

MERCURY RECYCLING GROUP PLC

Transition to International Financial Reporting Standards

1. Introduction

Mercury Recycling Group Plc releases an update on how International Financial Reporting Standards (IFRS) are likely to affect the Group's earnings and net assets. The purpose of this update is to provide information for the June half-year comparative, and to document the accounting policies to be used in the current year.

The Group is an AIM-listed company and is therefore required to adopt IFRS with effect from 1 January 2007. The first financial statements to be reported by the Group in accordance with IFRS will be for the six months to 30 June 2007, but the requirement to present comparative information means that a balance sheet prepared in accordance with IFRS at 1 January 2006 is required.

This announcement includes the results of the Group converted from a UK Generally Accepted Accounting Principles (UK GAAP) basis to an IFRS basis for the period to 30 June 2006, the year to 31 December 2006, and balance sheets as at 31 December 2005, as at 30 June 2006 and as at 31 December 2006.

This document explains the significant accounting policies to be adopted under IFRS and a summary of the significant changes from the accounting policies adopted under UK GAAP for the year ended 31 December 2006.

Attached are the Group Income Statements in IFRS format for the six months ended 30 June 2006 and for the year ended 31 December 2006, and the Group Balance Sheets in IFRS format as at 31 December 2005, as at 30 June 2006, and as at 31 December 2006.

2. Basis of preparation

IFRS 1 'First Time Adoption of International Financial Reporting Standards' (IFRS 1) sets out the rules for an entity preparing its first IFRS financial statements. The entity is required to determine the IFRS accounting policies in accordance with the IFRS that are in place at the date of transition (1 January 2006) and, in general, apply them retrospectively. There are a number of possible exemptions from the retrospective application to assist the entity in making the transition. The Group has taken the following exemptions:

a) Business combinations: the Group has elected not to restate business combinations prior to the transition date (1 January 2006).

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b) Share-based payments: the Group has elected to exclude share-based arrangements that were granted prior to 8 November 2002 or that have vested prior to the transition date.

3. Accounting policies

The accounting policies set out below are expected to be formally adopted by the Board when it prepares its first Annual Report for the financial year ended 31 December 2007.

First time adoption of IFRS

The Group's date of transition to IFRS is 1 January 2006. IFRS 1 'First Time Adoption of International Financial Reporting Standards' generally requires companies to apply their accounting policies retrospectively. There are a number of possible exemptions from this general rule to assist companies in making the transition to reporting under IFRS. The Group has taken the following exemptions:

a) Business combinations: the Group has elected not to restate business combinations prior to the transition date (1 January 2006).

b) Share-based payments: the Group has elected to exclude share-based arrangements that were granted prior to 8 November 2002 or that have vested prior to the transition date.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries) made up to 31 December each year. Control is achieved where the Company has power to govern the financial and operating policies of an investee entity so as to obtain benefits from its activities.

Subsidiaries are consolidated from the date of their acquisition, being the date on which the Group obtains control.

The acquisition of WEEE Recycling Limited was accounted for as a group reconstruction using merger accounting. Under IFRS 1, the group has elected not to restate business combinations prior to the transition date of 1 January 2006.

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Goodwill

Goodwill arising on consolidation represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets and liabilities of the subsidiary. Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses. Goodwill which is recognised as an asset is reviewed for impairment annually. Any impairment is immediately recognised in the income statement.

Foreign currencies

Monetary assets and liabilities denominated in foreign currencies are translated into sterling at the rates of exchange ruling at the balance sheet date. Transactions in foreign currencies are translated into sterling at the rate of exchange ruling at the date of transaction. All exchange rate differences are taken to the income statement.

Revenue

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods and services provided in the normal course of business, net of discounts and value added tax.

Property, plant and equipment

Depreciation is charged so as to write off the cost of assets over their estimated useful lives on the following bases:

Property alterations	10% straight line
Plant and machinery	10% - 25% straight line or basis or reducing balance basis
Fixtures, fittings & equipment	10% - 25% straight line basis
Motor vehicles	25% reducing balance basis

Leasing

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

Assets held under finance leases are recognised as assets of the Group at their fair value, or if lower, at the present value of future minimum lease payments. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation. Lease payments are apportioned between finance charges and reduction of the lease obligation using a sum of digits method.

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

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Research and development

Expenditure on research activities is recognised as an expense in the period in which it is incurred.

An internally-generated intangible asset arising from any research is recognised only if all of the following conditions are met:

- an asset is created that can be identified
- it is probable that the asset created will generate future economic benefits; and
- the development cost of the asset can be measured reliably.

Government grants

Grants towards property, plant and equipment are treated as deferred income and released to the income statement over the expected useful lives of the assets concerned. Grants towards expenditure are recognised as income over the periods necessary to match with the related costs and are deducted in reporting the related expense.

Taxation

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

Deferred tax is provided in full on all timing differences which result in an obligation at the balance sheet date to pay more tax or a right to pay less tax, at a future date, at rates expected to apply when they crystallise based on current tax rates and law. Timing differences arise from the inclusion of income and expenditure in taxation computations in periods different from those in which they are included in the financial statements. Deferred tax is not provided on timing differences arising from revaluation of fixed assets where there is no commitment to sell the asset. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered. Deferred tax assets and liabilities are not discounted.

Financial instruments

Financial assets and financial liabilities are recognised in the Group's balance sheet when the Group becomes a party to the contractual provisions of the instrument.

Trade receivables are measured at initial recognition at fair value, and are subsequently measured at amortised cost using the effective interest rate method except for short-term receivables when recognition of interest would be immaterial. Appropriate allowances for the estimated irrecoverable amounts are recognised in the income statement when there is objective evidence that the asset is impaired.

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Cash and cash equivalents comprise cash on hand and demand deposits, and other short term highly liquid investments that are readily convertible to a known amount of cash and are subject to an insignificant risk of change in value.

Interest bearing bank loans and overdrafts are recorded at the proceeds received, net of direct issue costs. Finance charges, including premiums payable on settlement or redemption and direct issue costs, are accounted for on an accrual basis in the income statement using the effective interest rate method and are added to the carrying amount of the instrument to the extent that they are not settled in the period in which they arise.

Trade payables and other financial liabilities are initially measured at fair value, and are subsequently measured at amortised cost, using the effective interest rate method.

The Group's activities expose it primarily to the financial risks of changes in interest rates on long term borrowings.

Retirement benefit costs

The Group contributes to defined contribution pension schemes. The assets of the scheme are held separately from those of the Group in an independently administered fund. Contributions payable for the period are charged in the income statement.

Share-based payments

The Group issues equity-settled share-based payments to certain employees. Equity settled share-based payments are measured at fair value at the date of grant. The fair value determined at the grant date is expensed on a straight-line basis over the vesting period, based on the group's estimate of shares that will eventually vest.

4. Effect on profits

There is no difference in results between UK GAAP and IFRS for the period ended 30 June 2006 and for the year ended 31 December 2006. Consequently, no reconciliation between UK GAAP and IFRS is included. The presentation of the Group Income Statement under IFRS is shown in section 5.

5. Effect on net assets

There is no difference in net assets between UK GAAP and IFRS as at 31 December 2005, as at 30 June 2006, and as at 31 December 2006. The presentation of the Group Balance Sheet under IFRS is shown in section 6. There are some differences within the classification of non-current assets, and with the classification of other reserves. These are explained in Appendices 1 to 3.

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6. Consolidated income statement in IFRS format

	6 Months ended 30.6.06 £'000	Year ended 31.12.06 £'000
Revenue	1,219	2,399
Cost of sales	<u>(104)</u>	<u>(193)</u>
Gross profit	1,115	2,206
Administrative expenses	<u>(1,034)</u>	<u>(2,096)</u>
Operating profit before goodwill impairment, relocation costs and share based payment costs	212	336
Relocation costs	(17)	-
Share-based payment expense	(12)	(22)
Goodwill impairment	(102)	(204)
Operating profit	81	110
Investment revenues	1	1
Finance costs	<u>(14)</u>	<u>(27)</u>
Profit before taxation	68	84
Tax	<u>-</u>	<u>-</u>
Profit for the period	<u>68</u>	<u>84</u>
Earnings per share :		
Basic (pence)	<u>0.20p</u>	<u>0.25p</u>
Diluted (pence)	<u>0.19p</u>	<u>0.24p</u>

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7. Consolidated balance sheet in IFRS format

	As at 30.6.06 £'000	As at 31.12.06 £'000
Non-current assets		
Goodwill	3,124	3,021
Other intangible assets	3	2
Property, plant and equipment	1,139	1,140
	<u>4,266</u>	<u>4,163</u>
Current assets		
Trade and other receivables	493	533
Cash and cash equivalents	29	135
	<u>522</u>	<u>668</u>
Total assets	<u>4,788</u>	<u>4,831</u>
Current liabilities		
Trade and other payables	(172)	(172)
Current tax liabilities	(86)	(93)
Obligations under finance leases	(42)	(21)
Bank overdrafts and loans	(7)	(26)
	<u>(307)</u>	<u>(312)</u>
Non-current liabilities		
Other payables	(79)	(73)
Bank loans	(290)	(259)
Obligations under finance leases	-	(12)
	<u>(369)</u>	<u>(344)</u>
Total liabilities	<u>(676)</u>	<u>(656)</u>
Net assets	<u>4,112</u>	<u>4,175</u>
Capital and reserves		
Share capital	3,336	3,373
Share premium	242	242
Other reserve	448	365
Retained earnings reserve	86	195
	<u>4,112</u>	<u>4,175</u>
Equity shareholders' funds	<u>4,112</u>	<u>4,175</u>

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8. Reconciliation from UK GAAP to IFRS

The reconciliation of equity below, together with the explanations of the changes are provided to facilitate the understanding of changes arising from the adoption of IFRS.

No reconciliation of profit has been provided on the basis that there have been no changes in profit as a result of the adoption of IFRS.

The following adjustments have been required:

Property, plant and equipment - IAS 16

Computer software has been reclassified from tangible fixed assets to intangible fixed assets.

Business combinations - IFRS 3

Under IFRS 3, merger accounting is prohibited and business combinations are required to be accounted for as acquisitions using the purchase method.

As a first time adopter of international accounting standards the company has elected under IFRS 1 not to apply IFRS 3 retrospectively to business combinations that occurred before the date of transition. As a result of this election the company has taken the opportunity to simplify the reserves by combining the 'merger' and 'retained earnings reserve'.

The distributable reserves of the company have not been affected by the reclassification of the 'merger reserve'.

Government grants - IAS 20

IAS 20 dictates that government grants relating to assets are recognised in the balance sheet by setting up the grant as deferred income with income recognised on a systematic and rational basis.

Under UK GAAP the government grant was deferred in the same systematic and rational basis, however was recognised in the balance sheet as a provision under non-current liabilities. The grant's reclassification to deferred income has therefore facilitated the disclosure of the deferment between current and non-current 'other payables'.

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a) As at 1 January 2006	UK GAAP in IFRS format £'000	Effect of transition to IFRS £'000	IFRS £'000
Non-current assets			
Goodwill	3,225	-	3,225
Other intangible assets	-	3	3
Property, plant and equipment	1,142	(3)	1,139
	4,367	-	4,367
Current assets			
Trade and other receivables	531	-	531
Cash and cash equivalents	1	-	1
	532	-	532
Total assets	4,899	-	4,899
Current liabilities			
Trade and other payables	(300)	(1)	(301)
Current tax liabilities	(59)	-	(59)
Obligations under finance leases	(24)	-	(24)
Bank overdrafts and loans	(132)	-	(132)
	(515)	(1)	(516)
Non-current liabilities			
Other payables	-	(43)	(43)
Bank loans	(275)	-	(275)
Obligations under finance leases	(33)	-	(33)
Provisions	(44)	44	-
	(352)	1	(351)
Total liabilities	(867)	-	(867)
Net assets	4,032	-	4,032
Capital and reserves			
Share capital	3,336	-	3,336
Share premium	242	-	242
Merger reserve	(111)	111	-
Other reserve	530	-	530
Retained earnings reserve	35	(111)	(76)
Equity shareholders' funds	4,032	-	4,032

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b) As at 30 June 2006	UK GAAP in IFRS format £'000	Effect of transition to IFRS £'000	IFRS £'000
Non-current assets			
Goodwill	3,124	-	3,124
Other intangible assets	-	3	3
Property, plant and equipment	1,142	(3)	1,139
	<u>4,266</u>	-	<u>4,266</u>
Current assets			
Trade and other receivables	493	-	493
Cash and cash equivalents	29	-	29
	<u>522</u>	-	<u>522</u>
Total assets	<u>4,788</u>	-	<u>4,788</u>
Current liabilities			
Trade and other payables	(167)	(5)	(172)
Current tax liabilities	(86)	-	(86)
Obligations under finance leases	(42)	-	(42)
Bank overdrafts and loans	(7)	-	(7)
	<u>(302)</u>	(5)	<u>(307)</u>
Non-current liabilities			
Other payables	-	(79)	(79)
Bank loans	(290)	-	(290)
Provisions	(84)	84	-
	<u>(374)</u>	5	<u>(369)</u>
Total liabilities	<u>(676)</u>	-	<u>(676)</u>
Net assets	<u>4,112</u>	-	<u>4,112</u>
Capital and reserves			
Share capital	3,336	-	3,336
Share premium	242	-	242
Merger reserve	(111)	111	-
Other reserve	448	-	448
Retained earnings reserve	197	(111)	86
Equity shareholders' funds	<u>4,112</u>	-	<u>4,112</u>

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c) As at 31 December 2006	UK GAAP in IFRS format £'000	Effect of transition to IFRS £'000	IFRS £'000
Non-current assets			
Goodwill	3,021	-	3,021
Other intangible assets	-	2	2
Property, plant and equipment	1,142	(2)	1,140
	4,163	-	4,163
Current assets			
Trade and other receivables	533	-	533
Cash and cash equivalents	135	-	135
	668	-	668
Total assets	4,831	-	4,831
Current liabilities			
Trade and other payables	(167)	(5)	(172)
Current tax liabilities	(93)	-	(93)
Obligations under finance leases	(21)	-	(21)
Bank overdrafts and loans	(26)	-	(26)
	(307)	(5)	(312)
Non-current liabilities			
Other payables	-	(73)	(73)
Bank loans	(259)	-	(259)
Obligations under finance leases	(12)	-	(12)
Provisions	(78)	78	-
	(349)	5	(344)
Total liabilities	(656)	-	(656)
Net assets	4,175	-	4,175
Capital and reserves			
Share capital	3,373	-	3,373
Share premium	242	-	242
Merger reserve	(111)	111	-
Other reserve	365	-	365
Retained earnings reserve	306	(111)	195
Equity shareholders' funds	4,175	-	4,175