



DELIVERING ENERGY
FOR THE FUTURE



ANNUAL REPORT & ACCOUNTS 2016



AFC Energy, the industrial fuel cell power company, is the leading developer of low-cost alkaline fuel cell systems using hydrogen to produce zero emission electricity.

AFC Energy fuel cell system at our plant in Stade, Germany.

Our fuel cell has the potential to be the catalyst which transforms the way in which industries of today produce energy for tomorrow.



→ Visit our website at www.afcenergy.com

WHAT WE DO

AFC Energy is focused on developing large-scale and distributed stationary fuel cell applications, utilising alkaline fuel cell technology, supplied by industry sourced hydrogen feedstock.

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WHY WE DO IT

The inexorable growth in demand for clean energy coupled with the fact that hydrogen is the number one industrial gas, based on number of molecules produced, means that hydrogen fuel cell technology is here today providing a wide range of power needs.

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HOW WE DO IT

Modularised fuel cell system design that can be repeatedly scaled to deliver much higher power outputs.

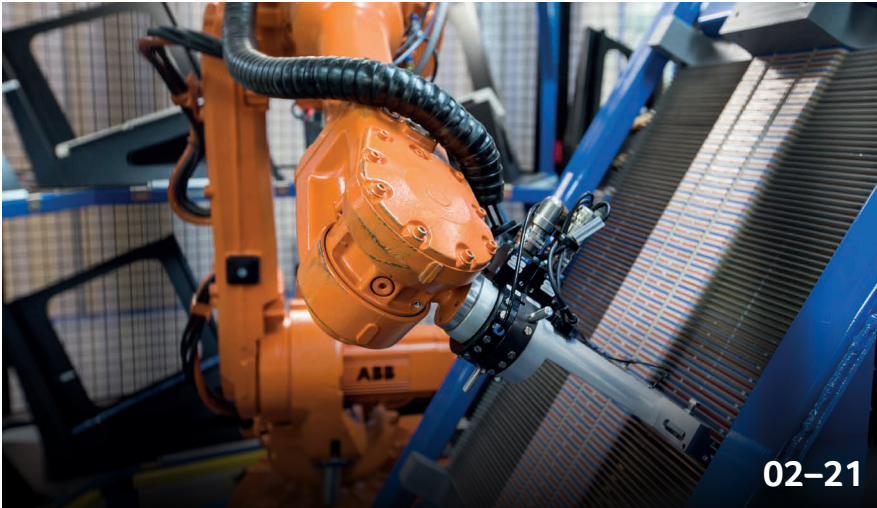
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WHY WE ARE DIFFERENT

AFC Energy is the only large-scale developer of alkaline fuel cells. Testimony of this was the delivery of a 240kW fuel cell ("240 FC") at our plant in Stade, Germany.

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WELCOME TO THE AFC ENERGY PLC ANNUAL REPORT & ACCOUNTS 2016

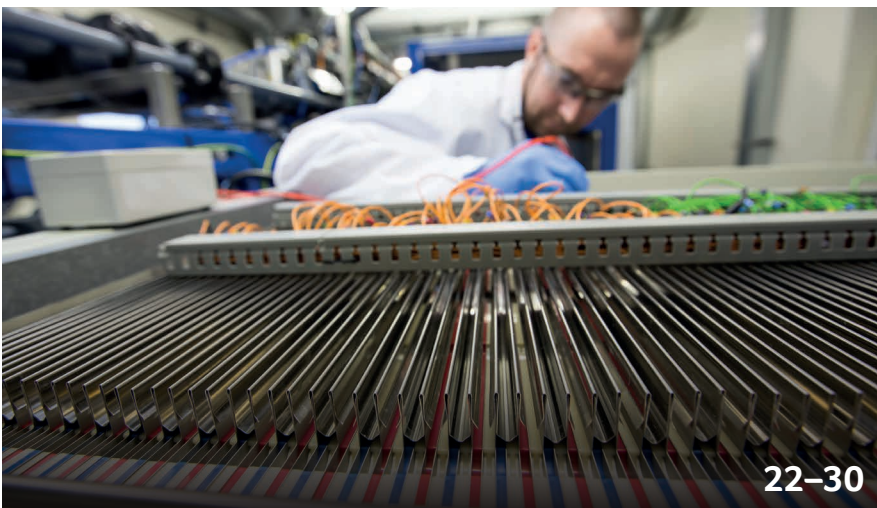


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AFC Energy's automated stack assembly robot.

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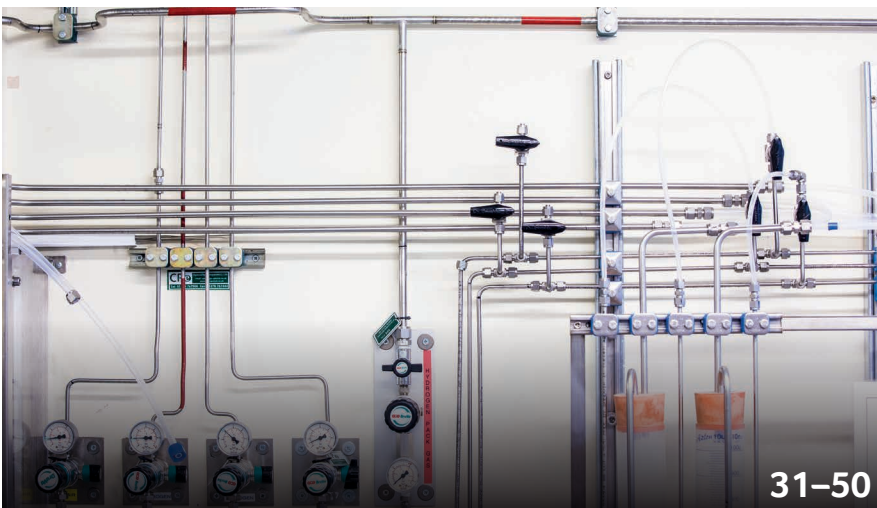


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AFC Energy's laboratory gas manifold.

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CHAIRMAN'S STATEMENT - STAYING THE COURSE



After good technical and strategic progress in 2016, AFC Energy is poised to move into commercialisation in 2017 with a strengthened management team and a now strengthened balance sheet.

TIM YEO
CHAIRMAN

OVERVIEW

In November 2016, the Paris Agreement on Climate Change came into force. For the first time, legally binding limits to global temperature rises have been agreed by nearly 200 countries. While the carbon emission curbs proposed are not themselves legally binding, the mechanism for periodically tightening those pledges is.

Governments including the US, China, India, and from the EU, are now collectively obliged to constrain global warming to no more than 2°C above pre-industrial levels (1.4°C above present levels).

While the journey to implement the required carbon emission reductions will inevitably face challenges along the way, not least given the recent pronouncements from the new US administration, it is evident that the wider international community remains committed to a lower carbon economy.

There is also support by global business leaders – one prime example being the recent announcement of the establishment of the Hydrogen Council, at the Davos 2017 World Economic Forum. Its members – including Royal Dutch Shell, Alstom, Air Liquide, Daimler and Toyota, among others – plan to invest €10 billion in hydrogen-related products within the next five years.

Hydrogen is expected to play a key role in supporting this transition to a low-carbon economy, especially within the transport, energy and petrochemical industry sectors, and the associated value chain.

The Board therefore continues to believe that stationary fuel cells have an important role to play globally and that AFC Energy has the technology and team to take a central position within this low-carbon economy, for both industrial scale and distributed generation applications.

KEY DEVELOPMENTS

The successful generation, in January 2016, of gross electrical output in excess of 200kW at the Company's first industrial scale fuel cell power plant in Germany, was a strong start to the year.

To maintain momentum, in March 2016, the Board issued the 2016 Strategic Milestones. Underpinning these milestones was the necessity to define, and share with our stakeholders, the fundamental metrics which the Company is focusing on to enable the commercialisation of the AFC Energy fuel cell system: Power, Longevity, Availability, Cost, and Efficiency. Both the management team and the Board remain focused on finalising the development of a readily deployable commercial product which is attractive to our target customer base.

Among other 2016 achievements, AFC Energy delivered the Generation 2 ("Gen2") fuel cell system which operated for more than 1,000 continuous hours (at which point the test was concluded), completed the basic design and engineering of the Company's new 10kW fuel cell system, and initiated and advanced dialogue for several commercial fuel cell opportunities. This was complemented by our success in establishing two new key strategic partnerships with Industrie De Nora S.p.A. and plantIng GmbH – both providing strong technical expertise and sector experience to support AFC Energy deliver its commercialisation objectives.

The journey continues into 2017 with the Company now prioritising its activities to enable the commercial deployment of its fuel cell systems. The successful completion of the £8.1 million equity fundraise in March 2017 provides the Company with a strong cash position to achieve this target.

While there may be challenges along the way, the Board and I remain confident that AFC Energy has set the appropriate course to achieve commercialisation. Our experienced leadership and strengthened management team should enable us to continue to make sound progress with our partners.

I would like to thank all the staff, partners and contractors working with AFC Energy, in addition to my fellow Board members and shareholders, for their continued support.

TIM YEO
CHAIRMAN

23 March 2017

A YEAR OF BREAKTHROUGHS

AFC Energy's achievements this year saw breakthrough steps with its technology and the successful completion of target Milestones.

2016

JULY 2016

Next iteration 10kW Fuel Cell Engineering Completed

Design and basic engineering of the next iteration 10kW fuel cell, including accompanying Balance of Plant ("BoP"), was completed, accomplishing Milestone 4 of the 2016 Strategic Milestones ahead of schedule. This included a thorough examination of key

performance metrics and a Hazard and Operability study ("HAZOP"). The HAZOP was conducted with participants from AFC Energy, planting GmbH and independent fuel cell and hydrogen expert consultancy Efficientics.

NOVEMBER 2016

Generation 2 Fuel Cell Testing Successfully Completed

AFC Energy successfully completed the development of its Gen2 fuel cell stack. Gen2 incorporates design changes to extend the operating life of the fuel cell stack, while increasing stack availability (i.e. the proportion of time the fuel cell stack is on average available to generate power) and reducing cost. These features represent three of AFC Energy's key metrics which have been identified for commercialisation.

"These two milestones, in addition to those achieved earlier in the year, position us for delivery of commercial contracts which we continue to pursue and in turn provide the traction needed with our partners for the deployment of units and the fulfilment of the outstanding 2016 Milestones."

ADAM BOND
CHIEF EXECUTIVE
OFFICER

JANUARY 2016

Power Output of 204kW Achieved

AFC Energy successfully achieved a total power output of 204kW at its 240kW fuel cell ("240 FC") power plant in Stade, Germany. This provided a number of significant technical "firsts" for the Company. The majority of the 24 stacks

trialled in Stade, achieved 10kW or more of power output. Automation of start-up, operation and shutdown were fully demonstrated. The fuel cell system was signed off by German engineers for safety and robustness of design.

AUGUST 2016

Strategic Technology Collaboration with De Nora Signed

AFC Energy entered a Joint Development Agreement ("JDA") with Industrie De Nora S.p.A. ("De Nora") targeting technological enhancements to AFC Energy's fuel cell system and to further accelerate commercialisation of AFC

Energy's technology platform. The parties plan to widen the collaboration to develop new product offerings, combining AFC Energy's fuel cell system with De Nora's complementary systems, to access new markets for mutual benefit.

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NOVEMBER 2016

Agreement with Peel Environmental for Assessment of Hydrogen Fuel Cell Precinct

AFC Energy signed an agreement with Peel Environmental Limited ("Peel") to assess the techno-economic feasibility of the UK's largest hydrogen fuel cell precinct at Peel's Protos industrial park in the UK. A positive outcome from the techno-economic assessment for the development of a 35MW

to 50MW fuel cell project at the Protos site could see the development of the UK's largest stationary fuel cell project and one of the largest in the world, confirming a growing transition towards a hydrogen-based economy, thereby positioning Protos and AFC Energy at the forefront of this movement.

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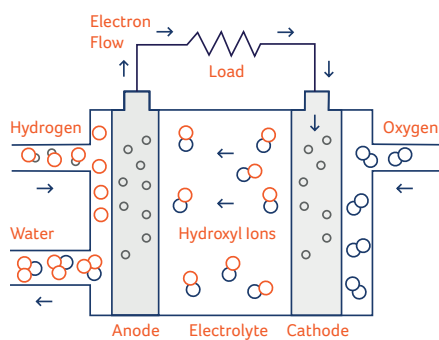
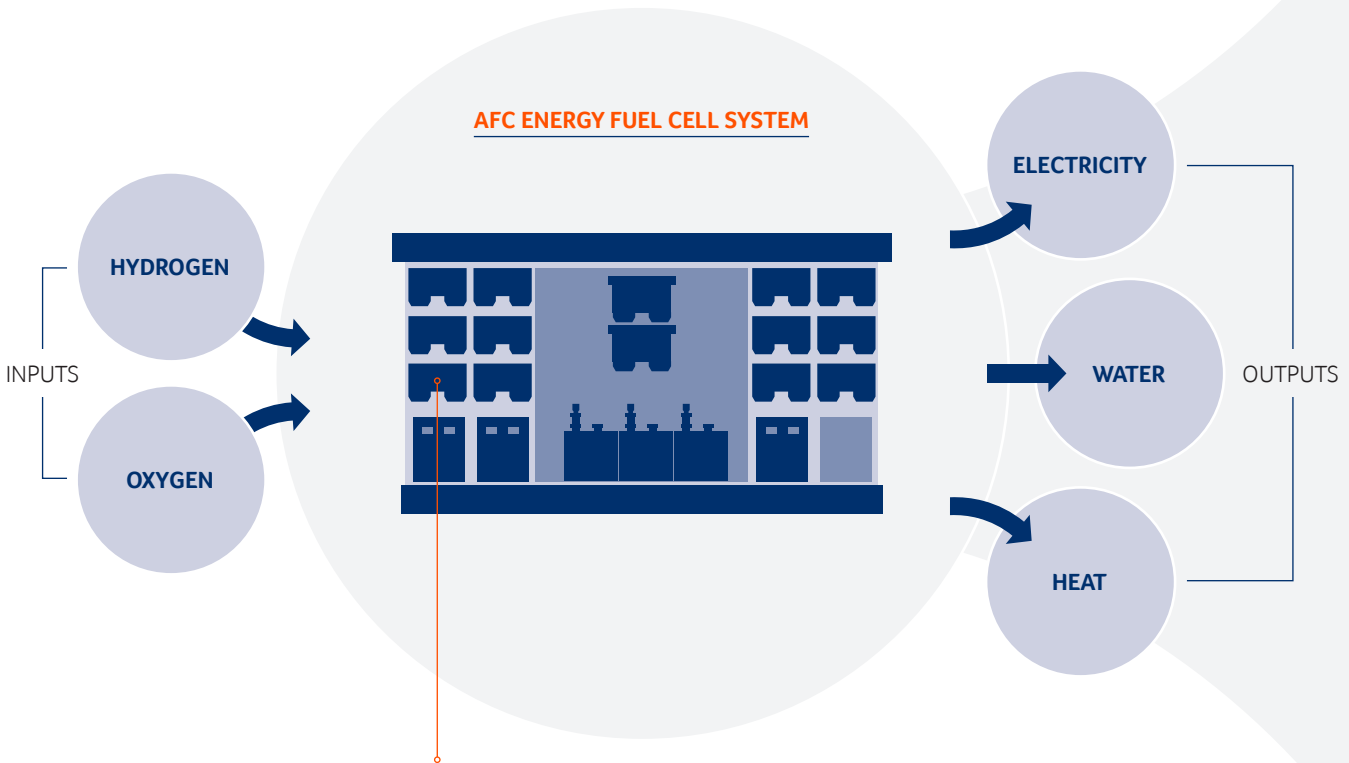
2017

[→ Please visit our website for more news at \[www.afcenergy.com\]\(http://www.afcenergy.com\)](#)

OUR TECHNOLOGY

Highly Fuel Efficient, Environmentally Acceptable Power Generation

Why alkaline fuel cells (“AFCs”)? A fuel cell hosts and facilitates the controlled chemical reaction of hydrogen and oxygen (from the air) to produce an electrical current. The direct conversion of chemical potential energy to electrical energy in a single step means that fuel cells are highly efficient. With their potential for up to 65% electrical efficiency, AFCs have the scope to be the most efficient of all fuel cell types.



ALKALINE FUEL CELL

An AFC is a device that implements the reaction of oxygen (from the air) with hydrogen (from an external supply source) to generate heat, electricity and water. Fuel cells are similar to batteries, but differ in one critical area: given the continuous supply of fuel and air, electricity, heat and water can in turn, be continuously generated (batteries have a finite amount of fuel and so, once this is exhausted, they stop operating). The only by-products of AFCs are demineralised water and heat – both of which have commercial value. Apart from water, an AFC is a zero-emission “green” generator.

Benefits of Alkaline Fuel Cells



AVAILABLE HYDROGEN

Hydrogen can be generated by renewable energy (such as wind and solar PV) in significant, sustainable quantities. By-product or vented hydrogen sources include: bio-mass, glass production, hydrocarbon processing and chlor-alkali facilities. Vented hydrogen arises as a by-product of many chemical processes, for example, the manufacture of chlorine can result in the generation of excess quantities of hydrogen.



WATER AND HEAT AS BY-PRODUCTS

AFC by-products consist of water and heat. The production of water is seen as a benefit in specific regions around the world, while the heat produced may be captured and used on site or in a local end-user's industrial process. This generates heat load, has the potential to further reduce both the end-user's energy requirements from the grid and their potential carbon emissions.



QUIET AND CLEAN AT POINT OF GENERATION

AFCs have few moving parts. Small electrical pumps and blowers move gases and liquids around the system. Therefore, it is quiet compared to traditional technologies. Its only by-products are water and heat.



LOW LIFETIME COST OF OWNERSHIP

We aim to reduce the cost of ownership through a lower operating temperature (i.e. below 100°C) with consequential use of more affordable materials. Additionally, we have the ability to recycle the materials we use in our fuel cell system.



AFC Energy's 240kW fuel cell system, the world's largest AFC installation, at our plant in Stade, Germany.



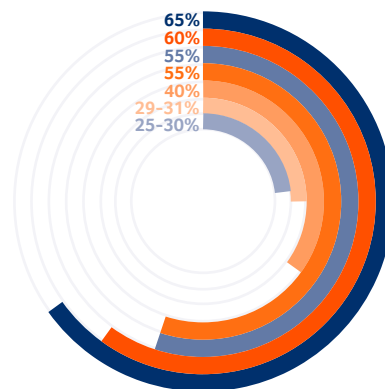
MORE EFFICIENT AT ALL LEVELS OF UTILISATION

An AFC does not burn fuel like an internal combustion engine or turbine so it does not need to drive pistons or turbines. Avoiding this intermediate mechanical step and having a direct conversion route to electricity is what makes an AFC so efficient. An AFC is also "scaleable" without impacting efficiency. The low operating temperature results in quicker start-up times and the use of lower cost construction materials.

OPERATING TEMPERATURE

Fuel Cell Type	Operating Temperature
SOLID OXIDE	500–1,000°C
MOLTEN CARBONATE	600–700°C
PHOSPHORIC ACID	120–150°C
POLYMER ELECTROLYTE MEMBRANE	<120°C
ALKALINE	<100°C

ELECTRICAL EFFICIENCY



65%	ALKALINE
UP TO 60%	SOLID OXIDE
UP TO 55%	POLYMER ELECTROLYTE MEMBRANE
UP TO 55%	MOLTEN CARBONATE
40%	PHOSPHORIC ACID
25-30%	DIESEL GENERATORS
29-31%	GAS TURBINE (SIMPLE CYCLE)

Source: www.afcenergy.com/technology/advantages; www.power.cummins.com; www.corporate.man.eu

MARKET OVERVIEW

The production of lower cost power from highly fuel efficient AFCs is competitive against mainstream forms of electricity generation and has enormous market potential in a wide range of industrial settings, sectors and environments.

Major Trends Impacting our Market

INTERNATIONAL CO-OPERATION

Governments are increasingly globally co-ordinated in tackling climate change (e.g. the Paris Agreement) through the adoption of decarbonisation policy agendas – this is evidenced by the targeting of large-scale, efficient energy integration. Hydrogen storage solutions, when combined with electrolysis and AFC technology can potentially provide a significant hydrogen battery solution for integration with intermittent renewable energy sources.

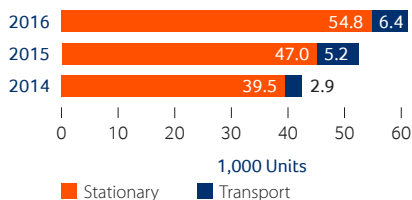
NATIONAL GOVERNMENT POLICIES

Governments are utilising fiscal incentive structures to prioritise the improved utilisation of limited resources. By-product hydrogen, vented as a waste product, is gaining increased scrutiny. For example, there is recognition of the need to significantly reduce oil-fired power generation in Saudi Arabia, with the utilisation of hydrogen from the petrochemical industry, with AFCs offering one such solution. Korea is also a firm advocate with fiscal incentives seeking to improve hydrogen utilisation.

GLOBAL INDUSTRY

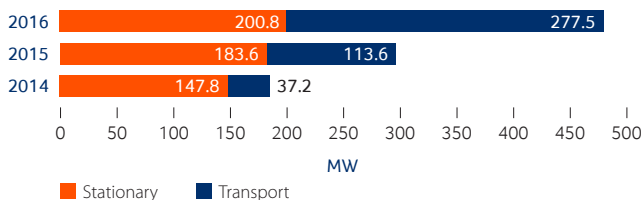
Energy intensive sectors are increasingly exposed to government carbon policy and rising power prices. Many international industrial groups now seek cleaner, off grid and long-term affordable energy solutions. The use of by-product vented hydrogen through the adoption of fuel cells will enable industry to mitigate the risk of rising power prices and Government policy.

FUEL CELL SHIPMENTS BY APPLICATION



Source: E4Tech (2016 is forecast)

MEGAWATTS BY APPLICATION



Source: E4Tech (2016 is forecast)

Growing International Commitment to the Hydrogen Economy

In January 2017, the Hydrogen Council launched a global initiative at the 2017 World Economic Forum.

The Council currently comprises 13 major industrial and energy companies that are committed to help achieve the ambitious goal of reaching the 2°C global warming target set in the 2015 Paris Agreement (COP21). The inaugural members are Air Liquide, Alstom, Anglo American, BMW, Daimler, Engie, Honda, Hyundai Motor Company, Kawasaki Heavy Industries, Royal Dutch Shell, The Linde Group, Total, and Toyota Motor Corporation.

Its 13 members collectively invest €1.4 billion annually into the hydrogen and fuel cell sectors and plan to boost this amount to €10 billion over the next five years.

The Hydrogen Council has called on governments to support the development of infrastructure for a “hydrogen ecosystem.”

Members will collaborate with each other, wider industry, other stakeholders and the public to progress hydrogen technology.

“Hydrogen is a versatile energy carrier with favourable energy characteristics since it does not release any CO₂ at the point of use as a clean fuel or energy source, and can play an important role in the transition to a clean, low-carbon, energy system...The council will work with, and provide recommendations to, a number of key stakeholders such as policy makers, business and hydrogen players, international agencies and civil society to achieve these goals.”

THE HYDROGEN COUNCIL

How we are Responding

AFC Energy is targeting a global opportunity - the generation of electricity that is competitive against mainstream sources has significant market potential across a wide range of regions, both in an industrial and distributed setting.

KEY TARGET REGIONS

We target partners in markets where there is supportive Government policy, with demonstrated private sector appetite to diversify energy sourcing, through the introduction of our fuel cells.



UK

Hydrogen could provide significant benefits to the UK's energy system and play a greater role in the UK's energy mix. In 2016, the UK launched a public-private roadmap exercise to drive sustainable economic growth in the UK hydrogen and fuel cell industry to 2025 and beyond.



GERMANY

Within the EU, Germany has led the introduction of fuel cells through the European Fuel Cells and Hydrogen Joint Undertaking ("FCH JU"). Assuming 90% renewables adoption, the Hydrogen Council expects c.170TWh/Year of curtailed renewable power by 2050, which may alone create an opportunity for c. 60GW of electrolysis capacity.

Source: "How hydrogen powers the energy transition", January 2017



UNITED ARAB EMIRATES AND OTHER MIDDLE EAST

The UAE is at the forefront of the development of renewable energy in the MENA region. AFC Energy is targeting the sale of both power and water into the local market, through utilisation of its fuel cell systems.



SOUTH KOREA

Financial incentives paid to producers of electricity generated from fuel cells make South Korea a particularly attractive target market for AFC Energy's fuel cell systems.

MARKET OPPORTUNITIES

The production of low-cost electricity that is competitive against mainstream forms of electricity generation has enormous market potential in a wide range of industrial settings, sectors and regions.



LARGE-SCALE STATIONARY INDUSTRIAL POWER PLANTS

We are focused on industries where hydrogen is easily available and offers low feedstock costs as a by-product from manufacturing processes. Large stationary units refer to multi-megawatt power plants providing primary power. These units are being developed to replace power from the grid and can also be used to provide grid expansion nodes.



OFF GRID DECENTRALISED POWER GENERATION

Decentralised or distributed applications can be targeted in areas where there is little or no grid infrastructure. This may include isolated, or island communities, remote facilities (e.g. mining), or as a substitute for diesel back up generation.



FUEL CELL INTEGRATION OPPORTUNITIES

Significant opportunities arise through the potential to develop a hydrogen battery which addresses the power supply/demand challenges encountered with intermittent renewable power. Further, the Company believes that material value can be created through the efficient integration of its fuel cell system, with water treatment and associated electrolysis technologies.

KEY TARGET INDUSTRIES

We are targeting large-scale stationary industrial power plants, and distributed off grid applications rather than nascent household or vehicle applications.



NATURAL AND BIOGAS

Natural gas and biogas are predominantly methane which is hydrogen-rich. Hydrogen is released using a standard industrial process known as steam methane reforming ("SMR"). Developments in this field are leading to improved economics for the smaller scale reforming of steam methane.



ENERGY FROM WASTE ("EFW")

Hydrogen can be generated economically from domestic and commercial waste – due to its high hydrocarbon content. AFC Energy's alkaline fuel cell systems have the potential to generate c. 40% more electrical power from the same waste, lowering carbon emissions by the same amount.



ELECTROLYSIS

Water electrolysis, using renewable electricity, offers significant benefits to the electricity sector in supporting the integration of renewable generating capacity and providing grid-balancing services. The hydrogen obtained with this technology has a high purity that can reach 99.999 vol.% once the produced hydrogen has been dried and oxygen impurities removed.

HOW WE MEASURE UP

AFC Energy has developed an alkaline fuel cell system which converts hydrogen into power. Its technology has the potential to be a catalyst in transforming the way today's industries produce energy for tomorrow.



Technology and Manufacturing

At the forefront of innovation, AFC Energy is re-engineering effective technology using modern materials readily available today.

→ PAGE 04

Commercial Potential

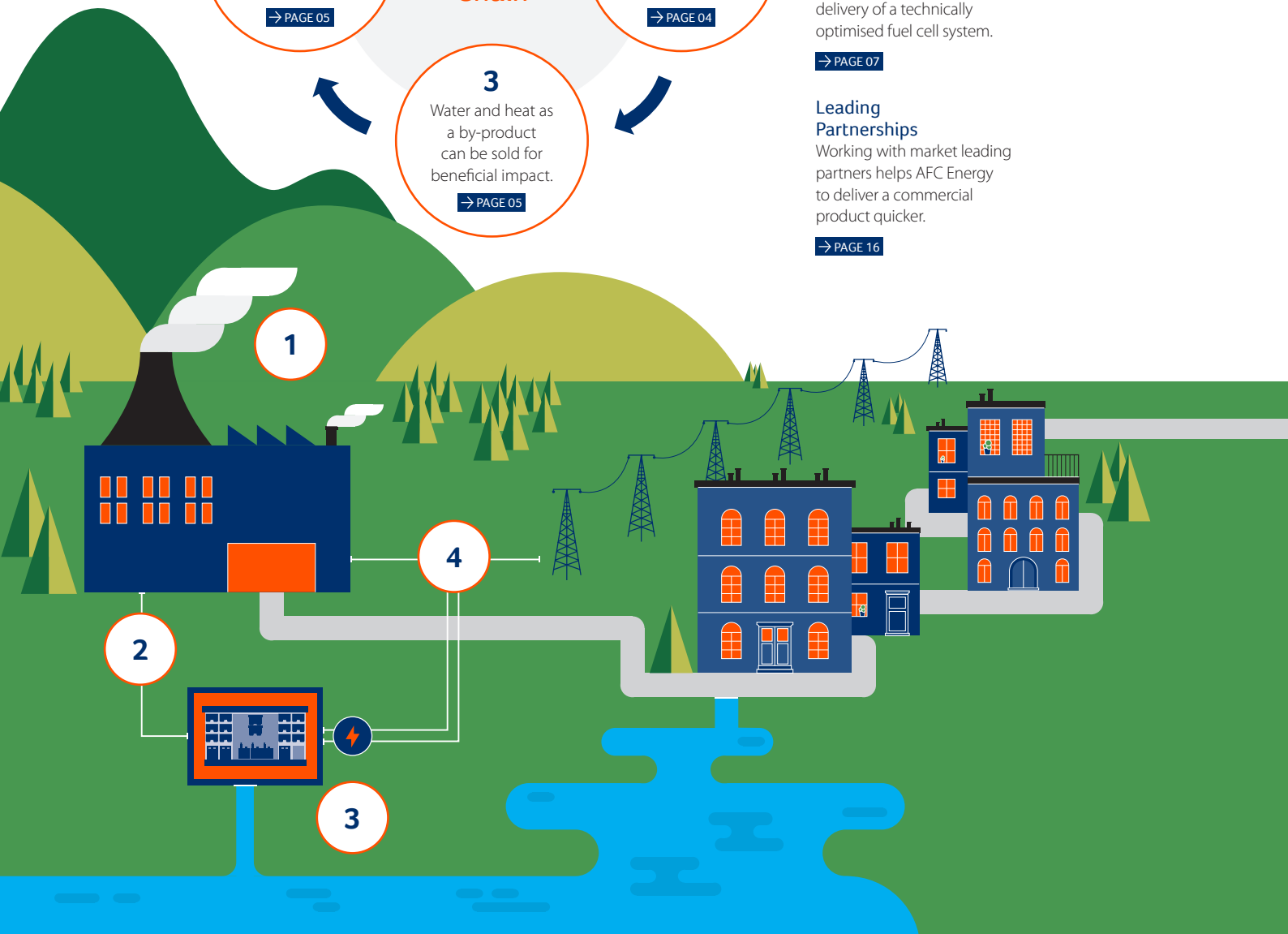
We are looking to build a pipeline of commercial opportunities through the delivery of a technically optimised fuel cell system.

→ PAGE 07

Leading Partnerships

Working with market leading partners helps AFC Energy to deliver a commercial product quicker.

→ PAGE 16



Technical Development Targeting Five Key Metrics Required for a Commercial Power Plant



POWER

- 204kW produced from first industrial scale fuel cell plant in Germany
- In excess of 10kW of power generated from multiple fuel cell stacks operating at the plant, against a 10kW design rating



LONGEVITY

- Delivered Gen2 fuel cell system which operated continuously for > 1,000 hours
- AFC Energy targeting minimum one year longevity



AVAILABILITY

- Already achieved over 90% availability on stack over one month's operation (against target of 90%)
- Automation of start up, operation and shutdown supporting enhanced system availability and control from offsite



COST

- Basic modular design, using standard industrial materials
- Ease of operation and maintenance



EFFICIENCY

- Alkaline fuel cells offer highest electrochemical efficiency of all fuel cells
- Potential to deliver up to 65% efficiency

WHAT MAKES OUR ALKALINE FUEL CELLS (AFCs) DIFFERENT?

The key differentiator for fuel cells, generally, is the high fuel efficiency. AFCs are at the top of the range in this regard. AFCs utilise a liquid electrolyte in the system.

Our liquid electrolyte facilitates lower operating temperatures of c. 60°C, versus hundreds or thousands of degrees Celsius for other fuel cell technologies.

We therefore have more flexibility to use standard and lower cost industrial materials across the entire fuel cell system – this allows ease of manufacture of modular skids and a lightweight overall unit, lowering capital and operating expenditure.

A key objective has been to design the AFC Energy fuel cell system for re-use or recycling, so that 80% is re-usable, making our systems more environmentally attractive whilst reducing the levelised cost of electricity through re-use.

All of which contribute to lower cost and competitive advantage.

There is scope to integrate our alkaline fuel cells with alkaline electrolysers (which generate hydrogen), which could form a "green" integrated hydrogen generation/conversion technology platform.

This gives us greater flexibility to integrate with parallel technology.

Our simple modular design basis for the fuel cell cartridges and balance of plant allow for volume scale up (from kW to MW), utilising the same standard 10kW fuel cell "building block" for each power plant.

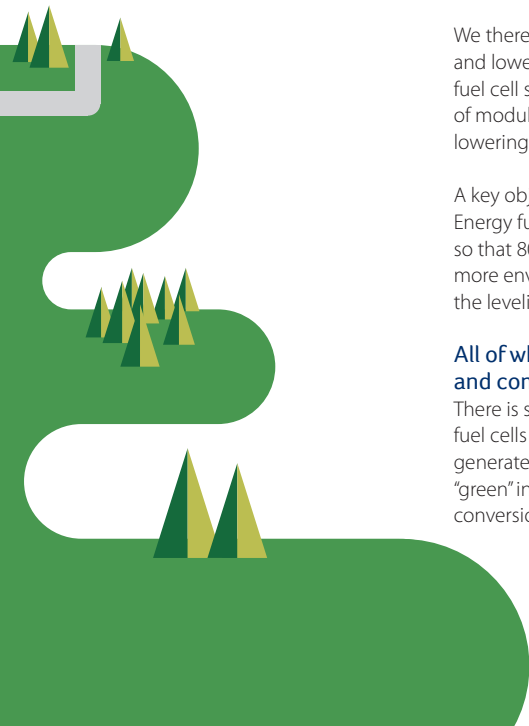
The modular approach assists with the standardisation of the manufacturing and assembly processes, streamlines procurement, disassembly and recycling, and simplifies power plant construction, operation and maintenance.

This enables us to provide scalable solutions to our prospective customers.

AFCs offer the highest electrochemical efficiency of all fuel cells.

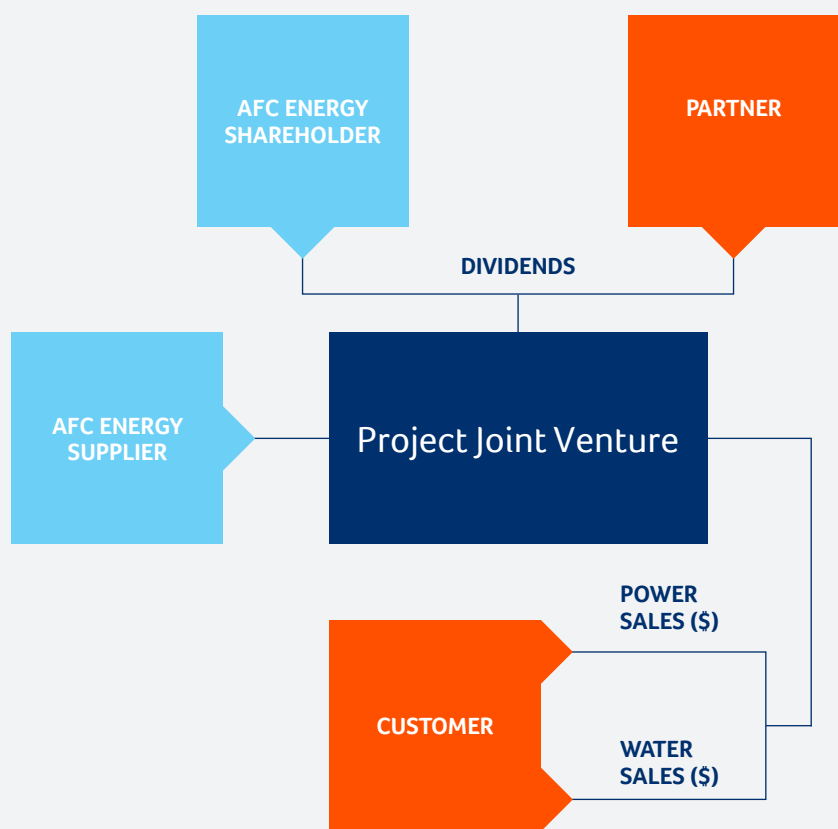
Our AFCs have the capacity to operate on lower grade industrial hydrogen – we are working to ensure they can accept hydrogen from industrial facilities, with limited required purification.

This allows more affordable and a broader range of available feedstock – all of which improve the viability and market potential of our alkaline fuel cells.



OUR BUSINESS MODEL

Our aim is to install, own, operate and maintain stationary alkaline fuel cell systems that generate durable power at the highest levels of fuel efficiency for the future. AFC Energy seeks to be a world-class energy company that deploys low cost, high performance alkaline fuel cell technology to the global market.



AFC Energy targets co-ownership of projects through joint ventures, where our interests are aligned with those of our partners, by having “skin in the game”.

The building block of every AFC Energy fuel cell system is, currently, the 10kW stack. AFC Energy aims to provide clean power solutions from as small as 10kW up to multi megawatts – the only difference being the associated BoP. We use the same basic fuel cell stack in all systems.

The 10kW modular unit provides a low cost “entry option” for prospective partners, which offers a smaller scale demonstration plant that may lead to a large-scale plant development by our partners and customers.

One of the trends in the global energy market is the movement towards off-grid, distributed power models where power demand may often be less than a “standard” 240 FC system, but is open to pricing which is substantially higher than conventional wholesale power pricing. Diesel generation is one obvious example where our fuel cells have the potential to displace existing plants.

AFC Energy plans to conclude the basic design and engineering on a 1MW capacity fuel cell system, which is capable of deployment in 2017.

Targeted Sources of Income

SALES REVENUES

Although, in the longer term, we may wish to retain ownership of our fuel cell systems, we will also remain open to opportunities to sell our fuel cell systems, where project and partner requirements require an alternative approach.

ELECTRICITY, HEAT AND WATER REVENUES

Revenues from the sale of power, heat and water, whether from AFC Energy alone projects, or in conjunction with partners and joint venture arrangements.

MAINTENANCE AND SECURITY

Our fuel cell projects will have a life of 20+ years operation, providing the opportunity to offer services and maintenance contracts for the fuel cell cartridges and systems, generating long-term annuity revenues.

LICENCE REVENUE

We remain open to opportunities to generate licence fee income for our fuel cells in markets, which have a longer sales/delivery process. Working in this way may minimise our business development costs and help deliver recognition in complementary markets earlier.

DEVELOPMENT INCOME

External agency funding enables our share capital to work harder. At AFC Energy, we look to fit our development needs within defined funding rules. This allows projects to be delivered earlier and with less call on internal financial resources for capital items.

OVERHEAD COVERAGE

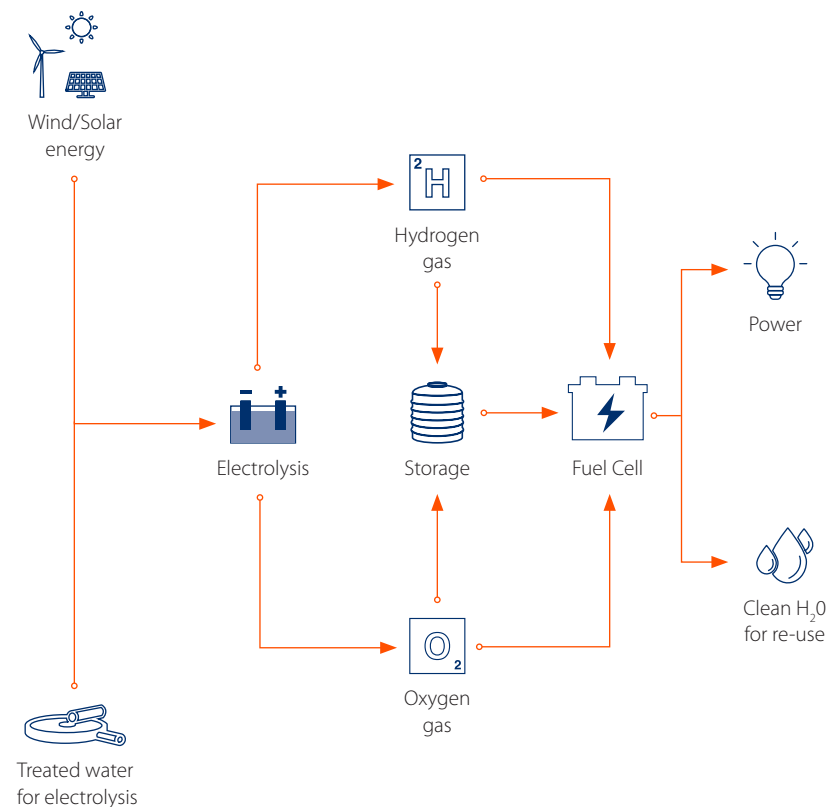
Many funding agencies fund direct time spent on key technical research, development and demonstration. A portion of overhead recovery is also permitted. This significantly mitigates our monthly cash burn rates.

Integrated Solutions Provider

We aim to provide our fuel cells not only for stand-alone power solutions, but also as a flexible building block which can be integrated with other related technologies, delivering a broad range of solutions for our customers.

HYDROGEN BATTERY

The AFC Energy fuel cell can be deployed as part of a "hydrogen battery" scheme. When grid demand is low, excess power generated from renewable sources, such as wind or solar, can be diverted to a water electrolyser for hydrogen generation.



The produced hydrogen can then be stored and optimally released to our fuel cells at periods of peak demand (with higher tariffs), to support grid power requirements, when required.

WASTE WATER TREATMENT

The AFC Energy fuel cell can also be deployed as part of a waste water treatment integrated solution. Following preliminary treatment, waste water can be electrolysed, to generate hydrogen and oxygen.

The by-product hydrogen and oxygen can then be delivered to the AFC Energy fuel cell system, to generate power and clean water, which can be re-used.

The electrolysis can be powered by, for example, renewable solar or wind power. Further, this system can be supplemented with hydrogen storage, to optimise delivery of power/water for peak demand periods.

Creating Value

AFC Energy is conscious of its obligation to effectively manage its relationships with a broad group of stakeholders which include:

SHAREHOLDERS

AFC Energy acknowledges the importance of creating sustained long-term shareholder value, which ultimately hinges on commercialisation of the technology and maintaining a broad-based competitive advantage over substitute or near substitute offerings.

PARTNERS

AFC Energy places high priority on the need to establish and nurture key strategic partnerships in which our partners can form a clear line of sight on how they will derive long-term exceptional value from their collaboration with us.

EMPLOYEES

Without our employees, AFC Energy is not able to deliver on our technical milestones and execute the power projects which are required to utilise our technology – AFC Energy is focused on the long-term development of all our staff to ensure they remain motivated to deliver outstanding performance for the business.

CUSTOMERS

We regard our customers as our partners – if they succeed, then so do we. The Company has identified priority performance metrics for a commercial product, which our customers will demand – it is our duty to supply this and ensure that our fuel cell system remains robust in divergent environments, reliable and available when power is required.

COMMUNITIES

AFC Energy is primarily targeting large-scale industrial applications for the fuel cell system but is also considering distributed and related applications (such as water treatment), which has tremendous potential to serve communities. AFC Energy also highly values the relationships it has with those parties with common interests in our project locations and seeks to maintain a positive dialogue and transparency with its local communities and neighbours.

OPERATIONAL REVIEW



2016 was an important year of consolidation for the Company with material improvements not only in the fuel cell technology platform, but also in the dialogue with several key commercial and strategic partners for AFC Energy. The corporate value gained from AFC Energy's collaboration with De Nora, and the commencement of commercial project developments with Peel Environmental, cannot be undervalued and positions the Company well for an accelerated programme of activities in 2017.

ADAM BOND
CHIEF EXECUTIVE OFFICER

In December 2014, the Board of AFC Energy made a conscious decision to switch its focus away from the laboratory to the acceleration of R&D and ultimately the commercialisation of an industrial-scale fuel cell system. In taking this decision, I outlined a three-year window of opportunity which would see AFC Energy progress from a company that had managed to deliver a "9 cell stack" (equivalent to less than 1kW of gross output) through to a technology platform capable of running multi-megawatt projects across several international jurisdictions.

It is safe to say 2015 saw significant progress not only in upscaling the stack from 9 cells to 101 cells in a few months, but also in delivering the world's largest alkaline fuel cell installation in Stade, Germany with a nameplate capacity of 240kW. The progress was tangible and outcomes were transparent insofar as for the first time in AFC Energy's history, the Company had a reference plant capable of demonstrating the operating capability of its proprietary fuel cell technology. Whilst many investors saw this as the end of the commercialisation roadmap, the process of accelerating the installation in Stade delivered for AFC Energy many findings which could only be

identified once a fully industrial system was up and running, and indeed, with these findings came the need for further refinement of the system. To this end, 2016 became the year of consolidation.

Having now done the hard yards and exhibited the technical discipline to bring AFC Energy's fuel cell technology back to where we believe it needs to be in order to drive commercial partnering opportunities, I believe 2017 to be the year in which we start to see the fruits of our collective labour as we close in on the final phase of the three-year window.

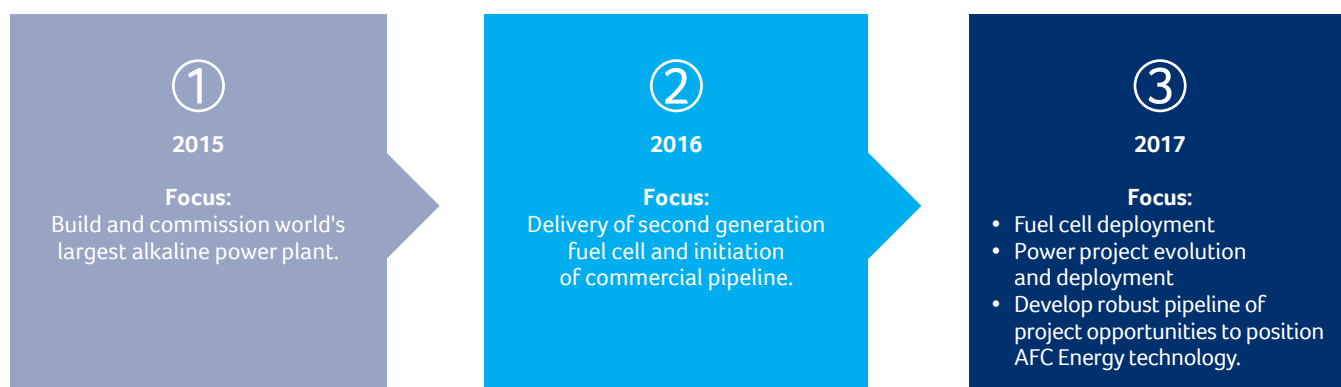
OPERATING REVIEW Technology

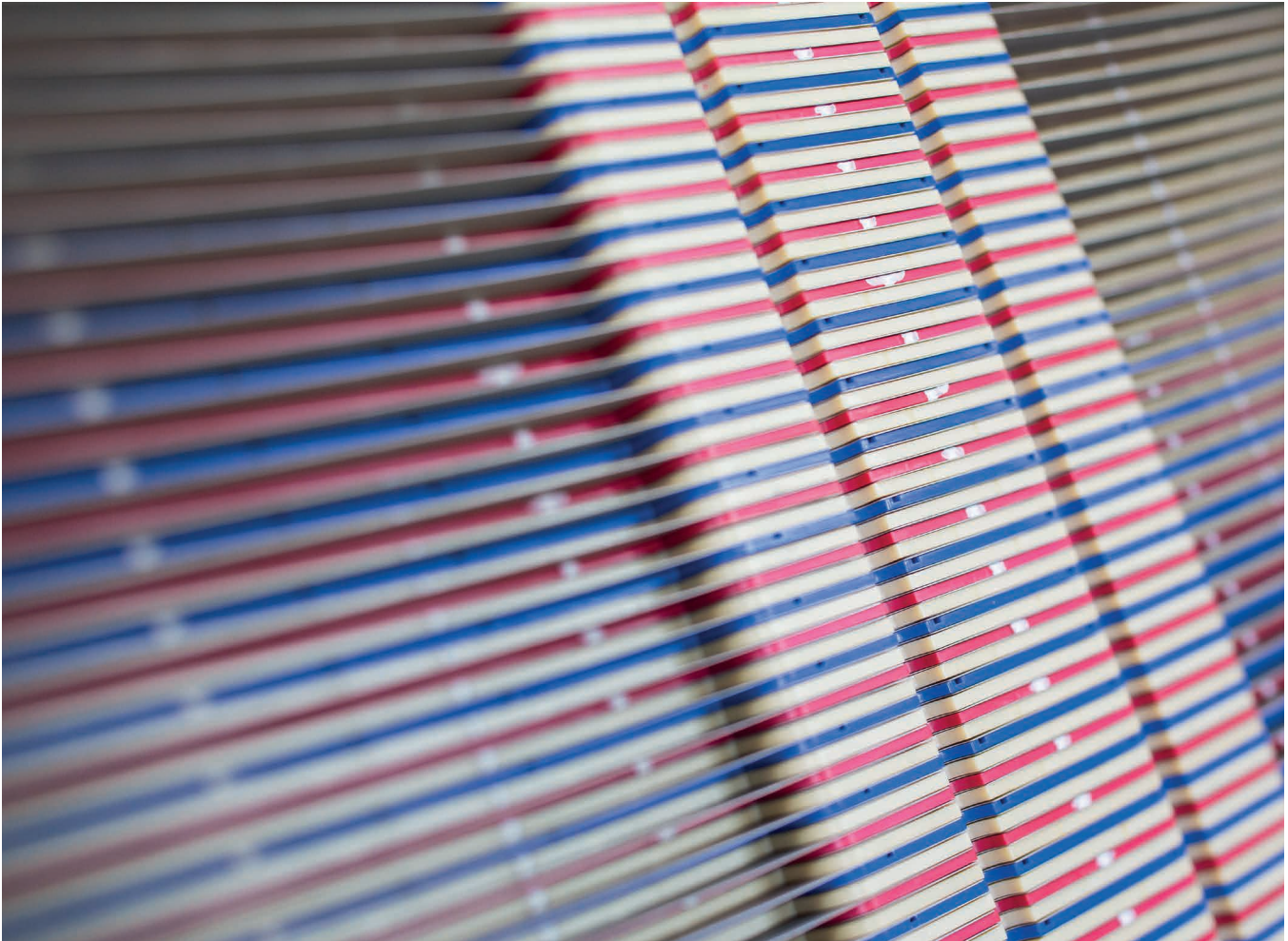
Having spent much of my career in the energy sector, the expectations of a power plant developer and owner on a generation technology provider always come back to their ability to demonstrate five key metrics which at AFC Energy have become known as the "metrics of commercialisation". These metrics, being Power, Longevity, Availability, Cost and Efficiency, have provided AFC Energy with its internal key performance indicators of success throughout the year.

The commissioning and demonstration of AFC Energy's 240kW system in Stade in January 2016 went a significant way to demonstrate the capability of the Company's proprietary fuel cell technology package. In particular, it demonstrated the ability of our system to deliver power from our fuel cell at or near nameplate on a cartridge by cartridge basis, providing empirical evidence for the first time of the technology's longevity, availability, cost and efficiency. In all cases, the Stade reference plant gave clear guidance as to those areas AFC Energy needed to address before its technology could be classed as "commercial".

Throughout 2016, AFC Energy embarked on a series of work packages, colloquially named "Gen2", which sought to address a number of the issues associated with our findings identified at Stade. The endeavours made on these work packages included a more focused discipline by which the technology development and rigorous assessment of these findings became solutions. To the credit of AFC Energy's team, the culmination of these work packages came in the latter quarter of the year when two of AFC Energy's stacks, operating at Stade and at the Company's facilities in Surrey, delivered in excess of 1,000 hours of continuous operation

Three-Year Accelerated Path to Commercialisation





AFC stack build.

at very high levels of availability over this period. This compared with a few tens of hours at Stade upon initial commissioning in January 2016, ahead of eventually meeting our milestones.

In addition to this achievement of longevity and availability was AFC Energy's demonstration that its technology could accept, without loss, hydrogen sourced at much lower qualities than had been tested previously. The lower grade hydrogen being used in these Gen2 trials was akin to that found at industrial gas plants and capable of being stripped direct from, for example, a chlor-alkali plant – one of AFC Energy's key target markets for fuel cell deployment. This outcome alone had an enormous impact not only on the size of market AFC Energy would now address, but also on the economics of each project which might otherwise have required extensive investment in hydrogen clean-up before being capable of acceptance by AFC Energy's fuel cell.

The Gen2 design, not only of the fuel cell stack and electrodes, but also the balance of plant, significantly built on the system employed at AFC Energy's industrial test facility at Stade, incorporating design changes to extend the operating life of the fuel cell stack, while increasing stack availability, and reducing stack cost.

In parallel to this work, we identified the significant value that could be extracted from partnering with one of the world's leading experts in the field of electro-chemistry, Industrie De Nora S.p.A. ("De Nora") – particularly in learning from their own

experiences in the successful provision of long life alkaline systems to the electrolysis and chlor-alkali markets over many decades. To this end, following months of technical due diligence and discussions, the parties entered a Joint Development Agreement ("JDA") in August 2016 which ran in parallel to the Gen2 development programme.

We have been extremely pleased with many of the outcomes from the JDA which are now giving renewed confidence to the delivery of a fuel cell cartridge capable of running for at least twelve months, and indeed, exceeding twelve months in due course. The collaboration between our two companies is progressing very well and we are delighted with the positive working relationship that has formed between our organisations over a relatively short time. We expect further announcements throughout 2017 regarding the success of this relationship and the tangible benefits we are starting to see from this strategic collaboration.

Additionally, through collaboration with De Nora, there is an opportunity for AFC Energy to better address the chlor-alkali sector, a significant producer of vented hydrogen, for which De Nora is a strong part of the supply chain. I believe this collaboration will deliver a technology platform that enhances the commercialisation timeline and our future success in the alkaline fuel cell space.

When put together, the advances achieved by AFC Energy as part of the Gen2 programme, with the outcomes of the JDA collaboration with De Nora,

“AFC Energy’s objective is to be a world-class energy company that leverages the deployment of low cost, high performance alkaline fuel cell technology to target global industrial scale opportunities.”

give me increasing confidence that we are nearing a point when the AFC Energy technology platform will be in a position to positively confirm its ability to meet the five metrics of commercialisation and therefore, position the Company for project collaboration and commercial deployment during the course of the next twelve months.

Market Opportunities

At the recent World Economic Forum in Davos, the 13-member Hydrogen Council announced its establishment, calling on Governments to support the development of infrastructure for a hydrogen "ecosystem". Given representation from leading global multinationals including Royal Dutch Shell, Alstom, Air Liquide, Daimler and Toyota, this illustrates the significant resources being devoted to the foundations of a global hydrogen economy. AFC Energy will centre itself

OPERATIONAL REVIEW CONTINUED

Key Commercialisation Metrics



firmly within that international “ecosystem”, initially across several targeted regions/countries, to support the commercialisation of our alkaline fuel cell systems, for industrial scale, distributed and related applications.

Addressable market opportunities identified by the Company include large-scale stationary industrial power plants, integration with industrial and chemical plants with surplus hydrogen, and off-grid decentralised power generation. To this end, our business model remains intact and robust in pushing forward with new project collaboration opportunities.

The past twelve months have seen an aggressive push by the Company into key target markets and industries within those markets. As a result of this investment, we have positioned AFC Energy well to now begin to capitalise on these opportunities, particularly as the robustness of the technology platform improves and we are able to extract real and empirical data from the operating cartridges that supports the metrics of commercialisation to our partners. It is fair to say that whilst expectations were set through the 2016 Milestones that commercial agreements would be reached within that year, the status of the technology at that time provided a challenging platform in which to conclude these transactions. However, each of the partners we have been in dialogue over this time remains open and we are hopeful that 2017 will give rise to an improved platform from which to progress several project deployment opportunities.

Whilst our target markets for the most part have remained unchanged, with focus on the Middle East, and North East Asia (Korea and Japan), we have also seen renewed interest from Europe, principally in the UK and Germany.

It remains the building block of AFC Energy’s commercialisation model to stay focussed on delivering a viable fuel cell system through adoption of our existing core fuel cell technology platform. Whilst a well-known pitfall of clean tech companies has been to diversify offerings too early and divert focus on what might otherwise be core factors in the development roadmap, we have

identified a number of deployment opportunities that, when integrated with other technologies, provide real and market-based solutions to existing market-based problems.

Key within this are two new models for AFC Energy’s fuel cell deployment which we believe could generate new growth markets for our technology platform. Firstly, in recognition of the growing need for energy storage solutions and the role of batteries within that mix, I have commissioned AFC Energy to develop a “Hydrogen Battery” which, when integrated with curtailed renewable energy sources, electrolysis and hydrogen buffers, provides an efficient, affordable and robust alternative to “conventional” battery technologies. This integration does not change the form or make-up of AFC Energy’s fuel cell technology, but provides a key conversion technology solution that provides a bridge between intermittent renewable power and flexible power demand profiling as is exhibited in any modern-day power market.

AFC Energy is also looking to properly integrate its fuel cell technology platform with tertiary water treatment and again, electrolysis, as a basis for remote water treatment solutions to reduce the cost of offsite wastewater transportation and subsequent treatment for many extractive industries, primarily in oil and gas. This is an early phase development but again, utilising AFC Energy’s existing fuel cell technology platform and architecture to integrate with other technologies to provide a market-based solution to an ever-increasing problem of contaminated water treatment and disposal.

POST YEAR-END DEVELOPMENTS

In November 2016, we entered into an important agreement with UK-based Peel Environmental (“Peel”), to assess a substantive fuel cell development opportunity at Peel’s Protos Industrial Park located in Chester, UK. This site provides several potential industrial hydrogen sources, some of which are currently venting hydrogen, which in turn, opens the door to scalable fuel cell opportunities.

As owner of the Protos site, Peel, together with its regional contacts and permitting and consenting capability, is an ideal partner for AFC Energy to collaborate in the UK’s “Northern Powerhouse”. This project has the potential, following commencement at the 1MW scale, to scale up to an estimated 35MW to 50MW of installed capacity. AFC Energy has already, in conjunction with Peel, commenced dialogue with stakeholders of such potential projects and for the necessary study phase work. With these steps underway, we will provide an update later in 2017.

More recently, in March 2017, we announced the successful completion of an £8.1 million fundraise by way of a placement, subscription and shareholder offer, which heralded the arrival of new financial institutions on the share register. In addition, we considered it important to provide our existing shareholders with an opportunity to participate, and this was rewarded with a full take up under the open offer. The fundraise will assist the Company to fulfil its strategy to deliver commercial contracts by 2018.

FUNDED PROJECTS: POWER-UP AND ALKAMMONIA

AFC Energy continues to pursue the requirements of the POWER-UP and ALKAMMONIA EU-funded programmes. Much of the work required to deliver POWER-UP was undertaken during the course of 2015 with further work throughout 2016 contributing to the overall objectives of the POWER-UP programme and its key stakeholders. AFC Energy continues to hold dialogue with the Fuel Cell and Hydrogen Joint Undertaking (“FCH JU”) with regards the programme and very much appreciates the support the FCH JU have provided the Company in delivering this significant project. The project is due to come to an end on 30 June 2017 and we expect to have delivered the vast majority of outcomes originally agreed with the EU when originally awarded this grant back in 2013.

In addition to POWER-UP, and despite a delay as a consequence of one of our key projects partners entering into administration back in 2014, the ALKAMMONIA project continues with the bulk of work required for AFC Energy's delivery of a small scale system completed (as announced during the course of 2016). We are now awaiting delivery of the pilot scale ammonia cracker from a project partner in the first half of 2017. We look forward to updating the market on this project over the coming months.

FINANCIAL OVERVIEW

In 2016, AFC Energy's EU grant and other income was £1.0 million (2015: £2.3 million). The Company continued to be engaged during the year, and at year-end, in three EU-funded projects, ALKAMMONIA, LASER-CELL and POWER-UP. Overall activity on these EU-funded projects was lower than in the previous year, in particular due to the high level of activity associated with the POWER-UP project in the previous year, resulting in lower expenditure through cost of sales.

Overall expenditure on research and development qualifying for R&D tax credits was £2.9 million (2015: £3.5 million), demonstrating the continued high-level of commitment to develop the Company's fuel cell system.

An operating loss to 31 October 2016 of £6.3 million (2015: £8.6 million) has been recorded. Cash balances at 31 October 2016, excluding restricted cash, were £2.9 million (2015: £1.8 million). As mentioned in "Post year-end developments" above, subsequent to the year-end in March 2017, the Company successfully raised £8.1 million before expenses through a placement, subscription and shareholder open offer.

OUTLOOK

In December 2014, AFC Energy's commercialisation strategy was updated to deliver technical and commercial progression over a three-year window. In 2015, the primary focus was on building and successfully commissioning the world's largest alkaline fuel cell power plant. In 2016, our focus progressed to the delivery of a second generation fuel cell system and initiation of a commercial pipeline. In 2017, that journey continues, with the opportunity for the commercial deployment of our fuel cell systems.

AFC Energy's objective is to be a world class energy company that leverages the deployment of low cost, high performance alkaline fuel cell technology to target global industrial scale, distributed generation and other related opportunities. Stationary fuel cell applications represent the largest sub-sector in a hydrogen economy that is rapidly building global momentum.

In 2017, as we further evaluate our project opportunities, our primary focus remains the deployment of our fuel cell systems in commercial opportunities. As we develop this commercial pipeline, our stakeholders will witness renewed emphasis on system and cartridge cost reductions to ensure our technology can operate in an increasingly competitive and efficient manner. To achieve this, we continue to review our supply chain and the scope for recycling our fuel cells, as well as opportunities to improve the design of key components and system engineering.

2017 will also see further focus on delivering the Company's commitments with its key partners, including those under the JDA with De Nora where significant advancements in the fuel cell system continue to be made. Our achievements to date optimally position AFC Energy for the delivery of commercial transactions and in turn support collaboration with our partners, for the international deployment of our fuel cell systems.

I would like to thank all the staff, partners and contractors working with AFC Energy, together with the EU's FCH JU, and the Board, for their continued support.

This Report, including the "Managing Our Risks" section on page 18, was approved by the Board on 23 March 2017.



ADAM BOND
CHIEF EXECUTIVE OFFICER

23 March 2017

STRONG PARTNERSHIPS

Strengthening a Complementary Relationship with De Nora

In August, AFC Energy signed a Joint Development Agreement with Italy's Industrie De Nora S.p.A., a global leader in the field of electrochemistry and electrodes.

De Nora is the pre-eminent provider of electrodes for electro-chemical processes and technologies internationally, including the chlor-alkali industry. Their Joint Venture with ThyssenKrupp (TK-UhdeChlorineEngineers) is the world's largest integrated EPC provider of chlor-alkali technology solutions. The chlor-alkali industry is one of the largest emitters of by-product hydrogen globally and therefore a key target for AFC Energy.

The JDA with De Nora aims to facilitate further material improvement in the performance characteristics of our fuel cell technology and accelerate the timescale for achieving our targeted key metrics for: power, longevity, availability, cost and efficiency.

The decision to collaborate followed extensive technical discussions. The JDA provides significant independent validation of AFC Energy and its technology by a world-leading industry player.

The parties intend to widen the collaboration to develop new product offerings. This combines the AFC Energy fuel cell system with De Nora's proprietary technologies in order to provide reliable and performing integrated solutions to open new markets for mutual benefit.

Technical and Commercial Benefits of Partnership

- Accelerate AFC Energy's technology platform for commercial deployment, unlocking market potential
- Fully compatible technology platform operating in alkaline environment
- Access to De Nora's world-leading experts in electro-chemical solutions, electrode structure and catalysts, from product development to mass manufacturing
- Integration with De Nora technology may create new combined solutions which include the AFC Energy fuel cell
- Access to De Nora's international network of chlor-alkali customers.

"We are excited to start the JDA with AFC Energy. Our technical teams have been very impressed by the advances which have been made to date by AFC Energy and are confident that further significant steps can be made by both parties working closely together. We look forward to progressing this mutually beneficial partnership with AFC Energy into a long-term strategic and commercial relationship."

LUCA BUONERBA

**DE NORA'S CHIEF
MARKETING AND BUSINESS
DEVELOPMENT OFFICER**



Liquid nitrogen tanks and evaporators.



Strategic Partnership With Peel Environmental

AFC Energy agrees with Peel Environmental Limited ("Peel") to assess the techno-economic feasibility of the UK's largest hydrogen fuel cell precinct at Peel's Protos industrial park.

Peel Environmental lies at the heart of The Peel Group, one of the foremost enterprises of new infrastructure for the waste, mineral and environmental technology sectors in the UK. The Group's specialist development teams have a proven track record in delivering high quality sustainable projects.

Protos is located between Manchester, Liverpool and Chester and will deliver 250 hectares of industrial development in the North West of England. It represents a strategic cluster of businesses encompassing energy intensive industries with associated supply chains. Importantly, it reflects Peel's vision for an energy generation hub that provides secure, low carbon and low cost energy generation to its onsite facilities.

AFC Energy will conduct the assessment in collaboration with Peel and other third party partners to review a range of hydrogen sources and offtake arrangements and work with local stakeholders that will see a proposed phasing of fuel cell projects at Protos commencing at 1MW, through to an estimated 35MW to 50MW of installed capacity at the site.

"We are delighted to partner with AFC Energy in investigating the feasibility of this commercial-scale hydrogen fuel cell techno-economic feasibility study... A successful hydrogen fuel cell project of this scale will be a first for the UK."

MYLES KITCHER
MANAGING DIRECTOR OF PEEL ENVIRONMENTAL AND PROTOS

A positive outcome from the techno-economic assessment for the development of a 35MW to 50MW fuel cell project at Peel's Protos site could see the development of the UK's largest stationary fuel cell project and one of the largest in the world, confirming a growing transition towards a hydrogen based economy, and thereby positioning Protos and AFC Energy at the forefront of this movement.

The feasibility study will be conducted over several months in 2017.

35-50MW

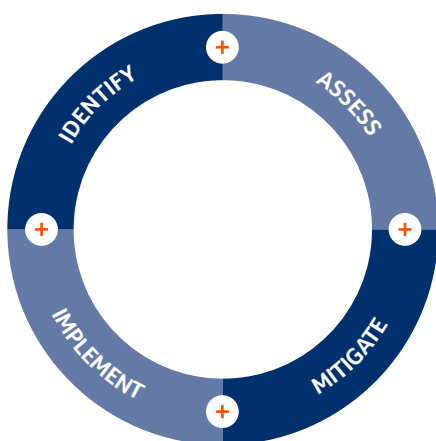
**Targeted installed capacity
at the site**



MANAGING OUR RISKS

Effective risk management underpins the delivery of our objectives. It is essential to protect our reputation and generate sustainable shareholder value. We aim to identify key risks at an early stage and develop actions to eliminate them or mitigate their impact and likelihood to an acceptable level.

RISK MANAGEMENT FRAMEWORK



OUR APPROACH TO RISK

There are a number of risks and uncertainties that could adversely impact the achievement of the Company's strategy. The Board of Directors has identified and discussed the risks that are considered to have the highest severity and likelihood, along with the mitigations the Company adopts to either avoid the risk occurring or manage the impact.

OUR RISK MANAGEMENT PROCESS

The Executive Directors are responsible for managing and mitigating the risks to the Company. The Audit Committee reviews the processes and controls for ensuring key risks are identified and managed appropriately. The Committee is responsible for monitoring the quality of internal controls and for ensuring that the financial performance of the Company is properly monitored, controlled, and reported. The AIM Rules Compliance Committee is responsible for, among other things, monitoring the quality of internal procedures, resources and controls to enable compliance by the Company with the AIM Rules and the AIM Rules for Nominated Advisers.

Risk management processes have been embedded at both Company and project levels, and form an integral day-to-day business activity. The processes support management and project teams to identify and understand the risks they face in delivering Company objectives and to develop mitigations to manage those risks.

Our Principal Risks

Risk

1 HEALTH AND SAFETY

The risk of health and safety incidents or breaches.

2 TECHNOLOGY

The risk is that we will not be able to successfully develop and apply the Company's alkaline fuel cell technology to potential products at the right cost or performance.

The risk that technology is successfully developed but slower than anticipated.

The risk that technical failure at product trials could affect ability to provide a product to customers.

3 COMPETITION AND MARKET OPPORTUNITY

The risk that the advantages of our technology are eroded by competitors and this impacts the Company's future profitability and growth opportunities.

4 INTELLECTUAL PROPERTY

The Company's competitive advantage is at risk from a loss or breach of its intellectual property rights.

5 OPERATIONAL

There is a risk that the Company has insufficient operational capability and capacity to deliver project contracts in compliance with contractual commitments.

6 DESIGN AND QUALITY

The risk of design and quality issues with our alkaline fuel cell technology.

7 ACCESS TO FINANCE

The risk the Company has insufficient capital to fund technology and early project development – this may require additional equity funding to achieve commercialisation.

8 REGULATORY AND COMPLIANCE

The risk that the Company or its staff breach applicable regulations.

9 KEY PERSONNEL

The risk that key technical personnel who possess critical design know-how, depart the Company.

Mitigation

Change During the Year

<p>Robust health and safety management, and continuous improvement and reinforcement of a safety-first culture in all work place environments, is paramount for the Company and enforced at all levels.</p>	<p>Adherence to codes and standards surrounding health and safety provides a transparent framework to minimise the risk of incidents, and ensures the integrity of AFC Energy's health and safety remains intact for the sake of our employees, partners, contractors and shareholders.</p>	
<p>The Company has implemented a robust control of technological progress against a budgeted plan, adopting principles of "technology readiness levels".</p>	<p>External partners have also been identified and where relevant, engaged to support the development plan with transparent KPIs and road maps to develop a product that meets commercial product metrics, relating to power, longevity, availability, cost and efficiency.</p>	
<p>The Company is targeting different regional markets and we are broadening the application of our product in order to minimise the risk of failure in a single market or product.</p>	<p>We continuously monitor market developments, and competitor activity.</p>	
<p>The Company benefits from external advice provided by qualified patent attorneys. The integrity of the Company's IP management and the manner in which all contractual negotiations with third parties takes place</p>	<p>to ensure IP protection and compliance are of critical importance to maintaining shareholder value. IP registers are reviewed regularly both in terms of existing patents, and also in terms of future and unregistered protection.</p>	
<p>The strategy for transition from technology development to commercial deployment focuses on long-term partnerships and collaboration with industry leading companies. Our partners and specialist external advisers are identified and developed to complement AFC Energy's</p>	<p>project execution capability, both in terms of understanding local regulatory environments, through to construction, funding, operational and logistical support. This strategy will continue to be employed over the short to medium term by the Company.</p>	
<p>As the Company progresses towards product commercialisation, design defects and poor quality management, within the manufacturing processes, could have a direct impact on the Company's market</p>	<p>reputation, with consequential loss of value. The Company adopts a high standard of manufacturing process and quality control to mitigate to a large extent the risk of product quality issues and failure.</p>	
<p>The Company adopts a budgeted technology development plan, aligned to pre-defined milestones, supported by prudent budgetary controls that can be measured and monitored to provide a robust means of mitigating risk of insufficient working capital.</p>	<p>The Company is targeting meeting its financing needs from a mix of grant funding, tax credits and equity funding, which may be sought from institutional, retail or strategic sources. Once it reaches project deployment, additional sources of debt funding, such as project finance will also be considered.</p>	
<p>The Company is publicly listed on the AIM market, which results in significant disclosure and reporting obligations to the regulator, investors and other stakeholders. The Board and management, in consultation with its Nomad</p>	<p>and legal advisers seek to ensure that applicable legislation is complied with. Further, the AIM Rules Compliance Committee actively supervises this area to ensure compliance.</p>	
<p>Key technical staff possess significant know-how regarding the ongoing development of the Company's technology. Loss of these staff members may adversely affect the ability of the Company to progress its research and development in a manner which is likely to achieve commercialisation.</p>	<p>The Company actively monitors remuneration policy to ensure that staff are incentivised to remain with the Company. The Company requires current and former employees and directors to comply with stringent confidentiality obligations.</p>	

CORPORATE SOCIAL RESPONSIBILITY

The following section provides an overview of our material corporate responsibility activities, explains why they are important to us, and how we manage them.

Governance and Business Ethics

We do not tolerate bribery and corruption, and are committed to acting with integrity in all our business dealings and relationships.

We strive to always comply with the UK Bribery Act 2010, and have adopted our own anti-bribery policy. We aim to always act ethically, and ensure our business partners adopt the same stringent standards.

Health, Safety and Security

We are committed to achieving and maintaining the highest health and safety standards.

We work positively and proactively to create an open culture, and to engage all employees to help maintain our excellent safety record.

To support this, we invest in specialist roles and systems. We commission regular reviews of our health and safety arrangements, calling on independent external practice experts to keep us informed of industry developments and insights – so we can continue to improve.

During the year ending 31 October 2016 there were no Lost-Time Accidents across the Company's sites.

During 2017 we will be working with Bureau Veritas, the global leader in testing, inspection and certification, to develop our processes and systems with the aim of achieving OHSAS 18001 (Occupational Health and Safety) accreditation.

Environment

AFC Energy's products are designed to minimise any adverse impact on the environment, while reducing the carbon footprint of our customers' electricity generation, and in particular, enhance the utilisation of sources of renewable energy that would otherwise be wasted.

Our Stade plant in Germany fully complies with the stringent environmental requirements of our partners.

Air travel and building operations have been identified as two of the major factors in the Company's carbon emissions, and consequently, the Company encourages recycling across the business and also acts responsibly to minimise its carbon footprint created by travel.

During the year ending 31 October 2016 we have complied with all environmental legislation and there were no reportable environmental incidents by the Company.

During 2017 we will also work with Bureau Veritas to develop our processes and systems, with the aim of achieving ISO 14001 (Environmental Management) accreditation.

Employees

At the heart of our business is a dedicated, innovative team committed to our vision of an affordable fuel cell for the industrial market.

We aim to recruit the best talent and be an equal opportunities employer, keeping our staff free from workplace discrimination and harassment. We also invest in their training and development, to equip our business with the skills and expertise to succeed.





AFC Energy's plant in Stade, Germany.

INTRODUCTION TO GOVERNANCE

The Board is highly committed to meeting the standards of corporate governance.

THE ROLE OF THE BOARD

The Board is collectively responsible for the long-term success of the Company and is ultimately responsible for its strategy, management, direction and performance. The Board sets the Company's strategic aims, ensures that the necessary financial and human resources are in place for the Company to meet its objectives, reviews progress towards the achievement of objectives and reviews the performance of management.

The Board establishes the values, culture, ethics and standards of the Company and sets the framework for prudent and effective controls which enable risk to be assessed and managed.

The Company does not comply with the UK Corporate Governance Code ("Code"). However, the Board has reported on the Company's Corporate Governance arrangements by drawing upon best practice available, including those aspects of the Code it considers to be relevant to the Company and best practice.

The Board has delegated authority to its Committees to carry out the tasks defined in the Committees' terms of reference. The Committees are – the Audit Committee; the Remuneration Committee; and the AIM Rules Compliance Committee. The Board has delegated the day-to-day management of the Company to the Chief Executive Officer.

AUDIT COMMITTEE

The Company's Audit Committee members during the financial year comprised of Mitchell Field (Chairman) and Eugene Tenenbaum. The Committee meets formally twice a year, on dates linked to the Company's financial calendar, and at any other time when it has been appropriate to discuss audit, accounting or control issues.

The Committee's principal responsibilities are:

- To monitor the integrity of the financial statements of the Company;
- To review the annual and interim financial statements to ensure that they present a balanced assessment of the Company's position;
- To review accounting policies and their application within the Company's financial statements;
- To review with the executive management and the Company's external Auditor the effectiveness of internal controls;
- To review with the Company's external Auditor the scope and results of their audit; and
- To oversee the relationship with the external Auditor.

The external Auditor attends meetings of the Committee except when their appointment or performance is being reviewed. Executive Directors attend as and when appropriate.

REMUNERATION COMMITTEE

The Company's Remuneration Committee members during the financial year comprised of Tim Yeo (Chairman) and Mitchell Field. The Committee reviews the performance of the Executive Directors and sets the scale and structure of their remuneration and the basis of their service agreements. In determining remuneration, the Committee seeks to enable the Company to attract and retain Executives of the highest calibre. In doing so, the Committee takes advice as appropriate from external advisers on executive remuneration. The Committee also makes recommendations to the Board concerning employee incentive schemes.

No Directors participate in discussions or decisions concerning their own remuneration.

This Committee is also responsible for nominating candidates, for the approval of the Board, to fill either Executive or Non-Executive vacancies or additional appointments to the Board. The Committee retained independent search consultants in respect of the appointment of the Chief Financial Officer.

Details of the Directors' remuneration, service agreements and their interests in the share capital of the Company are disclosed in the Directors' Report.

AIM RULES COMPLIANCE COMMITTEE

The Company's AIM Rules Compliance Committee members comprise of Tim Yeo (Chairman) and Mitchell Field. The Committee meets as appropriate.

The Committee is responsible for, among other things, monitoring the quality of internal procedures, resources and controls to enable compliance by the Company with the AIM Rules and the AIM Rules for Nominated Advisers.

BOARD AND COMMITTEE MEETINGS

The table below shows the number of Board and Committee meetings of the Company held during the year, and the attendance of the individual Directors.

It should be emphasised that this information does not fully reflect the contribution made to the Company's business by many of the Directors, who have also attended other meetings and events relating to the Company's business and activities during the year.

BOARD	
Number of meetings held	7
Attendance by:	
Tim Yeo	7
Adam Bond	7
Mitchell Field	6
Eugene Shvidler	5
Eugene Tenenbaum	6

EMPLOYEES

The Company's organisational structure has clearly documented and communicated levels of responsibility, delegated authority and reporting procedures. The professionalism and competence of employees is maintained through recruitment, performance appraisal, written job descriptions, personal training and development plans. The Board supports the highest levels of commitment and integrity from employees. Expected standards of behaviour are set out in the Staff Handbook, a copy of which is given to all employees.

The Company is an equal opportunities employer and it is our policy to ensure that all job applicants and employees are treated fairly and on merit, regardless of their race, gender, marital status, age, disability, religious belief or sexual orientation. In common with many organisations we operate a performance appraisal system, the aim of which is to support employees to contribute fully to the organisation and to assist them to fulfil their potential. The Company encourages the involvement of its employees in its performance through both its Save As You Earn Scheme and its Share Option plan.

RELATIONS WITH SHAREHOLDERS

The Board considers effective communication with shareholders to be very important, and encourages regular dialogue with investors. Shareholders will be given at least 21 days' notice of the Annual General Meeting, at which they will have the opportunity to discuss the Company's development and performance.

The Company's web site www.afcenergy.com contains full details of the Company's activities, press releases, Regulatory News Service announcements, share price details and other information.

MAINTENANCE OF A SOUND SYSTEM OF INTERNAL CONTROL

The Directors have overall responsibility for ensuring that the Company maintains a system of internal control to provide them with reasonable assurance that the assets of the Company are safeguarded and that shareholders' investments are protected. The system includes internal controls appropriate for a company of the size of AFC Energy, and covers financial, operational, compliance (including health and safety) controls and risk management.

Such systems are designed to manage, rather than eliminate, the risk of failure to achieve business objectives; any system can provide only reasonable, and not absolute, assurance against material misstatement or loss. The process in place for reviewing AFC Energy's system of internal control includes procedures designed to identify and evaluate failings and weaknesses, and to ensure that necessary action is taken to remedy the failings. The Board has considered its policies with regard to internal controls as set out in the Code and undertakes assessments of the major areas of the business and methods used to monitor and control them. In addition to financial risk, the review covers operational, commercial, regulatory and health and safety risks. The risk review is an ongoing process with reviews being undertaken on a regular basis. The key procedures designed to provide an effective system of internal controls that are operating up to the date of sign-off of this report are set out below.

CONTROL ENVIRONMENT

There is an organisational structure with clearly defined lines of responsibility and delegation of accountability and authority.

RISK MANAGEMENT

The Company employs Directors and senior personnel with the appropriate knowledge and experience for a business engaged in activities in its field of operations, and undertakes regular risk assessments and reviews of its activities. Details of risks to the business which the Board considers to be potentially material are set out in the Strategic Report on pages 18 and 19.

FINANCIAL INFORMATION

The Company prepares detailed budget and working capital projections which are approved annually by the Board and are maintained and updated regularly throughout the year. Detailed management accounts and working capital cash flows are prepared and compared to budgets and projections to identify any significant variances.

MANAGEMENT OF LIQUID RESOURCES

The Board is risk averse when investing the Company's surplus cash. The Company's treasury management policy is reviewed periodically, and sets out strict procedures and limits on how surplus funds are invested.

REVIEW OF CORPORATE GOVERNANCE

The Board strives to comply with the key principles of the Code given the size of the Company and the nature of its operations. These have not been formally reviewed by the Company's auditors. The auditors' responsibility extends only to reading this report as a part of the Annual Report and Accounts and considering whether it is consistent with the audited financial statements.

OUR EXPERIENCED LEADERSHIP

The Board is responsible for the overall conduct of the Company and meets regularly to discuss reviews and reports on the business and plans of the Company.

COMMITTEE MEMBERSHIP KEY

- Chair of Committee
- Member of Committee
- 1 Audit Committee
- 2 Remuneration Committee
- 3 AIM Rules Compliance Committee



② ③

TIM YEO NON-EXECUTIVE CHAIRMAN

YEAR APPOINTED
2007

SKILLS AND EXPERIENCE

Tim Yeo was formerly Member of Parliament for South Suffolk and Chairman of the House of Commons Energy and Climate Change Select Committee.

OTHER COMMITMENTS

He is a non-executive director of Groupe Eurotunnel SE, Chair of the University of Sheffield Energy 2050 Industrial Advisory Board, Chair of New Nuclear Watch Europe and Honorary Ambassador of Foreign Investment Promotion for South Korea.



ADAM BOND CHIEF EXECUTIVE OFFICER

YEAR APPOINTED*
2014

SKILLS AND EXPERIENCE

Adam has over 18 years' experience operating within the international energy sector both in executive management positions for listed energy companies, and in advisory capacities to both Governments and the private sector. Adam is well networked internationally across the conventional and unconventional energy sectors and has a strong understanding of energy markets and deal making within that sector. Adam's mandate is focused on driving AFC Energy's transition to an industry leading alkaline fuel cell company, whose focus is on project execution in defined key global markets. Adam was a Non-Executive Director of AFC Energy since 2012, and was formerly Director of both Waste2Tricity Ltd and JS Yerstogaz (Uzbekistan). He is qualified with Bachelors' degrees in commerce and law and a Master in Laws (Taxation).

* Previously Non-Executive Director from 2012.



JIM GIBSON
CHIEF OPERATING OFFICER

YEAR APPOINTED
2017

SKILLS AND EXPERIENCE

Jim has almost 30 years' experience in operations management and business development roles within the engineering contracting sector. Jim spent 23 years at Foster Wheeler working in operational, business and commercial roles. This was followed by two years at ThyssenKrupp working in process technology/business development.



① ② ③

MITCHELL FIELD
NON-EXECUTIVE DIRECTOR

YEAR APPOINTED
2008

SKILLS AND EXPERIENCE

Mitchell, who lives in Wales, is part owner of Richards and Appleby Holdings Ltd, a mid-sized manufacturing group engaged in the production, sales and distribution of branded personal care products. Among these are Leighton Denny, James Read and Joan Collins as well as several well-known heritage brands, including "Cyclax" which formerly held the Royal Warrant from Her Majesty the Queen.

OTHER COMMITMENTS

His principal role is sales and marketing, dealing with numerous blue-chip companies in the UK and over 60 companies internationally. Mitchell has other investments and manages interests in retailing, property, import/export and general trading.



①

EUGENE TENENBAUM
NON-EXECUTIVE DIRECTOR

YEAR APPOINTED
2013

SKILLS AND EXPERIENCE

Eugene served as head of corporate finance for OAO Sibneft in Moscow from 1998 through 2001. In 1994, he joined Salomon Brothers where he worked until 1998. Prior to that, he spent five years in corporate finance with KPMG in Toronto, Moscow and London. He was an auditor at PriceWaterhouse in Toronto from 1987 until 1989. Eugene is a chartered accountant and holds a Bachelors' degree in commerce and finance from the University of Toronto.

OTHER COMMITMENTS

He has numerous other directorships; notably, he is a member of the boards of Chelsea FC plc and Evraz plc (a FTSE 250-listed company).



EUGENE SHVIDLER
NON-EXECUTIVE DIRECTOR

YEAR APPOINTED
2013

SKILLS AND EXPERIENCE

Eugene worked at Russian oil major OAO Sibneft from 1996 through 2005, initially as senior vice president and, from 1998, as president of the company. Eugene is a graduate of the I. M. Gubkin Moscow Institute of Oil and Gas with a Masters in Applied Mathematics and he received an MBA and Masters in International Taxation from Fordham University in New York.

OTHER COMMITMENTS

He is currently executive Chairman of Highland Gold Mining Ltd, an AIM-quoted company, and is a member of the Board of Evraz plc, a FTSE 250-listed company.

DIRECTORS' INTERESTS AND THEIR REMUNERATION

INTRODUCTION

The Remuneration Committee is committed to maintaining high standards of corporate governance and has taken steps to comply with the principles of best practice in so far as it can be applied practically given the size of the Company and the nature of its operations. Since it is not a requirement for companies which have securities listed on the AIM market of the London Stock Exchange to comply with the disclosure requirements of the Directors' Remuneration Report Regulations 2013 or to comply with the UKLA Listing Rules and the disclosure provisions under schedule 8 to SI 2008/410 of the large and medium-sized companies and groups (accounts and reports) regulations 2008, certain disclosures are not included below.

DIRECTORS AND THEIR INTERESTS

The Directors who served during the year and during the period up until the signing of these financial statements were:

Tim Yeo	Non-Executive Chairman
Adam Bond	Chief Executive Officer
Jim Gibson	Chief Operating Officer (appointed 6 February 2017)
Christopher Tawney	Finance Director (resigned 26 August 2016)
Mitchell Field	Non-Executive
Eugene Shvidler	Non-Executive
Eugene Tenenbaum	Non-Executive

A Director appointed during or after the year must stand for re-appointment at the first Annual General Meeting after such appointment. Consequently, Jim Gibson offers himself for re-election. Mitchell Field is required to retire by rotation in accordance with the Company's Articles of Association and, being eligible, offers himself for re-election.

On 31 October 2016 the beneficial interests of Directors and their families in the equity share capital of the Company were:

	Number of Ordinary shares of 0.1p 2016	Number of Ordinary shares of 0.1p 2015
Tim Yeo	877,272	877,272
Adam Bond	2,750,000	2,250,000
Jim Gibson	90,000	90,000
Mitchell Field	2,894,810	2,644,810
Eugene Shvidler	14,432,737	13,853,633
Eugene Tenenbaum	–	–

On 31 October 2016 the Directors' interests over share capital of the Company were:

	1 November 2015	Options/ Warrants granted in year	Options/ Warrants exercised/ lapsed in year	31 October 2016	Exercise price	Date from which exercisable ¹	Expiry date	Type
Tim Yeo	1,100,000	–	–	1,100,000	£0.031	18/04/2012	17/04/2019	Warrant
	1,000,000	–	–	1,000,000	£0.240	14/04/2013	13/04/2020	Warrant
Mitchell Field	350,000	–	–	350,000	£0.031	18/04/2012	17/04/2019	Warrant
	750,000	–	–	750,000	£0.240	14/04/2013	13/04/2020	Warrant
Adam Bond	6,000,000	–	–	6,000,000	£0.510	17/07/2015	17/07/2025	Unapproved Option

Note:

1 Warrants/Options exercisable from/after 14 April 2013 are subject to achievement of performance conditions.

Eugene Tenenbaum and Jim Gibson had no direct interest over share capital during the reporting period.

DIRECTORS' REMUNERATION

The remuneration policy has been designed to ensure that Executive Directors receive appropriate incentive and reward given their performance, responsibility and experience. When assessing this, the Remuneration Committee seeks to ensure that the policy aligns the interests of the Executive Directors with those of shareholders. The Company's remuneration policy for Executive Directors is to:

- Consider the individual's experience and the nature, complexity and responsibilities of their work in order to set a competitive salary that attracts and retains management of the highest quality
- Link individual remuneration packages to the Company's long-term performance through long-term share-based plans
- Provide post-retirement benefits through payment into defined contribution pension schemes
- Provide employment-related benefits including company car and medical insurance.

The remuneration of the Non-Executive Directors is determined by the Executive members of the Board in consultation with the Chairman, based on a review of current practices in other equivalent companies. The Non-Executive Directors do not receive any pension payments, nor do they participate in any of the bonus schemes. Remuneration is based on a fixed fee, plus a separate fee for any additional consulting services.

Name	Salary £	Share-based payment expense £	Other compensation ¹ £	Company pension contributions £	Total 2016 £	Total 2015 £
Tim Yeo (see note 25)	16,375	–	40,200	–	56,575	57,346
Adam Bond (see note 25)	300,000	821,002	213,850	–	1,334,852	806,463
Christopher Tawney (resigned 26 August 2016)	92,093	–	30,377	2,504	124,974	134,679
Mitchell Field (see note 25)	13,600	–	11,400	–	25,000	–
Eugene Tenenbaum	11,200	–	–	–	11,200	–
Eugene Shvidler	11,200	–	–	–	11,200	–

Note:

- 1 Other compensation includes issuance of shares in the Company, private medical insurance, other benefits, consultancy fees and compensation for loss of office (in respect of Christopher Tawney). £91,250 of Adam Bond's other compensation was paid in shares.

DIRECTORS' SERVICE CONTRACTS

Tim Yeo's services as a Chairman and Non-Executive Director are provided under a service agreement with the Company dated 1 January 2012 for an indefinite term, subject to a minimum of six months' notice. Additional consultancy services are provided under an agreement between the Company and Locana Corporation (London) Ltd dated 1 January 2012.

Adam Bond's services as Chief Executive Officer and Director during the period were initially provided under a secondment agreement between the Company and Linc Energy Ltd. The secondment agreement expired on 31 December 2015, at which point he became an employee of the Company under a service agreement dated 1 January 2016. During the year ended 31 October 2016, a portion of Adam's remuneration was paid to him by Linc Energy Ltd. and recharged to the Company. A further portion of his salary, totalling £91,250, was settled during the year through the issuance of 500,000 shares in the Company. Included in Adam's other compensation is a £100,000 bonus that has been accrued for as a result of meeting certain performance conditions. The payment of the bonus has not yet been claimed by Adam and is pending final Board approval. During 2015, the Company remitted taxation to HMRC on Adam's behalf in relation to different tax jurisdictions between the UK and Australia. Management believes an amount of £187,000 to be recoverable. As part of Adam's contract with the Company, in 2015 he was granted 6,000,000 share options with an exercise price of £0.51 per share. These options have performance conditions attached to them; 3,000,000 of the options will only vest if specific operational targets for energy output are met, and the remaining options will only vest if the share price achieves and sustains targeted amounts with equal portions vesting at share prices of £1.00, £1.50 and £2.00. In accordance with IFRS 2 (Share-Based Payment), the Company recognises as an employee expense the fair value of options granted to employees. The fair value is determined using an appropriate pricing model, and the resulting expense is recognised over the period in which the performance and/or service conditions are fulfilled ending on the date on which the employee becomes fully entitled to the award. During the year the Company recorded a non-cash expense of £821,002 relating to the options granted to Adam. The vesting conditions for the options has not been reached and hence Adam has not received any cash benefit from the options in the year. Further details are contained in notes 2, 3 and 18.

Mitchell Field's services as a Non-Executive Director are provided under the terms of a Non-Executive letter dated 17 October 2013 for an indefinite term, subject to a minimum of six months' notice. Additional consultancy services are provided under an agreement between the Company and Richards & Appleby Ltd dated 17 October 2013. During the year to 31 October 2015 Mitchell agreed not to be remunerated.

Eugene Shvidler's services as a Non-Executive Director are provided under the terms of a letter of appointment, dated 17 October 2013, for an indefinite term, subject to a minimum of six months' notice. Additional consultancy services are provided under an agreement between the Company and Eugene Shvidler dated 17 October 2013. During the year to 31 October 2016 Eugene did not charge the Company for any consultancy services. During the year to 31 October 2015 Eugene agreed not to be remunerated.

Eugene Tenenbaum's services as a Non-Executive Director are provided under the terms of a letter of appointment, dated 17 October 2013, for an indefinite term, subject to a minimum of six months' notice. Additional consultancy services are provided under an agreement between the Company and Eugene Tenenbaum dated 17 October 2013. During the year to 31 October 2016 Eugene did not charge the Company for any consultancy services. During the year to 31 October 2015 Eugene agreed not to be remunerated.

DIRECTORS' REPORT

The Directors present their report together with the audited financial statements for the year ended 31 October 2016. The comparative period was from 1 November 2014 to 31 October 2015. Information required under the Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013 has been included within the Directors' Report and accounts.

PRINCIPAL ACTIVITY AND REVIEW OF BUSINESS DEVELOPMENTS

The principal activity of AFC Energy plc (or "the Company") is the development of fuel cells.

Reviews of operations, business developments and current projects are included in the Chairman's Statement, the Strategic Report and Operational Review.

RESULTS AND DIVIDEND

The results for the year are set out in the statement of comprehensive income on page 32.

No dividends were paid in the year. The Directors do not intend to declare a dividend in respect of the year.

BOARD CHANGES

Details of changes to the membership of the Board are disclosed within the "Directors and their Interests" section on page 26.

CAPITAL STRUCTURE

Details of the Company's share capital are disclosed in note 17 to the financial statements.

Shareholder funds have been used for the development and testing of industrial scale fuel cell systems than can compete with conventional electricity generation technologies.

On 20 March 2017, the Company was aware of the following holdings of 3% or more in the Company's issued share capital:

	Number of shares	Approximate percentage of the Company's issued share capital
Evington Investments Limited	39,610,494	10.13%
Schroder Investment Management Limited	33,000,000	8.44%
Barclayshare Nominees Limited	24,035,239	6.15%
Lynchwood Nominees Limited	22,473,954	5.75%
TD Direct Investing Nominees (Europe) Limited	19,408,708	4.96%
Pershing Nominees Limited	14,687,409	3.76%
Mr. Eugene Shvidler	14,432,737	3.69%
Hargreaves Lansdown (Nominees) Limited (15942)	14,326,728	3.66%
Hargreaves Lansdown (Nominees) Limited (HLNOM)	13,112,349	3.35%
Hargreaves Lansdown (Nominees) Limited (VRA)	12,653,110	3.24%
HSDL Nominees Limited	12,025,901	3.08%

FINANCIAL INSTRUMENTS

Financial instruments are disclosed in note 21.

POLITICAL AND CHARITABLE DONATIONS

Charitable donations in the year amounted to £nil (2015: £nil).

INFORMATION DISCLOSED IN THE STRATEGIC REPORT

The following matters required to be disclosed in this Report under the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 are covered in the Strategic Report on pages 12 to 15 and 18 to 19 respectively: the key performance indicators and the principal risks.

PAYMENTS TO CREDITORS

The Company's policy is to settle the terms of payment with its suppliers when agreeing the terms of each transaction, either by accepting the suppliers' terms or by making the suppliers aware of alternative terms, and to abide by the agreed terms. Trade creditors of the Company at 31 October 2016 represented 28 days (2015: 125 days) of annual purchases.

LIABILITY INSURANCE FOR COMPANY OFFICERS

The Company maintains Directors' and Officers' liability insurance cover for its Directors and officers to the extent permitted under the Companies Act 2006.

RESEARCH AND DEVELOPMENT

The Company invests substantially in research and development and makes claims under the Government's R&D tax credit scheme. In the year to 31 October 2016, relevant expenditure was £2,914,050 (2015: £3,475,657).

GOING CONCERN

The Company had cash of £2,910,862 at 31 October 2016. In order to ensure that the Company has sufficient cash resources to meet its short-term requirements, a placing, subscription and open offer was completed in March 2017, raising approximately £8.1 million before expenses.

The Directors now believe there is adequate financial resource available to continue operations for the next twelve months. The Directors believe that future fundraising will be necessary to help the Company achieve its milestones and future growth potential and are confident in the ability of the Company to raise additional funds through the market, or at the project level as deemed appropriate at the time.

POST-BALANCE SHEET EVENTS

Details of post-balance sheet events are provided in note 23 to the financial statements.

AUDITOR

A resolution to reappoint the Auditor of the Company, Grant Thornton UK LLP, will be proposed at the forthcoming Annual General Meeting. Grant Thornton UK LLP have expressed their willingness to continue as Auditor of the Company.

This report was approved by the Board on 23 March 2017 and signed on its behalf by



ADAM BOND

Chief Executive Officer

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The Directors are responsible for preparing the Annual Report and financial statements in accordance with applicable law and International Financial Reporting Standards.

Company law requires the Directors to prepare financial statements for each financial period. Under that law the Directors have elected to prepare the financial statements in accordance with International Financial Reporting Standards as adopted for use in the European Union. The financial statements are required by law to 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 period. In preparing those financial statements, the Directors are required to:

- Select suitable accounting policies and then apply them consistently
- Make judgements and estimates that are reasonable and prudent
- State whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements
- Prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business

The Directors confirm that they have complied with the above in preparing the financial statements.

The Directors are responsible for keeping adequate accounting records which 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.

The Directors are responsible for the maintenance and integrity of the Company's website (www.afcenergy.com) and legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

STATEMENT OF DISCLOSURE TO AUDITOR

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 Auditor is unaware, and each Director has taken all the steps that he ought to have taken as a Director in order to make himself aware of any relevant audit information and to establish that the Company's Auditor is aware of that information. This confirmation is given and should be interpreted in accordance with section 418 of the Companies Act 2006.

INDEPENDENT AUDITOR'S REPORT

TO THE SHAREHOLDERS OF AFC ENERGY PLC

We have audited the financial statements of AFC Energy PLC for the year ended 31 October 2016 which comprise the statement of comprehensive income, the statement of financial position, the statement of changes in equity, the cash flow statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards ("IFRSs") as adopted by the European Union.

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

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITOR

As explained more fully in the Directors' Responsibilities Statement set out on page 30, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

SCOPE OF THE AUDIT OF THE FINANCIAL STATEMENTS

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate.

OPINION ON FINANCIAL STATEMENTS

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 October 2016 and of its loss for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

OPINION ON OTHER MATTER PRESCRIBED BY THE COMPANIES ACT 2006

In our opinion the information given in the Strategic Report and Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION

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

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



CHRISTOPHER SMITH

Senior Statutory Auditor
for and on behalf of Grant Thornton UK LLP
Statutory Auditor, Chartered Accountants
London
23 March 2017

STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 OCTOBER 2016

	Year ended 31 October 2016	Year ended 31 October 2015
	Note £	£
EU Grant income	967,606	2,262,506
Cost of sales	(1,883,650)	(4,846,933)
Gross loss	(916,044)	(2,584,427)
Other income	146,479	51,080
Administrative expenses	(5,561,096)	(6,112,856)
Operating loss	5 (6,330,661)	(8,646,203)
Finance (cost)/income	8 (148,233)	3,294,272
Loss before tax	(6,478,894)	(5,351,931)
Taxation	9 822,830	569,706
Loss for the financial year and total comprehensive loss attributable to owners of the Company	(5,656,064)	(4,782,225)
Basic loss per share	10 (1.86)p	(1.66)p
Diluted loss per share	10 (1.86)p	(1.66)p

All amounts relate to continuing operations.

The notes on pages 36 to 49 form part of these financial statements.

STATEMENT OF FINANCIAL POSITION

AS AT 31 OCTOBER 2016

	Note	31 October 2016 £	31 October 2015 £
Assets			
Non-current assets			
Intangible assets	11	344,457	338,176
Property and equipment	12	89,384	116,328
Investment	13	–	–
		433,841	454,504
Current assets			
Inventory and work in progress	14	150,932	219,421
Derivative financial instrument	21	–	1,308,859
Trade and other receivables	15	2,595,963	3,458,340
Cash and cash equivalents	16	2,910,862	1,756,445
Restricted cash	16	112,077	91,105
		5,769,834	6,834,170
Total assets		6,203,675	7,288,674
Capital and reserves attributable to owners of the Company			
Share capital	17	310,014	289,904
Share premium	17	37,843,613	33,947,857
Other reserve		3,234,492	2,207,441
Retained deficit		(36,486,151)	(30,830,087)
Total equity attributable to Shareholders		4,901,968	5,615,115
Current liabilities			
Trade and other payables	19	1,295,904	1,673,559
		1,295,904	1,673,559
Non-current liabilities			
Trade and other payables	19	5,803	–
		5,803	–
Total equity and liabilities		6,203,675	7,288,674

The notes on pages 36 to 49 form part of these financial statements.

These financial statements were approved and authorised for issue by the Board on 23 March 2017.



TIM YEO
Chairman

ADAM BOND
Chief Executive Officer

STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 OCTOBER 2016

	Note	Share Capital £	Share Premium £	Other Reserve £	Retained Deficit £	Total Equity £
Balance at 1 November 2014		285,684	33,332,478	3,032,472	(27,089,095)	9,561,539
Comprehensive loss for the year		–	–	–	(4,782,225)	(4,782,225)
Issue of equity shares		4,220	615,379	–	–	619,599
Equity-settled share-based payments		–	–	(825,031)	1,041,233	216,202
Transactions with owners		4,220	615,379	(825,031)	1,041,233	835,801
Balance at 31 October 2015		289,904	33,947,857	2,207,441	(30,830,087)	5,615,115
Comprehensive loss for the year		–	–	–	(5,656,064)	(5,656,064)
Issue of equity shares	17	20,110	3,895,756	–	–	3,915,866
Equity-settled share-based payments	18	–	–	1,027,051	–	1,027,051
Transactions with owners		20,110	3,895,756	1,027,051	–	4,942,917
Balance at 31 October 2016		310,014	37,843,613	3,234,492	(36,486,151)	4,901,968

Share capital is the amount subscribed for shares at nominal value.

Share premium represents the excess of the amount subscribed for share capital over the nominal value of these shares net of share issue expenses.

Other reserve represents the charge to equity in respect of equity-settled share-based payments.

Retained deficit represents the cumulative loss of the Company attributable to equity Shareholders.

The notes on pages 36 to 49 form part of these financial statements.

CASH FLOW STATEMENT

FOR THE YEAR ENDED 31 OCTOBER 2016

	Note	31 October 2016 £	31 October 2015 £
Cash flows from operating activities			
Loss before tax for the year		(6,478,894)	(5,351,931)
Adjustments for:			
Depreciation and amortisation	11,12	172,608	278,291
Impairment of intangible asset investment		–	52,500
(Profit)/Loss on disposal of tangible assets		(40,750)	286,743
Equity-settled share-based payment expenses	18d	1,027,051	216,202
Payment of shares in lieu of cash		326,632	331,000
Interest received	8	(3,415)	(5,775)
R&D tax credits receivable		(104,291)	(174,937)
Loss/(Gain) on derivative financial investment	21	149,687	(3,288,497)
Cash flows from operating activities before changes in working capital and provisions		(4,951,372)	(7,656,404)
R&D tax credits received		927,121	813,696
Increase in restricted cash		(20,972)	(91,105)
Decrease/(Increase) in Inventory and Work in Progress		68,489	(62,373)
Decrease/(Increase) in trade and other receivables		862,377	(24,500)
(Decrease)/Increase in trade and other payables		(371,852)	542,271
Cash absorbed by operating activities		(3,486,209)	(6,478,415)
Cash flows from investing activities			
Purchase of plant and equipment	12	(81,424)	(36,845)
Additions to intangible assets	11	(70,287)	(98,980)
Proceeds of disposal of tangible assets		40,750	4,800
Interest received	8	3,415	5,775
Net cash absorbed by investing activities		(107,546)	(125,250)
Cash flows from financing activities			
Proceeds from the issue of share capital		3,600,000	288,599
Costs of issue of share capital		(11,000)	–
Derivative financial asset	21	1,159,172	3,213,308
Net cash from financing activities		4,748,172	3,501,907
Net increase/(decrease) in cash and cash equivalents		1,154,417	(3,101,758)
Cash and cash equivalents at start of year		1,756,445	4,858,203
Cash and cash equivalents at end of year	16	2,910,862	1,756,445

The notes on pages 36 to 49 form part of these financial statements.

NOTES FORMING PART OF THE FINANCIAL STATEMENTS

1. CORPORATE INFORMATION

AFC Energy plc ("the Company") is a public limited company incorporated in England & Wales and quoted on the Alternative Investment Market of the London Stock Exchange.

The address of its registered office is Finsgate, 5-7 Cranwood Street, London, EC1V 9EE.

2. BASIS OF PREPARATION AND ACCOUNTING POLICIES

The financial statements of AFC Energy plc have been prepared in accordance with International Financial Reporting Standards ("IFRSs"), International Accounting Standards ("IASs") and International Financial Reporting Interpretations Committee ("IFRIC") interpretations (collectively "IFRSs") as adopted for use in the European Union and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS.

The Company prepares cash flow forecasts based on current estimates of future revenues and expenditure. These are agreed by the Board and monitored against actual expenditure to ensure the Company's resources are sufficient for the Directors to prepare the accounts on a going concern basis. In March 2017 the Company successfully raised approximately £8.1 million before expenses through a placing, subscription and open offer. The Directors remain confident that they will continue to be able to raise money to fund the Company's continuing activities as required.

The accounting policies set out below have, unless otherwise stated, been applied consistently in these financial statements.

Judgements made by the Directors in the application of these accounting policies that have significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year are discussed in note 3.

a. Standards, Amendments and Interpretations to Published Standards not yet Effective

At the date of authorisation of these financial statements, the IASB and IFRIC have issued the following standards and interpretations, which are effective for annual accounting periods beginning on or after the stated effective date. These standards and interpretations are not effective for and have not been applied in the preparation of these financial statements:

- IFRS 9 Financial Instruments is effective from 1 January 2015. This standard includes requirements for recognition and measurement, derecognition and hedge accounting.
- IFRS 15 Revenue from contracts with customers. The new standard will replace IAS 18 Revenue and IAS 11 Construction contracts. It will become effective for accounting periods on or after 1 January 2018 at the earliest.
- IFRS 16 Leases is effective from 1 January 2019. Management has not yet analysed the input to the financial statements upon adoption.

The Company expects no impact from the adoption of IFRS 9. As the Company is not currently revenue generating, there would be no impact relating to the adoption of IFRS 15 on the current financial position. The Company will determine the effects of the adoption of IFRS 16 in future periods.

b. Capital Policy

The Company manages its equity as capital. Equity comprises the items detailed within the principal accounting policy for equity and financial details can be found in the statement of financial position. The Company adheres to the capital maintenance requirements as set out in the Companies Act.

c. Revenue

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Company and the revenue can be reliably measured. Revenue is measured at the fair value of the consideration received, excluding discounts, rebates, and other sales taxes or duty. Revenue arising from the provision of services is recognised when and to the extent that the Company obtains the right to consideration in exchange for the performance of its contractual obligations.

d. Grants

The Company participates in three projects, LASER-CELL, ALKAMMONIA and POWER-UP, which receive funding from the EU. These grants are based on periodic claims for qualifying expenditure incurred by all the entities participating in each project consortium. The Company acts as coordinator for all three projects and submits claims and receives funding on behalf of the other participants in each project consortium. Grant funds of other participants are paid over to them as soon as they are received and only the grant funding relating specifically to the Company's activities is reflected in the statement of comprehensive income. The qualifying expenditure is shown in the statement of comprehensive income as cost of sales. Grants, including grants from the European Union, are recognised in the statement of comprehensive income in the same period as the expenditure to which the grant relates.

e. Other Income

Other income represents sales by the Company of waste materials.

f. Development Costs

Development expenditure does not meet the strict criteria for capitalisation under IAS 38 and has been recognised as an expense. Expenditure on and relating to the Company's alkaline fuel cell system installed at Stade in Germany under the EU funded POWER-UP project is considered to be development expenditure to date, as the module is the first of its kind that has been produced and has not yet operated at full power output for an extended period.

2. BASIS OF PREPARATION AND ACCOUNTING POLICIES CONTINUED

g. Foreign Currency

The financial statements of the Company are presented in the currency of the primary economic environment in which it operates (the functional currency) which is pounds sterling. In accordance with IAS 21, transactions entered into by the Company in a currency other than the functional currency are recorded at the rates ruling when the transactions occur. At each balance sheet date, monetary items denominated in foreign currencies are retranslated at the rates prevailing at the balance sheet date.

h. Inventory and Work in Progress

Inventory is recorded at the lower of cost and net realisable value. Work in progress is valued at cost, less the cost of work invoiced on incomplete contracts and less foreseeable losses. Cost comprises purchase cost plus production overheads.

i. Trade and Other Receivables

Trade and other receivables arise principally through the provision by the Company of activities associated with grant-funded projects. They also include other types of contractual monetary assets. These assets are initially recognised at fair value and are subsequently measured at amortised cost less any provision for impairment.

j. Loans and Other Receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, loans and receivables are carried at amortised cost using the effective interest method less any allowance for impairment. Gains and losses are recognised in profit or loss when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

The Company's loans and receivables include cash and cash equivalents. These include cash in hand, and deposits held at call with banks.

k. Property and Equipment

Property and equipment are stated at cost less any subsequent accumulated depreciation and impairment losses.

Where parts of an item of property and equipment have different useful lives, they are accounted for as separate items of property and equipment.

Depreciation is charged to the statement of comprehensive income within cost of sales and administrative expenses on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment. The estimated useful lives are as follows:

- Leasehold improvements 1 to 3 years
- Fixtures, fittings and equipment 1 to 3 years
- Vehicles 3 to 4 years

Expenses incurred in respect of the maintenance and repair of property and equipment are charged against income when incurred. Refurbishment and improvement expenditure, where the benefit is expected to be long lasting, is capitalised as part of the appropriate asset.

The useful economic lives of property, plant and equipment and the carrying value of tangible fixed assets are assessed annually and any impairment is charged to the statement of comprehensive income.

l. Intangible Assets

Expenditure on research activities is recognised in the statement of comprehensive income as an expense as incurred. Expenditure in establishing a patent is capitalised and written off over its useful life.

Other intangible assets that are acquired by the Company are stated at cost less accumulated amortisation and impairment losses.

Amortisation of intangible assets is charged using the straight-line method to administrative expenses over the following period:

- Patents 20 years

Useful lives are based on the management's estimates of the period that the assets will generate revenue, which are periodically reviewed for continued appropriateness and any impairment is charged to the statement of comprehensive income.

m. Cash and Cash Equivalents

Cash and cash equivalents comprise cash balances and call deposits with major banking institutions realisable within three months. Restricted cash is €125,000 held in escrow to support a bank guarantee in favour of Air Products GmbH relating to contractual obligations by the Company in relation to the Stade site in Germany.

NOTES FORMING PART OF THE FINANCIAL STATEMENTS

CONTINUED

2. BASIS OF PREPARATION AND ACCOUNTING POLICIES CONTINUED

n. Other Financial Liabilities

The Company classifies its financial liabilities as:

Trade and Other Payables

These are initially recognised at invoiced value. These arise principally from the receipt of goods and services. There is no material difference between the invoiced value and the value calculated on an amortised cost basis or fair value.

Deferred Income

This is the carrying value of income received from a customer in advance which has not been fully recognised in the statement of comprehensive income pending delivery to the customer. The carrying value is fair value.

o. Leases

Finance Leases

Finance leases, which transfer to the Company substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased property. Capitalised leased assets are depreciated over the estimated useful life of the asset. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are reflected in the statement of comprehensive income.

Operating Leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases are charged to the statement of comprehensive income on a straight-line basis over the period of the lease.

p. Financial Assets

All of the Company's financial assets are loans and receivables and investments. Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets at fair value and comprise trade and other receivables and cash and cash equivalents. Investments are accounted for at cost less impairment.

q. Financial Instruments

Financial assets and liabilities are recognised on the balance sheet when the Company becomes a party to the contractual provisions of the instrument.

- Cash and cash equivalents comprise cash held at bank and short-term deposits
- Receivables are recognised initially at fair value and subsequently held at amortised cost less an allowance for any uncollectable amounts when the full amount is no longer considered receivable
- Trade payables are not interest bearing and are stated at their nominal value
- Equity instruments issued by the Company are recorded at the proceeds received except where those proceeds appear to be less than the fair value of the equity instruments issued, in which case the equity instruments are recorded at fair value. The difference between the proceeds received and the fair value is reflected in the share-based payments reserve.

r. Valuation of Derivative Financial Instrument

In 2014, the Company placed shares with Lanstead Capital L.P. and at the same time entered into an equity swap agreement in respect of the subscriptions for which consideration will be received monthly over an 18-month period as disclosed in the notes to these financial statements. The amount receivable each month was dependent on the Company's share price performance and gains and losses arising on monthly settlements are reflected in the statement of comprehensive income in administrative expenses. The financial instrument closed in April 2016 and, hence, as at 31 October 2016, the financial instrument had a zero value.

s. Share-Based Payment Transactions

The Company awards share options and warrants to certain Directors and employees to acquire shares of the Company. The fair value of options and warrants granted is recognised as an employee expense with a corresponding increase in equity. The fair value is measured at grant date and spread over the period during which the Directors and employees become unconditionally entitled to the options or warrants. The fair value of the options and warrants granted is measured using the Black-Scholes option valuation model, taking into account the terms and conditions upon which the options and warrants were granted. The amount recognised as an expense is adjusted to reflect the actual number of share options and warrants that vest only where vesting is dependent upon the satisfaction of service and non-market vesting conditions or where the vesting periods themselves are amended by the introduction of new schemes and the absorption of earlier schemes by agreement between the Company and the relevant Directors and employees. Where options or warrants granted are cancelled, all future charges arising in respect of the grant are charged to the statement of comprehensive income on the date of cancellation.

t. Provisions

Provisions are recognised when the Company has a present obligation as a result of a past event and it is probable that the Company will be required to settle the obligation. Provisions are measured at the present value of management's best estimate of the expenditure required to settle the present obligation at the balance sheet date and are discounted to present value where the effect is material.

2. BASIS OF PREPARATION AND ACCOUNTING POLICIES CONTINUED

u. Taxation

Tax on the profit or loss for the year comprises current and deferred tax. Tax is recognised in the statement of comprehensive income except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

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

Deferred tax assets are not recognised due to the uncertainty of their recovery.

v. R&D Tax Credits

The Company's research and development activities allow it to claim R&D tax credits from HMRC in respect of qualifying expenditure; these credits are reflected in the statement of comprehensive income in administrative expenses or in the taxation line depending on the nature of the credit.

w. Pension Contributions

The Company operates a defined contribution pension scheme which is open to all employees and makes monthly employer contributions to the scheme in respect of employees who join the scheme. These employer contributions are currently capped at 3% of the employee's salary and are reflected in the statement of comprehensive income in the period for which they are made.

3. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION AND UNCERTAINTY

In the preparation of the financial statements management makes certain judgements and estimates that impact the financial statements. While these judgements are continually reviewed, the facts and circumstances underlying these judgements may change, resulting in a change to the estimates that could impact the results of the Company. In particular:

Useful Lives and Impairment of Intangible Assets

Intangible assets are amortised over their useful lives. Useful lives are based on the management's estimates of the period that the assets will generate revenue, which are periodically reviewed for continued appropriateness. After undertaking a comprehensive review of intangible assets, management has concluded that no impairment has arisen with respect to intangible assets during the year and subsequent to 31 October 2016 (2015: £nil).

Income Taxes and Withholding Taxes

The Company believes that its receivables for tax recoverable are adequate for all open audit years based on its assessment of many factors, including past experience and interpretations of tax law. This assessment relies on estimates and assumptions and may involve a series of complex judgements about future events. To the extent that the final tax outcome of these matters is different from the amounts recorded, such differences will impact income tax expense in the period in which such determination is made.

Capitalisation of Development Expenditure

The Company uses the criteria of IAS 38 to determine whether development expenditure should be capitalised. After assessing these, management has concluded that, until the Company's fuel cell system is proven to be commercially deployable, it would not be appropriate to capitalise development expenditure. Consequently, all development expenditure has been charged to the statement of comprehensive income during the year ended 31 October 2016.

Share-Based Payments

Certain employees (including Directors and senior Executives) of the Company receive remuneration in the form of share-based payment transactions, whereby employees render services as consideration for equity instruments ("equity-settled transactions").

The fair value is determined using an appropriate pricing model.

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award ("the vesting date"). The cumulative expense recognised for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Company's best estimate of the number of equity instruments that will ultimately vest. The profit or loss charge or credit for a period represents the movement in cumulative expense recognised as at the beginning and end of that period.

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance and/or service conditions are satisfied. Where the terms of an equity-settled award are modified, the minimum expense recognised is the expense as if the terms had not been modified. An additional expense is recognised for any modification which increases the total fair value of the share-based payment arrangement, or is otherwise beneficial to the employee as measured at the date of modification.

Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. However, if a new award is substituted for the cancelled award, and designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award, as described in the previous paragraph.

NOTES FORMING PART OF THE FINANCIAL STATEMENTS

CONTINUED

4. SEGMENTAL ANALYSIS

Operating segments are determined by the chief operating decision maker based on information used to allocate the Company's resources. The information as presented to internal management is consistent with the statement of comprehensive income. It has been determined that there is one operating segment, the development of fuel cells. In the year to 31 October 2016, the Company operated mainly in the United Kingdom and in Germany. All non-current assets are located in the United Kingdom.

5. OPERATING LOSS

This has been stated after:

	Year ended 31 October 2016 £	Year ended 31 October 2015 £
R&D tax credit receivable	(59,487)	(174,937)
Depreciation/Impairment of property and equipment	238,414	198,769
Amortisation/Impairment of intangible assets	64,240	79,522
R&D expenditure	2,914,050	3,475,657
Write off of Waste2Tricity investment and receivable	–	558,983
Equity-settled share-based payment expense	1,027,051	216,202
Foreign exchange differences	(334,898)	42,975
Auditor's remuneration – audit	30,900	30,000
Auditor's remuneration – corporation tax	3,500	9,500
Auditor's remuneration – R&D tax credit services	19,500	–

6. STAFF NUMBERS AND COSTS, INCLUDING DIRECTORS

The average numbers of employees in the year were:

	Year ended 31 October 2016 Number	Year ended 31 October 2015 Number
Support, operations and technical	37	39
Administration	6	5
	43	44

The aggregate payroll costs for these persons were:

	£	£
Wages and salaries (including Directors' emoluments)	1,983,582	2,660,709
Social security	239,738	317,242
Employer's pension contributions	37,976	35,095
Equity-settled share-based payment expense	1,027,051	216,202
	3,288,347	3,229,248

7. DIRECTORS' REMUNERATION

	Year ended 31 October 2016 £	Year ended 31 October 2015 £
Wages and salaries	379,355	978,656
Social security	65,113	131,225
Equity-settled share-based payment expense	821,002	170,001
Other compensation	295,827	48,149
Company pension contributions	2,504	1,844
	1,563,801	1,329,875
The emoluments of the Chairman	56,575	57,346
The emoluments of the highest-paid Director	1,334,852	661,932
Company pension contributions of highest-paid Director	–	–

The remuneration, details of share options and interests in the Company's shares of each Director are shown in the Directors' Report on pages 26 and 27.

8. FINANCE COST

	Year ended 31 October 2016 £	Year ended 31 October 2015 £
(Loss)/Gain on derivative financial instrument	(149,687)	3,288,497
Interest on finance lease	(1,961)	–
Bank interest receivable	3,415	5,775
Total finance (cost)/income	(148,233)	3,294,272

9. TAXATION

	Year ended 31 October 2016 £	Year ended 31 October 2015 £
Recognised in the statement of comprehensive income		
R&D tax credit – current year	(613,732)	(569,706)
R&D tax credit – prior year	(209,098)	–
Total tax credit	(822,830)	(569,706)
<i>Reconciliation of effective tax rates</i>		
Loss before tax	(6,478,894)	(5,351,931)
Tax using the domestic rate of corporation tax of 20.00% (2015: 20.42%)	(1,295,779)	(1,092,864)
Effect of:		
R&D tax credit – prior year	(209,098)	–
Expenses not deductible for tax purposes	209,151	659,518
Above the line tax credit	–	185,396
R&D allowance	(478,253)	(450,148)
Tax credit on losses surrendered	(613,452)	(569,706)
Depreciation in excess of capital allowances	4,920	47,737
Losses surrendered for research and development	846,141	232,349
Unutilised losses carried forward	697,625	418,012
Fixed asset differences	15,915	–
Total tax credit	(822,830)	(569,706)

NOTES FORMING PART OF THE FINANCIAL STATEMENTS

CONTINUED

10. LOSS PER SHARE

The calculation of the basic loss per share is based upon the net loss after tax attributable to ordinary Shareholders of £5,656,064 (2015: loss of £4,782,225) and a weighted average number of shares in issue for the year.

	Year ended 31 October 2016	Year ended 31 October 2015
Basic loss per share (pence)	(1.86)p	(1.66)p
Diluted loss per share (pence)	(1.86)p	(1.66)p
Loss attributable to equity Shareholders	(5,656,064)	(4,782,225)
	Number	Number
Weighted average number of shares in issue	304,858,560	288,431,626

Diluted earnings per share

As set out in note 18, there are share options and warrants outstanding as at 31 October 2016 which, if exercised, would increase the number of shares in issue. However, the diluted loss per share is the same as the basic loss per share, as the loss for the year has an anti-dilutive effect.

11. INTANGIBLE ASSETS

	2016 Patents £	2015 Patents £
Cost		
Balance at 1 November	445,927	748,113
Retirements	–	(401,166)
Additions	70,521	98,980
Balance at 31 October	516,448	445,927
Amortisation		
Balance at 1 November	107,751	469,040
Retirements	–	(401,166)
Charge for the year	64,240	39,877
Balance at 31 October	171,991	107,751
Net book value	344,457	338,176

12. PROPERTY AND EQUIPMENT

	Leasehold improvements £	Fixtures, fittings and equipment £	Motor vehicles £	Total £
Cost				
At 31 October 2014	272,759	2,693,951	10,495	2,977,205
Transfers	45,852	(45,852)	–	–
Additions	18,851	–	17,994	36,845
Disposals	–	(1,326,821)	(10,495)	(1,337,316)
At 31 October 2015	337,462	1,321,278	17,994	1,676,734
Additions	–	81,424	–	81,424
Disposals	–	(238,797)	–	(238,797)
At 31 October 2016	337,462	1,163,905	17,994	1,519,361
Depreciation				
At 31 October 2014	240,104	2,117,457	10,203	2,367,764
Transfers	9,783	(9,783)	–	–
Charge for the year	39,645	194,882	3,887	238,414
Disposals	–	(1,035,277)	(10,495)	(1,045,772)
At 31 October 2015	289,532	1,267,279	3,595	1,560,406
Charge for the year	47,930	54,537	5,901	108,368
Disposals	–	(238,797)	–	(238,797)
At 31 October 2016	337,462	1,083,019	9,496	1,429,977
Net Book Value				
At 31 October 2016	–	80,886	8,498	89,384
At 31 October 2015	47,930	53,999	14,399	116,328

13. INVESTMENT

As at 31 October 2016 the Company held 230,000 shares representing 17.5% (2015: 230,000 shares representing 23%) of the share capital of Waste2Tricity Ltd ("W2T") (a company registered in England & Wales). In the view of the Directors this investment has no value currently and has been recognised at cost less impairment. No revenue was recognised in the period under the licence agreements with Waste2Tricity Limited and Waste2Tricity International (Thailand) Limited.

	Year ended 31 October 2016 £	Year ended 31 October 2015 £
Investment in W2T	–	–

14. INVENTORY AND WORK IN PROGRESS

	Year ended 31 October 2016 £	Year ended 31 October 2015 £
Inventory	150,932	219,421
Work in progress	–	–
	150,932	219,421

NOTES FORMING PART OF THE FINANCIAL STATEMENTS

CONTINUED

15. TRADE AND OTHER RECEIVABLES

	Year ended 31 October 2016 £	Year ended 31 October 2015 £
Current:		
R&D tax credits receivable	673,219	718,023
EU grants receivable	1,409,642	2,513,395
Other receivables	513,102	226,922
	2,595,963	3,458,340

There is no significant difference between the fair value of the receivables and the values stated above.

16. CASH AND CASH EQUIVALENTS

	Year ended 31 October 2016 £	Year ended 31 October 2015 £
Cash at bank	1,137,819	675,603
Bank deposits	1,773,043	1,080,842
	2,910,862	1,756,445

Cash at bank and bank deposits consist of cash. There is no material foreign exchange movement in respect of cash and cash equivalents. Restricted cash, not included in cash and cash equivalents, is €125,000 held in escrow to support a bank guarantee in favour of Air Products GmbH relating to contractual obligations by the Company in relation to the Stade site in Germany.

17. ISSUED SHARE CAPITAL

	Number	Ordinary shares £	Share premium £	Total £
At 31 October 2015	289,903,943	289,904	33,947,858	34,237,762
Issue of shares on 18 January 2016	18,000,000	18,000	3,571,000	3,589,000
Issue of shares on 21 January 2016	250,000	250	56,625	56,875
Issue of shares on 18 April 2016	190,000	190	28,785	28,975
Issue of shares on 19 May 2016	720,000	720	50,670	51,390
Issue of shares on 6 July 2016	250,000	250	34,125	34,375
Issue of shares on 19 August 2016	700,000	700	154,550	155,250
At 31 October 2016	310,013,943	310,014	37,843,613	38,153,627

All issued shares are fully paid.

The Company considers its capital and reserves attributable to equity Shareholders to be the Company's capital. In managing its capital, the Company's primary long-term objective is to provide a return for its equity Shareholders through capital growth. Going forward the Company will seek to maintain a gearing ratio that balances risks and returns at an acceptable level and also to maintain a sufficient funding base to enable the Company to meet its working capital needs. The Company's commercial activities are at an early stage and management considers that no useful target debt to equity gearing ratio can be identified at this time.

Details of the Company's capital are disclosed in the statement of changes in equity.

There have been no other significant changes to the Company's management objectives, policies and processes in the year nor has there been any change in what the Company considers to be capital.

18a. SHARE OPTIONS

	Number of options	Exercise price	Weighted average remaining contractual life
At 31 October 2014	7,980,000	3.13-35.75p	6.3 yrs
Options granted in the year	7,615,000	17-51p	
Options exercised in the year	(1,150,000)	3.13-24p	
Options lapsed in the year	(590,000)	32-41p	
At 31 October 2015	13,855,000	3.13-51p	7.7 yrs
Options granted in the year	–	–	
Options exercised in the year	(1,220,000)	3.13-20.75p	
Options lapsed in the year	(730,000)	17-34p	
At 31 October 2016	11,905,000	3.13-51p	7.1 yrs

18b. WARRANTS

	Number of warrants	Exercise price	Weighted average remaining contractual life
At 31 October 2014	7,047,800	3.13-24p	5.1 yrs
Warrants exercised in the year	100,000	3.13p	
Warrants lapsed in the year	–	–	
At 31 October 2015	6,947,800	3.13-24p	4.1 yrs
Warrants exercised in the year	–	–	
Warrants lapsed in the year	–	–	
At 31 October 2016	6,947,800	3.13-24p	3.1 yrs

18c. SAYE

During the year the Company operated a share save scheme.

	Number of SAYE	Exercise price	Weighted average remaining contractual life
At 31 October 2014	1,065,259	18.6-22p	2.2 yrs
SAYE issued during the year	–	–	
SAYE lapsed/cancelled during the year	(485,503)	18.6-22p	
SAYE exercised during the year	(8,409)	22p	
At 31 October 2015	571,347	18.6-22p	1.3 yrs
SAYE issued during the year	399,537	12p	
SAYE lapsed/cancelled during the previous year correction	488,714	18.6-22p	
SAYE lapsed/cancelled during the year	(141,516)	22p	
SAYE exercised during the year	–	–	
At 31 October 2016	1,318,082	18.6-22p	1.3 yrs

NOTES FORMING PART OF THE FINANCIAL STATEMENTS

CONTINUED

18d. EQUITY-SETTLED SHARE-BASED PAYMENTS CHARGE

Share Options

Option price (p)	Average grant date share price (p)	Average expected volatility (p.a.)	Average risk-free interest rate (p.a.)	Average dividend yield (p.a.)	Average implied option life (years)	Average fair value per option (p)	Amount expensed in the 2016 accounts £
3.13	3.13	113.8%	4.4%	0%	2.0	2	–
10	10	46%	4.4%	0%	2.5	2.5	–
17	17	80%	1.5%	0%	2.5	9.48	–
17.5	18.75	188%	4.4%	0%	2.5	14.07	–
24	23.75	188%	4.4%	0%	2.5	17.80	–
20.75	20	214.8%	4.4%	0%	2.0	15	–
32	31.75	243%	4.4%	0%	2.5	24	–
34	34	80%	1.5%	0%	2.5	18.96	9,552
35.75	35.75	124.7%	1.5%	0%	2.5	21.8	–
39.25	39.25	80%	1.5%	0%	2.5	21.89	40,489
41	41	80%	1.5%	0%	2.5	22.86	49,778
51	58	75%	2.1%	0%	2.5	32.00	821,002

Total charge for the year (2015: £210,779)

920,821

Warrants

Warrant price (p)	Average grant date share price (p)	Average expected volatility (p.a.)	Average risk-free interest rate (p.a.)	Average dividend yield (p.a.)	Average implied option life (years)	Average fair value per option (p)	Amount expensed in the 2016 accounts £
3.13	3.13	113.8%	4.4%	0%	2.0	2	–
24	23.75	188%	4.4%	0%	2.5	17.8	–

Total charge for the year (2015: £nil)

–

SAYE

SAYE price (p)	Average grant date share price (p)	Average expected volatility (p.a.)	Average risk-free interest rate (p.a.)	Average dividend yield (p.a.)	Average implied option life (years)	Average fair value per option (p)	Amount expensed in the 2016 accounts £
22	27.5	124.7%	1.5%	0%	2.5	21.69	50,511
18.6	23.25	137.5%	1.5%	0%	2.5	19.24	51,092
12	15	78.6%	0.7%	0%	2.0	8.4	4,627

Total charge for the year (2015: £5,423)

106,230

Total equity-settled share-based payment charge for the year (2015: £216,202)

1,027,051

Expected volatility has been based on the 3.5 year historical volatility of share price. Vesting requirements are three years for the exercise of warrants and options, except for 500,000 options granted which vest in two years. Certain options and warrants granted to Directors are also subject to performance conditions.

Adam Bond received 6,000,000 options on 17 July 2015 with vesting conditions that include market and non-market based conditions. Under the market-based conditions vesting is contingent on the average share price of the Company reaching certain targets. Under non-market based conditions vesting is contingent on the Company's fuel cell system installed at Stade in Germany reaching certain output of wattage targets and the Company entering into commercial contracts.

The fair value of services received in return for share options and other share-based incentives granted is measured by reference to the fair value of share options and incentives granted. This estimate is based on a Black-Scholes model for non-market based conditions and a Log-normal Monte Carlo stochastic model for market conditions. Both are appropriate considering the effects of the vesting conditions, expected exercise period and the dividend policy of the Company.

19. TRADE AND OTHER PAYABLES

	Year ended 31 October 2016 £	Year ended 31 October 2015 £
Current liabilities:		
Trade payables	357,118	1,066,600
Deferred income	105,727	115,698
Finance lease liability	16,246	–
Other payables	677,211	319,483
Accruals	139,602	171,778
	1,295,904	1,673,559
Non-current liabilities:		
Finance lease liability	5,803	–
	5,803	–

20. OPERATING LEASE COMMITMENTS

	Year ended 31 October 2016 £	Year ended 31 October 2015 £
Non-cancellable operating leases are as follows:		
Within one year	80,836	146,496
Between one and five years	11,717	69,260
Greater than five years	–	–
	92,553	215,756

The lease commitments relate to accommodation and three vehicles.

21. FINANCIAL INSTRUMENTS

In common with other businesses, the Company is exposed to risks that arise from its use of financial instruments. This note describes the Company's objectives, policies and processes for managing those risks and the methods used to measure them. Further quantitative information in respect of these risks is presented throughout these financial statements. The accounting policies regarding financial instruments are disclosed in note 2 and the significant accounting estimates and judgements are set out in note 3.

Principal Financial Instruments

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

	Year ended 31 October 2016 £	Year ended 31 October 2015 £
Loans and receivables:		
Cash and cash equivalents	2,910,862	1,756,445
Trade and other receivables	2,595,963	3,458,340
Fair value through profit and loss:		
Level 3 derivative financial instrument	–	1,308,859
Total financial assets	5,506,825	6,523,644
Trade and other payables	1,301,707	1,673,559
Total financial liabilities	1,301,707	1,673,559

NOTES FORMING PART OF THE FINANCIAL STATEMENTS

CONTINUED

21. FINANCIAL INSTRUMENTS CONTINUED

Financial instruments that are measured subsequent to initial recognition at fair value are grouped into three levels based on the degree to which the fair value is observable as defined by IFRS 7:

- Level 1 fair value measurements are those derived from unadjusted quoted prices in active markets for identical assets and liabilities;
- Level 2 fair value measurements are those derived from inputs, other than quoted prices included within Level 1, that are observable 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 asset or liability that are not based on observable market data.

The derivative financial instrument above, which was classified as a Level 3 derivative financial instrument, is the fair value of the equity swap with Lanstead Capital L.P. ("Lanstead"), entered in October 2014. The equity swap was for an 18-month period ending in April 2016. As at 31 October 2016, the derivative financial instrument is closed and the value is £nil (2015: £1,308,859).

In October 2014 the Company issued 22,000,000 new ordinary shares of 0.1p each in the capital of the Company ("Ordinary Shares") at a price of 10p per share to Lanstead for £2,200,000. The Company simultaneously entered into an equity swap with Lanstead for 75% of these shares with a reference price of 13.3333 per share (the "Reference Price"). All 22,000,000 Ordinary Shares were allotted with full rights on the date of the transaction. Of the subscription proceeds of £2,200,000 received from Lanstead, £1,870,000 (85%) was invested by the Company in the equity swap. Investment in the equity swap was a condition of the placing with Lanstead.

To the extent that the Company's volume weighted average share price was greater or lower than the Reference Price at each swap settlement, the Company received greater or lower consideration calculated on a pro-rata basis i.e. volume weighted average share price/Reference Price multiplied by the monthly transfer amount.

	£
Value in 2015	1,308,859
Losses recognised in profit and loss	(149,687)
Settlements received	(1,159,172)
Value in 2016	–

No financial instruments have been transferred between Levels during the year.

General Objectives, Policies and Processes

The Board has overall responsibility for the determination of the Company's risk management objectives and policies and, while retaining ultimate responsibility for them, it has delegated part of the authority for designing and operating processes that ensure the effective implementation of the objectives and policies to the Company's finance team. The Board receives reports from the financial team through which it reviews the effectiveness of the processes put in place and the appropriateness of the objectives and policies it sets.

The overall objective of the Board is to set policies that seek to reduce ongoing risk as far as possible without unduly affecting the Company's competitiveness and flexibility. Further details regarding these policies are set out overleaf.

Credit Risk

Credit risk arises principally from the Company's trade and other receivables and cash and cash equivalents. It is the risk that the counterparty fails to discharge its obligation in respect of the instrument. The maximum exposure to credit risk equals the carrying value of these items in the financial statements as shown below:

	Year ended 31 October 2016 £	Year ended 31 October 2015 £
Trade and other receivables	2,595,963	3,458,340
Cash and cash equivalents	2,910,862	1,756,445

The Company's principal trade and other receivables arose from: a) annual payments for various services held as pre-payments b) VAT debtors receivable from UK and German tax authorities c) an R&D tax credit d) grant funding receivable from the EU. Credit risk with cash and cash equivalents is reduced by placing funds with a range of banks with acceptable credit ratings and government support where applicable and on term deposits with a range of maturity dates. At the year end, most cash was temporarily held on short-term deposit, following maturity of term deposits.

21. FINANCIAL INSTRUMENTS CONTINUED

Liquidity Risk

Liquidity risk arises from the Company's management of working capital and the amount of funding required for the development programme. It is the risk that the Company will encounter difficulty in meeting its financial obligations as they fall due. The Company's policy is to ensure that it will always have sufficient cash to allow it to meet its liabilities when they become due.

The principal liabilities of the Company are trade and other payables in respect of the ongoing product development programme. Trade and other payables are all payable within two months. The Board receives cash flow projections on a regular basis as well as information on cash balances.

Interest Rate Risk

The Company is exposed to interest rate risk in respect of surplus funds held on deposit and uses fixed interest term deposits to mitigate this risk.

Fair Value of Financial Liabilities

	Year ended 31 October 2016 £	Year ended 31 October 2015 £
Trade and other payables	1,301,707	1,673,559

There is no difference between the fair value and book value of trade and other payables.

The Company does not enter into forward exchange contracts or otherwise hedge its potential foreign exchange exposure. The Board monitors and reviews its policies in respect of currency risk on a regular basis. At 31 October 2016 the Company held no monetary assets or liabilities in currencies other than the functional currency of the operating units involved (2015: £nil).

22. CAPITAL COMMITMENTS

The Company had no capital commitments outstanding at 31 October 2016 (2015: £nil).

23. BOARD CHANGES AND POST-BALANCE SHEET EVENTS

Board changes are reported under "Directors and their Interests". In March 2017, the Company undertook a placing, subscription and open offer, raising approximately £8.1 million before expenses.

24. ULTIMATE CONTROLLING PARTY

There is no ultimate controlling party.

25. RELATED PARTY TRANSACTIONS

During the year ended 31 October 2016:

£nil was invoiced by Richards and Appleby Ltd (a company registered in England & Wales) for the services of Mitchell Field as a Director of AFC Energy plc (2015: £2,280). Mr. Field is also a Director and Shareholder of Richards and Appleby Ltd. At 31 October 2016, the sum owing to Richards and Appleby Ltd was £nil (2015: £4,780).

£65,392 was invoiced by Linc Energy Ltd (a company registered in Australia) for the services of Adam Bond as Director of AFC Energy plc (2015: £212,438). Linc Energy Ltd was, until 30 September 2015, a major Shareholder in the Company. At 31 October 2016 the amount owing to Linc Energy Ltd was £nil (2015: £42,761).

£40,200 (plus VAT) was invoiced by Locana Corporation (London) Ltd (a company registered in England & Wales) for consultancy services (2015: £37,640). Mr. Yeo is also a Director and Shareholder of Locana Corporation (London) Ltd. At 31 October 2016, the sum owing to Locana was £3,350 (2015: £3,350).

COMPANY INFORMATION

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Adam Bond
Jim Gibson
Mitchell Field
Eugene Shvidler
Eugene Tenenbaum

Company Secretary

Richard Tuffill

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