

**INNOVATE UK LOANS LIMITED
REPORT AND FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 MARCH 2022**



CONTENTS OF THE FINANCIAL STATEMENTS

Company Information	3
Report of the Directors	4
Credit Risk Report	9
Supplementary Information to the Credit Risk Report	20
Report of the Independent Auditors	23
Statement of Profit or Loss and Other Comprehensive Income	27
Statement of Financial Position	28
Statement of Changes in Equity	29
Notes to the Financial Statements	30
Glossary	50

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

COMPANY INFORMATION

For the Year Ended 31 March 2022

DIRECTORS:	I M Mukerjee (Chairperson appointed 2 June 2021) R E Elliot (Deputy Chairperson & appointed Interim Chairperson for the period 8 December 2020 to 1 June 2021) N J McDaid (resigned 19 August 2022) T C Murley S J O' Brien R D Shaw L Simons (resigned 21 June 2022) N M Walker
SECRETARY:	R Viggers (appointed 14 May 2021) L Ellis - Holland (resigned 9 April 2021)
REGISTERED OFFICE:	Polaris House North Star Avenue Swindon Wiltshire SN2 1FL
REGISTERED NUMBER:	11220957 (England and Wales)
AUDITORS:	Comptroller and Auditor General National Audit Office 157-197 Buckingham Palace Road Victoria London SW1W 9SP
BANKERS:	National Westminster Bank Government Service Branch 2nd Floor 280 Bishopsgate London EC2 4RP
SOLICITORS	Simmons & Simmons Citypoint 1 Ropemaker Street London EC2Y 9SS

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

REPORT OF THE DIRECTORS

For the Year Ended 31 March 2022

The directors present their report with the financial statements of the Company for the year ended 31 March 2022.

DIRECTORS

The directors shown below have held office during the financial year to the date of this report, unless otherwise stated.

I M Mukerjee (Chairperson appointed 2 June 2021)

R E Elliot (Deputy Chairperson & appointed Interim Chairperson for the period 8 December 2020 to 1 June 2021)

N McDaid (resigned date 19 August 2022)

T C Murley

S J O' Brien

R D Shaw

L Simons (resigned 21 June 2022)

N M Walker

PRINCIPAL ACTIVITY

Innovate UK Loans Limited exists principally to deliver the Innovation Loans programme and, over the last two financial years, variations to it in response to COVID 19. Like all of Innovate UK's programmes, the role of innovation loans is to support business-led innovation to drive economic growth in the UK. The focus of innovation loans is on providing funding for later stage research and development projects with a clear route to commercial success for suitable, but credit-constrained, micro, small and medium sized enterprises (SMEs).

The programme is a response to the challenges faced by innovative SMEs in accessing finance to carry out specific innovation activities from which commercial and economic benefits might flow. As such the Company's appetite for innovation risk exceeds that typically seen in the private sector, even where other forms of Government support such as guarantees and co-investment might be available.

Where private investors look for a commercial return, the return on innovation loans combines a financial return with the wider economic benefit to the taxpayer. Innovation loans are offered with terms that are intended to provide stimulus and support for innovative SMEs within the scope of State Aid and UK Subsidy Control frameworks. The Company only accepts credit risk where this results from businesses having taken on highly innovative activities targeting unproven markets, rather than as a result of other credit or business failures.

Innovate UK Loans Limited is a wholly-owned subsidiary of UK Research and Innovation (UKRI) and is managed by Innovate UK, a Council of UKRI, a non-departmental public body funded by grant-in aid from the UK Government. As such Innovate UK Loans Limited is a non-regulated lender with its financial products outside the scope of the NCCP (National Consumer Credit Protection Act 2009). The Company's Statement of Financial Position and results are audited by the National Audit Office. As the scope of the Company's functions expands and its business model evolves, the directors regularly consider its position in respect of regulatory oversight and/or registration with the FCA. This consideration will continue into the next period.

Innovate UK Loan Limited's funding for innovation loans is through its repayable capital grant from the Department for Business, Energy and Industrial Strategy (BEIS) via UKRI. This repayable capital grant is written down for fair value adjustments and credit impairment which offsets the Company's financial exposure to loan defaults. This means the Company is only required to repay BEIS to the extent that it recovers loan repayments and so does not have financial exposure to loan defaults. As a consequence, the results of the Company are not directly comparable to those of a commercial lender with more traditional source of funding.

As the Company is funded by grant-in aid by the UK Government there has been no interruption of funding to the Company or its borrowers during the COVID-19 pandemic through 2020/21 and 2021/22 or subsequently.

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

Staff working for Innovate UK Loans Limited are employed directly by UKRI and are assigned to work with the Company.

PERFORMANCE ANALYSIS AND KEY PERFORMANCE INDICATORS

Since the Company is only required to repay its repayable capital grant liability to BEIS to the extent that it recovers loan repayments, it does not have financial exposure to loan defaults. Credit losses on the loan advances of the Company are offset by a write down of the repayable capital grant financial liability that funds the loan advance. As a consequence, the results of the Company are not directly comparable to those of a commercial lender with more traditional sources of funding. In the 2021/22 accounts, a profit is disclosed (2021/22 pre-tax operating profit £1,240 thousand, 2020/21 operating loss £732 thousand). The Company will typically report losses in a financial year (such as 2020/21) when new irrevocable commitments exceed new loan advances. Conversely, in financial years (such as this year) when loans advanced are greater than new commitments, the Company will typically report a profit. This is because operating losses arise at the point that a loan commitment is entered into as the Company is required to recognise a financial liability. This loss is reversed, at the point the commitment is extinguished by a loan advance, as the replacement ECL provision on loan advances is itself offset by a write down of the repayable capital grant financial liability that funds the loan advance. Although the Company will report losses when overall loan commitments increase this does not take account of the Company's overall exposure to loan defaults.

The wider benefit to the UK economy of innovation loans activity is not reflected in the financial statements of the Company.

It is too early at this stage for economic benefits to the UK economy to be unequivocally demonstrated, although initial indications shown in independent interim evaluations of the programme are positive. The Company will continue to report on the evaluation of innovation loans as further evidence emerges. The position set out in its accounts should be considered alongside this evaluation to give a fuller picture of overall impact.

The Company is continuing to develop new and innovative forms of support for innovation in the UK economy.

- In previous years' Competitions 1 to 7 £75 million pilot funding and commitments, plus £5 million additional funding and the COVID-19 support package of innovation continuity loans (ICLs) of £74.6 million launched in 2020/21.
- In 2021/22 the Company announced the following new funding initiatives: Competition 8 £20 million availability (which included £5 million allocated for the Women in Innovation programme) and a joint initiative for defence innovation loans with DASA (Defence and Security Accelerator, part of the Ministry of Defence). By 31 March 2022 £6.4 million for Competition 8 had been committed and £1.1 million committed for the DASA programme.
- In addition, HM Treasury have agreed 3 years' innovation loan funding of £40 million in 2022/23, £50 million in 2023/24 and £60 million in 2024/25, thus securing the Company's medium term lending capability. On 10 March 2022 the first round of this new programme was launched with the Innovation Loans Future Economy Competition.

ICLs, of between £250,000 and £1.6 million for a period of up to seven years, were made available to support the continuation of innovation by Innovate UK award recipients who are SMEs or third sector organisations that found themselves facing a sudden shortage or unavailability of funds resulting directly from the COVID-19 pandemic. Due to an additional contractual feature of ICLs, an equity conversion clause, the IFRS 9 classification of these loans is fair value through profit and loss (FVTPL) which contrasts with the classification of the other loan cohorts which are classified as amortised cost as they do not have the equity conversion contractual term. The implications for the accounting of ICLs are discussed in the overview section of the Credit Risk Report on page 9 and a Supplementary section of the Credit Risk Report on pages 20 to 22, as well other relevant sections of this Annual Report and Financial Statements.

During the year, the Company lent £67.1 million in new innovation loan advances (2021: £38.8 million) and had £13.7 million of irrevocable commitments outstanding at 31 March 2022 (2021: £72.3 million) before fair value adjustments. Of this, ICL advances totalled £53.0 million (2021: £17.2 million) and £2.8 million outstanding (2021: £56.1 million) of irrevocable commitments at the end of the financial year.

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

The Company has developed several key performance indicators (KPIs) to measure performance. These KPIs include measures at 31 March 2022 for:

- Average innovation project score: 79% (2021 79%) from independent technical and commercial assessors for innovation project proposals;
- Average portfolio credit risk rating: B+ (2021 BB-) from the internal credit team, benchmarked against Moody's Analytics ratings;
- Loan performance measures: 17 covenant breaches at 31 March 2022 with 20 others during 2021/22 which were resolved by the year end (2021 4 at 31 March 2021 with 4 others resolved during 2020/21).

MEASUREMENT UNCERTAINTY

The financial results of the Company comply with the requirements of UK adopted International Accounting Standards particularly IFRS (International Financial Reporting Standards) 9 *Financial Instruments*. The directors are mindful of the developing macroeconomic position, known or emerging, and the anticipated, if not yet objectively evidenced, specific credit risk events that may occur as a result of the highly innovative nature of the products and services under development and the subsequent market risk to reach a successful commercialisation to repay innovation loans.

More information is set out on measurement uncertainty, future economic conditions and critical judgements and estimates contained within the financial results are in the following sections of this Report and Financial Statements.

Issue	Location of further information
Accounting for ICLs with FVTPL classification including being out of scope of IFRS 9 expected credit loss provisioning.	Supplementary information to the Credit Risk Report; Not included in the financial results of this Company on pages 20 to 22 on additional credit risk.
Future economic uncertainty including the post COVID-19 economy and the economic consequences of the invasion of Ukraine.	Critical accounting judgements and the use of forward-looking economic information on pages 37 to 39 – this includes the use of a deep recession scenario for the potential worst case economic impact and sensitivity analysis (including the current economic outlook and residual COVID-19 risks). The Company's analysis of the credit risk exposure to borrowers with Russian connections is also discussed on pages 9-10.
Inherent risk in all innovation loans and the evidence available at the reporting date in developing provisions for future credit losses – particularly as more loans enter their capital repayment phase.	Future developments of ECL methodology in the Credit Risk Report on page 13 to 14.

EVENTS AFTER THE REPORTING DATE

Since the end of the financial year, the company has as at 31 August 2022 advanced a further £6.9 million innovation loans, including £1.8 million ICLs.

On 10 March 2022 the first round of the Innovation Loans Future Economy Competition was launched with a series of subsequent rounds in the 2022/23 financial year. These innovation loans will be advanced for highly innovative late-stage research and development (R&D) projects with the best potential for the future with a scope that focuses on the future economy as described in the Innovate UK action plan for business innovation 2021-2025. There should be a clear route to commercialisation and economic impact. In addition, on 19 April 2022 DASA supported by the Company IUKL launched a further series of defence innovation loans competitions with £10 million funding available to fund innovative defence solutions. Defence innovation loans will be advanced by the Company, funded by DASA/MOD.

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

GOING CONCERN

The Company's business activities together with factors likely to affect its future development, financial position and exposure to risk are considered in this report.

The Company is fully funded by grant income for its lending activities and operational expenses from BEIS through UKRI. These sources of funding will continue to fund the Company's activities for the foreseeable

future. The foreseeable future is considered for this purpose to be a period for at least 12 months from the date of approval of the financial statements. Taking this into account the directors have a reasonable expectation that the Company has adequate resources to continue in business for the foreseeable future.

IMPACT OF CLIMATE CHANGE AND ENVIRONMENTAL SUSTAINABILITY STRATEGY

The Company, as part of the UKRI Group, has a responsibility to minimise the negative environmental impact of its activity and to support the wider innovation sector to do the same. This responsibility is reflected in the UKRI Group's Environmental Sustainability Strategy which commits the Group and the Company to:

- The efficient use of resources and to protect and enhance the natural environment.
- Achieve net zero greenhouse gases (GHG) emissions from the UKRI Group's owned operations by 2040.
- Act as agents of change and support an environmentally sustainable innovation sector.

Further details are contained in the UKRI Group Environmental Sustainability Report in their 2021/22 Annual Report and Accounts.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The directors are responsible for preparing the Report of the Directors and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with UK adopted International Financial Reporting Standards in conformity with the requirements of the Companies Act 2006. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the Company for that financial year. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state that the financial statements comply with UK adopted International Financial Reporting Standards in conformity with the requirements of the Companies Act 2006;
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

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

STATEMENT AS TO DISCLOSURE OF INFORMATION TO AUDITORS

So far as the directors are aware, there is no relevant audit information (as defined by Section 418 of the Companies Act 2006) of which the Company's auditors are unaware, and each director has taken all the steps that he or she ought to have taken as a director to make himself or herself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

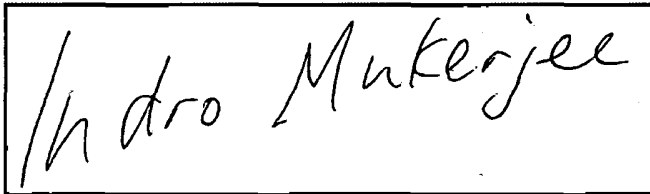
INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

AUDITORS

The auditor, National Audit Office, will be proposed for reappointment in accordance with Section 485 of the Companies Act 2006.

This report has been prepared in accordance with the provisions of Part 15 of the Companies Act 2006 relating to small companies.

SIGNED ON BEHALF OF THE BOARD OF DIRECTORS:

A rectangular box containing a handwritten signature in black ink. The signature reads "Indro Mukerjee" in a cursive script.

.....
I M Mukerjee – Chairperson

7 September 2022

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

Credit risk report – Innovation Loans

Credit risk - Overview

Innovate UK Loans Limited was established to deliver a programme of innovation loans to small and medium-sized enterprises (SMEs) in the UK. Innovation loans are designed to stimulate later stage innovation to drive productivity and growth in the UK economy. Loans of normally between £100,000 and £1.6m, with a term of up to 10 years, are offered to SMEs to fund up to 100% of the eligible project costs of highly innovative later stage research and development (R&D) projects with the best game-changing and/or disruptive ideas or concepts. Borrowers need to be suitable to take on a long-term loan commitment, need to show a clear route to commercialisation and economic impact from their R&D project and are required to show a need for public funding for their project.

Innovation loans are made on non-commercial terms, including with a low rate of interest, and were offered originally under Innovate UK's notified State Aid exemption for support for R&D under the European Commission's General Block Exemption Regulations, and are now offered under the UK Government's subsidy control regime. These non-commercial terms are offered because the Company anticipates generating positive returns for the UK economy from the innovation loans advanced. This offering of non-commercial terms is in line with the stated objectives of the Company as determined by its shareholder and its sponsors. Since the Company is only required to repay BEIS to the extent that it recovers loan repayments it does not have financial exposure to loan defaults. As a consequence, the results of the Company are not directly comparable to those of a commercial lender with more traditional sources of funding.

Under IFRS 9, impairment provisions on financial assets are calculated on an expected credit loss (ECL) basis for assets held at amortised cost which included the Competition 1 to 5 and 6 to 7 innovation loan cohorts which were approved in the last three previous financial years and new funding initiatives announced in 2021/22 – Competition 8 (including Women in Innovation) and the joint initiative with DASA. In the previous financial year, a new cohort of innovation continuity loans (ICLs) was approved, with a classification of fair value through profit and loss (FVTPL). FVTPL loans are outside the scope of the IFRS 9 impairment requirements so no ECL provisions are provided for this classification of loans. Details are given in a separate section at the end of this credit risk report on how to compare amortised cost and FVTPL loan cohorts on a consistent basis.

COVID-19, the post COVID-19 economy and credit losses

Since the end of the 2019/20 financial year, COVID-19 had a significant impact on the UK economy and potentially on our innovation loan borrowers. During 2020/21 there was widespread evidence of a significant contraction of economic activity despite the UK Government and the Bank of England taking significant measures to reduce the economic effects of the pandemic. However, in 2021/22 as the country emerged from the pandemic there had been evidence of recovery particularly in the last six months of 2021.

ECLs provisions in 2021/22 reflect the Company's forward-looking view of the macroeconomic position as a result of the current outlook from the post COVID-19 economy including current indicators such as unemployment, inflation and interest rates on innovation loan borrowers in the Statement of Profit or Loss and Other Comprehensive Income. Further details are contained in the use of forward-looking economic information in the critical accounting judgement note to these financial statements.

The economic consequences of the invasion of Ukraine

The war in Ukraine has had severe economic and humanitarian consequences, particularly in eastern Europe. The macroeconomic impact on our lending cohorts is reflected through scenario modelling and reflects the application of industry standards to the Moody's Impairment Studio model.

The Company has reviewed the portfolio for links to the participants in the conflict including the identification of the impact on supply chains. No innovation borrower loans have been paused due to links with Russia. The Company has identified one borrower with a minority shareholder with links to Russia – this borrower is

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

expected to repay in full in 2022/23. This is clearly an emerging issue and the directors will continue to monitor and take account on the impact on the Company's lending exposures.

Measuring credit losses

ECLs represent the present value of expected cash shortfalls following the default of a loan or undrawn financial commitment. A cash shortfall is the difference between the cash flows that are due in accordance with the contractual terms of the loan and the cash flows that the Company expects to receive.

The allowance for ECLs is based on an assessment of the probability of default (PD), exposure at default (EAD) and loss given default (LGD), discounted at the effective interest rate to give a net present value. The estimation of ECLs is unbiased and probability weighted, taking account all reasonable and supportable information, including forward looking economic assumptions and a range of possible outcomes.

ECL is calculated using the following formula:

$$PD \times EAD \times LGD \times \text{discount rate}$$

These terms are defined in the glossary located at the end of the notes to the financial statements.

Modelled ECL provisions may be adjusted by management if it is considered that they do not adequately reflect known credit risks, for example, risks where there is insufficient historic data on which to complete all risk characteristics in the model. Any such post model adjustments are subject to thorough internal review before being applied.

This report summarises:

- the maximum exposure to credit risk;
- the stage distribution of loans and provisions;
- credit quality;
- other risk factors and concentrations;
- the impact on the FVTPL ICL loans if they had been classified as amortised cost. This information is included in the Supplementary Information section of this report and includes data that is not included in the financial results of the Company but has been disclosed for comparison purposes with the amortised cost cohorts.

Maximum exposure to credit risk (Audited)

	31 March 2022					
	Gross balances (note i)	Less impairment provisions	Carrying value	Commitments	Less provisions on commitments	Maximum credit risk exposure (note ii)
	£'000	£'000	£'000	£'000	£'000	£'000
Innovation loans – contractual advances amortised cost	64,551	(8,061)	56,490	9,894	(549)	65,835
Innovation loans – contractual advances FVTPL	70,437	-	70,437	2,845	(39)	73,243
Commitments over 12 months – Innovation loans – contractual advances amortised cost	-	-	-	991	-	991
Total	134,988	(8,061)	126,927	13,730	(588)	140,069

Gross balances of amortised cost loans of £64,551 thousand plus gross balances of FVTPL loans of £70,437 thousand totalling £134,988 thousand innovation loans (2021: £54,535 thousand gross balances of amortised

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

cost loans plus gross balances of FVTPL loans of £17,214 thousand, totalling £71,749 thousand innovation loans). The total innovation loans carrying value in the Statement of Financial Position is £126,927 thousand

(2021: £65,486 thousand). This balance includes innovation loans classified as amortised cost of £56,490 thousand and ICLs of £70,437 thousand (2021: amortised cost £48,272 thousand and ICLs of £17,214 thousand). Further details on the ICL FVTPL classification are given on pages 20 and 33 to 34.

Maximum exposure to credit risk (Audited)

	31 March 2021					
	Gross balances (note i)	Less impairment provisions	Carrying value	Commitments	Less provisions on commitments	Maximum credit risk exposure (note ii)
	£'000	£'000	£'000	£'000	£'000	£'000
Innovation loans – contractual advances amortised cost	54,535	(6,263)	48,272	13,668	(969)	60,971
Innovation loans – contractual advances FVTPL	17,214	-	17,214	56,110	(774)	72,550
Commitments over 12 months – Innovation loans – contractual advances amortised cost	-	-	-	2,534	-	2,534
Total	71,749	(6,263)	65,486	72,312	(1,743)	136,055

Note:

- The gross balances amount is stated at amortised cost or FVTPL including a fair value adjustment on initial recognition.
- Maximum credit exposure is calculated by adding innovation loans carrying value after provisions to commitments less provisions.

Commitments

Irrevocable undrawn commitments to lend are within the scope of IFRS 9 provision requirements.

These commitments are not recognised in the Statement of Financial Position until the loans are advanced. IFRS 9 requires provisions on irrevocable commitments for below market rate loans classified as amortised cost at the higher of the estimated fair value decrease that will be written down when the loan is advanced or the ECL calculated on a probability weighted basis. The fair value calculation is made on the same basis as the calculation for loans advanced. In addition, the requirements for the classification of financial assets for below market rate loans also allows for provisions for commitments for FVTPL loans (i.e., on ICLs) on a FV basis only.

Provisions on irrevocable commitments for loans classified as amortised cost that are assessed at commercial terms are calculated on an ECL basis.

The provision for irrevocable commitments is included within provisions for liabilities and charges in the Statement of Financial Position.

Contractual terms of an innovation loan

The loan term is for a maximum of 10 years (7 years for loans entered into since 2020, including innovation continuity loans) with a period for research and development of up to 3 years (availability period), and a time to establish a clear route to market and commercialisation of up to 2 years (extension period). Interest only is paid in the availability and extension periods. There then follows a period for repayment of capital with interest of up to 5 years. This means that the outstanding balance (EAD) only starts to be repaid when this

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

repayment period begins, unless a default event triggers an early start to the repayment period, or a borrower chooses to repay their loan early.

For innovation loans competitions 1 to 5 interest is paid quarterly at a contractual rate of interest of 3.7% per annum on the amount borrowed.

For innovation loans competitions 6 to 8, innovation continuity loans and defence innovation loans, a total contractual interest rate of 7.4% is payable. During the availability and extension periods, interest is paid quarterly at 3.7% per annum and a further 3.7% interest per annum is deferred and accrued on the amount borrowed. The accrued interest is deferred to the first day of the repayment period when it is added to the principal amount. During the repayment period, interest is payable quarterly at 7.4% on the amount outstanding.

The year ended 31 March 2022 was the Company's fourth year of activity and so the current innovation loan book is still relatively immature with most loans in their availability period phase. It is feasible that a higher incidence of future credit risk events may be identified as the loan cycle progresses and innovation loans enter into their extension and repayment of capital phases. At the moment the Company's experience of arrears and default is still relatively low.

A further contractual term for the ICL cohort only is the defensive conversion to equity feature which is described on page 20 and the impact on the classification to FVTPL is discussed on pages 33 to 34. FVTPL innovation loans are outside the scope of the IFRS 9 impairment requirements and therefore are not disclosed in the Staging table below.

Staging

Impairment provisions are calculated using a three stage approach depending on changes in credit risk since original recognition of the assets:

- an asset that is not credit impaired on initial recognition is classified in Stage 1, with a provision equal to a 12 month ECL (losses arising on default events expected to occur within 12 months);
- where a loan's credit risk increases significantly, it will be moved into Stage 2. The provision recognised will be equal to the loan's lifetime ECL (losses on default events expected to occur at any point during the life of the asset); and
- if a loan meets the definition of credit impaired, it will be moved to Stage 3 with a provision equal to its lifetime ECL.

Unlike Stage 1 and Stage 2 loans where interest income is calculated on the gross contractual balance of the innovation loans, Stage 3 loans interest income is recognised in the Statement of Profit or Loss and Other Comprehensive Income, on the innovation loan balance net of ECL provision.

Amortised cost innovation loans staging analysis (Audited)

31 March 2022	Stage 1	Stage 2	Stage 3	Total
	£'000	£'000	£'000	£'000
Gross balances				
Innovation Loans	54,080	6,681	3,790	64,551
Total	54,080	6,681	3,790	64,551
Provisions				
Innovation Loans	2,390	1,881	3,790	8,061
Total	2,390	1,881	3,790	8,061
Provisions as a % of total balance				
	%	%	%	%
Innovation Loans	4.42	28.16	100.00	12.49
Total	4.42	28.16	100.00	12.49

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

During the year the Company transferred its ECL modelling approach from a Moody's based spreadsheet system to Impairment Studio, a cloud-based software application. This meant that the model generated results

to fully provide for 7 stage 3 credit impaired loans (2021: 5 loans). In prior years a management overlay (also known as a temporary adjustment) was to generate an additional provision (2021: £1,567 thousand). In Management's view, the Company is unlikely to receive any further repayments of capital or interest towards the extinguishment of these loans.

Amortised cost innovation loans staging analysis (Audited)

31 March 2021	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000
Gross balances				
Innovation Loans	50,414	1,590	2,531	54,535
Total	50,414	1,590	2,531	54,535
Provisions				
Innovation Loans	3,167	565	2,531	6,263
Total	3,167	565	2,531	6,263
Provisions as a % of total balance				
Innovation Loans	6.28	35.53	100.00	11.48
Total	6.28	35.53	100.00	11.48

For loans advanced at a commercial interest rate the coverage ratio (ECL divided by the gross carrying amount of the loans) gives a useful benchmark of the size of provisions for comparability between stages, lending portfolios and peer group lenders. In the case of loans on non-commercial terms, there is the additional reduction of carrying values as the result of day 1 fair value adjustments. Innovation loan advances for all classifications at 31 March 2022 totalled £133,946 thousand (2021: £74,817 thousand) adjusted for redemptions and capital repaid with a total accumulated fair value adjustment on initial recognition of £6,300 thousand (2021: £4,945 thousand) giving a FV writeback ratio of 4.70% (2021: 6.61%). This ratio has decreased due to most recent lending being at a higher contractual interest rate of 7.40% with the result that a smaller proportion of new loans have a day 1 fair value adjustment.

Credit quality

The nature of innovation loans is such that this lending is expected to have a relatively higher credit risk profile compared to lower risk commercial lending secured on a range of tangible and intangible assets at market interest rates that private sector financial institutions typically offer. The Company adopts robust credit risk management policies designed to recognise and manage the risks arising from the portfolio. At 31 March 2022 there were 14 innovation loans with a significant increase of credit risk and 8 loans that were credit impaired (defaults) (at 31 March 2021 there were 3 innovation loans with a significant increase of credit risk and 5 loan that were credit impaired). It is expected that given the higher credit risk profile of the loans the Company will experience loans transferring into Stage 2 and 3 in future years.

Future developments of ECL methodology

The directors recognise the need to develop further the provisions methodology in future accounting periods for Stage 1 innovation loans, where there has not been a significant increase in credit risk since origination, as more loans enter their capital repayment period. The conditions under which the Company is currently making its ECL estimate is based on the best available evidence, but this estimate is inherently uncertain, due to the lack of repayment experience, given the immaturity of the portfolio and the lack of close comparators in the lending industry. When more loans start to enter the repayment of capital phase further evidence in credit risk and default is expected to become available. The existing monitoring and watchlist process look at credit information currently available but with limited information on loan performance in the repayment of capital

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

phase. More information will become available in 2022/23 as 49 innovation loans are due to start repayments of capital. The directors will look at the earliest opportunity to enhance the modelled results as soon as there is evidence to support such an approach.

The table below shows the amortised cost loan balances and provisions for innovation loans for amortised cost loans, by risk grade. Risk grades are initially determined as part of the innovation loans application assessment and approval processes using Moody's risk assessment software. Risk grades of innovation loans are regularly reviewed by the Credit Committee as part of the monitoring and assessment of borrowers' regular management information submissions.

Amortised cost loan balance and provisions by risk grade

(Audited)

31 March 2022

Risk grade	Loan balance				Provisions				%
	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000	
Strong (AAA to A-)	-	-	-	-	-	-	-	-	-
Good (BBB+ to BBB-)	4,776	-	-	4,776	44	-	-	44	0.92%
Satisfactory (BB+ to BB-)	30,939	670	-	31,609	817	16	-	833	2.64%
Weak (B+ to B-)	18,365	2,530	-	20,895	1,529	501	-	2,030	9.72%
Bad/Financial difficulties (CCC+ and below)	-	3,481	-	3,481	-	1,364	-	1,364	39.18%
Default/credit impaired (D)	-	-	3,790	3,790	-	-	3,790	3,790	100.00%
Total	54,080	6,681	3,790	64,551	2,390	1,881	3,790	8,061	12.49%

Further details on the risk grades of FVTPL ICLs are given in the section below on ICLs and the financial impact if the loans had been classified as amortised cost is disclosed on page 20.

Amortised cost loan balance and provisions by risk grade

(Audited)

31 March 2021

Risk grade	Loan balance				Provisions				%
	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000	
Strong (AAA to A-)	-	-	-	-	-	-	-	-	-
Good (BBB+ to BBB-)	6,060	-	-	6,060	83	-	-	83	1.37%
Satisfactory (BB+ to BB-)	25,514	-	-	25,514	958	-	-	958	3.75%
Weak (B+ to B-)	18,199	1,141	-	19,340	2,054	438	-	2,492	12.89%
Bad/Financial difficulties (CCC+ and below)	641	449	-	1,090	72	127	-	199	18.26%
Default/credit impaired (D)	-	-	2,531	2,531	-	-	2,531	2,531	100.00%
Total	50,414	1,590	2,531	54,535	3,167	565	2,531	6,263	11.48%

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

Credit risk concentration

Innovation loan balances by industry sector and region

(Audited)

31 March 2022

	Greater London	Central England	Northern England	South East England	South West England	Scotland	Wales	Northern Ireland	Total	%
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	
Stage 1 and 2 amortised cost loans										
Digital, software, technology	4,661	1,089	1,792	2,445	1,725	736	982	768	14,198	10.5
Healthcare	1,797	1,952	634	-	-	-	-	835	5,218	3.9
Manufacturing	3,456	7,046	3,972	2,617	6,638	-	858	-	24,587	18.3
Other (Note i)	4,290	3,347	4,186	1,974	1,161	410	-	1,390	16,758	12.4
Stage 3 loans										
Digital, software, technology	651	-	-	-	39	-	-	582	1,272	0.9
Healthcare	-	400	841	-	-	-	-	-	1,241	0.9
Manufacturing	-	717	-	-	560	-	-	-	1,277	1.0
Total amortised cost	14,855	14,551	11,425	7,036	10,123	1,146	1,840	3,575	64,551	47.8
FVTPL loans										
Stage 1 and 2										
Digital, software, technology	5,260	2,400	2,195	3,365	931	1,218	450	400	16,219	12.0
Healthcare	2,426	1,779	361	2,131	-	274	1,167	-	8,138	6.0
Manufacturing	3,744	4,508	3,761	1,984	758	-	2,318	-	17,073	12.7
Other (Note i)	11,087	4,098	910	6,479	2,260	1,491	-	2,682	29,007	21.5
Total FVTPL	22,517	12,785	7,227	13,959	3,949	2,983	3,935	3,082	70,437	52.2
Total Geographic concentration	37,372	27,336	18,652	20,995	14,072	4,129	5,775	6,657	134,988	100.0

Note:

i) The other category comprises professional, scientific and technical activities along with management consultancy, other information services and educational support activities.

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

**Innovation loan balances by industry sector and region
(Audited)
31 March 2021**

	Greater London	Central England	Northern England	South East England	South West England	Scotland	Wales	Northern Ireland	Total	%
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	
Stage 1 and 2 amortised cost loans										
Digital, software, technology	3,370	621	1,468	2,386	1,078	728	1,178	1,103	11,932	16.6
Healthcare	1,641	1,336	350	-	-	-	-	799	4,126	5.8
Manufacturing	4,568	5,504	2,665	2,549	4,372	-	422	-	20,080	28.0
Other (Note i)	5,205	2,271	2,912	2,338	1,037	406	435	1,262	15,866	22.1
Stage 3 loans										
Digital, software, technology	651	-	-	-	79	-	-	-	730	1.0
Healthcare	1,241	-	-	-	-	-	-	-	1,241	1.7
Manufacturing	560	-	-	-	-	-	-	-	560	0.8
Total amortised cost	17,236	9,732	7,395	7,273	6,566	1,134	2,035	3,164	54,535	76.0
FVTPL loans										
Digital, software, technology	1,117	406	162	761	372	-	-	99	2,917	4.1
Healthcare	471	554	-	200	-	-	-	-	1,225	1.7
Manufacturing	2,296	1,281	-	-	-	-	326	-	3,903	5.4
Other (Note i)	2,940	893	1,210	1,555	1,105	173	-	1,293	9,169	12.8
Total FVTPL	6,824	3,134	1,372	2,516	1,477	173	326	1,392	17,214	24.0
Total Geographic concentration	24,060	12,866	8,767	9,789	8,043	1,307	2,361	4,556	71,749	100.0

Note:

- i) The other category comprises professional, scientific and technical activities along with management consultancy, other information services and educational support activities.

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)
Reconciliation of movements in gross balances and impairment provisions

The table below summarises the movements in gross loans held at amortised cost, including the impact of ECL provisions and excluding the fair value adjustment for non-commercial terms interest. The lines within the tables are an aggregation of the movements over the year.

(Audited)

	Non-credit impaired				Credit impaired		Total	
	Subject to 12 months ECL		Subject to lifetime ECL		Subject to lifetime ECL			
	Stage 1		Stage 2		Stage 3		Total Gross balances	Total Provisions
	Gross balances	Provisions	Gross balances	Provisions	Gross balances	Provisions		
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	
31 March 2022								
At 1 April 2021	50,414	(3,167)	1,590	(565)	2,531	(2,531)	54,535	(6,263)
Stage transfers:								
Transfers from Stage 1 to Stage 2	(6,672)	489	6,672	(489)	-	-	-	-
Transfers to Stage 3	-	-	(1,539)	314	1,539	(314)	-	-
Transfers from Stage 2 to Stage 1	-	-	-	-	-	-	-	-
Transfers from Stage 3	-	-	-	-	-	-	-	-
Net remeasurement of ECL arising from transfer of stage	-	-	-	(1,141)	-	(1,225)	-	(2,366)
Net movement arising from transfer of stage (note i)	(6,672)	489	5,133	(1,316)	1,539	(1,539)	-	(2,366)
Net assets originated (note ii)	14,155	(127)	-	-	-	-	14,155	(127)
Other items impacting the SOFP (note iii)	587	-	207	-	-	-	794	-
Repayments and changes in risk parameters (note iv)	(533)	40	(249)	-	(280)	280	(1,062)	320
Redemptions (note v)	(3,871)	375	-	-	-	-	(3,871)	375
Profit or loss charge for 2021/22								(1,798)
Decrease due to write offs	-	-	-	-	-	-	-	-
Other provision movements	-	-	-	-	-	-	-	-
31 March 2022	54,080	(2,390)	6,681	(1,881)	3,790	(3,790)	64,551	(8,061)
Net carrying amount		51,690		4,800		-		56,490

Notes:

- i) The remeasurement of provisions arising from a change in stage is reported within the stage to which assets are transferred.
- ii) Net assets originated include the fair value adjustment on original recognition. If a new loan is recognised in the month, the value is included in the closing gross balance and provisions for the month. New advances are normally included in Stage 1, except for advances on existing commitments on loans that were originated in Stage 1 which have been subsequently transferred to Stage 2.
- iii) Other items impacting the SOFP include the addition of commercial interest calculated on an arm's length commercial interest rate.
- iv) This line comprises contractual interest received. This line includes capital repayments where the asset is not derecognised, changes in risk parameters, and changes to modelling inputs and methodology.
- v) For any asset that is derecognised in the month, the value disclosed is the provision at the start of that month.

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

The table below summarises the movements in gross FVTPL loans which are outside the scope of IFRS 9 ECL impairment requirements.

(Audited)

FVTPL Loans	2022 £'000	2021 £'000
At 1 April	17,214	-
Net assets originated	52,975	17,313
FV adjustment on origination	(624)	(259)
Subsequent FV movement	872	160
Total change in FV	248	(99)
At 31 March	70,437	17,214

(Audited)

	Non-credit impaired				Credit impaired		Total	
	Subject to 12 months ECL		Subject to lifetime ECL		Subject to lifetime ECL			
	Stage 1		Stage 2		Stage 3			
	Gross balances	Provisions	Gross balances	Provisions	Gross balances	Provisions	Total Gross balances	Total Provisions
£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	
31 March 2021								
At 1 April 2020	32,488	(2,587)	1,451	(283)	407	(407)	34,346	(3,277)
Stage transfers:								
Transfers from Stage 1 to Stage 2	(2,364)	443	2,364	(443)	-	-	-	-
Transfers to Stage 3	-	-	(2,131)	890	2,131	(890)	-	-
Transfers from Stage 2 to Stage 1	419	(107)	(419)	107	-	-	-	-
Transfers from Stage 3	-	-	-	-	-	-	-	-
Net remeasurement of ECL arising from transfer of stage		20		(408)		(1,241)		(1,629)
Net movement arising from transfer of stage (note i)	(1,945)	356	(186)	146	2,131	(2,131)	-	(1,629)
Net assets originated (note ii)	20,045	(1,196)	331	(428)	-	-	20,376	(1,624)
Other items impacting the SOFP (note iii)	2,568	-	93	-	-	-	2,661	-
Repayments and changes in risk parameters (note iv)	(1,650)	215	(99)	-	(7)	7	(1,756)	222
Redemptions (note v)	(1,092)	45	-	-	-	-	(1,092)	45
Profit or loss charge for 2020/21								(2,987)
Decrease due to write offs	-	-	-	-	-	-	-	-
Other provision movements	-	-	-	-	-	-	-	-
31 March 2021	50,414	(3,167)	1,590	(565)	2,531	(2,531)	54,535	(6,263)
Net carrying amount		47,247		1,025		-		48,272

Notes:

- The remeasurement of provisions arising from a change in stage is reported within the stage to which assets are transferred.
- Net assets originated include the fair value adjustment on original recognition. If a new loan is recognised in the month, the value is included in the closing gross balance and provisions for the month. New advances are normally included in Stage 1, except for advances on existing commitments on loans that that were originated in Stage 1 which have been subsequently transferred to Stage 2.
- Other items impacting the SOFP include the addition of commercial interest calculated on an arm's length commercial interest rate.
- This line comprises contractual interest received. This line includes capital repayments where the asset is not derecognised, changes in risk parameters, and changes to modelling inputs and methodology.
- For any asset that is derecognised in the month, the value disclosed is the provision at the start of that month.

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

Innovation loans by payment status and interest payment holidays

The impact of arrears and payment holidays on ECL staging is described in the accounting policies: impairment of financial assets and Note 3 critical accounting judgements. At 31 March 2022 there were £168 thousand arrears (4 cases) due to borrower late payments on the innovation loan balances (31 March 2021 there were £173 thousand arrears – 4 cases). It is expected that arrears levels will increase as loan become more mature and enter their repayment of capital phases. 3 of the 4 arrears cases are Stage 3 credit impaired loans which are fully provided for.

As at 31 March 2022 there were 7 loans where borrowers had requested interest payment holidays and £143 thousand interest deferred for the period up to 31 March 2022 (31 March 2021 there were 6 loans where borrowers had requested interest payment holidays and £85 thousand interest deferred).

Forbearance

Forbearance occurs from concession events that potentially apply to all lending, including impaired exposures and borrowers subject to enforcement and recovery action. Modifications which may be considered as forbearance are those which alter a borrower's terms and conditions such that the new contract is more favourable to the borrower than the existing contract. The concessions are driven by the borrower's inability to comply with the existing terms and the following concession events are included within forbearance reporting:

- Extension/alteration: repayment terms amended to interest only, granting of a repayment holiday or general deferral/term extension.
- Forgiveness: partial debt forgiveness whereby part of the loan is written off and is no longer payable by the borrower. This is subject to separate approval from the Department for Business, Energy and Industrial Strategy (BEIS) and HM Treasury.
- Waivers/amendments: covenant re-set or waiver/other conditions waived or amended. This is subject to Credit Committee discretion.
- Capitalisation: the ad hoc addition of past due arrears amounts to the principal of the loan.
- Combination: the application of multiple types of forbearance mentioned above.

An additional type of potential forbearance in the future is for ICLs, which have a defensive conversion to equity contractual term. If, at the end of the extension period commercialisation of the project has not been achieved by the borrower, or if at any time default seems likely, the Company may give notice to commence consultation with the borrower to convert the principal of the loan and accrued interest into shares with a view to sales of such shares to complete the repayment of the loan. The intention being to recover only outstanding capital and interest. Further details are given in the accounting policy section of the notes on innovation continuity loan classification. To date there have been no cases of this type of forbearance.

Extension of terms

Innovation Loans contractual terms envisage that refinements of plans are a normal part of the development of the new product particularly in the availability and extension periods of the project. Hence a drawdown change request (DCR), or a project change request (PCR) are not automatically an indication that the borrower's financial position is stressed or that a concession event has occurred.

During the year 39 loans had extensions of their final redemption dates with a range of 3 to 24 months (2021: 29). Interest will continue to be paid at the contractual interest rate on the principal outstanding over the extended life of the loan.

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

Supplementary information to the Credit Risk Report: not included in the financial results of the Company.

FVTPL loans and the financial impact had these loans been classified as amortised cost

ICLs are a cohort of innovation loans which were first offered and advanced in 2020/21. ICLs have the same contractual features as Competition 6 to 8 loans with one exception – a defensive conversion to equity contractual feature. If, at the end of the extension period commercialisation of the project has not been achieved by the borrower, or if at any time default seems likely, the Company may give notice to commence consultation with the borrower to convert the principal of the loan and accrued interest into shares with a view to sales of such shares to support the repayment of the loan. The intention being to recover only outstanding capital and interest. The equity conversion clauses at 31 March 2022 have been assessed to have a nil financial value.

The consequence of the equity conversion feature is that ICLs do not meet the test to show that the IFRS 9 cash flow characteristics are solely payments of principal and interest to be classified as amortised cost loans and therefore these loans have been classified as FVTPL. The result of this accounting classification is that FVTPL is outside the scope of ECL provisions and provisions for irrevocable commitments.

The Company manages the credit risks of ICLs on the same basis as other innovation loans and are exposed to the same risks of default. Therefore, the tables below disclose the ECLs that would have been provided for ICL loans advanced and provisions that would have been made for ICL irrevocable commitments if the loans had been classified in the same way as the rest of the portfolio. The figures in the tables below have not been posted to the Company's 2021/22 results.

FVTPL loans – the impact of alternative amortised cost classification (not included in the Statement of Financial Position) on loans advanced

(Audited)

31 March 2022	Stage 1	Stage 2	Stage 3	Total	2021 Total
	£'000	£'000	£'000	£'000	£'000
Gross balances ICLs classified as amortised cost					
FVTPL Innovation Loans if reclassified as amortised cost (Note 1)	67,133	3,304	0	70,437	17,214
Total	67,133	3,304	0	70,437	17,232
Additional provisions if FVTPL loans classified as amortised cost					
Innovation Loans classified as FVTPL (Note 2)	3,512	1,072	0	4,584	1,295
Total	3,512	1,072	0	4,584	1,295
FVTPL provisions as a % of total balance if FVTPL loans classified as amortised cost					
Innovation Loans classified as FVTPL	5.23	32.45	N/a	6.51%	7.52
Total	5.23	32.45	N/a	6.51%	7.52

Note 1: FVTPL gross balance is the balance sheet carrying value of £70,437 thousand (2021: £17,214 thousand) which has been used as the exposure (EAD) figure in the ECL calculation which has been reduced by cumulative day 1 and FV at reporting date adjustments of £2,267 thousand (2021 £276 thousand). In 2021 all FVTPL loans were ICLs and would have been classified as Stage 1 loans. The gross balance of ICL figure in the supplementary Staging table above is stated as per the value in Note 11 innovation loans to show the linkage with the value in the Statement of Financial Position and to reflect the way loan values for ICL ECLs are monitored by Management. If the ICL loans were actually restated as amortised cost, the FV changes subsequent to the amortised Day 1 FV adjustments, would also need to be taken into account.

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

Note 2: ICLs classified as FVTPL are outside the scope of IFRS 9 impairment requirements so do not have ECL provisions.

The table below shows the loan balances and provisions for ICLs by risk grade if these loans had been classified as amortised cost.

Loan balance and provisions of FVTPL loans if were classified as amortised cost by risk grade

(Audited)

31 March 2022

Risk grade	Loan balance				Provisions				%
	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000	
Strong (AAA to A-)	-	-	-	-	-	-	-	-	-
Good (BBB+ to BBB-)	6,550	-	-	6,550	47	-	-	47	0.71%
Satisfactory (BB+ to BB-)	24,584	-	-	24,584	639	-	-	639	2.60%
Weak (B+ to B-)	35,379	1,287	-	36,666	2,697	187	-	2,884	7.87%
Bad/Financial difficulties (CCC+ and below)	620	2,017	-	2,637	129	885	-	1,014	38.47%
Default/credit impaired (D)	-	-	-	-	-	-	-	-	-
Total (Note 1)	67,133	3,304	-	70,437	3,512	1,072	-	4,584	6.51%

Note 1: FVTPL gross balances would be £1,261 thousand more than the FVTPL gross balance of £70,437 thousand as the fair value adjustment at reporting date would be reversed.

31 March 2021

Risk grade	Loan balance				Provisions				%
	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000	
Strong (AAA to A-)	-	-	-	-	-	-	-	-	-
Good (BBB+ to BBB-)	1,966	-	-	1,966	19	-	-	19	0.97%
Satisfactory (BB+ to BB-)	5,776	-	-	5,776	236	-	-	236	4.09%
Weak (B+ to B-)	9,234	-	-	9,234	1,009	-	-	1,009	10.93%
Bad/Financial difficulties (CCC+ and below)	256	-	-	256	31	-	-	31	12.11%
Default/credit impaired (D)	-	-	-	-	-	-	-	-	-
Total (Note 1)	17,232	-	-	17,232	1,295	-	-	1,295	7.52%

Note 1: FVTPL gross balances would be £18 thousand more than the FVTPL gross balance of £17,214 thousand as the fair value adjustment at reporting date would be reversed.

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

Irrevocable commitments – impact on provisions on FVTPL loans if classified as amortised cost

ICL irrevocable commitments at 31 March 2022 totalled £2,845 thousand (31 March 2021: £56,110 thousand). The IFRS 9 FVTPL classification means that provisions for these financial liabilities cannot be made on a consistent amortised cost classification basis with irrevocable commitments despite having the same contractual features except for the equity conversion clause. The table below discloses the provisions that would have been made for ICL loans irrevocable commitments if this cohort had been classified at amortised cost.

(Audited)

Irrevocable commitments provisions that would have been made	2022 £'000	2021 £'000
At 1 April	4,765	-
Provisions utilised	-	-
FV provisions on irrevocable commitments reflected in financial statements (made)	39	774
Additional ECL provisions on irrevocable commitments if ICLs were classified as amortised cost	81	3,991
Release for the period	(4,765)	-
Net Statement of Profit or Loss (credit)/charge	(4,645)	4,765
At 31 March provisions on ICLs would have been	120	4,765

Net assets if FVTPL loans were classified as amortised cost

The total impact on net assets for the Company at 31 March 2022, if ICLs were classified at amortised cost, would be a further increase of net assets of £3,167 thousand (2021: £3,233 thousand reduction) to net assets of £2,477 thousand (2021: net liabilities £4,928 thousand). This calculation takes account of the consequential additional increase of write down of repayable capital grant and the tax credit of additional losses that would result.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF INNOVATE UK LOANS LIMITED

Opinion on financial statements

I have audited the financial statements of Innovate UK Loans Limited for the year ended 31 March 2022 which comprise the Innovate UK Loans Limited's:

- Statement of Profit or Loss and Other Comprehensive Income for the year ended 31 March 2022;
- Statement of Financial Position as at 31 March 2022;
- Statement of Changes in Equity for the year then ended; and
- the related notes including the significant accounting policies.

The financial reporting framework that has been applied in the preparation of the financial statements is applicable law and the UK adopted International Accounting Standards.

In my opinion the financial statements:

- give a true and fair view of the state of Innovate UK Loans Limited's affairs as at 31 March 2022 and its profit for the year then ended;
- have been properly prepared in accordance with UK adopted international accounting standards; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on regularity

In my opinion, in all material respects the income and expenditure recorded in the financial statements have been applied to the purposes intended by Parliament and the financial transactions recorded in the financial statements conform to the authorities which govern them.

Basis of opinions

I conducted my audit in accordance with International Standards on Auditing (ISAs) (UK) and Practice Note 10 '*Audit of Financial Statements of Public Sector Entities in the United Kingdom*'. My responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of my report.

Those standards require me and my staff to comply with the Financial Reporting Council's *Revised Ethical Standard 2019*. I have also elected to apply the ethical standards relevant to listed entities. I am independent of Innovate UK Loans Limited in accordance with the ethical requirements that are relevant to my audit and the financial statements in the UK. My staff and I have fulfilled our other ethical responsibilities in accordance with these requirements.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Conclusions relating to going concern

In auditing the financial statements, I have concluded that the Innovate UK Loans Limited's use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

Based on the work I have performed, I have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on Innovate UK Loans Limited's ability to continue as a going concern for a period of at least twelve months from when the financial statements are authorised for issue.

My responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF INNOVATE UK LOANS LIMITED (CONTINUED)

Other Information

The other information comprises information included in the Report of the Directors and Credit Risk Report (including the Supplementary Information to the Credit Risk Report) but does not include the financial statements and my auditor's report thereon. The directors are responsible for the other information.

My opinion on the financial statements does not cover the other information and except to the extent otherwise explicitly stated in my report, I do not express any form of assurance conclusion thereon.

In connection with my audit of the financial statements, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or my knowledge obtained in the audit or otherwise appears to be materially misstated.

If I identify such material inconsistencies or apparent material misstatements, I am required to determine whether this gives rise to a material misstatement in the financial statements themselves. If, based on the work I have performed, I conclude that there is a material misstatement of this other information, I am required to report that fact.

I have nothing to report in this regard.

Opinion on other matters prescribed by the Companies Act 2006

In my opinion, based on the work undertaken in the course of the audit:

- the Report of the Directors has been prepared in accordance with applicable legal requirements; and
- the information given in the Report of the Directors for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which I report by exception

In the light of the knowledge and understanding of Innovate UK Loans Limited and its environment obtained in the course of the audit, I have not identified material misstatements in the Report of the Directors or the Credit Risk Report (including the Supplementary Information to the Credit Risk Report).

I have nothing to report in respect of the following matters in relation to which the Companies Act 2006 requires me to report to you if, in my opinion:

- adequate accounting records have not been kept or returns adequate for my audit have not been received from branches not visited by my staff; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of director's remuneration specified by law are not made; or
- the directors were not entitled to prepare the financial statements in accordance with the small companies regime and take advantage of the small companies exemption in preparing the Report of the Directors; or
- I have not received all of the information and explanations I require for my audit.

Responsibilities of the directors for the financial statements

As explained more fully in the Directors' Responsibilities Statement, the directors are responsible for:

- the preparation of the financial statements in accordance with the applicable financial reporting framework and for being satisfied that they give a true and fair view;
- internal control as directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.
- assessing the Innovate UK Loan's Limited's ability to continue as a going concern, disclosing, if applicable, matters relating to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the entity or to cease operations, or have no realistic alternative but to do so.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF INNOVATE UK LOANS LIMITED (CONTINUED)

Auditor's responsibilities for the audit of the financial statements

My responsibility is to audit and report on the financial statements in accordance with applicable law and International Standards on Auditing (ISAs) (UK).

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

Extent to which the audit was considered capable of detecting non-compliance with laws and regulations including fraud

I design procedures in line with my responsibilities, outlined above, to detect material misstatements in respect of non-compliance with laws and regulation, including fraud. The extent to which my procedures are capable of detecting non-compliance with laws and regulations, including fraud is detailed below.

Identifying and assessing potential risks related to non-compliance with laws and regulations, including fraud

In identifying and assessing risks of material misstatement in respect of non-compliance with laws and regulations, including fraud, we considered the following:

- the nature of the sector and control environment including the design of Innovate UK Loans Limited's accounting policies and key performance indicators;
- inquiring of management and those charged with governance, including obtaining and reviewing supporting documentation relating to Innovate UK Loans Limited's policies and procedures in respect of:
 - identifying, evaluating and complying with laws and regulations and whether they were aware of any instances of non-compliance;
 - detecting and responding to the risks of fraud and whether they have knowledge of any actual, suspected or alleged fraud; and
 - the internal controls established to mitigate risks related to fraud or non-compliance with laws and regulations including Innovate UK Loans Limited's controls relating to the Companies Act 2006 and Managing Public Money.
- discussing among the engagement team regarding how and where fraud might occur in the financial statements and any potential indicators of fraud.

As a result of these procedures, I considered the opportunities and incentives that may exist within Innovate UK Loans Limited for fraud and identified the greatest potential for fraud in the following areas: revenue recognition, posting of unusual journals, complex transactions, and bias in management estimates. In common with all audits under ISAs (UK), I am also required to perform specific procedures to respond to the risk of management override of controls.

I also obtained an understanding of Innovate UK Loans Limited's framework of authority as well as other legal and regulatory frameworks in which Innovate UK Loans Limited operates, focusing on those laws and regulations that had a direct effect on material amounts and disclosures in the financial statements or that had a fundamental effect on the operations of Innovate UK Loans Limited. The key laws and regulations I considered in this context included Companies Act 2006, Managing Public Money, tax Legislation and Innovate UK Loans Limited's Management Framework.

In addition, I considered the assessment prepared by Innovate UK Loans Limited in respect of risk and impact from sanctions resulting from the crisis in Ukraine as well as Internal Audit findings in relation to the susceptibility of Innovate UK Loans Limited's lending activities to fraud.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF INNOVATE UK LOANS LIMITED (CONTINUED)

Audit response to identified risk

As a result of performing the above, the procedures I implemented to respond to identified risks included the following:

- reviewing the financial statement disclosures and testing to supporting documentation to assess compliance with relevant laws and regulations discussed above as having direct effect on the financial statements;
- enquiring of management, the Audit and Risk Committee and in-house legal counsel concerning actual and potential litigation and claims;
- reading minutes of meetings of those charged with governance and the Board and internal audit reports;
- in addressing the risk of fraud through management override of controls, testing the appropriateness of journal entries and other adjustments; assessing whether the judgements made in making accounting estimates are indicative of a potential bias; and evaluating the business rationale of any significant transactions that are unusual or outside the normal course of business; and
- in addressing the risk of fraud through the recognition of interest income, assessing the reasonableness of the Effective Interest Rate estimated; and assessing the accuracy of the interest income calculated by Innovate UK Loans Limited's models by testing the reasonableness of the assumptions used, the logical integrity of the models and the reliability of data inputs.

I also communicated relevant identified laws and regulations and potential fraud risks to all engagement team members including internal specialists and remained alert to any indications of fraud or non-compliance with laws and regulations throughout the audit.

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

Other auditor's responsibilities

In addition, I am required to obtain evidence sufficient to give reasonable assurance that the income and expenditure reported in the financial statements have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

I communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.



Susan Clark (Senior Statutory Auditor)

8 September 2022

for and on behalf of

Comptroller and Auditor General (Statutory Auditor)

National Audit Office
157-197 Buckingham Palace Road
Victoria
London
SW1W 9SP

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

Financial Statements for the year ended 31 March 2022

Statement of Profit or Loss and Other Comprehensive Income**Statement of Profit or Loss and Other
Comprehensive Income**

		2022	2021
	Note	£'000	£'000
Grant income	4	1,127	2,611
Write down of repayable capital grant received	5	756	3,244
Interest receivable	6	5,083	2,561
Other income - fair value changes	6	872	160
Total revenue and other income		7,838	8,576
Administrative expenses	8	(4,609)	(4,429)
Fair value adjustment on initial recognition	11	(1,346)	(1,367)
Impairment losses on loans	10	(1,798)	(2,987)
Provisions on irrevocable loan commitments	15	1,155	(525)
Operating result		1,240	(732)
Tax (charge)/credit for the year	9	(235)	139
Profit/(Loss) for the year		1,005	(593)
Other comprehensive income		-	-
Total comprehensive income/(expenditure)		1,005	(593)

The Company has no recognised gains or losses, other than those set out above. The notes on pages 30 to 49 form an integral part of the financial statements.

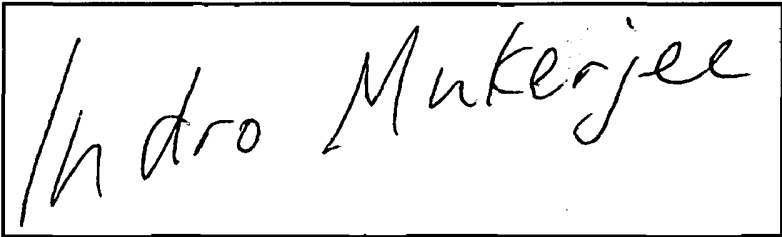
INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

Financial Statements for the year ended 31 March 2022 (continued)

Statement of Financial Position at 31 March 2022	Note	2022 £'000	2021 £'000
Assets			
Non-current assets			
Innovation loans	11	126,927	65,486
Current assets			
Cash and cash equivalents	12	7,894	23,286
Debtors and prepayments	13	36	239
Total assets		134,857	89,011
Liabilities			
Non-current liabilities			
Repayable capital grant		(128,235)	(85,891)
Current liabilities			
Trade and other payables	14	(6,724)	(3,072)
Provisions for liabilities and charges	15	(588)	(1,743)
Total liabilities		(135,547)	(90,706)
Net assets/(liabilities)		(690)	(1,695)
Capital and reserves			
Share capital	19	-	-
Retained losses		(690)	(1,695)
Total capital and reserves		(690)	(1,695)
Total capital		(690)	(1,695)

The notes on pages 30 to 49 are an integral part of these financial statements. This report has been prepared in accordance with the provisions of Part 15 of the Companies Act 2006 relating to small companies.

The financial statements on pages 27 to 29 were approved and authorised for issue by the Board of Directors on 7 September 2022 and were signed on its behalf by:



I M Mukerjee
Chairperson
7 September 2022

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

Financial Statements for the year ended 31 March 2022 (continued)

Statement of Changes in Equity	2022			2021		
	Share capital £'000	General reserve £'000	Total equity £'000	Share capital £'000	General reserve £'000	Total equity £'000
At 1 April 2021/2020	-	(1,695)	(1,695)	-	(1,102)	(1,102)
Share capital	-	-	-	-	-	-
Total comprehensive income/(expenditure) for the year	-	1,005	1,005	-	(593)	(593)
At 31 March 2022/2021	-	(690)	(690)	-	(1,695)	(1,695)

The notes on pages 30 to 49 are an integral part of these financial statements.

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

Notes to the financial statements for the year ended 31 March 2022

1. STATUTORY INFORMATION

Innovate UK Limited is a private company, limited by shares, registered in England and Wales. The Company's registered number and registered office address can be found on the Company Information page.

The principal activity of the Company is disclosed on page 4.

2. ACCOUNTING POLICIES

Basis of preparation

These financial statements have been prepared in accordance with UK adopted International Accounting Standards in conformity with the requirements of the Companies Act 2006 applicable to companies reporting under International Financial Reporting Standards (IFRS) and IFRIC interpretations as applicable to companies using Financial Reporting Standard 101 *Reduced Disclosure Framework* (FRS 101). The financial statements have been prepared under the historical cost convention, with Competitions 1 to 5, Competitions 6 to 8 innovation loans and defence innovation loans initially recognised at fair value and subsequently measured at amortised cost over the term of the loan, and the going concern basis. ICLs have been classified as FVTPL.

Comparatives for the twelve months of the 2020/21 Financial Year are disclosed.

The financial statements are presented in pound Sterling, the primary currency in which the Company operates. The financial statements are rounded to the nearest whole thousand pounds (£'000) except where otherwise stated.

The Company has taken advantage of the following disclosure exemptions under FRS 101:

- the requirements of International Accounting Standard (IAS) 7 *Statement of Cash Flows*.
- The requirements in IAS 24 *Related Party Disclosures* to disclose related party transactions entered into between two or more members of a group, provided that any subsidiary which is party to the transaction is wholly owned by such a member.

Going concern

The Company's ultimate parent is UK Research & Innovation (UKRI). UKRI is dependent on funding from the Department for Business, Energy and Industrial Strategy (BEIS) to meet liabilities falling due within future years. UKRI has no reason to believe that future funding will not be forthcoming beyond the current spending review period, particularly given the commitment in the Spending Review of October 2021 to increase public R&D investment to £20 billion per year by 2024/25, including a commitment for overall funding for Innovate UK to exceed £1 billion by 2024/25. In addition, HM Treasury have agreed 3 years' innovation loan funding of £40 million in 2022/23, £50 million in 2023/24 and £60 million in 2024/25, thus securing the Company's medium term lending capability. Therefore, the directors of the Company consider it is appropriate to adopt a going concern basis for the financial statements of the Company. The Company monitors future levels of commitment to ensure they remain within the anticipated budget. Further details of the liquidity and funding risk of the Company are contained in Note 16.

Change of accounting estimate

During the financial year, the Company has transferred its ECL modelling approach from a Moody's spreadsheet-based system to Moody's Impairment Studio, a cloud-based software application. Impairment Studio is an industry leading, IFRS9 compliant solution, which allows for enhanced credit risk calculations as well as improved reporting and analysis. The solution also removes the end user computing spreadsheet risks by automating the workflow and providing a clear audit trail.

During the implementation review process certain new risk assumptions have been adopted which are described in the critical accounting judgements note below which has resulted in a change of accounting estimate under IAS 8 with a one-off pre-tax adjustment of ECL provisions of £883 thousand which has been taken in the current

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)
Notes to the financial statements for the year ended 31 March 2022 (continued)

financial year and, in line with the accounting treatment of a change in accounting estimates, comparatives have not been adjusted.

Adoption of new and revised IFRSs

There have been no new standards that the Company has adopted during the financial year.

Future accounting developments

IFRS 17: Insurance Contracts

IFRS 17 establishes the principles for the recognition, measurement, presentation and disclosure of insurance contracts within the scope of the standard. The effective date of the standard is for years beginning on or after 1 January 2023. It is not expected that the new standard will have a material impact on the Company.

Amendments resulting from Annual Improvements

Minor amendments to various accounting standards. The IASB has not published any minor amendments that were effective from 1 January 2021. However, the IASB has published several minor amendments to IFRSs that are effective from 1 January 2022 and 1 January 2023. The Company expects to adopt the amendments for the first time in the 2022/23 annual financial statements but does not expect them to have a material impact on the financial statements

Summary of significant accounting policies

The principal accounting policies applied in the preparation of these accounts are set out below.

Grant income

Grant income for the Company's lending activities and operating costs receivable from the Department of Business, Energy and Industrial Strategy (BEIS) via UKRI has been recognised in income to run the 2021/22 programme and is non-repayable. Grant income is reduced by the contractual interest received on loans.

Write down of repayable capital grant received

The Company measures the capital grant funding from BEIS via UKRI as a financial liability at the amount initially received. This funding is used to advance innovation loan lending to borrowers. Subsequently the Company adjusts the funding for repayments made and with amounts that the Company believes will not be recoverable from borrowers. The write down of the liability equals the unamortised portion of the fair value adjustment on initial recognition of the innovation loans and the impairment losses for the underlying innovation loans. The carrying value of the funding financial liability reflects the amount that the Company expects to settle the liabilities with BEIS via UKRI. This means the Company is only required to repay BEIS to the extent that it recovers loan repayments and so does not have financial exposure to loan defaults. As a consequence, the results of the Company are not directly comparable to those of a commercial lender with more traditional sources of funding.

Interest receivable

For financial instruments measured at amortised cost the effective interest rate (EIR) method is used to measure the carrying value of a financial asset or liability and to allocate associated interest income or expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts over the expected life of the financial instrument or, when appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability.

To calculate a fair value for loans at recognition offered at a below market-rate, an adjustment is made for an arm's length commercial interest rate. Over the life of a loan the commercial interest rate less the fair value on initial recognition will net back to the contractual interest rate (i.e., the below market interest rate) for amortised cost loans.

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)
Notes to the financial statements for the year ended 31 March 2022 (continued)

Interest income is calculated by applying the EIR to the gross carrying amount of non-credit impaired loans. For amortised cost credit-impaired loans the interest income is calculated by applying the EIR to the amortised cost of the credit-impaired loans (i.e., net of the allowance for expected credit losses (ECLs) – known as the net EIR approach). No loans have been recognised as credit-impaired at origination.

FVTPL loans are outside the scope of IFRS 9 EIR requirements. Interest income accrued is part of the FV calculation. The net EIR approach does not apply to FVTPL loans as these loans are outside the scope of IFRS 9 ECL impairment.

Taxation

The Company is subject to corporation tax on taxable profits. Current tax assets and liabilities are measured at the amount expected to be recovered from or paid to HM Revenue and Customs, based on tax rates and laws that are enacted or substantively enacted by the reporting date.

Cash and cash equivalents

Cash and cash equivalents comprise cash in hand and other short-term liquid investments which are readily convertible to known amounts of cash, are subject to insignificant risk of changes in value and have an original maturity of three months or less. Any bank overdraft amounts without the right of offset are included within trade payables and other liabilities.

Financial instruments

Recognition and derecognition

The Company recognises and measures financial instruments in accordance with IFRS 9 Financial Instruments.

Financial assets and financial liabilities are recognised in the Company's Statement of Financial Position when the Company becomes a party to the contractual provisions of the instrument. For innovation loans recognition and derecognition is accounted for at the trade date when the Company has authorised the third-party administrators to pay the loan advance as at that point the Company is contractually committed.

A financial asset or financial liability is measured initially at fair value plus, for an item not at fair value through profit or loss, transaction costs that are directly attributable to its acquisition or issue.

The Company derecognises a financial asset when the contractual rights to receive future cash flows from the financial asset expire or it transfers the rights to receive the contractual cash flow in a transaction in which all of the risks and rewards of ownership and it does not retain control of the financial asset.

The Company derecognises a financial liability when its contractual obligations are discharged, cancelled or expire.

Classification and measurement

The classification and subsequent measurement of financial assets is based on an assessment of the Company's business models for managing the assets and their contractual cashflow characteristics. Innovation loans are valued at fair value at initial recognition. IFRS 9 allows the following three classification categories:

Amortised cost

In accordance with IFRS 9 Financial Instruments, a financial asset must subsequently be held at amortised cost if it meets the business model test, where the objective of the Company's business model is to hold the financial asset to collect the contractual cash flows, and the cash flow characteristics test, where the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest (SPPI) on the principal amount outstanding.

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)
Notes to the financial statements for the year ended 31 March 2022 (continued)

Interest income is calculated using the effective interest method and is recognised in the Statement of Profit or Loss and Other Comprehensive Income.

Fair value through other comprehensive income (FVOCI)

Financial assets held in a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets, and where the contractual terms comprise SPPI, are classified as FVOCI. The Company currently does not hold any financial assets with this classification.

Fair value through profit or loss (FVTPL)

Financial assets measured at FVTPL have contractual cash flow characteristics which do not meet the SPPI criteria. The contractual terms for these cash flows include returns that are not only interest and capital repayments such as returns based on increases in value on equity instruments.

Innovation loans

Fair value at initial recognition of innovation loans and application of a true and fair override

In accordance with IFRS 9 the fair value adjustment at initial recognition, which is the difference between the transaction value of the innovation loans and their fair value, if based on a valuation technique that does not only use data from observable markets, would usually be deferred and amortised over the life of the loan. However, the directors have determined that it is appropriate in this circumstance to apply a true and fair override, and consequently a fair value adjustment arising on the innovation loan book will be recognised immediately through the Statement of Profit or Loss and Other Comprehensive Income because this reflects the commercial position more appropriately.

This fair value adjustment for innovation loans is required because the Company charges a rate of interest which is a below market rate (non-commercial terms) that does not reflect the credit risk of the borrower. This means that the future expected cash flows from these loans discounted by an appropriate discount rate, does not equate to the nominal value (transaction cost) of the amount advanced on the loan.

UK adopted International Financial Reporting Standard 13 *Fair Value Measurement* (IFRS 13) requires an entity to disclose at fair value by applying a hierarchy that reflects the significance of observable market inputs. A Level 3 valuation technique is where significant unobservable inputs are used. A valuation input is considered observable if it can be directly observed from transactions in an active market, or if there is compelling external evidence demonstrating an executable exit price. An input is deemed significant if it is shown to contribute more than 10% of the valuation of a financial instrument. Unobservable input levels are generally determined based on observable inputs of a similar nature, historical observations or other analytical techniques. The fair value adjustment for innovation loans uses Level 3 valuation techniques with significant unobservable inputs.

Innovation loans Competitions 1 to 5 and 6 to 8 - amortised cost classification

The innovation loans from Competitions 1 to 5 and 6 to 8, which were held on the Company's Statement of Financial Position in previous financial years, met the business model test and the cash flow characteristics test; and therefore, these loans are held at amortised cost.

Innovation continuity loans classification and equity conversion feature - FVTPL classification

Innovation continuity loans (ICLs) have been separately assessed for the business model and cash flow characteristics tests. ICLs have the same contractual terms as the Competitions 6 to 8 loans with one additional feature, which is a defensive conversion to equity contractual term. If, at the end of the extension period commercialisation of the project has not been achieved by the borrower, or if at any time default seems likely, the Company may give notice to commence consultation with the borrower to convert the principal of the loan and accrued interest into shares with a view to sales of such shares to complete the repayment of the loan. The intention being to recover only outstanding capital and interest.

The equity conversion feature does not meet the SPPI cash flow characteristics test, which results in the ICLs being classified as fair value through the profit and loss. However, the directors have made a judgement to

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)
Notes to the financial statements for the year ended 31 March 2022 (continued)

provide additional disclosure in the credit risk report on the impact that an amortised cost classification would have had on the ICLs. This reflects the way the loans are managed and enables comparison with the other innovation loans.

As at 31 March 2022, management have not started any discussions on ICLs to negotiate applying the conversion to equity contractual term. Since there is no data available (because there have been no actual cases of the equity conversion contractual feature being applied and there is resulting estimation uncertainty) a judgement has been made that there is a nil value that would be applied to the right to convert loans into equity.

This view has been taken since:

- the right to convert will only be exercised when a business is otherwise at risk of imminent failure
- in converting, the Company will be accepting a weaker position in the capital structure and
- any conversion will be taken with a view to sale of the equity to facilitate the repayment of the loan.

It is therefore not realistic to assume a value greater than simply retaining a senior secured position.

If the clause was invoked and the Company and the Borrower cannot jointly agree the financial valuation of the shares into which the loan will convert with a view to sale to facilitate the repayment of the loan, an independent valuation expert will be appointed to determine the valuation.

Irrevocable commitments provisions

Irrevocable undrawn commitments to lend are within the scope of IFRS 9 provision requirements. This provision for irrevocable commitments is included within provisions for liabilities and charges in the Statement of Financial Position.

These commitments are not recognised in the Statement of Financial Position until the loans are advanced. IFRS 9 requires provisions on irrevocable commitments for loans below market rate loans classified as amortised cost at the higher of the estimated fair value decrease that will be written down when the loan is advanced or the ECL calculated on a probability weighted basis. The fair value calculation is made on the same basis as the calculation for loan advances. In addition, the requirements for the classification of financial assets for below market rate loans also allows for provisions for commitments for FVTPL loans (i.e., on ICLs) on a FV basis only. Provisions on irrevocable commitments for loans classified as amortised cost that are assessed at commercial terms are calculated on an ECL basis.

When the loan commitment is drawn, the provision for irrevocable commitment is released and is replaced by either a FV adjustment and/or ECL provision on the drawn loan.

Impairment of financial assets

Financial assets within the scope of IFRS 9 expected credit loss (ECL) requirements comprise all financial debt instruments measured at either amortised cost or FVOCI. Financial assets that are measured as FVTPL are outside the scope of IFRS 9 ECL requirements.

ECLs represents the present value of expected cash shortfalls following the default of a financial asset. A cash shortfall is the difference between the cash flows that are due in accordance with the contractual terms of the financial asset and the cash flows that the Company expects to receive.

The allowance for ECLs is based on an assessment of the probability of default (PD), exposure at default (EAD) and loss given default (LGD), discounted at the effective interest rate to give a net present value. The estimation of ECLs is unbiased and probability weighted, taking account all reasonable and supportable information, including forward looking economic assumptions and a range of possible outcomes.

For loans that are recognised in the Statement of Financial Position at amortised cost, the allowance for ECLs is offset against gross carrying values so that the amount presented is net of impairment provisions.

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)
Notes to the financial statements for the year ended 31 March 2022 (continued)

Forward looking economic inputs

ECLs are calculated by reference to information on past events, current conditions and forecasts of future economic conditions. Multiple economic scenarios are incorporated into the ECL calculation models. These scenarios are based on external sources where available and appropriate, and internally generated assumptions.

in all other cases. To capture any non-linear relationship between economic assumptions and credit losses, three economic scenarios have been adopted. This includes a base scenario which reflects the Company's view of the most likely economic conditions, together with an upside and a downside scenario representing alternative plausible views of economic conditions, weighted based on management's view of their probability.

Credit risk categorisation

IFRS 9 Financial Instruments outlines a three-stage model for impairment based on changes in credit quality after initial recognition. At each reporting date, loans are reviewed for changes in credit risk since the loans were initially recognised. If, at the reporting date, the credit risk on a financial instrument has not increased significantly since initial recognition, a loss allowance equal to 12-month expected credit losses (based on the probability of default within the next 12 months) is recognised. Where credit risk has increased significantly since initial recognition lifetime expected losses are recognised. In these circumstances, interest revenue is calculated on the gross carrying amount of the asset.

All innovation loans with payments falling 90 days past due or with other indications of default are assessed to be credit-impaired, where a lifetime expected credit loss is recognised and interest revenue is calculated on the net carrying amount (net of credit allowance).

Stage 2: significant increase in credit risk

A loan will be assessed as entering Stage 2 when there is a significant increase in credit risk. This is determined by either:

- Loan payments being more than 30 days past due but less than 90 days past due;
- The risk banding has shifted by more than 3 notches from when assessed at loan origination e.g., BBB down to BB-;
- Concession events such as interest payment holidays or
- The Credit Committee determining that a loan is Stage 2 using a watchlist approach where the borrower is experiencing difficulties which may threaten their ability to fulfil their credit obligations including covenant breaches, slowdowns in business activities, the project is significantly off track as reported by the monitoring officer or an adverse trend in operations that signals a potential weakness in the financial strength of the borrower.

Stage 3: credit impaired (or defaulted) loans

Stage 3 reflects the point at which an underperforming loan asset become credit impaired. As a backstop, all loans with payments falling 90 days past due will be moved automatically to Stage 3. In addition, default can be classified at the discretion of the Credit Committee.

A loan can be moved to Stage 3 if there are other indications that the borrower is unlikely to pay, such as signs of financial difficulty, probable bankruptcy, breaches of contract and concession events which have a detrimental impact on the present value of future cashflows; or if the loan is otherwise considered to be in default or evidence is discovered that indicates a business failure has – or is likely to – occurred, for example:

- Notice of insolvency;
- Cross-default; or
- Significant deterioration in the financial performance and/or standing of the borrower

Interest income on Stage 3 credit impaired innovation loans is recognised in the Statement of Profit or Loss and Other Comprehensive Income on the loan balance net of the ECL provision.

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)
Notes to the financial statements for the year ended 31 March 2022 (continued)

Transfers between stages

Transfers from Stage 1 to 2 occur when there has been a significant increase in credit risk and from Stage 2 to 3 when credit impairment is indicated as described above.

For assets in Stage 2 or 3, loans can transfer back to Stage 1 or 2 once the criteria for a significant increase in credit risk or impairment no longer apply. For loans subject to concession events such as forbearance, accounts must first be up to date for a period of 6 months before they can transfer back to Stage 1 or 2.

Write-offs

Innovation loans will be written off at the point when the Credit Committee determines that any further recoveries are unlikely or become uneconomical to pursue. At this point, it is written off against the related provision for loan impairment once all necessary procedures have been completed, including any realisation of proceeds of collateral, and the amount of the loss has been determined. Any subsequent recoveries of amounts previously written off decrease the value of impairment losses recorded in the Statement of Profit or Loss and Other Comprehensive Income. The commercial decision taken by the Credit Committee that future recoveries are unlikely are distinct from partial debt forgiveness, where explicit BEIS and HM Treasury approval is required.

Modifications

An instrument that is renegotiated is derecognised if the existing agreement is cancelled and a new agreement is made on substantially different terms (such as renegotiations of innovation loans).

Where an instrument is renegotiated and not derecognised (*for example forbearance*), the change is considered a modification of contractual terms. Where this arises and there is a modification that would result in a gain or loss on a time value basis, the gross carrying amount of the loan is recalculated as the present value of the renegotiated or modified contractual cash flows, discounted at the loan's original effective interest rate. Any gain or loss on recalculation is recognised immediately in the Statement of Profit or Loss and Other Comprehensive Income.

Further details on modifications are included in the credit risk report under the heading extension of terms.

Financial liabilities

Financial liabilities such as trade payables and other payables are measured initially at fair value less transaction costs. These financial liabilities are subsequently measured at amortised cost using the effective interest method.

Trade and other payables

Trade and other payables are recognised in the period in which related money, goods or services are received or when a legally enforceable claim against the Company is established or when the corresponding assets or expenses are recognised.

Repayable capital grant

The Company has received funding from BEIS via UKRI for a repayable capital grant for the innovation loan advances. This agreement does not have a maturity date and carries an interest rate of zero. This repayable capital grant may become repayable on demand, in whole or in part, if at the absolute discretion of BEIS certain conditions arise that affect the principal activities of the Company adversely. However, the directors expect that the funding would normally remain in place for the contractual life of the individual innovation loans that have been financed by this funding. The funding is recognised in non-current liabilities. Credit losses on the loan advances of the Company are offset by a write down of the repayable capital grant financial liability that funds the loan advance. This means the Company is only required to repay BEIS to the extent that it recovers loan repayments and so does not have financial exposure to loan defaults.

3. CRITICAL ACCOUNTING JUDGEMENTS

The Company's principal accounting policies are set out above. Management is required to exercise significant judgement and make use of estimates and assumptions in the application of these policies.

Areas which management believes to require the most critical accounting judgements are:

- the approach to applying the staging requirements – identifying significant increases in credit risk and identifying credit impaired loans and the definition of default;
- the basis of forward-looking information and multiple economic scenarios and the application of weightings of ECL models for the sensitivity of systemic risk factors;
- the approach of calculating a fair value at origination of an innovation loan including discount rate;
- the approach to calculating a fair value at the reporting date for loans classified as FVTPL.

The Company's approach to these judgements is described in more detail below:

Identifying significant increases in credit risk (Stage 2)

The identification of significant increases in credit risk for the innovation loans is expected to be the most judgemental element of the staging criteria. Management monitors the Company's loans to determine whether there have been changes in credit risk. Indicators of a significant increase in credit risk are:

- Objective criteria - loan payments being more than 30 days past due but less than 90 days past due and/or the risk banding has shifted by more than 3 notches from when assessed at loan origination e.g., BBB down to BB;
- Judgemental criterion - the Credit Committee can determine that a loan is Stage 2 using a watchlist approach to identify that the borrower is experiencing difficulties which may threaten their ability to fulfil their credit obligations. This includes covenant breaches, slowdowns in business activities, or if a project is significantly off track or indicates adverse trends in operations that signal a potential weakness in the financial strength of the borrower.

Identifying credit impaired loans and the definition of default (Stage 3)

The identification of credit impaired loans and the definition of default is another important judgement within the IFRS 9 staging approach. A loan is credit impaired when the arrears status has increased to 90 days past due or there are other indications that the borrower is unlikely to pay such as signs of financial difficulty, probable bankruptcy, breaches of contract and concession events that have a detrimental impact on the present value of future cashflows; or that the loan is otherwise considered to be in default.

Use of forward-looking economic information

Forward looking information is incorporated into provisions as an input to the calculation of ECL and as a factor in assessing the staging of a loan. Expectations of future economic conditions are included through the modelling of multiple economic scenarios (MES).

The use of MES ensures that the calculation of ECL captures a range of possible outcomes. This includes the risk of non-linearity in the relationship between credit losses and economic conditions, with provisions increasing more in unfavourable conditions (particularly severe downturns) than they reduce in favourable economic conditions.

The Company has adopted three economic scenarios, a baseline scenario, an upside and downside scenarios which includes consideration of a downturn cliff edge to take account of potential non-linearities. The projection period for forecasting used is 2022-26.

The baseline scenario is expected to be the most likely economic outcome. As part of the implementation of the Moody's Impairment Studio model during the year the macroeconomic assumptions were changed from being based on Moody's Analytics eurozone macroeconomic outlook baseline and alternative scenarios to Moody's Analytics UK forecasts as a more appropriate measure. The baseline scenario was assigned a probability weighting of 40% as at 31 March 2022 with the upside and downside scenarios having each been assigned 30% probabilities (there have been no changes in probabilities assigned during the year).

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)
Notes to the financial statements for the year ended 31 March 2022 (continued)

From 31 March 2020 onwards, the Moody's Analytics approach has adopted the deep recession scenario as the downside scenario to take account of an estimate of the potential worst case economic impact of COVID-19. The uncertainty resulting from COVID-19 mainly arises from the uncertainty in the UK economic recovery path that is yet to unfold and how it will impact the size and timing of the impact on PDs and the transition from Stage 1 to Stage 2 loans. This has been considered by the adoption of the deep recession scenario. The effect of this uncertainty is that there is significant risk of economic volatility resulting in a material adjustment to the carrying amounts of the loan balances within the next financial year.

The key macroeconomic assumptions that are built into the Moody's Analytics UK outlook in the model are:

Economic variables (average %)

31 March 2022	Baseline scenario	Upside scenario	Deep recession scenario
GDP growth	2.01%	2.53%	0.94%
Unemployment	4.42%	3.81%	6.48%
10 year Government Bond Yield	2.94%	3.25%	1.82%

31 March 2021	Baseline scenario	Upside scenario	Deep recession scenario
GDP growth	3.73%	4.16%	3.11%
Unemployment	5.96%	5.22%	7.65%
10 year Government Bond Yield	1.92%	2.46%	1.08%

The sensitivity of the amortised cost ECLs included in the primary financial statements to multiple economic scenarios showing the impact of 100% weightings to the ECL provision for amortised cost innovation loans in the Statement of Financial Position (SOFP) is illustrated in the following table:

Sensitivity impact of multiple economic scenarios (SOFP)

31 March 2022	Baseline scenario	Upside scenario	Deep recession scenario
	£'000	£'000	£'000
ECL loans	6,868	5,891	11,820
Total	6,868	5,891	11,820

Sensitivity impact of multiple economic scenarios (SOFP)

31 March 2021	Baseline scenario	Upside scenario	Deep recession scenario
	£'000	£'000	£'000
ECL loans	5,800	5,372	7,780
Total	5,800	5,372	7,780

The ECL for each scenario multiplied by the scenario probability will not necessarily reconcile to the final probability weighted ECL, since the stage allocation of loans can vary in each scenario. In the probability

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)
Notes to the financial statements for the year ended 31 March 2022 (continued)

weighted ECL, each loan is allocated to a discrete stage based on the weighted average PD under the economic scenarios.

For amortised cost innovation loans, the judgement of staging is the key assumption in estimating the ECL rather than the PD. The table below shows the sensitivity of provisions in the probability weighted scenario only as a change of 1 credit risk grade variation and transferring all loans to Stage 2 with no other changes to assumptions.

Sensitivity impact of single factor changes (SOFP)

31 March 2022	Probability weighted ECL	1 credit rating grade increase	1 credit rating grade decrease	All loans in Stage 2 or lifetime ECLs (note i)
	£'000	£'000	£'000	£'000
ECL loans	8,061	6,459	10,049	11,537
Total	8,061	6,459	10,049	11,537

Note:

- i. Includes innovation loans assessed at the year end, as a Stage 3 credit impaired loan, at a lifetime Stage 3 ECL provision rather than a Stage 2 ECL provision.

Sensitivity impact of single factor changes (SOFP)

31 March 2021	Probability weighted ECL	1 credit rating grade increase	1 credit rating grade decrease	All loans in Stage 2
	£'000	£'000	£'000	£'000
ECL loans	6,263	5,152	6,905	13,290
Total	6,263	5,152	6,905	13,290

The impact of the sensitivity of moving credit rating grades up or down on the ECL provision is not linear. This is because the relationship between credit losses for a single company and the macro-economic variables are non-linear as well. In this approach, forward looking credit rating grades (and the PDs that derived for different economic scenarios) are grouped in buckets and the impact of the 1 credit rating grade shift will have a different effect on the ECLs of individual loans. This will depend on whether or not this shift will result in the forward-looking PD of the individual loans moving into the next bucket.

Application of weighting of ECL models for sensitivity of systemic risk factors

Systemic risk is the risk attached to the economy or the business sector a borrower operates in, rather than the borrower's specific credit risk. Moody's standard modelling methodology is to assign lower risk weightings (R squared correlations) to PDs for smaller companies. Larger companies are expected to be more highly exposed to macroeconomic conditions. However, a critical accounting judgement has been made that non-commercial terms innovation loans have higher systemic risks than standard commercial terms small businesses which would include more mature, profitable enterprises. This is because innovation borrowers are generally micro-companies /start-ups focused on innovative business ideas that are highly exposed to successfully finding new markets and therefore, would be very vulnerable to downturns in the economy and supply chain problems, with less likelihood of diversification and reserves to fall back on. The sensitivity of this judgement is that balance sheet ECL provision of £8,061 thousand would reduce by £662 thousand if a low systemic risk weighting was applied.

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)
Notes to the financial statements for the year ended 31 March 2022 (continued)

Fair value at origination of innovation loans including discount rate

A critical accounting judgement required is the adjustment for the credit rating of a borrower to calculate a fair value of an innovation loan at origination which is also used for the discount rate. Innovation loans are offered at below market-rates, which is independent of the credit quality of the borrower. A proxy for an arm's length commercial interest rate is estimated using EU risk finance guidelines and reference rate, which incorporate adjustments for the level and nature of collateral and for potential subordination to other senior lenders, and which takes account of an individual borrower's credit rating. The proxy rate is used due to a lack of historic information on loan performance for innovation lending. The Board will continue to monitor the position regarding BEIS UK subsidy control guidance which has replaced EU risk finance guidance.

A cashflow projection is calculated for each loan over its life tracking drawdowns, contracted capital and interest repayments discounted back at the commercial interest rate calculated at the origination of the loan to estimate a fair value. The sensitivity of this fair value calculation is disclosed in note 17: fair values of financial assets and liabilities measured at amortised cost. This commercial interest rate is also used for discounting ECL provisions. Where the credit risk adjusted interest rate is below the contractual rate, the contractual rate has been applied. In such cases, mainly in Competitions 6 to 8 and the ICLs cohorts, no day 1 FV adjustments have been made. This approach has been taken on the basis that the contractual interest rate is a market rate and notwithstanding this, it is more prudent not to take a FV gain.

Fair value at reporting date for loans classified as FVTPL

The approach used to calculate the FV at origination of innovation loans including discount rates is refreshed for the recalculation of the FVs of loans classified as FVTPL at the reporting date. The assumptions for estimating the arm's length commercial interest rate taking account of an individual borrower's credit rating using EU risk finance guidelines and the cashflow projections are updated to the position at the reporting date to arrive at a proxy FV at the reporting date.

4. GRANT INCOME

	2022 £'000	2021 £'000
Grant income received from BEIS via UKRI	1,127	2,611

Grant income for the Company's lending activities and operating costs receivable from BEIS via UKRI has been recognised in income to run the 2021/22 programme and is non-repayable. In 2021/22 £3,567 thousand contractual interest received was deducted from grant income received (2020/21 £1,607 thousand contractual interest deducted).

5. WRITE DOWN OF REPAYABLE CAPITAL GRANT RECEIVED

	2022 £'000	2021 £'000
Write down of capital grant received	756	3,244

On the expiry of the capital grant funding from BEIS via UKRI, the Company will repay the amount of cash held in its bank accounts representing capital repaid from innovation loans. The repayable capital grant will be reduced by any unrecovered amounts from the beneficiaries of the innovation loans. The write down of repayable capital grant represents the reduction in the liability for write-offs and impairment losses incurred on the amortised cost innovation loans in the financial year as well as the reduction or increase in the liability for the fair value adjustment on the innovation loans on initial recognition of amortised cost and FVTPL innovation loans and the subsequent amortisation of this adjustment. The write down of the repayable capital grant is not adjusted for provisions on irrevocable commitments as the liability is not funded by the repayable capital grant until the commitment is extinguished by a loan advance.

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)
Notes to the financial statements for the year ended 31 March 2022 (continued)

6. INTEREST RECEIVABLE AND OTHER INCOME – FAIR VALUE CHANGES

	2022	2021
	£'000	£'000
Amortised cost commercial interest	3,683	2,521
FVTPL contractual interest received	1,399	37
Bank interest	1	3
Interest receivable	5,083	2,561

The commercial interest receivable is calculated using the effective interest rate income from innovation loans held at amortised cost.

The Innovate UK Loans scheme is designed to stimulate innovation in order to drive productivity and growth in the UK economy. Hence innovation loans are offered at a below market-rate (currently a fixed interest rate of 3.7% for Competitions 1 to 5 loans and 7.4% for Competitions 6 to 8 and ICLs). Therefore, in order to calculate a fair value of the loans at recognition, an adjustment is made for an arm's length commercial interest rate. Over the life of a loan the commercial interest rate less the fair value adjustment on initial recognition will net back to the contractual rate of interest (i.e., the below market interest rate).

	2022	2021
	£'000	£'000
Other income – Fair Value changes	872	160

Other income is a £872 thousand increase (2021: £160 thousand) of fair value on FVTPL ICLs for the period to the 31 March 2022 reporting date after the fair value adjustment on initial recognition has been made, excluding contractual interest receivable.

7. EMPLOYEES AND DIRECTORS

There were no employees of the Company during the financial year to 31 March 2022 and it does not incur any expenses in respect of the services of its directors. No directors receive remuneration from the Company for their services as directors of the Company. These directors are remunerated for their other responsibilities through the Innovate UK Council or UK Research and Innovation.

8. ADMINISTRATIVE EXPENSES

The (loss)/profit before corporation tax is stated after charging the following administrative expenses:

	2022	2021
	£'000	£'000
Recharged staff costs	2,706	2,919
Auditor remuneration	121	121
Other professional fees	1,737	958
Marketing & media	-	26
Travel	9	1
External training	11	11
Other IT costs	25	392
Total	4,609	4,429

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)
Notes to the financial statements for the year ended 31 March 2022 (continued)

No remuneration was paid to the external auditors in respect of non-audit work in 2021/22 £nil (2020/21 £nil). Audit fees disclosed in the table above include VAT. The amount receivable by the auditor in 2021/22 is £101 thousand plus VAT (2020/21: £101 thousand plus VAT).

9. TAX ON PROFIT/LOSS ON ORDINARY ACTIVITIES

Tax charge/(credit) in the Statement of Profit or Loss and Other Comprehensive Income	2022	2021
	£'000	£'000
Current tax:		
Group relief receivable	-	(139)
Tax charge	235	-
Tax charge/(credit) for the year	235	(139)

The charge/(credit) for the year can be reconciled to the loss per the Statement of Profit or Loss and Other Comprehensive Income as follows:

	2022	2021
	£'000	£'000
Profit/(Loss) for the period - continuing activities	1,240	(732)
Tax on profit/(loss) at standard UK tax rate of 19%	235	(139)
Tax charge/(credit) for the year	235	(139)

Factors that may affect future tax changes

Legislation has been passed to maintain the rate of corporation tax at 19% from 1 April 2021 (2020/21 19%). A corporation tax rate of 25% has been set with effect from 1 April 2023.

10. IMPAIRMENT LOSSES ON INNOVATION LOANS

The following table sets out impairment losses charged to the Statement of Profit or Loss and Other Comprehensive Income and the closing provision balance which is deducted from the amortised cost innovation loan balance in the Statement of Financial Position. Loans that are classified as FVTPL are out of scope of the IFRS 9 impairment requirements – see additional information in the Supplementary information for the Credit Risk Report on page 20.

Impairment losses	2022	2021
	£'000	£'000
Total innovation loans	1,798	2,987

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)
Notes to the financial statements for the year ended 31 March 2022 (continued)

11. INNOVATION LOANS

	Gross balances (note i, ii) £'000	Provisions £'000	Total £'000
2022			
Amortised cost	64,551	(8,061)	56,490
FVTPL	70,437	-	70,437
At 31 March	134,988	(8,061)	126,927

	Gross balances (note i, ii) £'000	Provisions £'000	Total £'000
2021			
Amortised cost	54,535	(6,263)	48,272
FVTPL	17,214	-	17,214
At 31 March	71,749	(6,263)	65,486

Note:

i. Innovation loans held at amortised cost include a reduction of the value at loan origination for the below market rates of interest that are charged which do not reflect the credit risk of the borrower. The cumulative contractual value of the loans advanced up to 31 March 2022 was £66,725 thousand (31 March 2021: £57,502 thousand) adjusted for redemptions and capital repaid and the cumulative fair value adjustment on initial recognition totalled £5,408 thousand (31 March 2021: £4,686 thousand). FVTPL loans of £70,287 thousand were advanced up to 31 March 2022 (31 March 2021: £17,313 thousand) with a cumulative fair value adjustment on initial recognition of £149 thousand (31 March 2021: £259 thousand). The outstanding gross amortised cost loan balances disclosed in the above table and held on the Statement of Financial Position also includes the impact of commercial interest earned less contractual interest received.

ii. The innovation loan balance includes £1,436 thousand of loans that have been recognised on the Statement of Financial Position when the Company has become a party to the contractual provisions of the loan by 31 March 2022 (31 March 2021: £2,265 thousand) by instructing the Company's third-party administration company GC Business Finance to advance the loans, as at that point the Company is contractually committed. In these cases, the borrowers have not received funds until just after the yearend. This balance is all for loans held at FVTPL (31 March 2021: £63 thousand to loans classified as amortised cost and £2,202 thousand for loans held at FVTPL). The Company's cash and cash equivalent holdings have been reduced by an equivalent amount.

Maturity analysis

The following table shows the residual maturity of the innovation loans, based on their contractual maturity:

Residual maturity of innovation loans	2022 £'000	2021 £'000
Repayable:		
In not more than three months	899	436
In more than three months but not more than one year	5,691	2,242
In more than one year but not more than five years	111,046	52,946
In more than five years	17,352	16,125
Impairment provisions	(8,061)	(6,263)
At 31 March	126,927	65,486

The maturity analysis is produced on the basis that each repayment instalment is treated as a separate repayment up to contractual maturity. No redemption level estimation is built into the analysis. There are no arrears to be taken into account which would have been spread across the remaining term of the loan.

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)
Notes to the financial statements for the year ended 31 March 2022 (continued)

12. CASH AND CASH EQUIVALENTS

Bank accounts	2022	2021
	£'000	£'000
Bank account	5,976	13,147
Bank account operated by third party loan administrators	1,918	10,139
At 31 March	7,894	23,286

The bank account operated by the third-party loan administrators GC Business Finance, the trading name of The Enterprise Fund Limited, is ring fenced for the use of managing the Company's innovation loan portfolio. The Company retains control and ownership of the funds held in this account.

13. DEBTORS AND PREPAYMENTS

	2022	2021
	£'000	£'000
Group tax relief debtor	-	139
Debtor	12	-
Prepayments	24	100
At 31 March	36	239

14. TRADE AND OTHER PAYABLES

	2022	2021
	£'000	£'000
Trade creditors	337	487
Current tax liabilities	235	-
Intra group grant income refund	6,152	2,585
At 31 March	6,724	3,072

The intra group grant income refund relates to contractual interest by borrowers on innovation loans which is offset against grant income that is received for the Company's lending activities and operating costs.

15. PROVISIONS FOR LIABILITIES AND CHARGES

Irrevocable commitments	2022	2021
	£'000	£'000
At 1 April	1,743	1,218
Provisions utilised	-	-
Charge for the period	307	1,373
Release for the period	(1,462)	(848)
Net Statement of Profit or Loss (credit) /charge	(1,155)	525
At 31 March	588	1,743

Provisions on irrevocable innovation loan commitments are recognised in the Statement of Profit or Loss and Other Comprehensive Income before the related loan is advanced and recognised in the Statement of Financial Position as a provision for liabilities and charges.

IFRS 9 requires provisions on irrevocable commitments for loans below market rates classified as amortised cost (i.e., Competitions 1 to 5 and 6 to 8 innovation loans) to be calculated at the higher of the estimated fair value decrease that will be written down when the loan is advanced or the ECL calculated on a probability

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)
Notes to the financial statements for the year ended 31 March 2022 (continued)

weighted basis. The fair value calculation is made on the same basis as the calculation for loan advances. In addition, the requirements for the classification of financial liabilities for below market rate loans also allows for provisions for commitments for FVTPL loans (i.e., on ICLs) on a FV basis only.

During the year, a higher proportion of provisions for irrevocable commitments for amortised cost loans, was required to be calculated on an ECL basis. It is expected that, the sensitivity of these provisions for irrevocable commitments calculated on an ECL basis is proportionate to the sensitivity on ECL provisions on loans advanced which is disclosed on page 39.

Release for the period amounts are provisions on irrevocable commitments which have been replaced by provisions on loans at the point that the irrevocable commitment is superseded by the payment of a loan to the borrower. Provisions on loan advances are netted off against gross loans.

16. RISK MANAGEMENT AND CONTROL

Credit Risk

Credit risk is the risk of a customer or a counterparty failing to meet their financial obligations. Credit risk also encompasses refinance risk and concentration risk. Refinance risk is the risk of loss arising when a repayment of a loan occurs later than originally anticipated. Concentration risk is the risk of loss arising from insufficient diversification. A separate credit risk report is disclosed in pages 9 to 19 in this set of financial statements.

Liquidity and funding risk

The Company has minimal liquidity and funding risk provided that the Company's parent UK Research and Innovation, continues to fund the Company's activities in accordance with its current funding arrangements. This includes funding via UKRI from BEIS for capital funding of innovation loan advances. Assurance as to the continuance of these arrangements forms part of the going concern basis in preparing the financial statements.

The UKRI Group manages its liquidity and funding risks within a comprehensive risk framework which includes its policy, strategy, limit setting and monitoring, stress testing and robust governance controls. This ensures that there is no significant risk that liabilities cannot be met as they fall due.

Residual maturity of financial assets and liabilities

The table below analyses the carrying value of financial assets and financial liabilities into relevant maturity groupings based on contractual maturity date (residual maturity).

Residual maturity	Due less than one month	Due between one and three months	Due between three and twelve months	Due between one and five years	Due after more than five years	Total
	£'000	£'000	£'000	£'000	£'000	£'000
31 March 2022						
Financial assets						
Cash	7,894	-	-	-	-	7,894
Innovation loans	-	899	5,691	111,046	17,352	134,988
Financial liabilities						
Repayable capital grant	-	-	-	-	(128,235)	(128,235)
Net funding difference	7,894	899	5,691	111,046	(110,883)	14,647

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)
Notes to the financial statements for the year ended 31 March 2022 (continued)

Residual maturity	Due less than one month	Due between one and three months	Due between three and twelve months	Due between one and five years	Due after more than five years	Total
31 March 2021	£'000	£'000	£'000	£'000	£'000	£'000
Financial assets						
Cash	23,286	-	-	-	-	23,286
Innovation loans	-	436	2,242	52,946	16,125	71,749
Financial liabilities						
Repayable capital grant	-	-	-	-	(85,891)	(85,891)
Net funding difference	23,286	436	2,242	52,946	(69,766)	9,144

The Innovation loans have been written down to fair values at initial recognition whilst the repayable capital grant from BEIS via UKRI is written down for amounts that the Company believes will not be recoverable from borrowers. Any net liquidity difference from innovation loan lending activities that is realised over the life of the loan will be funded by the write off of capital funding. Drawdowns for current irrevocable commitments will be funded by future drawdowns from repayable capital grant funding from BEIS via UKRI so have been excluded from the above table.

Interest rate risk

The Company is not exposed to interest rate risk. The cohort of Competitions 1 to 5 innovation loans charge a fixed rate of interest of 3.7% to borrowers. The cohorts of Competitions 6 to 8 and ICLs charge a fixed interest of 7.4% to borrowers. The Company is funded for innovation loan lending by BEIS via UKRI without being charged interest. Hence the Company does not have any material interest rate risk exposure and does not hold any derivatives to hedge interest rate risk.

Repayment Risk

The Company is not exposed to a repayment risk from the capital funding from BEIS via UKRI. If a borrower fails to repay on time, the Company will retain this funding until there is a subsequent repayment or restructuring of the underlying funding. The repayable capital grant from BEIS via UKRI is written down for amounts that the Company believes will not be recoverable from borrowers.

17. FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES MEASURED AT AMORTISED COST

The following table summarises the carrying value and the fair value of financial assets and liabilities measured at amortised cost on the Company's Statement of Financial Position.

At 31 March	2022		2021	
	Carrying value £'000	Fair value £'000	Carrying value £'000	Fair value £'000
Financial assets				
Cash and cash equivalents	7,894	7,894	23,286	23,286
Amortised cost Innovation loans	64,551	64,002	54,535	54,984
Total	72,445	71,896	77,821	78,270
Financial liabilities				
Repayable capital grant	128,235	128,235	85,891	85,891
Total	128,235	128,235	85,891	85,891

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

Notes to the financial statements for the year ended 31 March 2022 (continued)

Note:

The fair value of cash and capital grant funding from BEIS via UKRI is the carrying value. The innovation loan balance is before ECL provisions.

The information set out above provides information about how the Company determines the fair values of various financial assets and financial liabilities. Fair value is the price that would be received on sale of an asset or transfer of a liability in an orderly transaction between market participants, regardless of whether that price is directly observable or estimated using another valuation technique.

For financial reporting purposes, fair value measurements are categorised into Level 1,2 or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value are described as follows:

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets;
- Level 2 fair value measurements are those derived from inputs other than quoted prices that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices); and
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the assets or liability that are not based on observable market data (unobservable inputs).

Innovation loans are financial assets with a rate of interest which is a below market rate (non-commercial terms) that does not reflect the credit risk of the borrower. Loans are recognised when the Company becomes a party to the contractual provisions of the instrument and is initially recognised at fair value.

The Company has developed a future expected cash flow calculation. This approach is not based on a valuation technique that uses only data from observable markets, so the innovation loans are classified as Level 3 assets.

The future expected cash flows derived from the calculator are discounted using an appropriate discount rate which has been calculated using a credit risk adjusted interest rate. This credit adjusted interest rate used to calculate an arm's length commercial interest rate is based on EU reference rates set out in State Aid guidelines. The Board will continue to monitor the position regarding BEIS UK subsidy control guidance which has replaced EU risk finance guidance.

The fair value of the funding from BEIS via UKRI is equivalent to its nominal value because the funding has no maturity date and may become repayable on demand, in whole or in part, under certain circumstances.

Level 3 sensitivity analysis of valuations using unobservable inputs

An unobservable input is deemed to be significant if it is shown to contribute more than 10% to the valuation of a financial instrument. A 1% increase in the commercial interest rate for the amortised cost innovation loan advances could lead to approximately a £1,535 thousand decrease (2021: £1,309 thousand decrease) in the gross carrying value of loans at 31 March 2022 from £64,551 thousand to £63,016 thousand. For the FVTPL this could lead to a £1,102 thousand decrease (2021: £169 thousand decrease) in the gross carrying value of loans at 31 March 2022 from £70,437 thousand to £69,335 thousand.

In practice, the fair value adjustment on initial recognition for innovation loans is fixed at origination. Therefore, for loans already advanced, the loans are carried in the Statement of Financial Position at amortised cost and the commercial interest rate is not subject to further volatility. Commercial interest rates are reassessed at each reporting date for the purposes of determining current fair value for disclosure in this note.

INNOVATE UK LOANS LIMITED (REGISTERED NUMBER: 11220957)

Notes to the financial statements for the year ended 31 March 2022 (continued)

18. CONTINGENT LIABILITIES

At 31 March 2022, there were no contingent liabilities.

19. SHARE CAPITAL

	2022	2021
	£	£
Authorised, issued and fully paid		
share of £1 nominal value	1	1

The Company has one class of ordinary shares which carry no right to fixed income.

20. ULTIMATE PARENT UNDERTAKING AND CONTROLLING PARTY

The shares in Innovate UK Loans are owned by UK Research and Innovation (UKRI), a non-departmental public body funded by a grant-in-aid from the UK Government. The directors regard UKRI as the Company's ultimate parent. The financial statements of UKRI are available from UK Research and Innovation, Polaris House, North Star Avenue, Swindon, SN2 1ET.

UKRI is a non-departmental public body funded by grant-in aid from the UK Government by sponsorship from BEIS (the Department of Business, Energy and Industrial Strategy). UKRI describe BEIS as their controlling body in their Annual Report and Accounts for 2021/22.

21. RELATED PARTIES

The Company's ultimate parent is UKRI. UKRI is also the ultimate parent of STFC Innovations Limited (SIL). SIL has an equity investment in the following companies to which the Company has also advanced an innovation loan:

Entity	SIL's equity holding	IUKL loan advanced	IUKL loan commitment
31 March 2022	%	£'000	£'000
The Electrospinning Company Limited	18.9	715	-
Keit Limited	10.3	819	135

Entity	SIL's equity holding	IUKL loan advanced	IUKL loan commitment
31 March 2021	%	£'000	£'000
The Electrospinning Company Limited	23.6	690	25
Keit Limited	10.3	339	615

22. EVENTS AFTER THE REPORTING PERIOD

Since the end of the financial year, the company has as at 31 August 2022 advanced a further £6.9 million innovation loans, including £1.8 million ICLs.

On 10 March 2022 the first round of the Innovation Loans Future Economy Competition was launched with a series of subsequent rounds in the 2022/23 financial. These innovation loans will be advanced for highly innovative late-stage research and development (R&D) projects with the best potential for the future with a scope that focuses on the future economy as described in the Innovate UK action plan for business innovation 2021-2025. There should be a clear route to commercialisation and economic impact. In addition, on 19 April 2022 DASA supported by the Company launched a further series of defence innovation loans competitions with £10 million funding available to fund innovative defence solutions. Defence innovation loans will be advanced by the Company, funded by DASA/MOD.

GLOSSARY

Term	Definition
Amortised cost	A classification of loans which meets the IFRS 9 business model and SPPI cashflow characteristic tests (see below). The only return for these loans is repayment of capital and interest on capital outstanding.
Expected credit loss (ECL)	The present value of all cash shortfalls over the expected life of the financial instrument. The term is used for the accounting for impairment provisions under the IFRS 9 standard.
ECL – 12 month	Cash shortfalls resulting from default events that are possible in the next 12 months weighted by the probability of that default occurring.
ECL - lifetime	Cash shortfalls resulting from default events that are possible over the remaining expected life of the loan, weighted by the probability of that default occurring.
Exposure at Default (EAD)	The expected outstanding balance of the asset at default, considering the repayment of principal (where a repayment of capital period has begun) and interest from the reporting date to the date of default, together with any expected drawdown of committed facilities.
Fair value through profit and loss (FVTPL)	A classification of loans which does not meet the IFRS 9 business model and SPPI cashflow characteristic tests (see below). There is a potential of return of more than just repayment of capital and interest on capital outstanding.
Innovation continuity loans (ICLs)	ICLs are a type of innovation loans issued in 2020/21 as a response to COVID-19.
Loss given default (LGD)	The proportion of the exposure that is expected to be lost in the event of default, taking account of the impact of collateral (not a material issue for Innovate UK) and its expected value at the point of realisation, as well as recoveries and other means of loss mitigation. Security is taken over intellectual property or assets purchased with the loans, alongside a debenture, which may sit subordinate to other senior secured lenders, subject to an agreed deed of priority being entered into. The Company does not seek charges over bricks and mortar assets owned or leased by the borrower; neither is any form of personal guarantee taken, whether supported or unsupported, from individuals.
Non-linearity	Non-linearity in the relationship between ECLs and economic conditions occurs when a change to an economic assumption or scenario has a greater effect on the level of credit losses, when compared to an equivalent change in the assumption or scenario in the opposite direction.
Probability of default (PD)	The probability of a default event occurring, based on conditions existing at the reporting date and future economic conditions that affect credit risk. Probability of default has been determined based on the unlikelihood to pay indicators, plus backstop criteria based upon a measure of days past due. The lifetime PD forms part of the IFRS 9 stage assessment as well as the ECL calculation.
Significant increase in credit risk	A significant increase in credit risk on a financial asset is judged to have occurred when an assessment, using quantitative and qualitative factors identifies at a reporting date that the credit risk has moved significantly since the asset was originally recognised.
SPPI test	An assessment of whether the contractual terms of the financial asset give rise to cash flows that are in substance solely payments of principal and interest.

GLOSSARY (continued)

Term	Definition
Stage 1	Stage 1 assets are assets which have not experienced a significant increase in credit risk since the asset was originally recognised on the balance sheet. 12 month ECL are recognised as the impairment provision for all financial assets on initial recognition. Interest revenue is the EIR on the gross carrying amount.
Stage 2	Stage 2 assets have experienced a significant increase in credit risk since initial recognition. Lifetime ECL is recognised as an impairment provision. Interest revenue is the EIR on the gross carrying amount.
Stage 3	Stage 3 assets are identified as in default and considered credit impaired. Lifetime ECL is recognised as an impairment provision. Interest revenue is the EIR on the net carrying amount.