LIMITED**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)****FOR THE YEAR ENDED 31 DECEMBER 2022**

1 Accounting policies**(Continued)*****Deferred tax***

Deferred tax liabilities are generally recognised for all timing differences and deferred tax assets are recognised to the extent that it is probable that they will be recovered against the reversal of deferred tax liabilities or other future taxable profits. Such assets and liabilities are not recognised if the timing difference arises from goodwill or from the initial recognition of other assets and liabilities in a transaction that affects neither the tax profit nor the accounting profit.

The carrying amount of deferred tax assets is reviewed at each reporting end 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 in the profit and loss account, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity. Deferred tax assets and liabilities are offset when the company has a legally enforceable right to offset current tax assets and liabilities and the deferred tax assets and liabilities relate to taxes levied by the same tax authority.

1.10 Employee benefits

The costs of short-term employee benefits are recognised as a liability and an expense, unless those costs are required to be recognised as part of the cost of stock or fixed assets.

The cost of any unused holiday entitlement is recognised in the period in which the employee's services are received.

Termination benefits are recognised immediately as an expense when the company is demonstrably committed to terminate the employment of an employee or to provide termination benefits.

1.11 Retirement benefits

Payments to defined contribution retirement benefit schemes are charged as an expense as they fall due.

1.12 Share-based payments

Equity-settled share-based payments are measured at fair value at the date of grant by reference to the fair value of the equity instruments granted using the Black-Scholes model. The fair value determined at the grant date is expensed on a straight-line basis over the vesting period, based on the estimate of shares that will eventually vest. A corresponding adjustment is made to equity.

When the terms and conditions of equity-settled share-based payments at the time they were granted are subsequently modified, the fair value of the share-based payment under the original terms and conditions and under the modified terms and conditions are both determined at the date of the modification. Any excess of the modified fair value over the original fair value is recognised over the remaining vesting period in addition to the grant date fair value of the original share-based payment. The share-based payment expense is not adjusted if the modified fair value is less than the original fair value.

Cancellations or settlements (including those resulting from employee redundancies) are treated as an acceleration of vesting and the amount that would have been recognised over the remaining vesting period is recognised immediately.

1.13 Leases

Rentals payable under operating leases, including any lease incentives received, are charged to profit or loss on a straight line basis over the term of the relevant lease except where another more systematic basis is more representative of the time pattern in which economic benefits from the leases asset are consumed.

Rental income from operating leases is recognised on a straight line basis over the term of the relevant lease. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised on a straight line basis over the lease term.

SMARTKEM LIMITED**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)****FOR THE YEAR ENDED 31 DECEMBER 2022****1 Accounting policies****(Continued)****1.14 Government grants**

Government grants are recognised at the fair value of the asset received or receivable when there is reasonable assurance that the grant conditions will be met and the grants will be received.

A grant that specifies performance conditions is recognised in income when the performance conditions are met. Where a grant does not specify performance conditions it is recognised in income when the proceeds are received or receivable. A grant received before the recognition criteria are satisfied is recognised as a liability.

1.15 Foreign exchange

Transactions in currencies other than pounds sterling are recorded at the rates of exchange prevailing at the dates of the transactions. At each reporting end date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at the rates prevailing on the reporting end date. Gains and losses arising on translation in the period are included in profit or loss.

2 Judgements and key sources of estimation uncertainty

In the application of the company's accounting policies, the directors are required to make judgements, estimates and assumptions about the carrying amount of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised where the revision affects only that period, or in the period of the revision and future periods where the revision affects both current and future periods.

Key sources of estimation uncertainty

The estimates and assumptions which have a significant risk of causing a material adjustment to the carrying amount of assets and liabilities are as follows.

Share-based payments

The fair value of share options granted have been obtained using the Black-Scholes pricing model. Assumptions include expected volatility, expected life, risk-free rate and expected dividend yield. Any changes in the estimates or inputs utilised to determine fair value could result in a significant impact on the Company's reported operating results, liabilities or other components of shareholders' equity.

3 Employees

The average monthly number of persons (including directors) employed by the company during the year was:

	2022	2021
	Number	Number
Total	43	37
	<u> </u>	<u> </u>

SMARTKEM LIMITED**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)****FOR THE YEAR ENDED 31 DECEMBER 2022****4 Tangible fixed assets**

	Plant and equipment £	Fixtures and fittings £	Computers £	Total £
Cost				
At 1 January 2022	1,211,849	181,487	19,334	1,412,670
Additions	65,471	-	-	65,471
Disposals	(48,989)	-	-	(48,989)
At 31 December 2022	1,228,331	181,487	19,334	1,429,152
Depreciation and impairment				
At 1 January 2022	710,897	88,164	18,854	817,915
Depreciation charged in the year	131,909	23,331	120	155,360
Eliminated in respect of disposals	(44,335)	-	-	(44,335)
At 31 December 2022	798,471	111,495	18,974	928,940
Carrying amount				
At 31 December 2022	429,860	69,992	360	500,212
At 31 December 2021	500,952	93,323	480	594,755

5 Debtors

	2022 £	2021 £
Amounts falling due within one year:		
Trade debtors	24,934	-
Amounts owed by group undertakings	2,535,951	1,049,303
Other debtors	939,059	846,368
Prepayments and accrued income	245,814	213,659
	3,745,758	2,109,330

6 Creditors: amounts falling due within one year

	2022 £	2021 £
Trade creditors	174,494	329,068
Amounts owed to group undertakings	1,869,878	886,606
Taxation and social security	212,684	71,408
Other creditors	401,758	409,784
	2,658,814	1,696,866

SMARTKEM LIMITED**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)****FOR THE YEAR ENDED 31 DECEMBER 2022****7 Creditors: amounts falling due after more than one year**

	2022 £	2021 £
Other creditors	15,494,702	12,739,080

8 Share-based payment transactions

The company has an EMI share option plan available to employees and an unapproved share option scheme. All schemes have similar terms. Each option is equal to one share of the company's Ordinary share capital. The exercise price is equal to the fair market value of the company's Common Stock at the date of grant, as determined by an independent valuation advisor.

The options vest over four years of employment and lapse after 10 years or termination of employment.

The company did not recognise a charge in the prior year as it was immaterial to the financial statements.

	Number of share options		Weighted average exercise price	
	2022 Number	2021 Number	2022 £	2021 £
Outstanding at 1 January 2022	1,320,757	160,472,967	1.14	-
Granted	288,000	1,386,787	1.66	1.14
Forfeited	(42,126)	(36,021,278)	1.66	-
Exercised	-	(124,517,719)	-	-
Outstanding at 31 December 2022	<u>1,566,631</u>	<u>1,320,757</u>	<u>1.37</u>	<u>1.14</u>
Exercisable at 31 December 2022	<u>709,645</u>	<u>336,556</u>	<u>1.03</u>	<u>0.39</u>

The options outstanding at 31 December 2022 had an exercise price of \$0.001 and \$2 and a remaining contractual life of 9 years.

The weighted average fair value of options granted in the year was determined using the Black-Scholes option pricing model. The Black-Scholes model is considered to apply the most appropriate valuation method due to the relatively short contractual lives of the options and the requirement to exercise within a short period after the employee becomes entitled to the shares (the "vesting date").

The expected life used in the model has been adjusted, based on management's best estimate, for the effect of non-transferability, exercise restrictions, and behavioural considerations.

Non-vesting conditions and market conditions are taken into account when estimating the fair value of the option at grant date. Service conditions and non-market performance conditions are taken into account by adjusting the number of options expected to vest at each reporting date.

Liabilities and expenses

During the year, the company recognised total share-based payment expenses of £256,386 (2021-£3,840,237) which related to equity settled share based payment transactions.

SMARTKEM LIMITED**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)****FOR THE YEAR ENDED 31 DECEMBER 2022**

9 Called up share capital	2022	2021	2022	2021
	Number	Number	£	£
Ordinary share capital				
Issued and fully paid				
Ordinary shares of 0.001p each	1,127,720,477	1,127,720,477	11,277	11,277
Deferred shares of 0.001p each of 0.001p each	204,513,996	204,513,996	2,045	2,045
	<u>1,332,234,473</u>	<u>1,332,234,473</u>	<u>13,322</u>	<u>13,322</u>

The rights of each class of share are as follows:

Deferred shares have no voting rights and are not entitled to receive a dividend. In priority to the Ordinary shares, the owners are entitled to payment of £1 for the entire class of deferred shares.

Ordinary shares have voting rights and are entitled to receive dividends. All remaining profits following payment to Deferred shareholders will be distributed to the holders of Ordinary Shares.

10 Operating lease commitments**Lessee**

At the reporting end date the company had outstanding commitments for future minimum lease payments under non-cancellable operating leases, as follows:

2022	2021
£	£
280,593	128,775
<u>280,593</u>	<u>128,775</u>

11 Related party transactions

The company has taken advantage of the exemption available under FRS 102 from the requirement to make disclosures concerning transactions with 100% owned fellow group companies.

12 Capital commitments

The company have a commitment to a minimum annual spend for asset usage at a location which is held under an operating lease arrangement. The company is committed to a minimum of £375,000 within one year and £51,370 within 2-5 years.

13 Parent company

100% of the issued share capital was are owned by Smartkem, Inc., a company incorporated in Delaware, USA.