

Seven Arts Entertainment Inc.  
Form 20-F/A  
June 06, 2012

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 20-F/A

- o REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE  
SECURITIES EXCHANGE ACT OF 1934

OR

- o ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended June 30, 2011

OR

- o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

OR

- o SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

Date of event requiring this shell company report \_\_\_\_\_

Seven Arts Pictures Plc.  
(Exact name of Registrant as specified in its charter)

England  
(Jurisdiction of incorporation or organization)

136-144 New Kings Road, London SW6 4LZ  
(Address of principal executive offices)

Securities registered pursuant to Section 12(b) of the Act:  
None

Securities registered pursuant to Section 12(g) of the Act:  
Ordinary Shares, £0.25 par value  
(Title of Class)

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: None

Indicate the number of outstanding shares of each of the Company's classes of capital or ordinary stock as of the close of the period covered by the annual report:

2,643,131 ordinary shares

13,184,000 deferred shares of £0.45

2,268,120 deferred shares of £1.00

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Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  
Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Act of 1934. Yes  No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past ninety days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of “accelerated filer and large accelerated filer” in Rule 12b-2 of the Exchange Act.

|                         |                       |                           |                                     |
|-------------------------|-----------------------|---------------------------|-------------------------------------|
| Large Accelerated Filer | <input type="radio"/> | Non- Accelerated Filer    | <input type="radio"/>               |
| Accelerated Filer       | <input type="radio"/> | Smaller Reporting Company | <input checked="" type="checkbox"/> |

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP  International Financial Reporting Standards as issued by the International Accounting Standards Board

If “Other” has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow.

Indicate by check mark which financial statement item the registrant has elected to follow: Item 17  Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No  N/A

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes  No  N/A

EXPLANATORY NOTE

This Form 20-F/A-1 (the “Amendment”) amends the Annual Report on Form 20-F of Seven Arts Pictures Plc. for the year ended June 30, 2011, which was filed with the Securities and Exchange Commission on December 21, 2011 (the “Original Filing”). This Amendment is being filed solely to remove the word “DRAFT” on the front sheet in the Original Filing as set forth in the attached. No other changes are hereby made to the Original Filing.

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Seven Arts Pictures PLC

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## INTRODUCTION

Unless otherwise indicated, all references to “the Group”, “we”, “us” “our” and or “PLC” refer to Seven Arts Pictures Plc. and wholly owned subsidiaries.

We use United States dollars as our reporting currency and our consolidated financial statements are prepared in accordance with Generally Accepted Accounting Principles of the United States of America (“US GAAP”) as issued by the Financial Accounting Standards Board.

PLC was incorporated as Glasgow Park Investments Plc. on August 24, 2001 under the English Companies Act of 1985. Pursuant to a resolution passed at a meeting of the shareholders of PLC held on September 11, 2001, the Group changed its name from Glasgow Park Investments Plc. to The Cabouchon Collection Plc. Pursuant to a resolution passed at a meeting of the shareholders of the Group that was held on November 6, 2003, the name of the Group was changed to Cabouchon Plc. Pursuant to a resolution passed at a meeting of the shareholders of the Group that was held on September 2, 2004, the name of the Group was changed to Seven Arts Pictures Plc., at the time all motion picture business assets of Seven Arts Pictures Inc. (“SAP, Inc.”) were transferred to a subsidiary of the Group, (Seven Arts Filmed Entertainment Limited) (“SAFE, Ltd.”) pursuant to an asset transfer agreement in exchange for ordinary shares of the Group. Documents concerning the Group which are referred to herein may be inspected during regular hours at the Group’s Los Angeles affiliate office located at 8439 Sunset Blvd., 4th Floor, West Hollywood, CA 90069, U.S.A.

On January 27, 2011, Seven Arts Entertainment Inc. (“SAE”), a Nevada Corporation, became a 100% subsidiary of PLC. We entered into an asset transfer agreement, as amended on December 15, 2010, to transfer all of the assets of PLC (including ownership of certain subsidiaries) to SAE, in exchange for assumption by SAE of certain indebtedness and for one share of common stock of SAE for each ordinary share of PLC which is expected to be distributed, subject to a future registration statement, to be filed by the PLC. This transfer was agreed to by our shareholders at our extraordinary general meeting on June 11, 2010. The purpose of this transfer was to eliminate our status as a foreign private issuer and to assume compliance with all obligations of a domestic issuer under all applicable state and federal securities laws. Our intention is to redomicile our business with no change in the economic interests of our shareholders.

All operating assets of PLC have been transferred to SAE as of January 27, 2011. PLC’s NASDAQ listing was transferred to SAE on August 31, 2011. PLC’s and all members of the Group, other than SAFE Ltd. have been placed in creditors liquidation. As a result this is the last Form 20-F to be filed by the Group and all future filings will be by SAE, as a United States issuer. See additional information regarding the asset transfer in NOTE 1 to the financial statements presented herein.

## BUSINESS OF SEVEN ARTS PICTURES PLC.

PLC, an English corporation, is the successor of Seven Arts Pictures Inc. (“SAP Inc.”) as a result of an asset transfer agreement under which all motion picture business assets of SAP Inc. were transferred to a subsidiary of the PLC for ordinary shares of PLC. SAP Inc. was founded in 2002 as an independent motion picture production Group engaged in developing, financing, producing and licensing theatrical motion pictures with budgets in the range of \$2 million to \$15 million for exhibition in domestic (i.e. the United States and Canada) and foreign theatrical markets and for subsequent post theatrical worldwide release in other forms of media, including DVD, home video, pay-per-view, and free television. SAP Inc. continued the motion picture production and distribution activities of CineVisions Incorporated in 1992, which SAP Inc. acquired on SAP Inc.'s initial capitalization pursuant to an asset transfer agreement in October, 2002, which was intended to qualify as a Section 351 transaction under the Internal Revenue Code of 1986, as amended. The Group currently owns interests in 33 completed motion pictures subject in certain instances to the prior financial interests of other parties. (listed in Table 8)

## FORWARD-LOOKING STATEMENTS

Certain statements in this document might constitute “forward-looking statements”. Some, but not all, forward-looking statements can be identified by the use of words such as “anticipate,” “believe,” “plan,” “estimate,” “expect,” and “intend” or other similar expressions. Although the Group has attempted to identify important factors that could cause actual results to differ materially from expected results, such forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Group, or other future events, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such factors include, among others, the following risks: the need for additional financing; uncertainties and risks related to carrying on business in foreign countries; risks associated with third party infringement of copyrights and other intellectual property, especially the unauthorized duplication of motion picture DVDs and unauthorized distribution of motion pictures through the world wide web; risks associated with the lack of enforcement of applicable copyright and intellectual property laws, especially in foreign countries; risks associated with changing copyright and applicable intellectual property laws, especially in foreign countries; risks associated with changing distribution models for motion pictures, especially on the world wide web; risks associated with restrictions of motion picture content, especially in foreign countries; reliance on key personnel; the potential for conflicts of interest among certain officer, directors or promoters of the Group; the absence of dividends; currency fluctuations; competition; dilution; the volatility of the Group’s ordinary share price and volume; and tax consequences to United States shareholders. Except as required by law, the Group undertakes no obligation to revise any forward-looking statements because of new information, future events or otherwise.



## PART I

## ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISORS

N/A

## ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE.

N/A

## ITEM 3. KEY INFORMATION.

All data in this report reflects a 5:1 reverse stock split enacted on the last day of the December 31, 2008 fiscal period and a second 5 for 1 reverse stock split enacted on May 12, 2011.

## 3.A.1. Selected Financial Data

The following sets forth a summary of consolidated balance sheets and statements of operations for the fiscal years ended June 30, 2011 and June 30, 2010, prepared under US GAAP. All of the foregoing have been derived from our audited consolidated financial statements and related notes included elsewhere in this Form 20-F. The summary consolidated historical financial and operating information should be read in conjunction with and the consolidated financial statements and the related notes thereto and the other financial information included elsewhere in this annual report.

## Summary Financial Data

(in \$ 000's, except per share data)

## Summary Profit and Loss Statements

|   | Fiscal<br>Year<br>Ended<br>June 30,<br>2011 | Fiscal<br>Year<br>Ended<br>June 30,<br>2010 |
|---|---|---|
| Total Revenue (1)   | \$3,328                                     | \$6,417                                     |
| Gross Profit/(Loss)   | (120 )                                      | 4,018                                       |
| Net Income/(Loss) (2)   | 1,462                                       | (476 )                                      |
| Weighted Average Primary Shares Outstanding (in 000's)        | 1,889                                       | 1,403                                       |
| Weighted Average Fully Diluted Shares Outstanding (in 000's)  | 1,889                                       | 1,403                                       |
| Weighted Average Earnings Per Share (cents)(3)                | \$0.77                                      | \$(0.34 )                                   |
| Weighted Average Fully Diluted Earnings Per Share (cents) (3) | \$0.77                                      | \$(0.34 )                                   |

## Summary Balance Sheet

|             |        |        |
|-------------|--------|--------|
| Total Loans | 12,646 | 18,301 |
|-------------|--------|--------|

|                              |        |        |
|------------------------------|--------|--------|
| Total Assets                 | 27,946 | 28,625 |
| Shareholders' Equity (4) (5) | 7,958  | 2,200  |

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(1) Fee related revenues in the year ended June 30, 2011, included \$70,097 of additional producers fees resulting from excess tax credits received on Night of the Demons and \$500,000 of fees associated with films produced in Louisiana.

(2) Net Income includes other income of \$4,458,621 recorded in the year ended June 30, 2011 reflecting cancellation of indebtedness:

(a) Arrowhead \$1,788,904

(b) Palm Finance-forgiveness of interest of \$2,669,717

(3) The included audited Consolidated Financial Statements for the fiscal years ended June 30, 2011 and 2010, prepared under US GAAP show income per share figures calculated using the weighted average number of shares outstanding in each period. A 5-for-1 reverse stock split occurred on May 12, 2011. The income per share figures in the table above have been adjusted from the figures shown in prior financial statements to show the effect of the 5:1 reverse stock split as if it had occurred on the first day of the fiscal year ended June 30, 2010.

(4) Convertible Debentures with no redemption date owned by Langley Park Investment Trust Plc. (“Langley”) are treated as Shareholders’ Equity as they have no redemption date. As of June 30, 2011 and 2010, the value of such debentures outstanding was \$3,432,450.

(5) Convertible Preference Shares owned by Armadillo Investment Plc. until November 2008, and then by the Group’s Employee Benefit Trust (“EBT”), are treated as Shareholders’ Equity. As of June 30 2011, all preference shares had been converted to ordinary shares. EBT converted 2,500,000 of the preference shares into 2,000,000 ordinary shares on November 20, 2008 and the remaining 500,000 preference shares into 400,000 ordinary shares on May 25, 2010.

### 3.A.3. Exchange Rates

The Company translates foreign currency transactions and balances in Pounds Sterling (“GBP”) into United States Dollars (“USD”) using the year or reporting period end or average exchange rates. Assets and liabilities of the foreign entities are translated at exchange rates in effect for the periods presented. The cumulative translation adjustment is included in shareholders’ equity (deficit). Foreign currency transaction gains and losses arising from exchange rate fluctuations on transactions denominated in a currency other than the functional currency are included in the consolidated results of operations.

| Exchange Rate Table                   | As of June<br>30, 2011 | As of June<br>30, 2010 |
|---------------------------------------|------------------------|------------------------|
| Average rate USD/GBP                  | 1.5655                 | 1.5721                 |
| Balance Sheet Period end rate USD/GBP | 1.6056                 | 1.4962                 |

### 3.B. Capitalization and Indebtedness

N/A

### 3.C. Reasons For The Offer And Use Of Proceeds

N/A



### 3.D. Risk Factors

#### Risks Relating to the Group's Business

All references to “we” or “our” refer to the Group and its consolidated subsidiaries.

Our success depends on certain key employees.

Our success depends to a significant extent on the performance of a number of senior management and other key employees, including production and creative personnel. We particularly depend upon our Chief Executive Officer, Peter Hoffman, whose employment agreement grants him the right, as long as he is employed by us, to approve or control all artistic and business decisions regarding motion pictures that we acquire, produce or distribute. As a result, our success depends to a significant extent on Mr. Hoffman's creative and business decisions regarding the motion pictures we acquire, produce and distribute.

We do not have "key person" insurance on the lives of any of our officers or directors. We have entered into employment agreements with our top executive officers. These agreements entitle us to possible injunctive relief for breach of the agreements, and include six-month “non-compete” covenants. These agreements cannot assure us of the continued services of such employees. In addition, competition for the limited number of business, production and creative personnel necessary to create and distribute our entertainment content is intense and may grow in the future. Our inability to retain or successfully replace where necessary members of our senior management and other key employees could have a material adverse effect on our business, results of operations and financial condition.

Our interests may conflict with those of our Chief Executive Officer.

We have entered into a series of agreements with Mr. Hoffman, and his affiliated companies that may result in our interests differing from theirs (see “Certain Related Transactions”). One of these agreements concerns a financing arrangement, in an aggregate amount of \$7,500,000, that we entered into with Cheyne Specialty Finance Fund L.P. (“Cheyne”) for the production of our movies, which has been secured with (i) six of our motion pictures and (ii) 321,400 of our ordinary shares beneficially owned by Mr. Hoffman through SAP Inc. Upon repayment of the \$6,500,000 the senior debt (“Cheyne loan”) was acquired by SAFE Ltd. in April 2008, Mr Hoffman believes that the 321,400 pledged shares were released, and the pledged shares were not passed on to the \$1,000,000 subordinated noteholder, Arrowhead Consulting Group Limited. Our satisfaction of our debts to Cheyne may provide divergent benefits to us and to Mr. Hoffman, in that Mr. Hoffman claims a full release from this pledge of our ordinary shares owned by SAP Inc. Other agreements that we have entered into with Mr. Hoffman and his affiliates that may result in conflicts of interest include his employment agreement and an Inter-Group Agreement, which provides that SAP Inc. will own limited liability companies in the United States, with all distribution rights and profits thereof for our account and provide other services for our account and according to which SAP Inc. has assigned to us any results and proceeds arising from services performed by SAP Inc. on our behalf. See “Certain Related Transactions.”

We have several transactions with affiliates controlled by our Chief Executive Officer which may provide benefits to him.

Certain of our affiliates, controlled by Mr. Hoffman, are entitled to be reimbursed by us for general overhead incurred by each to conduct business for us in amounts approved by us and then to be reimbursed for certain third party costs on motion pictures controlled by us and to be indemnified for loss costs or damages arising from the conduct of business on our behalf if approved by us.

In addition, we license distribution rights to pictures controlled by us to our affiliate, Seven Arts Pictures Louisiana LLC ("SAPLA") which performs distribution services for our motion pictures. All fees payable to SAPLA are subject to the agreements with Mr. Hoffman and his affiliates described above. See Risk Factors- Relating to Our Business and Certain Related Transactions. Finally upon commencement of business of our production and post-production facility in New Orleans, Louisiana, SAPLA and an affiliate, Seven Arts Filmed Entertainment Louisiana LLC ("SAFE LA") will be the lessee of those facilities and under the Inter-Group Agreement all profits of SAFE LA if any will be returned to us under the agreements with Mr. Hoffman and his affiliates. See Certain Related Transactions for further detail and discussion of all transactions with affiliates.

We have and exercise the right to control through our management all material decisions of all affiliates controlled by Mr. Hoffman to the extent such decisions have any material effect on our results of operations.

Our failure to repay obligations under the Arrowhead Loan and Cheyne Loan has resulted in the loss of control of assets that we pledged and could result in the loss of our Chief Executive Officer's beneficial interest in our ordinary shares and ownership of these assets.

Seven Arts Future Flow I ("SFF"), a limited liability company owned by SAP Inc., one of our affiliates and a company controlled by Mr. Hoffman, obtained financing from the Arrowhead Target Fund, Ltd. ("Arrowhead") of approximately \$8,300,000 (the "Arrowhead Loan"). The Group secured the Arrowhead Loan with liens on 12 motion pictures that generated revenues of \$820,026 in the year ended June 30, 2009, \$2,739,800 in the year ended March 31, 2008. The Arrowhead Loan had been recorded in our audited financial statements as an \$8,300,000 liability as of June 30, 2008. Although the loan is secured by certain assets of SFF, the Group is not required to repay the Arrowhead Loan from any of our other assets or revenues. We made certain representation regarding ownership of these twelve motion pictures and agreed to continue to license these twelve motion pictures, collect money received therefrom and to deposit such collections in a designated bank account.

The Arrowhead Loan was due on February 15, 2009, and SFF did not pay the outstanding principal and interest due thereon. Arrowhead had the right to foreclose on the pledged film assets, but has not done so. SFF has, however; received a default notice to that effect, and, as a result, Arrowhead is now collecting directly all sums receivable from us with respect to these motion pictures, and has appointed a new servicing agent for these motion pictures, with the result that we no longer control the licensing of these motion pictures. Failure to repay or refinance the Arrowhead Loan could result in a material disposition of assets through the loss of our rights to twelve motion pictures and related loss of revenues in amounts that are difficult to predict. Arrowhead continues to have the right to foreclose on the twelve motion pictures, which are Asylum, The Hustler, I'll Sleep When I'm Dead, Johnny Mnemonic, Never Talk to Strangers, No Good Deed, Popstar, Red Riding Hood, Shattered Image, A Shot At Glory, Stander, and Supercross. As a result of the foregoing, we have removed all investment in and receivables relating to the twelve motion pictures pledged to Arrowhead as assets and have removed all limited recourse indebtedness related to these motion pictures as liabilities from our consolidated balance sheet for the fiscal year ended June 30, 2009.



The Arrowhead Target Fund Ltd. ("Arrowhead") filed an action on September 22, 2010 which seeks recovery from the Group of the monies which the Group has retained under its interpretation of the relevant agreements with Arrowhead. In addition, Arrowhead makes substantial additional claims against the Group, Mr. Hoffman and SAP Inc. regarding claimed breaches of the terms of the operative agreements, including failure to properly account, failure to turn over materials, failure to remit monies collected, and similar matters. The claims against the Group for these breaches of warranties for damages are \$8,300,000 although Arrowhead states no basis for this amount. The Group had moved to dismiss the action against all defendants other than SFF, which is not part of the Group. On August 9, 2011, the New York Supreme Court granted the Group's motion and dismissed all defendants except SAFE Ltd. in its capacity as a collateral agent, which is not a material element of Arrowhead claim. The Group continues to believe that Arrowhead's claims against the Group are without substantial merit.

We also obtained financing of an aggregate of approximately \$7,500,000 from Arrowhead Consulting Group LLC ("ACG") for \$1,000,000 ("ACG Loan") and Cheyne for \$6,500,000 ("Cheyne Loan") at a rate of interest of 19% and 18% per annum, respectively. SAP Inc., one of our affiliates, which is controlled by Mr. Hoffman, our Chief Executive Officer, secured the ACG Loan and the Cheyne Loan with 1,607,000 of our ordinary shares beneficially owned by Mr. Hoffman, and we secured the ACG Loan and the Cheyne Loan with liens on six motion pictures that generated cumulative revenues of approximately \$2,326,078 as of June 30, 2009, plus a second position security interest in the motion pictures pledged under the Arrowhead Loan. The Cheyne Loan matured on September 30, 2007. A subsidiary of ours acquired the debt from then due to Cheyne, a sum of approximately \$6,500,000, on or about April 2008, and received an assignment from Cheyne of their senior secured position on the film assets, including Cheyne's subordination agreement with ACG. Management believes that the 321,400 pledged shares were released, and the pledged shares were not passed on to the \$1,000,000 subordinated noteholder, ACG.

ACG has demanded payment of the ACG Loan of \$1,000,000 and has filed suit therefore. The group is in litigation with the liquidator of ACG regarding the \$1,000,000 plus accrued interest as it believes this debt will never be paid due to its subordination to the senior loan. Failure to prevail in this litigation or to repay or refinance the ACG Loan could result in the loss of our rights to six motion pictures.

We face substantial capital requirements and financial risks.

Our business requires substantial investments of capital. The production, acquisition and distribution of motion pictures require a significant amount of capital. A significant amount of time may elapse between our expenditure of funds and the receipt of commercial revenues or tax credits derived from the production of our motion pictures. This time lapse requires us to fund a significant portion of our capital requirements from various financing sources. We cannot be certain that we can continue to successfully implement these financing arrangements or that we will not be subject to substantial financial risks relating to the production, acquisition, completion and release of future motion pictures. We currently employ a variety of structuring techniques, including debt or equity financing, in efforts to achieve our investment objectives. We cannot be certain that we will be able to negotiate structures that accomplish our objectives. We intend to increase (through internal growth or acquisition) our production slate or our production budgets, and, if we do, we will be required to increase overhead and/or make larger up-front payments to talent and, consequently, bear greater financial risks. Any of the foregoing could have a material adverse effect on our business, results of operations and financial condition.

The costs of producing and marketing feature films have steadily increased and may further increase in the future, making it more difficult for a film to generate a profit. The costs of producing and marketing feature films have generally increased in recent years. These costs may continue to increase in the future, which may make it more difficult for our films to generate a profit or compete against other films. Historically, production costs and marketing costs have risen at a higher rate than increases in either the number of domestic admissions to movie theaters or admission ticket prices. A continuation of this trend would leave us more dependent on other media, such as home



video, television, international markets and new media for revenue, which may not be sufficient to offset an increase in the cost of motion picture production. If we cannot successfully exploit these other media, it could have a material adverse effect on our business, results of operations and financial condition.

Budget overruns may adversely affect our business. Our business model requires that we be efficient in the production of our motion pictures. Actual motion picture production costs often exceed their budgets, sometimes significantly. The production, completion and distribution of motion pictures are subject to a number of uncertainties, including delays and increased expenditures due to creative differences among key cast members and other key creative personnel or other disruptions or events beyond our control. Risks such as death or disability of star performers, technical complications with special effects or other aspects of production, shortages of necessary equipment, damage to film negatives, master tapes and recordings or adverse weather conditions may cause cost overruns and delay or frustrate completion of a production. If a motion picture incurs substantial budget overruns, we may have to seek additional financing from outside sources to complete production, which may not be available on suitable terms. We cannot assure you that such financing on terms acceptable to us will be available, and the lack of such financing could have a material adverse effect on our business, results of operations and financial condition.

In addition, if a motion picture production incurs substantial budget overruns, we cannot assure you that we will recoup these costs, which could have a material adverse effect on our business, results of operations and financial condition. Increased costs incurred with respect to a particular film may result in any such film not being ready for release at the intended time and the postponement to a potentially less favorable time, all of which could cause a decline in box office performance, and, thus, the overall financial success of such film. Budget overruns could also prevent a picture from being completed or released. Although none of these events has occurred to us to date, any of the foregoing could have a material adverse effect on our business, results of operations and financial condition.

A substantial number of our motion pictures did not generate enough revenue to satisfy financing obligations related to those motion pictures, and our future motion pictures may not generate enough revenue to satisfy obligations entered into to finance their production.

We have obtained financing for most of our motion pictures and secured those financings with the assets from those and other motion pictures. If we are unable to generate sufficient revenues to repay those obligations under the terms of the financings, we lose those motion picture assets and any future revenues that we could derive from those assets. As noted, the revenues of the 12 and 6 motion pictures securing the Arrowhead Loan and the ACG Loan, respectively, have not met our estimates, and, as a result, we have not been able to repay those loans in the periods set out in those loans. If we are unable to amend the terms of those loans or satisfy them otherwise, we could lose those motion picture assets.

Additionally, our net revenues from a certain tax advantaged transaction after accounting for expenses for that transaction were not sufficient to enable us to satisfy a £1,000,000 convertible debenture loan from Trafalgar Capital Special Investment Fund ("Trafalgar") that came due on June 30, 2009, which we had expected to repay from that funding source even though that funding source was not pledged to repay the Trafalgar loan. As a result, we defaulted on a payment of £1,000,000 plus interest to Trafalgar in June 2009. On September 2, 2009 the Group repaid Trafalgar \$1,000,000 (about £698,934) as a partial payment against this loan, with the remaining balance subject to repayment in cash or convertible to the ordinary shares of the Group at the conversion terms as agreed between Trafalgar and the Group. On June 22, 2010 an amended agreement was entered into with Trafalgar for an extension of the due date of the convertible debentures to December 31, 2010, and the Group agreed to issue 340,000 ordinary shares to settle a portion of the debt. Trafalgar agreed to reduce the loan amount from the proceeds it received from selling the 340,000 ordinary shares and all 340,000 had been sold through the market by December 31, 2010. Subsequent to June 30, 2010, a further amended agreement was entered into with Trafalgar for an extension of the due date of the convertible debentures to March 31, 2011, and the Group agreed to issue 425,000 ordinary shares to settle a portion of the debt. Trafalgar agreed to reduce the loan amount from the proceeds it received from selling the 425,000 ordinary shares.

We entered into two senior financing loan and security agreements with Palm Finance Corp ("Palm") to finance the production costs of The Pool Boys, Autopsy and Nine Miles Down dated May 7, 2007 and December 17,

2007. These loans are secured by the revenues to be collected from these motion pictures. The revenues so far collected have been insufficient to repay the majority of these loans, primarily as result of management's decision to delay the release of these films. We have entered into a forbearance agreement with Palm extending the due date of these loans to December 31, 2011. The original principal amounts of the Palm loan for The Pool Boys and Autopsy are \$ 5,250,000 including a \$500,000 accrued interest, and for Nine Miles Down was \$4,000,000 including a \$750,000 accrued interest. The lender agreed to write off the accrued interest at the end of the year giving rise to forgiveness of debt income of \$2,669,717. Subsequent to the date of the financial statements the lender sold \$2,750,000 of his debt and converted 50% of the monies he received to Series A preference shares in SAE Inc.

On August 27, 2007, we borrowed \$1,650,000 from Blue Rider Financial (“Blue Rider”) to pay for the domestic prints and advertising costs for the motion picture Deal (“Blue Rider Loan”) and arranged that the revenues due from Metro-Goldwyn-Mayer Studios Inc. (“MGM”) to us for the distribution of that motion picture be assigned to Blue Rider Financial as partial security for that loan. To date the revenues paid to us from MGM have not yet been sufficient to repay the Blue Rider Loan. We have, therefore, entered into an accommodation agreement with Blue Rider to redeem the loan due for \$2,200,000, less approximately \$812,000 of collections that have been received by Blue Rider to date from MGM. We expect this indebtedness will be repaid from proceeds due from MGM on or before December 31, 2011.

We cannot assure you that a failure to repay these obligations will not make the terms of future financings more onerous or prohibitive. We also cannot assure you that our estimates of revenues from motion pictures securing any other current or future financings will be accurate, and that we will be able to satisfy those financings with the revenues from the motion pictures securing those financings. The loss of motion picture or other assets as a result of any such default would adversely affect our business.

Our revenues and results of operations may fluctuate significantly.

Revenues and results of operations are difficult to predict and depend on a variety of factors. Our revenues and results of operations depend significantly upon the performance of the motion pictures that we license for distribution, which we cannot predict with certainty. Accordingly, our revenues and results of operations may fluctuate significantly from period to period, and the results of any one period may not be indicative of the results for any future periods. Furthermore, largely as a result of these predictive difficulties, we may not be able to achieve analysts’ projected earnings. Revisions to projected earnings could cause investors to lose confidence in us, which in turn could materially and adversely affect our business, our financial condition and the market value of our securities.

Accounting practices used in our industry may accentuate fluctuations in operating results. In addition to the cyclical nature of the entertainment industry, industry accounting practices may accentuate fluctuations in our operating results. While such fluctuations have not occurred to date, we may in the future experience such fluctuations due to industry-wide accounting practices. In accordance with US GAAP and industry practice, we amortize film and television programming costs using the “individual-film-forecast” method, whereby these costs are amortized and participations and residuals costs are accrued in the proportion that current year’s revenue bears to management’s estimate of ultimate revenue at the beginning of the current year expected to be recognized from the exploitation, exhibition or sale of the films. The great majority of a film’s costs (80% or more) are generally amortized within three years of the picture’s initial release.

Ultimate revenue includes estimates over a period not to exceed ten years following the date of initial release. Film costs are stated at the lower of amortized cost or the film’s estimated fair value. Individual film costs are reviewed on a title-by-title basis, when an event or change in circumstances indicates that the fair value of a film is less than its unamortized cost. The fair value of the film is determined using management’s future revenue and cost estimates and a discounted cash flow approach. Additional amortization is recorded in the amount by which the unamortized costs exceed the estimated fair value of the film. Estimates of future revenue involve measurement uncertainty and it is therefore possible that reductions in the carrying value of investment in films may be required as a consequence of changes in management’s future revenue estimates.

We depend on a limited number of projects, and the loss or failure of a major project could have a material adverse effect on our business. Our revenue is generated from a limited number of films, principally Autopsy, Nine Miles Down, Deal, Noise, Drunkboat, and Night of the Demons. Films that we develop, finance, or license for distribution vary due to the opportunities available to us and to targeted audience response, both of which are unpredictable and subject to change. The loss or failure of a major project could have a material adverse effect on our results of

operations and financial condition as well as on the market price of our securities. We cannot assure you that any project we undertake or participate in will be successful.

We rely upon pre-sales, advances and guarantees.

We attempt to minimize some of the financial risks normally associated with motion picture production by obtaining, at various stages prior to release of our motion pictures, advances and guarantees from distributors in exchange for distribution rights to such pictures in particular territories. Advances and guarantees paid by a distributor for distribution rights to a film generally represent a minimum purchase price for such rights. While advances and guarantees reduce some of the financial risk of our motion pictures, they do not assure the profitability of our motion pictures or our Group's operations and, it may also result in our receiving lower revenues with respect to successful films. We believe that international "pre-sales" have become increasingly difficult to obtain resulting in fewer "pre-sales" with lower minimum guarantees, and this situation may continue for the indefinite future. As the international marketplace demands increasingly costly motion pictures, we cannot be certain that the amount of advances and guarantees which we anticipate generating on a given film project will exceed our cost of producing such motion picture.

In today's rapidly changing and competitive marketplace for motion pictures, it is possible that the amount of such advances and guarantees alone, after payment of our operating expenses, even if greater than our direct cost of producing a specific film, will not be sufficient to provide us with a significant return on our invested capital. Should we incur higher than expected overhead or production expenses, that amount may not be sufficient to provide a return of all or substantially all of our invested capital. To the extent that we do not produce one or more films that generate overages for us, there may be a material adverse effect upon our Group and the potential for returns on, and even the return of, our capital.

We rely on tax preference and tax credit transactions for a substantial portion of our revenues and recovery of film costs.

We have received substantial monies as revenues where relevant producer's contracts are in place, and recovery of investments in motion picture production and distribution costs from tax preference and tax credit transactions in the United States and other countries, which transactions have provided between 25% to 50% of film production costs on our pictures (approximately \$1,000,000 to \$3,500,000 per film). We cannot be certain that such revenues and cost recoveries will be available to us in future periods. These benefits accrue pursuant principally by means of statutes in Louisiana, the United Kingdom, Canada and Hungary, which could be repealed or amended based on general income tax considerations or political changes. We are aware of no such changes proposed or threatened at the present time.

We have a limited operating history.

Our predecessor was formed in 1992, and later transferred all its motion picture assets to SAP Inc. in October, 2002. SAP Inc. acquired control of our Group in September 2004 by a transfer of all its motion picture rights to SAFE, Ltd., our wholly owned subsidiary. Although our predecessors have a more extensive operating history, our Group began operations in its current form and business strategy in October, 2004. As a result, investors will have only a limited period of motion picture operations to evaluate our performance.

We currently lack a credit facility.

We do not have any credit facility with respect to financing production of our motion pictures (Although we do have a line of credit available to our affiliate, SAPLA, to finish the restoration of the post-production facility at 807 Esplanade, New Orleans). We have primarily depended upon financing arrangements tied to specific motion pictures for the funding of our productions. Given the tightening of credit markets, we are seeking to establish a credit facility to provide us with more flexibility in the funding of our productions or operations. We cannot assure you that we can secure a credit facility or that, if we secure a credit facility, the terms will be favorable to us. Without a credit facility,

we will not have the same flexibility with our financing arrangements as some of our competitors and will need to continue to rely upon financing arrangements tied to specific motion pictures for the funding of our productions.

We face risks from doing business internationally.

We distribute motion pictures outside the United States through third-party licensees and derive revenues from these sources. As a result, our business is subject to certain risks inherent in international business, many of which are beyond our control. These risks include:

laws and policies affecting trade, investment and taxes, including laws and policies relating to the repatriation of funds and withholding taxes, and changes in these laws,

changes in local regulatory requirements, including restrictions on content,

differing cultural tastes and attitudes,

differing degrees of protection for intellectual property,

financial instability and increased market concentration of buyers in foreign television markets, including in European pay television markets,

the instability of foreign economies and governments and

war and acts of terrorism.

Events or developments related to these and other risks associated with international trade could adversely affect our revenues from non-U.S. sources, which could have a material adverse effect on our business, financial condition and results of operations.

Amendments to current laws and regulations governing our operations could have a material adverse impact on our business.

Our operations are subject to substantial government regulation, particularly regulations governing the use of tax credits granted during film production in Louisiana, the United Kingdom, Canada and Hungary. We receive a substantial portion of the financing for our motion picture production from tax credits and other tax-preferred financings. Amendments to current laws and regulations governing these tax credits or other aspects of our business, including intellectual property and censorship laws, could increase our costs of operations, reduce our revenues, jeopardize the ownership of certain assets or increase the cost of financing our motion pictures. Tax regulations, intellectual property laws or other rules and regulations affecting our business may be changed in a manner which may adversely affect us and our ability to operate our business plan.

The production of a larger budget motion picture may adversely affect our operating results.

Historically, we have primarily produced motion pictures with budgets of between \$2 million and \$15 million. We may occasionally produce a motion picture with a larger budget of between \$30 million and \$50 million. To produce such a motion picture, we believe that we will need to co-produce such motion pictures with major studios and ensure a studio-wide release and a commitment to cover prints and advertising (“P&A”) costs or with one or more other independent production companies. To date, we have not produced or co-produced a motion picture with a budget in that range. We cannot assure you that we can successfully produce and distribute motion pictures in that budgetary range, that we can find a major studio to co-produce such motion pictures or that we can secure a studio-wide release or a commitment from a studio to cover P&A costs.





### Risks Relating to the Motion Picture Industry

Our success depends on the commercial success of motion pictures, which is unpredictable. Operating in the motion picture industry involves a substantial degree of risk. Each motion picture is an individual artistic work, and inherently unpredictable audience reactions primarily determine commercial success. Generally, the popularity of our motion pictures depends on many factors, including public reception, the formats of their initial releases, for example, theatrical or direct-to-video, the actors and other key talent, their genre and their specific subject matter. The commercial success of our motion pictures also depends upon the quality and acceptance of motion pictures that our competitors release into the marketplace at or near the same time, critical reviews, the availability of alternative forms of entertainment and leisure activities, general economic conditions and other tangible and intangible factors, many of which we do not control and all of which may change. We cannot predict the future effects of these factors with certainty, any of which factors could have a material adverse effect on our business, results of operations and financial condition.

In addition, because a motion picture's performance in ancillary markets, such as home video and pay and free television, is often directly related to its box office performance or television ratings, poor box office results or poor television ratings may negatively affect future revenue streams. Our success will depend on the experience and judgment of our management to select and develop new investment and production opportunities. We cannot assure you that our motion pictures will obtain favorable reviews or ratings, or that our motion pictures will perform well at the box office or in ancillary markets. The failure to achieve any of the foregoing could have a material adverse effect on our business, results of operations and financial condition.

Changes in the United States, global or regional economic conditions could adversely affect the profitability of our business. The current severe decrease in economic activity in the United States or in other regions of the world in which we do business could adversely affect demand for our films, thus reducing our revenue and earnings. A decline in economic conditions could reduce performance of our theatrical, television and home entertainment releases. In addition, an increase in consumer costs generally, or consumer costs in a particular sector of the entertainment industry, could result in a shift in consumer demand away from the entertainment we offer, which could also adversely affect our revenues and, at the same time, increase our costs.

Distributors' failure to promote our programs may adversely affect our business. Licensed distributors' decisions regarding the timing of release and promotional support of our motion pictures and related products are important in determining the success of these pictures and products. We do not control the timing and manner in which our licensed distributors distribute our motion pictures. Any decision by those distributors not to distribute or promote one of our motion pictures or related products or to promote our competitors' motion pictures or related products to a greater extent than they promote ours could have a material adverse effect on our business, results of operations and financial condition.

We could be adversely affected by strikes, potential strikes or other union job actions. We directly or indirectly depend upon highly specialized union members who are essential to the production of motion pictures. A strike by, or a lockout of, one or more of the unions that provide personnel essential to the production of motion pictures could delay or halt our ongoing production activities. In November 2007, the members of the Writer's Guild of America went on strike, and a new agreement was not approved until February 2008. Additionally, the Directors Guild of America and Screen Actors Guild ("SAG") collective bargaining agreements expired in 2008. An agreement has now been reached with the Directors Guild and SAG. A SAG or other union strike or action, depending on the length of time, could cause a delay or interruption in our production and release of new motion pictures, which could have a material adverse effect on our business, results of operations and financial condition.

Almost all financing of the production of motion pictures by independent production companies involves third parties providing film production completion bonds to guarantee the repayment of the financings upon the abandonment of production if certain conditions are met. Such film completion bonds do not provide for the repayment of the financing if a production is abandoned due to a strike. Without such waivers and in view of a potential strike, there may be dramatically less financing of the production of motion pictures by independent production companies as it will be difficult or impossible to obtain a film production completion bond, and it may be too risky to start films where production could be interrupted by a strike.

We face substantial competition in all aspects of our business.

We are smaller and less diversified than many of our competitors. As an independent distributor and producer, we constantly compete with major U.S. and international studios and independent producers and distributors. Most of the major U.S. studios are part of large diversified corporate groups with a variety of other operations, including television networks and cable channels, which can provide both the means of distributing their products and stable sources of earnings that may allow them better to offset fluctuations in the financial performance of their motion picture operations. In addition, the major studios and larger independent producers and distributors have more resources with which to compete for ideas, storylines and scripts created by third parties as well as for actors, directors and other personnel required for production. The resources of the major studios and larger independent producers and distributors may also give them an advantage in acquiring other businesses or assets, including film libraries, that we might also be interested in acquiring. Our inability to compete successfully could have a material adverse effect on our business, results of operations and financial condition.

The motion picture industry is highly competitive and at times may create an oversupply of motion pictures in the market. The number of motion pictures released by our competitors may create an oversupply of product in the market, reduce our share of box office receipts and make it more difficult for our films to succeed commercially. Oversupply may become most pronounced during peak release times, such as school holidays and national holidays, when theater attendance is expected to be highest. For this reason, and because of our more limited production and advertising budgets, generally provided by third party distributors, we typically do not release our films during peak release times, which may also reduce our potential revenues for a particular release. Moreover, we cannot guarantee that we can release all of our films when they are otherwise scheduled. In addition to production or other delays that might cause us to alter our release schedule, a change in the schedule of a major studio may force us to alter the release date of a film because we cannot always compete with a major studio's larger promotion campaign. Any such change could adversely impact a film's financial performance. In addition, if we cannot change our schedule after such a change by a major studio because we are too close to the release date, the major studio's release and its typically larger promotion budget may adversely impact the financial performance of our film. The foregoing could have a material adverse effect on our business, results of operations and financial condition.

The limited supply of motion picture screens compounds this product oversupply problem. Currently, a substantial majority of the motion picture screens in the U.S. typically are committed at any one time to only ten to fifteen films distributed nationally by major studio distributors. In addition, as a result of changes in the theatrical exhibition industry, including reorganizations and consolidations and the fact that major studio releases occupy more screens, the number of screens available to us when we want to release a picture may decrease. If the number of motion picture screens decreases, box office receipts, and the correlating future revenue streams, such as from home video and pay and free television, of our motion pictures may also decrease, which could have a material adverse effect on our business, results of operations and financial condition.

DVD sales have been declining, which may adversely affect our growth prospects and results of operations.

Several factors, including weakening economic conditions, the deteriorating financial condition of major retailers, the maturation of the DVD format, increasing competition for consumer discretionary spending and leisure time, piracy and increased competition for retailer shelf space, are contributing to an industry-wide decline in DVD sales both domestically and internationally. The high definition format war between the HD DVD and Blu-ray formats ended in February 2008 with Toshiba Corporation's announcement of its decision to discontinue its HD DVD businesses, however; reduced consumer discretionary spending in a challenging economic environment, may slow widespread adoption of the Blu-ray format or lead consumers to forego adopting a high definition DVD format altogether, which would adversely affect DVD sales. DVD sales also may be negatively affected as consumers increasingly shift from consuming physical entertainment products to digital forms of entertainment. The motion picture industry faces a

challenge in managing the transition from physical to electronic formats in a manner that continues to support the current DVD business and its relationships with large retail customers and yet meets the growing consumer demand for delivery of motion pictures in a variety of electronic formats. We cannot assure you that home video wholesale prices can be maintained at current levels, due to aggressive retail pricing, digital competition and other factors. In addition, in the event of a protracted economic downturn, reduced consumer discretionary spending could lead to further declines in DVD sales. A decline in DVD sales may have a disproportionate effect on us and our results of operations as a number of our releases only have a limited theatrical release or are released direct-to-DVD.

We must successfully respond to rapid technological changes and alternative forms of delivery or storage to remain competitive.

Advances in technologies or alternative methods of product delivery or storage or certain changes in consumer behavior driven by these or other technologies and methods of delivery and storage could have a negative effect on our business. Examples of such advances in technologies include video-on-demand, new video formats and downloading and streaming from the internet. An increase in video-on-demand could decrease home video rentals. Similarly, further increases in the use of portable digital devices that allow users to view content of their own choosing while avoiding traditional commercial advertisements could adversely affect our revenues. Other larger entertainment distribution companies will have larger budgets to exploit these growing trends. We cannot predict how we will financially participate in the exploitation of our motion pictures through these emerging technologies or whether we have the right to do so for certain of our library titles. If we cannot successfully exploit these and other emerging technologies, it could have a material adverse effect on our business, results of operations and financial condition.

Protecting and defending against intellectual property claims may have a material adverse effect on our business.

Our ability to compete depends, in part, upon successful protection of our intellectual property. We do not have the financial resources to protect our rights to the same extent as major studios. We are not a member of the Motion Picture Association of America (“MPAA”) as are the major studios and as a result we cannot rely on MPAA resources to prevent piracy and copyright infringements. We attempt to protect proprietary and intellectual property rights to our productions through available copyright and trademark laws and licensing and distribution arrangements with reputable international companies in specific territories and media for limited durations. Despite these precautions, existing copyright and trademark laws afford only limited practical protection in certain countries. We also distribute our products in other countries in which there is no copyright or trademark protection. As a result, it may be possible for unauthorized third parties to copy and distribute our productions or certain portions or applications of our intended productions, which could have a material adverse effect on our business, results of operations and financial condition.

Litigation may also be necessary in the future to enforce our intellectual property rights, to protect our trade secrets, or to determine the validity and scope of the proprietary rights of others or to defend against claims of infringement or invalidity. Any such litigation could result in substantial costs and the diversion of resources and could have a material adverse effect on our business, results of operations and financial condition. We cannot assure you that infringement or invalidity claims will not materially adversely affect our business, results of operations and financial condition. Regardless of the validity or the success of the assertion of these claims, we could incur significant costs and diversion of resources in enforcing our intellectual property rights or in defending against such claims, which could have a material adverse effect on our business, results of operations and financial condition.

Others may assert intellectual property infringement claims against us.

One of the risks of the film production business is the possibility that others may claim that our productions and production techniques misappropriate or infringe the intellectual property rights of third parties with respect to their previously developed films, stories, characters, other entertainment or intellectual property. We may receive in the future claims of infringement or misappropriation of other parties’ proprietary rights, although we have had to date been served with only one such claim which was settled on favorable terms. Any such assertions or claims may materially adversely affect our business, financial condition or results of operations. Irrespective of the validity or the successful assertion of such claims, we could incur significant costs and diversion of resources in defending against them, which could have a material adverse effect on our business, financial condition or results of operations. If any claims or actions are asserted against us, we may seek to settle such claim by obtaining a license from the plaintiff covering the disputed intellectual property rights. We cannot assure you, however, that under such circumstances a

license, or any other form of settlement, would be available on reasonable terms or at all.

Our business involves risks of liability claims for media content, which could adversely affect our business, results of operations and financial condition.

As a licensor of media content, we may face potential liability for:

defamation,

invasion of privacy,

negligence,

copyright or trademark infringement (as discussed above), and

other claims based on the nature and content of the materials distributed.

These types of claims have been brought, sometimes successfully, against producers and licensors of media content. Any imposition of liability that is not covered by insurance or is in excess of insurance coverage could have a material adverse effect on our business, results of operations, and financial condition.

Piracy of motion pictures, including digital and internet piracy, may reduce the gross receipts from the exploitation of our films.

Motion picture piracy is extensive in many parts of the world and is made easier by technological advances and the conversion of motion pictures into digital formats. This trend facilitates the creation, transmission and sharing of high quality unauthorized copies of motion pictures in theatrical release, on videotapes and DVDs, from pay-per-view through set top boxes and other devices and through unlicensed broadcasts on free television and the internet. The proliferation of unauthorized copies of these products has had and will likely continue to have an adverse effect on our business, because these unauthorized pirated copies reduce the revenue we receive from our products. Additionally, to contain this problem, we may have to implement elaborate and costly security and anti-piracy measures, which could result in significant expenses and losses of revenue. We cannot assure you that even the highest levels of security and anti-piracy measures will prevent piracy.

In particular, unauthorized copying and piracy are prevalent in countries outside of the United States, Canada and Western Europe, whose legal systems may make it difficult for us to enforce our intellectual property rights. While the U.S. government has publicly considered implementing trade sanctions against specific countries that, in its opinion, do not make appropriate efforts to prevent copyright infringements of U.S. produced motion pictures, we cannot assure you that any such sanctions will be enacted or, if enacted, will be effective. In addition, if enacted, such sanctions could impact the amount of revenue that we realize from the international exploitation of motion pictures. If no embargoes or sanctions are enacted, or if other measures are not taken, we may lose revenue as a result of motion picture piracy.

There is a potential for disputes and litigation in the motion picture business.

There are risks of disputes and litigation with financiers, competitors, putative rights owners, unions, producers and other talent, and with distributors. We cannot assure you that we will prevail in the event of any disputes or litigation. We have failed to prevail in an arbitration regarding 9 ½ Weeks II, which could result in payment of as much as approximately \$1,000,000 of which \$800,000 was accrued by Seven Arts as of June 30, 2011 with the balance to be paid by an affiliate. This arbitration result was made by default in a proceeding involving a motion picture not produced by us and related to legal fees assessed against us. The difference in our accrual and the accruals



claimed by the claimant in their proceeding related to interest accrued on the arbitration award prior to the date we were held responsible for the award.

### Risks Relating to the Group's Shares

We have not paid dividends to date and do not intend to pay any dividends in the near future.

We have never paid dividends on our common stock and presently intend to retain any future earnings to finance the operations of our business. You may never receive any dividends on our shares.

The exercise of stock options, the conversion of redeemable debentures, or preference shares or the later sales of our common stock may further dilute your shares of common stock.

We have 136,000 stock options that have not been exercised, issued redeemable debentures with no redemption date convertible into a maximum of 280,000 shares. We also have approximately \$300,000 of convertible debentures due before the end of 2011. The due balance remaining on the Trafalgar debenture is convertible into approximately 500,000 shares at the current trading price of our shares of common stock, representing payment of the remaining balances of the Trafalgar debentures at the median price on the date of this document. The balance of the Trafalgar debenture may be paid in cash but, if not, can be converted at the volume weighted average price of our common stock on the date of conversion. The conversion is only at the option of the Group.

Our Board of Directors is authorized to sell additional ordinary shares or securities convertible into common stock, if in their discretion they determine that such action would be beneficial to us. Any such issuance below the offering price of the common stock in this prospectus would dilute the interest of persons acquiring shares of common stock in this offering.

Our articles and by-laws provide indemnification for officers, directors and employees.

Our governing instruments provide that officers, directors, employees and other agents and their affiliates shall only be liable to our Group for losses, judgments, liabilities and expenses that result from the negligence, misconduct, fraud or other breach of fiduciary obligations. Thus certain alleged errors or omissions might not be actionable by us. The governing instruments also provide that, under the broadest circumstances allowed under law, we must indemnify our officers, directors, employees and other agents and their affiliates for losses, judgments, liabilities, expenses and amounts paid in settlement of any claims sustained by them in connection with our Group, including liabilities under applicable securities laws.

The trustees of the Seven Arts Employee Benefit Trust may exercise its discretion to our detriment.

The trustees of the Seven Arts Employee Benefit Trust own approximately 200,000 of our shares of common stock as at September 2011 and have the power to dispose of those shares for the benefit of the beneficiaries of the Employee Benefit Trust. Exercise of such power to sell our shares could adversely affect the market for our shares on NASDAQ or could result in acquisition of such shares by third parties, who may seek control of our assets.

Our share price may be volatile, and you may not be able to sell your ordinary shares at or above the public offering price.

The stock market in general, and the market for motion picture stocks in particular, has experienced extreme price and volume fluctuations. These broad market and industry fluctuations may adversely affect the market price of our ordinary shares, irrespective of our actual operating performance. Additional factors which could influence the market price of our ordinary shares include statements and claims made by us and other participants in our industry and public officials. The public offering price for the ordinary shares may not be above that which will subsequently prevail in the market.

If large amounts of our shares held by existing shareholders are sold in the future, the market price of our ordinary shares could decline.

The market price of our ordinary shares could fall substantially if our existing shareholders or existing creditors who levy on or convert into one ordinary share sell large amounts of our ordinary shares in the public market following this offering. These sales, or the possibility that these sales may occur, could also make it more difficult for us to sell equity or equity-related securities if we need to do so in the future to address then-existing financing needs. U.S. federal securities laws requiring the registration or exemption from registration in connection with the sale of securities limit the number of ordinary shares available for sale in the public market. In addition, lock-up agreements that restrict us, our directors and officers and certain of our existing shareholders from selling or otherwise disposing of any ordinary shares for a period of 180 days after the date of this prospectus without the prior written consent of the underwriters' representative also restrict sales of our ordinary shares. The underwriters' representative may, however, in its sole discretion and without notice, release all or any portion of the ordinary shares from the restrictions in the lock-up agreements.

## ITEM 4. INFORMATION ON THE GROUP

### 4.A. History and Development of the Group

#### Introduction

Seven Arts' executive offices are located at:

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Website: [www.7artspictures.com](http://www.7artspictures.com)

Email: [info@7artspictures.com](mailto:info@7artspictures.com)

The contact person is: Peter M. Hoffman, CEO.

Seven Arts' fiscal year ends June 30.

The Group's ordinary shares have traded in the past five years on several different markets. Starting in February of 2009, Seven Arts' shares have been quoted on the NASDAQ Capital Market under the symbol "SAPX". Starting in March of 2008 and continuing until February 12, 2009, the Group's shares had been quoted on the Over-the-Counter Bulletin Board under the symbol "SAPxf". The Group's ordinary shares traded on the Alternative Investment Market in London, England from September 2004 until February 2007 under the symbol "SAPP". Ordinary shares of the Group were listed on the PLUS Market in London, England starting in April 2007 under the symbol "SAPP". The Group notified its shareholders of the decision to de-list the Group's ordinary shares from the PLUS Market on February 25, 2009 and this de-listing was approved by the shareholders at an extraordinary general meeting on March 16, 2009 and the de-listing was effective on March 24, 2009.

The authorized capital of Seven Arts consists of 20,527,360 ordinary shares par value of £0.25 each, and 13,184,000 deferred shares of £0.45 each and 6,000,000 convertible redeemable preference shares of £1.00 each.

According to the Group's register on June 30, 2011, there were 2,643,131 ordinary shares of £0.25 each, and 2,268,120 deferred shares of £1 and 13,184,000 deferred shares of £0.45 each.

On May 9 2011 the shareholders approved a 1:5 reverse split and then the division of the new share into £0.25 ordinary share and £1.00 deferred share. All per share amounts in the financial statements have been retroactively adjusted to the earliest period presented for the effect of this reverse split.

In the fiscal year ended June 30, 2011 the Group issued an aggregate of 1,147,671 shares of ordinary stock comprised of:

- a) 342,000 shares issued to consultants in exchange for services rendered
- b) 153,000 shares issued to Trafalgar Capital Specialized Investment Fund pursuant to an amended loan agreement and 100,000 issued to Eden Corporate Finance in part payment of their debt
- c) 53,668 shares issued to Asher Enterprises in exchange for conversion of notes payable in the aggregate amount of \$200,000.
- d) Pledges of stock issued to SAP Inc. (23,800) for an insurance policy, New Moon LLC (150,000) pledged against Armadillo's debt, Palm Finance (150,000) and TCA (175,000) pledged against a loan of \$125,000 given to the Company in March 2011.

In the year ended June 30, 2010 the Group issued an aggregate of 110,000 shares of ordinary stock comprised of:

- a) 80,000 shares issued to the EBT on conversion of 500,000 convertible preferred shares. The EBT conversion resulted in an addition of \$149,620 to the share capital account and \$1,390,180 to the additional paid in capital account and a reduction of \$1,539,800 in the carrying value of the preferred shares in the capital account.
- b) 2,000 share options were converted to 10,000 ordinary shares by a former employee. As the excess 8,000 ordinary shares were issued in error, a related party (SAP Inc.) has promised to advance and pledge 8,000 of its shares of Seven Arts Pictures Plc. to the Group until it can arrange for the cancellation of these shares and replace with the correct shares to be issued and sent to the former employee. As of June 30, 2010 the Group had not received these shares.
- c) 20,000 shares were issued to Eden Finance to cover loan, interest and fees in April 2010.

#### Incorporation and Name Changes

The Group was incorporated as Glasgow Park Investments PLC on August 24, 2001, under the English Group Act of 1985. Pursuant to a resolution passed at a meeting of the shareholders of the Group that was held on September 11, 2001, the Group changed its name from Glasgow Park Investments PLC to The Cabouchon Collection PLC. Pursuant to a resolution passed at a meeting of the shareholders of the Group that was held on November 6, 2003, the name of the Group was changed to Cabouchon PLC. Pursuant to a resolution passed at a meeting of the shareholders of the Group that was held on September 2, 2004, the name of the Group was changed to Seven Arts Pictures PLC, at the time all motion picture business assets of Seven Arts Pictures Inc. were transferred to a subsidiary of the Group (Seven Arts Filmed Entertainment Limited) pursuant to an Asset Transfer Agreement in exchange for ordinary shares of the Group. Documents concerning the Group which are referred to herein may be inspected during regular hours at the Group's Los Angeles affiliate office located at 1801 Century Park East., Suite 1830, Los Angeles, CA 90067 U.S.A.

On June 11, 2010, our shareholders approved the transfer of all of our assets, underlying the ordinary shares of our subsidiaries to a newly formed Nevada corporation, Seven Arts Entertainment Inc. ("SAE"), which will be the new holding company for all operations described herein subject to a proposed registration. Membership on NASDAQ and issuance of ordinary shares of SAE occurred on August 31, 2011. We do not believe that this redomiciling will have any material effect on the Group's business or operation, except that all the assets and liabilities of Seven Arts Pictures plc (including ownership of certain subsidiaries) have been transferred to SAE, and shareholders of PLC will receive one share of common stock of SAE for each ordinary share of PLC they owned.

#### Financings

During the year ended March 31, 2005, we issued:

(A) £3,000,000, of convertible debt to Langley Park Investment Trust PLC (“Langley”) in return for 3,000,000 ordinary shares in Langley valued at approximately \$5,204,000, and

(B) Approximately £3,000,000 of convertible redeemable preference shares to Armadillo Investments plc (“Armadillo”) in return for 3,000,000 ordinary shares from Armadillo, valued at \$5,669,000.

We received cash in fiscal year 2005 of approximately \$2,232,000 through the sale of ordinary shares of Armadillo Investments plc (approximately \$1,302,000) and Langley Park Investment Trust PLC, (approximately \$930,000). The amounts that we received from the sale of a portion of our Armadillo shares and all of our Langley shares were substantially less than the stated value of the debenture and preference shares.

Langley converted £1,250,000 of its convertible debenture (£1,250,000 or approximately \$1,875,000) into 1,000,000 ordinary shares on March 15, 2007. The remaining convertible debt due to Langley is £1,750,000 (or approximately \$3,432,450) as of the date of this document.

The convertible redeemable preference shares held by Armadillo were acquired by the Seven Arts Employee Benefit Trust ("Trust") on October 30, 2008, and 2,500,000 of the preference shares were converted into 2,000,000 of Seven Arts Pictures Plc ordinary shares on November 20, 2008. The remaining 500,000 preference shares were converted into 400,000 ordinary shares on June 30, 2010. The convertible preference shares were originally issued at a value of £3,000,000 (approximately \$4,500,000). All the foregoing conversions were based on conversion at 25 pence (approximately \$0.375) for each ordinary share issued.

On December 2008, the Seven Arts Employee Benefit Trust acquired 3,000,000 of our convertible Preference Shares from Armadillo Investments Plc ("Armadillo") for £1,500,000, to be paid in three equal installments of £500,000 and the return to Armadillo of 1,600,000 ordinary shares of Armadillo, valued at £800,000, for an aggregate purchase price of £2,300,000. The agreed upon purchase price was to be loaned to the EBT by the Group valued at a nominal interest rate and to date the Group have advanced £500,000 as the first of the three equal installments, together with the 1,600,000 ordinary shares of Armadillo, valued at £800,000 in the Group's books, to the EBT, which has paid them over to Armadillo. The Group has guaranteed the EBT's remaining debt of £1,000,000 representing second and third installments, but has not yet advanced these amounts. The EBT has repaid £598,594 (\$1,035,167) of the £1,300,000 in the year ended June 30, 2011 by transferring ordinary shares owned by EBT to creditors of the Group. The Group charged interest £44,822 (\$71,966 USD) to EBT during the year ended June 30, 2011. The total balance due from the EBT to the Group as at June 30, 2011 amounted to £643,084 or \$1,237,417 USD. The EBT has transferred or sold 246,800 ordinary shares of the Group it owned and transferred the proceeds back to the Group.

## LOANS

Seven Arts Future Flow I ("SFF"), a limited liability Group owned by SAP Inc., one of our affiliates and a Group that is owned by Peter Hoffman, our Chief Executive Officer, obtained financing of \$8,300,000 (the "Arrowhead Loan") from Arrowhead Target Fund Ltd. ("Arrowhead") in February 2006, at an interest rate of 15% per annum. Although the loan is secured by certain assets of Seven Arts Future Flows I, LLC, we are not required to repay the Arrowhead Loan from any of our other assets or revenues.

The specific film assets which secure the Arrowhead Loan were our distribution rights in the following motion pictures: Asylum, Stander, I'll Sleep When I'm Dead, No Good Deed, Supercross, Popstar, Red Riding Hood, Johnny Mnemonic, Shattered Image, Never Talk to Strangers, The Hustle, and A Shot at Glory.

Our estimates of the amount of time it would take to repay the Arrowhead Loan from the proceeds of the film assets securing the loan have not been met. The Arrowhead Loan matured on February 15, 2009, and was then due in full. SFF received a default notice from Arrowhead to that effect, and as a result Arrowhead is now collecting directly all sums receivable by us with respect to these motion pictures and has appointed a new servicing agent for these motion pictures, with the result that we no longer control the licensing of these motion pictures. As a result of the foregoing, we have removed all investment and receivables related to the twelve motion pictures pledged to Arrowhead as assets and have removed all limited recourse indebtedness relating to these motion pictures as a liability.





The Arrowhead Target Fund Ltd (“Arrowhead”) filed an action on September 22, 2010 which seeks recovery from the Group of the monies which the Group has retained under its interpretation of the relevant agreements with Arrowhead. In addition, Arrowhead makes substantial additional claims against the Group, Mr. Hoffman and Seven Arts Pictures Inc. regarding claimed breaches of the terms of the operative agreements, including failure to properly account, failure to turn over materials, failure to remit monies collected, and similar matters. The claims against the Group for these breaches of warranties for damages are \$8,300,000 although Arrowhead states no basis for this amount. The Group had moved to dismiss the action against all defendants other than Seven Arts Future Flows I LLC, which is not part of the Group. On August 9, 2011, the New York Supreme Court granted the Group’s motion and dismissed all defendants except Seven Arts Filmed Entertainment Limited in its capacity as a collateral agent, which is not a material element of Arrowhead claim. The Group continues to believe that Arrowhead’s claims against the Group are without substantial merit.

We borrowed an aggregate of \$7,500,000 from (i) Arrowhead Consulting Group LLC (“ACG”) for \$1,000,000 (“ACG Loan”) and (ii) Cheyne Specialty Finance Fund L.P. (“Cheyne”) for \$6,500,000 (“Cheyne Loan”) in December 2006, secured by certain of our motion picture assets. The ACG Loan and Cheyne Loan bear interest at 19% and 18% per annum, respectively. The Cheyne Loan matured on April 2008, and a subsidiary acquired the Cheyne Loan plus interest thereon for \$6,500,000, and obtained an assignment of their senior position and subordination agreement with Arrowhead. The remaining ACG Loan of \$1,000,000 is now due. Our estimates of the amount of time it would take to repay the ACG Loan from the proceeds of the film assets securing the loan have not been met. In October 2008, we received a notice of default from ACG in connection with this loan. The ACG Loan is secured by Noise, Deal, Pool Hall Prophets, Boo, A Broken Life, and Mirror Wars and a second position security interest in the motion pictures listed above which are pledged to Arrowhead. ACG has now filed suit to collect the ACG Loan. See Legal Proceedings.

On October 15, 2008 the Group borrowed £1,000,000 from Trafalgar Capital Special Investment Fund (“Trafalgar”). A portion of this loan the Group advanced to the EBT for it to use as the first installment for the acquisition of all the Preference Shares owned by Armadillo. On September 2, 2009 the Group repaid Trafalgar \$1,000,000 (about £698,934) as a partial payment against this loan, with the remaining balance subject to repayment in cash or convertible to the ordinary shares of the Group at the conversion terms as agreed between Trafalgar and the Group. On June 22, 2010 an amended agreement was entered into with Trafalgar for an extension of the due date of the convertible debentures to December 31, 2010, and the Group agreed to issue 340,000 ordinary shares to settle a portion of the debt. Trafalgar agreed to reduce the loan amount from the proceeds it received from selling the 340,000 ordinary shares. The transaction was consummated subsequent to the date of the financial statements. Subsequent to June 30, 2010, a further amended agreement was entered into with Trafalgar for an extension of the due date of the convertible debentures to March 31, 2011, and the Group agreed to issue 425,000 ordinary shares to settle a portion of the debt (see subsequent events NOTE 20). Trafalgar agreed to reduce the loan amount from the proceeds it receives from selling the 425,000 ordinary shares. The per-share value is determined as the amount recovered by Trafalgar on sale thereof in the market and Trafalgar may “put” these shares to us at £1.00 per share on April 30, 2011, if not sold. This put option was not exercised by Trafalgar.

The Group has entered into two senior financing loan and security agreements with Palm Finance Corp (“Palm”) to finance the production costs of The Pool Boys, Autopsy and Nine Miles Down dated May 7, 2007 and December 17, 2007. These loans are secured by the revenues to be collected from these motion pictures. The revenues so far collected have been insufficient to repay the majority of these loans, primarily as result of management’s decision to delay the release of these films. We have entered into an agreement with Palm extending the due date of these loans to December 31, 2011. The original principal amount of the Palm loan for The Pool Boys and Autopsy are \$5,250,000 including \$500,000 accrued interest, and for Nine Miles Down was \$4,000,000 including \$750,000 accrued interest.

The Group has also entered into a financing agreement with Palm in November, 2010 to refinance the existing indebtedness secured by our production and post production facility in New Orleans, Louisiana under which Palm has acquired the existing credit facility of \$3,700,000 plus accrued interest of our affiliate SAP LA for \$1,000,000 and agreed to advance an additional \$1,850,000 to complete renovation and construction of this facility. Palm's advance and interest at the rate of 15% per annum are due and payable within five years and are secured by the property at 807 Esplanade Avenue in New Orleans ("Property") and Louisiana film infrastructure and historical rehabilitation credits, as well as Federal historical rehabilitation credits ("Credits") associated with the Property. See Our Business – Production.

The lender agreed to write off the accrued interest at the end of the year giving rise to forgiveness of debt income of \$2,669,717. The outstanding balance on these loans as at June 30, 2011 was \$4,910,052 (Pool Boys/Autopsy) and \$3,176,018 (Nine Miles Down).

Subsequent to the date of the financial statements the lender sold \$2,750,000 of his debt and converted 50% of the monies received to Series A preference shares in SAE Inc.

On August 27, 2007, we borrowed \$1,650,000 from Blue Rider Financial (“Blue Rider”) to pay for the domestic prints and advertising costs for the motion picture Deal (“Blue Rider Loan”) and arranged that the revenues due from Metro-Goldwyn-Mayer Studios Inc. (“MGM”) to us for the distribution of that motion picture be assigned to Blue Rider Financial as partial security for that loan. To date the revenues paid to us from MGM have not been sufficient to repay the Blue Rider Loan. We have therefore entered into an accommodation agreement with Blue Rider to redeem the loan due for \$2,200,000, less approximately \$812,000 of collections that have been received by Blue Rider to date from MGM. We anticipate this indebtedness will be repaid from proceeds due from MGM on or before December 31, 2011.

On August 30, 2010, the Group issued an aggregate of \$470,000 Convertible Debt to qualified investors that mature on February 28, 2011. The Convertible Debts bear interest at a rate of 15.0% per annum and could be converted into the Group’s ordinary shares beginning on the date which is one hundred twenty (120) days following the issuance of the Convertible Debt, at the conversion rate of \$3.75 per share, subject to certain changes.

On March 22, 2011, an additional 300,000 convertible notes were issued to Runway Investments Ltd on the same terms as above. At the same time the original notes were extended to July 31 2011.

All \$770,000 of these notes were extended on May 24, 2011 to September 30, 2011, and the conversion terms were changed as follows:

- The Scarborough’s note’s principal and interest to convert into common stock its principal and interest now at \$0.50 per share.
- For extending the maturity date until December 31, 2011, Sendero and Runway will reduce their conversion price to \$0.60 per share.
- For extending the maturity date until September 30, 2011, Agua Alta will reduce its conversion price to \$0.75 per share.
- The average conversion price of the three remaining notes is \$0.64 per share.

\$225,000 of the Scarborough notes were converted to 507,000 shares on July 29, 2011.

\$170,000 Agua Alta and \$75,000 Sendero notes were converted into 1,786,374 shares on October 19, 2011.

In May and June 2010 the Group issued \$150,000 of its convertible notes and additional \$50,000 in September 2010 to Asher Enterprises which were due on or before March and June 2011 and which are convertible into the Group’s ordinary stock at a discount to the volume weighted average price of the Group’s ordinary shares on conversion with certain reset provisions. The notes were all converted by December 31, 2010.

The Group had entered into an agreement with BRG Investments, LLC (“BRG”), an affiliate of Fletcher Asset Management (“Fletcher”), for the investment by BRG of up to \$30,000,000 in preferred stock of Seven Arts and the formation of a joint venture (“Venture”).



BRG purported to cancel the agreement in May 2011.

Seven Arts settled this issue on October 5, 2011, whereon the Company arranged a mutually acceptable settlement of its dispute with Fletcher arising out of an investment agreement purported terminated by Fletcher as we announced on June 7, 2011 in a press release. In the settlement with Fletcher, the Company waived all claims against Fletcher. Fletcher agreed to acquire and did acquire 250,000 shares of our common stock at a price of \$1.00 per share. Fletcher received a warrant to buy an additional 100,000 shares at \$1.00, Fletcher has the right within six months to buy an additional 250,000 shares of our common stock based on a volume weighted average price but no less than \$1.00 or more than \$1.50, and if it buys these shares, Fletcher will receive an additional warrant to buy an additional 100,000 shares of our common stock on the same terms as the warrant we have issued. Seven Arts intends to use the proceeds of this transaction to partially fund its next motion picture production in Louisiana entitled Schism, written and to be directed by Adam Gierasch, the director of Autopsy and Night of the Demons, two recent releases by the Company.

We currently borrow funds for the financing of each of our motion pictures from several banks and other production lenders. There can be no assurances given that the Group will be able to borrow funds to finance our motion pictures in the future. We are currently seeking a revolving credit facility for the financing of our future motion picture productions. Our cash flow is derived from license fees earned from the delivery and distribution of our motion pictures in the United States and territories around the world.

#### 4.B. Business Overview

SAP Inc. was incorporated in Nevada in October 2002 and acquired control of the Group in September 2004 through an Asset Transfer Agreement under which SAP Inc. transferred all its motion picture assets to a subsidiary of Group for ordinary share of the Group. The predecessor Group to SAP Inc. was CineVisions, a California corporation founded in 1992, and Seven Arts Pictures Limited (“SAPL”), a UK corporation, which was founded in 2000 by Chief Executive Officer and Director Peter Hoffman. Both were created respectively to produce and distribute independent motion pictures, and to provide consulting and financing services within the industry. Upon formation of Seven Arts, motion picture assets previously held by CineVisions and SAPL, including interests in 18 completed films (including the Fireworks Pictures included below) and expenditures on projects in development were transferred to the Group.

Between 1996 and 1998, CineVisions successfully produced and distributed four motion pictures, including:

Table 6A: Films Produced and Distributed from 1996-1998\*

| Film Title              | Budget   | Talent  |
|-------------------------|----------|---|
| Johnny Mnemonic         | \$ 24.5M | Cast: Keanu Reeves, Dolph Lundgren, Ice T<br>Director: Robert Longo<br>Writer: William Gibson |
| Never Talk To Strangers | \$ 11.7M | Cast: Rebecca De Mornay, Antonio Banderas, Dennis Miller<br>Director: Sir Peter Hall          |
| 9 1/2 Weeks II          | \$ 12M   | Cast: Mickey Rourke, Angie Everhart<br>Director: Anne Goursaud                                |
| Shattered Image         | \$ 7.25M | Cast: Anne Parillaud, William Baldwin   |

Director: Raul Ruiz

Producer: Barbet Schroeder, Lloyd Silverman

\*Ownership interests in these films were transferred to SAP Inc. on October 1, 2002. All interest in 9 ½ Weeks II was transferred by court order (under appeal) to a rights owner.

On or about September 1998, SAPL entered into a joint venture agreement for the production and distribution of motion pictures with Fireworks Pictures, Inc. ("Fireworks") a subsidiary of CanWest Global Entertainment, Inc., a large diversified Canadian media Group with interests in broadcasting and newspapers. Pursuant to that joint venture, Fireworks and SAPL have produced or acquired and distributed 11 motion pictures (the "Fireworks Pictures"), including certain motion pictures described below. SAPL's interest in the Fireworks Pictures (but no liability) and all of the CineVisions pictures were transferred to the Group in September 2004, pursuant to an Asset Transfer Agreement with a subsidiary of the Group in exchange for the Group's ordinary shares.

Through SAPL, Mr. Hoffman successfully produced and acquired the following films with Fireworks:

Table 6B: Films Produced and Acquired by SAPL and Fireworks<sup>1, 2</sup>

<sup>1</sup> See "Risk Factors" on Fireworks litigation.

<sup>2</sup> SAPL ownership interests in these films were transferred to SAP Inc. on October 1, 2002, and to Seven Arts in September 2004.

| Film Title        | Budget   | Talent  |
|-------------------|----------|---|
| Onegin            | \$ 15.0M | Cast: Ralph Fiennes, Liv Tyler<br>Director: Martha Fiennes<br>Writer: Michael Ignatieff, Peter Eitedgui   |
| The Believer (3)  | \$ 3.0M  | Cast: Ryan Gosling, Billy Zane<br>Writer/Director: Henry Bean   |
| American Rhapsody | \$ 3.5M  | Cast: Nastassja Kinski, Tony Goldwyn, Scarlett Johansson<br>Writer/Director: Eva Gardos                   |
| Cletis Tout       | \$ 15.0M | Cast: Christian Slater, Tim Allen, Portia DeRossi, Richard Dreyfuss<br>Director: Chris Ver Weil           |
| Interstate 60     | \$ 10.0M | Cast: James Marsden, Kurt Russell, Amy Smart, Gary Oldman<br>Director: Bob Gale<br>Writer: Chris Ver Weil |

Through SAPL, Mr. Hoffman co-financed three additional motion pictures in conjunction with Fireworks and Paramount. These pictures include:

Table 6C: Films Produced and Acquired by SAPL <sup>1</sup> and Fireworks <sup>2</sup>

<sup>1</sup> SAPL ownership interests in these films were transferred to SAP Inc. on October 1, 2002, and to Seven Arts in September 2004.

<sup>2</sup> See "Risk Factors" on Fireworks litigation.





| Film Title          | Budget   | Talent   |
|---------------------|----------|--|
| Rules of Engagement | \$ 52.0M | Cast: Tommy Lee Jones, Samuel Jackson<br>Director: William Friedkin<br>Writer: Stephan Gagan, James Webb |
| Rat Race            | \$ 55.0M | Cast: Cuba Gooding Jr., Rowan Atkinson<br>Director: Jerry Zucker   |
| Hardball            | \$ 47.0M | Cast: Keanu Reeves<br>Writer/Director: Brian Robbins   |

#### Completed Films.

In total the Group and its predecessors have produced or acquired interest in the 33 feature films to date described below in Table 8, exclusive of the Fireworks Pictures. The Group owns (directly or through grants of all rights in perpetuity) the copyright to each picture designated as "CR" in Table 8 and for all other pictures in Table 8 own the distribution rights for at least all territories outside the United States and Canada for no less than 15 years.

#### Production.

Since 1996, we and our predecessors have developed, financed, produced, and licensed 16 motion pictures, primarily with budgets in range of \$2 million to \$15 million, for domestic and international markets. Most of our pictures have either received only limited theatrical releases or were released directly to post-theatrical markets, primarily DVD. We may produce the occasional higher cost motion picture (production budgets of \$30 - \$50 million), and if we do so, we will most likely choose to co-produce any such project with a major studio if they guarantee a studio-wide release and provide a commitment to cover a portion or all of P&A costs or with one or more other independent production companies. The number of pictures that we are able to produce and the size of the budget of those films depend upon the funds available to us.

We receive between 50 and 100 submissions of potential film projects or completed films every year, which generally include a "package" of a screenplay and certain talent elements (e.g. producer, director and cast). In certain limited cases, we will arrange for the creation of a screenplay and the "packaging" of creative elements. We commission independent production budgets of certain projects to evaluate the project's suitability for production or distribution. The pictures we produce are selected according to several key criteria formulated to maximize the profit potential of our films, including the potential to license the worldwide distribution rights to the film for an amount greater than the projected production budget (e.g. a minimum profit margin of at least 20%), the potential for the film to be widely accepted as a "quality" or "good" film, whether the key creative talent, including directors and two most prominent cast members, are likely to be both responsible and artistically gifted in creating the motion picture. There are no "rules" or specific strategic limitations on our choice of motion pictures to produce. The decision to move forward with a project is our Chief Executive Officer's decision based on highly subjective factors. However, we believe that the vast experience of our management team is critical to this decision-making process. We will, however, only consider a motion picture with a production cost in excess of \$15,000,000 if we are able to manage the risks of production through "pre-sales" or equity contribution to production of that picture.

In 2007, Seven Arts Pictures Louisiana LLC ("SAPLA"), a subsidiary of SAP Inc., acquired real property in New Orleans, Louisiana, which they are in the process of developing as a production and post production facility for motion pictures in Louisiana. Over the past five years, Louisiana has become a popular destination for the production

of motion pictures due to very favorable tax incentives. Since 2005, we have produced five motion pictures under the Louisiana Motion Picture Incentive Act (the “Louisiana Incentives”), which provides substantial transferable tax credits for film production activities in Louisiana accredited to us whether we produce or acquire a motion picture. The Louisiana Incentives provide generally that the producer will receive both a 25% (now 30%) transferable investment tax credit on all film expenditures on Louisiana vendors and a 10% (now 5%) transferable labor tax credit on all expenditures for labor performed in Louisiana by Louisiana residents. We generally obtain loans during production of a motion picture in Louisiana secured by these tax credits after a “pre-certification” by the Louisiana Film Office that the applicable motion picture qualifies for the Louisiana Incentives. We are then able to transfer these tax credits at a discount to third parties upon completion of the motion picture, audit by independent accountants of the applicable expenditures and “certification” by the Louisiana Film Office of tax credits payable based on the audited expenditures. We use the proceeds from the transfer of the tax credits to third parties to repay the loan secured by the tax credits, at which time the lender releases its security interest in the tax credits.

We are able to obtain similar refundable (but not transferable) tax credits arising from film production expenditures in the United Kingdom, Canada, Ireland, Italy and Hungary which offer refundable tax credits for production expenditures in each of their territories.

We expect the post production facility in Louisiana will open for operation by early 2012. When completed, we anticipate that this facility will be leased to our motion picture productions in Louisiana and to other motion picture productions produced by unrelated parties. In accordance with the Inter-Group Agreements any and all such engagements with the Group will provide no profit to our affiliates and we will pay only out of pocket costs incurred by our affiliates with no mark-up. SAPLA secured a credit facility in the aggregate principal amount of \$3,700,000, which has been used to acquire and begin the improvements on the property. This credit facility carries an annual interest rate of 2% plus the Prime Rate as published in The Wall Street Journal. We have guaranteed the amounts that SAPLA borrows under this facility and no additional consideration is provided for this guarantee beyond the existing agreement between SAPLA and us.

We have also entered into a new financing agreement with Palm in November, 2010 to refinance the existing indebtedness secured by our production and post production facility in New Orleans, Louisiana under which Palm has acquired the existing credit facility of \$3,700,000 plus accrued interest of our affiliate SAPLA for \$1,000,000 and agreed to advance an additional \$1,800,000 to complete renovation and construction of this facility. Palm's advance and interest at the rate of 15% per annum are due and payable within five years and are secured by the property at 807 Esplanade Avenue in New Orleans ("Property") and Louisiana film infrastructure and historical rehabilitation credits, as well as Federal historical rehabilitation credits ("Credits") associated with the Property. See Our Business – Production.

We do not anticipate the use of any material amount of our working capital to complete and operate this facility, and we expect to realize substantial film production, film infrastructure, historic rehabilitation and other state and federal tax credits and other tax incentives from the acquisition, renovation, and operation of this property as a post production facility. In particular SAPLA anticipates approximately \$4,000,000 in Louisiana Film Infrastructure tax credits, \$3,000,000 in Louisiana State Rehabilitation tax credits and \$3,000,000 in Federal Historic Preservation tax credits will be available from expenditures in connection with our facility.

#### Distribution.

We license distribution rights in our motion pictures in the United States and in most foreign territories prior to and during the production or upon the acquisition of rights to distribute a picture. We share in the commissions generated by the sales of the pictures. Sale of a license to distribute a motion picture prior to its delivery is termed a "pre-sale" and may occur at any time during the development and production process. In a typical license agreement, we license a picture to a distributor before it is produced or completed for an advance from the licensee, which advance is recoverable by the distributor from our share of the revenues generated by the distribution of the picture in the licensee's territory, after deduction of the distributor's expenses and distributor fee. The advance usually is in the form of a cash deposit plus a letter of credit or "bank letter" for the balance payable 10-20% on execution (i.e., the cash deposit) and the balance on delivery (i.e., the letter of credit or "bank letter"). The license grants the distributor the right to the post-theatrical release of the picture in all or certain media in their territory for a predetermined time period. After this time, the distribution rights revert back to us and we are then free to re-license the picture. The license specifies that the distributor is entitled to recoup its advance from the revenue generated by the release of the picture in all markets in its territory, as well as its release costs and distribution fees. After the distributor has recouped its advance, costs, and fees, any remaining revenue is shared with us according to a predetermined formula. This is known as an "overage" and can be a significant source of revenue for us from successful films. However, a film's poor reception in one market does not preclude it from achieving success in another market and generating significant additional revenue for us in the form of an "overage" in that territory. In all of our licensing arrangements, we retain ownership of our films and maintain our control of each copyright. We intend to continue the

practice of retaining underlying rights to our film projects in order to continue to build our motion picture library to license or sell in the future.

## Finance.

We create a separate finance plan for each motion picture we produce. Accordingly, the sources of the funds for production of each motion picture vary according to each finance plan. We utilize financing based on state and foreign country tax credits (e.g. Louisiana, United Kingdom and Hungary) and direct subsidies), "mezzanine" or "gap" funds, which are senior to our equity, and senior secured financing with commercial banks or private lenders, together in certain cases with a limited investment from us, which is customarily less than 10% of the production budget. Since each finance plan is unique to each motion picture, we cannot generalize as to the amount we will utilize any of these sources of funds for a particular motion picture. We generally obtain some advances or guarantees prior to commitment to production of a motion picture project, but those amounts may not be substantial on smaller budgeted motion picture (e.g., under \$10,000,000), and in certain cases we have committed to production with an insubstantial amount of advances and guarantees. Unless we can manage the risks of production through the use of these financing techniques, we will not likely commit to production of larger budget motion pictures (e.g., over \$15,000,000), and we have never in the past committed to such productions, without substantial advances or guarantees from third-party distributors, or the equivalent in "non-recourse" financings.

## Plan of Operations

### Source of Funds for Years Ended June 30, 2011, and 2010

Seven Arts' primary source of funds since incorporation has been funds provided from the distribution of films, loans secured by the Group's motion pictures, tax credits, third party investments and tax preferred investments in the Group's motion pictures, and the proceeds of the sale of redeemable convertible preferred stock and debentures.

### Use of Funds for Years Ended June 30, 2011 and 2010

In each of the last two fiscal years, Seven Arts has expended between \$1,800,000 and \$2,600,000 on general and administrative expenses, which principally include salaries, payroll taxes, rents, travel and entertainment, and outside professional fees (legal, audit, sales, and tax advice) and the Group anticipates that it will expend a similar amount in fiscal year 2012. The Group's major cash outlay in these years has been for the acquisition and production of motion pictures. In fiscal years 2011 and 2010, Seven Arts expended approximately \$1,000,000 and \$2,000,000, respectively on the acquisition or production of motion pictures. The Group anticipates expenditure of a larger amount on production and acquisition of motion pictures in fiscal year ended June 30, 2012.

### Anticipated Changes to Facilities/Employees

The Group's employees and locations are two rented premises in Los Angeles and London and approximately 13 employees and consultants as of June 30, 2011. Management anticipates no changes to either facilities or employees in the near future.

### United States vs. Foreign Film Revenues

|                                      | June 30,<br>2011 | June 30,<br>2010 |
|--------------------------------------|------------------|------------------|
| Revenues and profits before taxes    |                  |                  |
| Information about geographical areas |                  |                  |
| Europe                               | \$969,077        | \$110,285        |
| North America                        | 1,113,074        | 1,714,271        |
| South America                        | 378,763          | 24,000           |

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|                        |             |             |
|------------------------|-------------|-------------|
| Africa and Middle East | 39,416      | 0           |
| Asia                   | 209,030     | 91,942      |
| Australia              | 48,999      | 34,018      |
| Total                  | \$2,758,359 | \$1,974,516 |

The net assets of the Group are also considered to relate to the above geographical markets in approximately the same proportion as total revenues.

Film revenues consist of minimum guarantees from distributors recognized when a film becomes available for release in that territory, royalties either collected or receivable and other fees or income associated with the sale of the Group's motion pictures.

#### Fee-related Revenues

All fee related revenues for the year ended June 30, 2011 and June 30, 2010 were generated in North America and through related party (as described below).

Fee related revenues in the fiscal year ended June 30, 2011 consisted of:

- a. Producer's fees of \$70,097 resulting from excess tax credits received on *Night of the Demons*. This item was collected by SAPLA who then paid or will pay it over to the Group under the agreement between the Group and SAPLA.
- b. \$500,000 of fees relating to *Esplanade Pictures*.

All of the Group's revenues and profits before taxes in each of the two periods are derived from the financing, production and distribution of films. The net assets of the Group are also considered to relate to the above geographical markets in approximately the same proportion as total revenues.

#### Regulation of the Motion Picture Industry

A key element in the motion picture industry involves intellectual property law. In this respect, the Group conducts its business through the control and exploitation of the copyrights and trademarks that may underlie its properties; therefore, domestic and international laws affecting intellectual property have a significant importance to the Group. Distribution rights to motion pictures are granted legal protection under the copyright laws of the United States and most foreign countries, which laws provide substantial civil and criminal actions for unauthorized duplication and exhibition of motion pictures. Motion pictures, musical works, sound recordings, art work, still photography and motion picture properties are separate works subject to copyright under most copyright laws, including the United States Copyright Act of 1976, as amended (the "Copyright Act"). Under the Copyright Act, motion pictures are allowed a copyright term of 95 years.

The Group currently takes appropriate and reasonable measures to secure, protect and maintain certain agreements to secure, protect and maintain copyright protection for all Group pictures under the laws of applicable jurisdictions; however, there can be no assurance that such measures will adequately protect the Group's properties, or that enforcement of its rights will not be financially prohibitive. Management is aware of reports of extensive unauthorized misappropriation of video rights to motion pictures, which may include the Group's motion pictures. Further, the Group is aware of reports of outright "pirating" of video properties, especially outside of the United States where enforcement of copyright laws is more difficult, if not impossible.

The Code and Ratings Administration of the MPAA (Motion Picture Association of America), an industry trade association, assigns ratings indicating age-group suitability for theatrical distribution of motion pictures. The Group will follow the practice of submitting its motion pictures for such ratings. A substantial number of the Group's films may be rated "R" by the MPAA, which means that children under certain ages may, under rules enforced by theatrical exhibitors, view the applicable motion picture only if accompanied by an adult. The Group's general policy is to produce or acquire motion pictures that qualify for a rating no more restrictive than "R." The NC-17 rating and its acceptance by distributors also presents an uncertainty in the demand for the feature films with this rating, as there is a very limited history of films with this rating. The Group does not anticipate that any of its films will be rated NC-17.

United States television stations and networks, as well as foreign governments, impose additional restrictions on the content of motion pictures, which may restrict in whole or in part theatrical or television exhibition in particular, territories. Management's practice will be to produce motion pictures for which there will be no material restrictions on exhibition in any major territories or media. This practice often requires the production of "cover shots" or different photography and recording of certain scenes for insertion in versions of motion picture exhibited on television or theatrically in certain territories where governmental restrictions are relatively more stringent. No assurance can be given that current and future restrictions on the content of the Group's motion pictures may not limit or affect the Group's ability to exhibit certain of its pictures in certain territories and media.



#### Seasonality

#### Dependency upon Patents/Licenses/Contracts/Processes

During the year ended June 30, 2011, revenue from two major customers approximated \$1,096,000 and \$327,850, or 40% and 12%, respectively, of film revenues. Accounts receivable due from these two customers approximated \$0 and \$0 respectively.

During the year ended June 30, 2010, revenue from two major customers approximated \$1,020,000 and \$518,000, or 52% and 26%, respectively, of film revenues. Accounts receivable due from these two customers approximated \$212,000 and \$518,000, or 14% and 35%, respectively, of the total accounts receivable at June 30, 2010.

During the year ended June 30, 2011, 100% of fee related revenues in the amount of \$570,029 were generated through SAPLA, of which this was all paid to the Group. Overall receivable due from SAPLA (including SAPLOU Equicap) through the due to related parties account was approximately \$1.6 million at June 30, 2011.

During the year ended June 30, 2010, 100% of fee related revenues in the amount of \$4,442,919 were generated through SAPLA, \$3,288,191 of which has been paid to the Group. Overall receivable due from SAPLA (including SAPLOU Equicap) through the due to related parties account was approximately \$2.5 million at June 30, 2010, and reflected in due from related parties.

The Group had no other dependency on patents, or licenses, or other industrial, commercial or financial contracts or new manufacturing processes, where such factors are material to the Group's business or profitability.

#### Sources/Availability of Raw Materials

N/A

#### 4.C. Organization Structure

The following is the corporate organization chart of Seven Arts and its subsidiaries as of June 30, 2011:

Table 7

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## 4.D. Property, Plant and Equipment

Seven Arts' executive offices are located in rented premises of approximately 1,500 sq. ft. at 8439 Sunset Boulevard, 4th Floor, West Hollywood, CA US 90069 (rented by its affiliate Seven Arts Pictures Inc.) and 136-144 New Kings Road, London SW6 4LZ. Seven Arts and its affiliates began occupying these facilities in November 2010 (US) and March 2011 (UK). Monthly rent is approximately \$11,000 for both facilities.

In total Seven Arts and its predecessors have produced or acquired interests in the following 33 motion pictures described below in Table 8. Seven Arts owns (directly or through grants of all rights in perpetuity or theatrical, video, and television rights) the copyright to each picture designated as "CR" in the table below, which are the pictures produced or co-produced by the Group, and for all other pictures in table below Seven Arts owns all material and distribution rights in the markets in which the Group operates for at least all territories outside the United States and Canada for no less than 15 years, which generally are the motion pictures the Group acquires for distribution only. Historically, in any financial period a small number of motion pictures have accounted for the vast majority of Seven Arts' revenues generated from the Group's motion picture library.

The Group has lost the right to manage twelve motion pictures (designated "+" in the table below) by way of the exercise by the Arrowhead Target Fund of its rights under the Arrowhead Loan described above in "Risk Factors"

Table 8

| Title   | Talent                        |   | Delivery date | First US release | Date Distribution Rights Terminate |
|---|-------------------------------|---|---------------|------------------|------------------------------------|
| American Summer aka The Pool Boys (CR)<br>(All Territories) | Director:<br>Cast:            | J.B. Rogers<br>Matthew Lillard<br>Efren Ramirez                         | 06/08         | Scheduled 9/11   | n/a                                |
| +Asylum (CR)<br>(All Territories)                           | Writer:<br>Director:<br>Cast: | Patrick Marber<br>David MacKenzie<br>Ian McKellan<br>Natasha Richardson | 05/04         | 08/05            | n/a                                |
| Autopsy (CR)<br>(All Territories)                           | Director:<br>Cast:            | Adam Gierasch<br>Robert Patrick   | 06/08         | 01/09            | n/a                                |
| Back In The Day<br>(All International Territories)          | Writer:<br>Director:<br>Cast: | Michael Raffanello<br>James Hunter<br>Ving Rhames<br>Ja Rule            | 03/05         | 05/05            | 11/11/2019                         |
| Boo (1)<br>(All International Territories)                  | Writer/Director:<br>Cast:     | Anthony C. Ferrante<br>Trish Cohen                                      | 03/05         | 10/05            | 5/14/2008                          |

Happy Mahaney

|   |           |   |       |       |            |
|---|-----------|---|-------|-------|------------|
| A Broken Life<br>(All International<br>Territories) | Writers:  | Neil Coombs,<br>Anna Lee                                    | 06/08 | 09/08 | 10/26/2026 |
|   | Director: | & Grace Kosaka<br>Neil Coombs                               |       |       |            |
|   | Cast:     | Tom Sizemore<br>Ving Rhames<br>Grace Kosaka<br>Saul Rubinek |       |       |            |
|   |           |   |       |       |            |

|   |                                |   |       |                   |            |
|---|--------------------------------|---|-------|-------------------|------------|
| Captivity<br>(All International<br>Territories)                                     | Writer:<br>Director:<br>Cast:  | Larry Cohen<br>Roland Joffe<br>Elisha Cuthbert  | 03/06 | 07/07             | 05/10/2008 |
| Cemetery Gates (1)<br>(All International<br>Territories)                            | Writer:<br>Director:<br>Cast:  | Brian Patrick<br>O'Tolle<br>Roy Knyrim<br>Reggie Bannister  | 03/05 | 05/06             | 04/04/2020 |
| Deal (CR)<br>(All Territories)  | Writers:<br>Director:<br>Cast: | Gil Cates, Jr.<br>& Marc<br>Weinstock<br>Gil Cates, Jr.<br>Burt Reynolds<br>Bret Harrison<br>Shannon<br>Elizabeth<br>Jennifer Tilly | 03/07 | 04/08             | n/a        |
| Drunkboat<br>(All Territories)  | Writers:<br>Director:<br>Cast: | Bob Meyer &<br>Randy Buescher<br>Bob Meyer<br>John Malkovich<br>John Goodman<br>Dana Delaney  | 12/08 | not yet scheduled | 4/28/2011  |
| Gettin' It<br>(All Territories)   | Writer/Director:<br>Cast:      | Nick Gaitatjis<br>Jessica Canseco<br>Patrick<br>Censoplano<br>Cheryl Dent<br>Sandra Staggs  | 12/06 | 08/07             | 04/04/2017 |
| Hades aka<br>The Black Waters of<br>Echo Pond<br>(All International<br>Territories) | Director:<br>Cast:             | Gabriel Bologna<br>Robert Patrick<br>Danielle Harris  | 05/09 | not yet scheduled | 10/26/2027 |
| + The Hustle (CR)<br>(All Territories except<br>Germany and Canada)                 | Writers:<br>Director:<br>Cast: | David Howard<br>& Michael<br>Capellupo<br>Stuart Cooper<br>Bobbie Phillips<br>Robert Wagner   | 10/02 | 12/02             | n/a        |

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|  |           |  |       |       |     |
|--|-----------|--|-------|-------|-----|
| + I'll Sleep When I'm Dead (CR) (1)<br>(All International Territories) | Writer:   | Trevor Preston   | 06/04 | 06/04 | n/a |
|  | Director: | Mike Hodges  |       |       |     |
|  | Cast:     | Clive Owen<br>Malcolm McDowell<br>Jonathan Rhys Meyers |       |       |     |
| + Johnny Mnemonic (CR)<br>(All Territories)                            | Writer:   | William Gibson   | 12/94 | 05/95 | n/a |
|  | Director: | Robert Longo   |       |       |     |
|  | Cast:     | Keanu Reeves<br>Dolph Lundgren                         |       |       |     |

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|   |  |   |                      |                   |            |
|---|--|---|----------------------|-------------------|------------|
| Knife Edge<br>(All Territories)                               | Director:<br>Cast:                     | Anthony Hickox<br>Joan Plowright<br>Natalie Press   | 06/08                | 03/10             | 03/23/2031 |
| Men Don't Lie<br>(All Territories)                            | Director:<br>Cast:                     | Jane Spencer<br>Michael Madsen<br>Jean-Hughes<br>Anglade  | not yet<br>scheduled | not yet scheduled | n/a        |
| The Mesmerist<br>(All International<br>Territories)           | Writers:<br><br>Director:<br><br>Cast: | Ron Marasco<br>& Michael<br>Goorjian<br>Gil Cates, Jr.<br>Neil Patrick<br>Harris<br>Jessica Capshaw                     | 06/02                | 09/02             | n/a        |
| Mirror Wars<br>(All International<br>Territories)             | Writers:<br><br>Director:<br>Cast:     | Alex<br>Kustanovich<br><br>& Oleg Kapanets<br>Vasily Chiginsky<br>Armand Assante<br>Malcolm<br>McDowell<br>Rutger Hauer | 11/06                | 07/07             | 02/03/2011 |
| + Never Talk To<br>Strangers<br>(CR) (1)<br>(All Territories) | Writers:<br><br>Director:<br><br>Cast: | Lewis A. Green<br>& Jordan Rush<br>Peter Hall<br>Antonio<br>Banderas<br>Rebecca<br>DeMornay                             | 09/95                | 10/95             | n/a        |
| Night of the Demons<br>(CR)<br><br>(All Territories)          | Director:<br><br>Cast:                 | Adam Gierasch<br>Shannon<br>Elizabeth<br>Edward Furlong<br>Diora Baird  | 06/10                | 10/10             | n/a        |
| Nine Miles Down<br>(CR)<br>(All Territories)                  | Director:<br>Cast:                     | Anthony Waller<br>Adrian Paul<br>Kate Nauta   | 06/09                | not yet scheduled | n/a        |

|   |                                |  |       |       |     |
|---|--------------------------------|--|-------|-------|-----|
| Noise aka The Rectifier (CR)<br>(All Territories) | Writer/Director:<br>Cast:      | Henry Bean<br>Tim Robbins<br>William Hurt<br>Bridget Moynahan<br>William Baldwin           | 03/07 | 05/08 | n/a |
| + No Good Deed (CR)<br>(All Territories)          | Writers:<br>Director:<br>Cast: | Christopher Canaan & Steve Banancik<br>Bob Rafelson<br>Samuel L. Jackson<br>Milla Jovovich | 05/02 | 09/03 | n/a |

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|   |                               |  |       |                   |            |
|---|-------------------------------|--|-------|-------------------|------------|
| Pool Hall Prophets aka<br>Shooting Gallery (CR)<br>(All Territories)  | Writer/Director:<br>Cast:     | Keoni Waxman<br>Freddie<br>Prinze, Jr.<br>Ving Rhames                | 09/05 | 12/05             | n/a        |
| + Popstar<br>(All International<br>Territories)   | Writer:<br>Director:<br>Cast: | Timothy Barton<br>Richard Gabai<br>Aaron Carter<br>Alana Austin      | 03/05 | 11/05             | 10/19/2014 |
| Radio Free Albemuth<br>(International<br>Territories)   | Writer/Director:<br>Cast:     | John Alan Simon<br>Alanis<br>Morissette                              | 06/10 | not yet scheduled | 01/06/2025 |
| + Red Riding Hood<br>(All International<br>Territories excl<br>Indonesia, Israel,<br>Japan, Latin American<br>Satellite TV, Mexico,<br>Middle East, Pan Asian<br>Satellite TV, Portugal,<br>Russia,<br>Slovenia/Croatia,<br>Thailand, Turkey) | Writer:<br>Director:<br>Cast: | Timothy Dolan<br>Randall Kleiser<br>Lainie Kazan                     | 03/06 | 06/06             | 05/02/2015 |
| + Shattered Image<br>(CR) (1)<br>(All Territories)  | Writer:<br>Director:<br>Cast: | Duane Poole<br>Raul Ruiz<br>William Baldwin<br>Anne Parillaud        | 06/98 | 12/98             | n/a        |
| + A Shot At Glory<br>(All International<br>Territories)   | Writer:<br>Director:<br>Cast: | Denis O'Neill<br>Michael Corrente<br>Robert Duvall<br>Michael Keaton | 01/02 | 05/02             | 09/30/2016 |
| + Stander (CR)<br>(All Territories)   | Writer:<br>Director:<br>Cast: | Bima Stagg<br>Bronwen Hughes<br>Thomas Jane<br>Deborah Unger         | 10/03 | 08/04             | n/a        |
| + Supercross<br>(All International<br>Territories)  | Writer:<br>Director:          | Ken Solarz<br>Steve Boyum  | 08/05 | 08/05             | 05/25/2019 |



|  |                               |  |       |                   |            |
|--|-------------------------------|--|-------|-------------------|------------|
|  | Cast:                         | Sophia Bush<br>Steve Howey<br>Cameron<br>Richardson                              |       |                   |            |
| The Wedding Chest<br>(All International<br>Territories excluding<br>Russia, Germany and<br>France) | Writer:<br>Director:<br>Cast: | Ekaterina<br>Tirdatova<br>Nurbek Egen<br>Natasha Regnier<br>Bolot<br>Tentimyshov | 03/08 | not yet scheduled | 10/04/2021 |

## ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The following discussion for the years ended June 30, 2011 and 2010, should be read in conjunction with the financial statements of the Group attached hereto and the notes thereof.

All references to “we” and “our” refer to the Group and its consolidated subsidiaries.

### 5.A. Operating Results.

The principal factors that affected our results of operations have been the number of motion pictures delivered in a fiscal period, the distribution rights of motion pictures produced by others acquired in a fiscal period, the choice of motion pictures produced or acquired by us, management’s and talents’ execution of the screenplay and production plan for each picture, the distribution and market reactions to the motion pictures once completed, management’s ability to obtain financing and to re-negotiate financing on beneficial terms, the performance of our third-party distributors and our ability to take advantage of tax-incentivized financing. These factors will continue to be, in our opinion, the principal factors affecting future results of operation and our future financial condition. No particular factor has had a primary or principal effect on our operations and financial condition in the periods discussed below.

Our revenues principally consist of amounts we earned from third-party distributors of its motion pictures. We recognize revenue from license fees as and when a motion picture is delivered to the territory to which the license relates if we have a contractual commitment and the term of license has begun or upon receipt of a royalty statement or other reliable information from a distributor of the amounts due to us from distribution of that picture. A motion picture is “delivered” when we have completed all aspects of production and may make playable copies of the motion picture for exhibition in a medium of exhibition such as theatrical, video, or television distribution.

We also recognize revenue beyond an initial license fee from our share of gross receipts on motion pictures which we recognize as revenue when we are notified of the amounts that are due to us. In some fiscal periods, a significant portion of our revenue is derived from sources other than motion picture distribution, including the cancellation of debt and interest income on a financing transaction, but we have not derived any such income in the successive comparative financial periods described below.

We have also benefited significantly from our ability to raise third party film equity investments such as in tax advantaged transactions under which we transfer to third party investor’s tax benefits for motion picture production and distribution. These types of investments have enabled us to substantially reduce the cost basis of our motion pictures and even to record significant fee-related revenues, particularly in the fiscal years ended June 30, 2010 and June 30, 2011.

We may however lose ownership of and have lost control of certain of our motion pictures due to our inability to repay indebtedness for such monies such as the Arrowhead Loan and the Cheyne Loan as described in Risk Factors – Risks Related To Our Business – Our failure to repay obligations under the Arrowhead and Cheyne Loans has resulted in the loss of control of asset that we pledged.

### Fiscal Year Ended June 30, 2011 Compared To Fiscal Year Ended June 30, 2010

Our total revenues decreased from \$6,417,435 for the fiscal year ended June 30, 2010 to \$3,328,388 in the fiscal year ended June 30, 2011. Revenues derived from the licensing and distribution of motion pictures increased from \$1,974,516 in the previous fiscal year to \$2,758,359 in this fiscal year, principally reflecting the recording of deferred income sales on American Summer.



Fee-related revenues in the fiscal year ended June 30, 2011 derived from:

- a) Producer's fees of \$70,097 resulting from excess tax credits received on Night of the Demons. This item was collected by SAPLA who then paid or will pay it over to the Group under the agreement between the Group and SAPLA.
- b) \$500,000 of fees relating to Esplanade Pictures based in Louisiana.

Amortization of film costs was \$2,843,734 in the fiscal year ended June 30, 2011, including an impairment charge of \$820,951. The amortization charge represents approximately 76% of the film revenues recognized from films currently in release.

Other cost of sales increased from \$2,398,976 in the prior year to \$3,447,996 in the current period and included certain distribution costs, producers' costs and other third party payments. This increase can be mainly attributed to the increase in the amortization/impairment charge this year. There has been a change in the sales team in 2011 who prepared the revenue forecasts several of which have been reduced leading to increased amortization and an impairment charge of in excess of \$820,000.

Consequently, the Group recorded a gross loss of \$119,608 in the year-ended June 30, 2011 compared to a gross profit of \$4,018,459 in the year-ended June 30, 2010.

General and administrative expenses amounted to \$1,852,303 in the fiscal year ended June 30, 2011, compared to \$2,619,205 in the fiscal year ended June 30, 2010. The Group significantly reduced operating expenses during 2011 due to expected lower revenue levels. External professional fees were significantly reduced by approximately \$721,000 including accountants, lawyers and tax advisors as more work was carried out in-house. In addition, there were significant salary reductions of approximately \$274,000 in 2011 as vacancies were not replaced. Management reserved for doubtful accounts of \$234,429 during the fiscal year ended June 30, 2011 compared to \$319,345 in 2010.

Net interest expense decreased from \$2,199,844 in the fiscal year ended June 30, 2010 to \$758,197 in the most recent fiscal year, reflecting settlement agreements with senior lenders Palm Finance and Arrowhead.

We recorded \$4,458,621 in other income in this fiscal year reflecting forgiveness of debt mainly from a settlement agreement reached with Palm Finance and release of Arrowhead accrual. This compares to \$583,874 in "other income" in the fiscal year ended June 30, 2010.

We recorded no tax provision in the fiscal year ended June 30, 2011, because we have an excess of tax-loss carry forwards against which we can offset any taxes that might be currently accruable.

As result of the aforementioned results, we recorded a net profit of \$1,461,554 in the period ended June 30, 2011 compared to a loss of \$ 475,651 for the fiscal ended June 30, 2010.

## 5.B. Liquidity and Capital Resources.

During the year ended March 31, 2005, we issued (A) £3,000,000, of convertible debt to Langley Park Investment Trust PLC ("Langley") in return for 3,000,000 ordinary shares in Langley valued at approximately \$5,204,000, and (B) approximately £3,000,000 of convertible redeemable preference shares to Armadillo Investments Plc. ("Armadillo") in return for 3,000,000 ordinary shares from Armadillo, valued at \$5,669,000. We received actual cash in fiscal year 2005 of approximately \$2,232,000 through the sale of ordinary shares of Armadillo Investments plc (approximately \$1,302,000) and Langley Park Investment Trust PLC, (approximately \$930,000). The amounts that we received from the sale of a portion of our Armadillo shares and all of our Langley shares were substantially less than the stated value

of the debenture and preference shares.

Langley converted £1,250,000 of its convertible debenture (£1,250,000 or approximately \$1,875,000) into 1,000,000 ordinary shares on March 15, 2007. The remaining convertible debt due to Langley is £1,750,000 (or approximately \$2,500,000) as of the date of this annual report.

The convertible redeemable preference shares held by Armadillo were acquired by the Seven Arts Employee Benefit Trust ("Trust") on October 30, 2008, and 2,500,000 of the preference shares were converted into 2,000,000 of our ordinary shares on November 20, 2008. The remaining 500,000 preference shares were converted into 400,000 ordinary shares on May 25, 2010. The convertible preference shares were originally issued at a value of £3,000,000 (approximately \$4,500,000). All the foregoing conversions were based on conversion at 25 pence (approximately \$0.375) for each ordinary share issued.

On October 30, 2008, the Seven Arts Employee Benefit Trust acquired 3,000,000 of our convertible Preference Shares from Armadillo Investments Plc ("Armadillo") for £1,500,000, to be paid in three equal installments of £500,000 and the return to Armadillo of 1,600,000 ordinary shares of Armadillo, valued at £800,000, for an aggregate purchase price of £2,300,000. The purchase price was to be loaned to the EBT by us at a nominal interest rate and to date we have advanced £500,000 as the first of the installments, together with the 1,600,000 ordinary shares of Armadillo to the EBT, which has paid them over to Armadillo. These 1,600,000 ordinary shares of Armadillo were all the remaining preferred shares of Armadillo owned by us. We have guaranteed the remaining £1,000,000 due to Armadillo, but have not made any further advances to EBT, we are currently in default on the second and third payments. We expect to pay the remaining amount due to Armadillo from the proceeds of a future offering. As at June 30, 2011 the EBT owes us £643,433 (\$1,107,357) at the balance sheet date's exchange rate) and this amount has been booked as a contra asset under share premium, which is a deduction from shareholders' equity. The EBT will owe us an additional £1,000,000 when we have made good on our obligation.

Seven Arts Future Flow I ("SFF"), a limited liability Group owned by SAP Inc., one of our affiliates and a company that is owned by Peter Hoffman, our Chief Executive Officer, obtained financing of \$8,300,000 (the "Arrowhead Loan") from Arrowhead Target Fund Ltd. ("Arrowhead") in February 2006, at an interest rate of 15% per annum. Although the loan is secured by certain assets of Seven Arts Future Flows I, LLC, we are not required to repay the Arrowhead Loan from any of our other assets or revenues.

The specific film assets which secure the Arrowhead Loan were our distribution rights in the following motion pictures: Asylum, Stander, I'll Sleep When I'm Dead, No Good Deed, Supercross, Popstar, Red Riding Hood, Johnny Mnemonic, Shattered Image, Never Talk to Strangers, The Hustle, and A Shot at Glory.

Our estimates of the amount of time it would take to repay the Arrowhead Loan from the proceeds of the film assets securing the loan have not been met. The Arrowhead Loan matured on February 15, 2009, and was then due in full. SFF received a default notice from Arrowhead to that effect, and as a result Arrowhead is now collecting directly all sums receivable by us with respect to these motion pictures and has appointed a new servicing agent for these motion pictures, with the result that we no longer control the licensing of these motion pictures. As a result of the foregoing, we have removed all investment and receivables related to the twelve motion pictures pledged to Arrowhead as assets and have removed all limited recourse indebtedness relating to these motion pictures as a liability.

The Arrowhead Target Fund Ltd ("Arrowhead") filed an action on September 22, 2010 which seeks recovery from the Group of the monies which the Group has retained under its interpretation of the relevant agreements with Arrowhead. In addition, Arrowhead makes substantial additional claims against the Group, Mr. Hoffman and Seven Arts Pictures Inc. regarding claimed breaches of the terms of the operative agreements, including failure to properly account, failure to turn over materials, failure to remit monies collected, and similar matters. The claims against the Group for these breaches of warranties for damages are \$8,300,000 although Arrowhead states no basis for this amount. The Group had moved to dismiss the action against all defendants other than Seven Arts Future Flows I LLC, which is not part of the Group. On August 9, 2011, the New York Supreme Court granted the Group's motion and dismissed all defendants except Seven Arts Filmed Entertainment Limited in its capacity as a collateral agent, which is not a material element of Arrowhead claim. The Group continues to believe that Arrowhead's claims against the Group are without substantial merit.

We borrowed an aggregate of \$7,500,000 from (i) Arrowhead Consulting Group LLC (“ACG”) for \$1,000,000 (“ACG Loan”) and (ii) Cheyne Specialty Finance Fund L.P. (“Cheyne”) for \$6,500,000 (“Cheyne Loan”) in December 2006, secured by certain of our motion picture assets. The ACG Loan and Cheyne Loan bear interest at 19% and 18% per annum, respectively. The Cheyne Loan matured on September 30, 2007, and a subsidiary acquired the Cheyne Loan plus interest thereon for payment of \$6,500,000, and obtained an assignment of their senior position and subordination agreement with Arrowhead. Our estimates of the amount of time it would take to repay the ACG Loan from the proceeds of the film assets securing the loan have not been met. In October 2008, we received a notice of default from ACG in connection with this loan. The ACG Loan is secured by Noise, Deal, Pool Hall Prophets, Boo, A Broken Life, and Mirror Wars and a second position security interest in the motion pictures listed above which are pledged to Arrowhead. ACG has now filed suit to collect the ACG Loan See Legal Proceedings.

On October 15, 2008 the Group borrowed £1,000,000 from Trafalgar Capital Special Investment Fund (“Trafalgar”). A portion of this loan the Group advanced to the EBT for it to use as the first installment for the acquisition of all the Preference Shares owned by Armadillo. On September 2, 2009 the Group repaid Trafalgar \$1,000,000 (about £698,934) as a partial payment against this loan, with the remaining balance subject to repayment in cash or convertible to the ordinary shares of the Group at the conversion terms as agreed between Trafalgar and the Group. On June 22, 2010 an amended agreement was entered into with Trafalgar for an extension of the due date of the convertible debentures to December 31, 2010, and the Group agreed to issue 68,000 ordinary shares to settle a portion of the debt. Trafalgar agreed to reduce the loan amount from the proceeds it received from selling the 68,000 ordinary shares. The transaction was consummated subsequent to the date of the financial statements and all of the 68,000 shares have been sold in the market before December 31, 2011. Subsequent to June 30, 2010, a further amended agreement was entered into with Trafalgar for an extension of the due date of the convertible debentures to March 31, 2011, and the Group agreed to issue 85,000 ordinary shares to settle a portion of the debt (see subsequent events note 22). Trafalgar agreed to reduce the loan amount from the proceeds it received from selling the 85,000 ordinary shares. The balance outstanding on the loan after sale of these 85,000 shares is expected to be approximately \$500,000. The per-share value is determined as the amount recovered by Trafalgar on sale thereof in the market and Trafalgar may “put” these shares to us at \$1.00 per share on March 31, 2011 if not previously sold. We intend to pay the balance of the sum due to Trafalgar by similar conversion of our shares

We entered into two senior financing loan and security agreements with Palm Finance Corp (“Palm”) to finance the production costs of The Pool Boys, Autopsy and Nine Miles Down dated May 7, 2007 and December 17, 2007. These loans are secured by the revenues to be collected from these motion pictures. The revenues so far collected have been insufficient to repay the majority of these loans, primarily as result of management’s decision to delay the release of these films. We have entered into an agreement with Palm extending the due date of these loans to December 31, 2011. The original principal amount of the Palm loan for The Pool Boys and Autopsy are \$5,250,000 including \$500,000 accrued interest, and for Nine Miles Down was \$4,000,000 including \$750,000 accrued interest.

We have also entered into a new financing agreement with Palm in November, 2010 to refinance the existing indebtedness secured by our production and post production facility in New Orleans, Louisiana under which Palm has acquired the existing credit facility of \$3,700,000 plus accrued interest of our affiliate SAPLA for \$1,000,000 and agreed to advance an additional \$1,800,000 to complete renovation and construction of this facility. Palm’s advance and interest at the rate of 15% per annum are due and payable within five years and are secured by the property at 807 Esplanade Avenue in New Orleans (“Property”) and Louisiana film infrastructure and historical rehabilitation credits, as well as Federal historical rehabilitation credits (“Credits”) associated with the Property. See Our Business – Production.

On August 27, 2007, we borrowed \$1,650,000 from Blue Rider Financial (“Blue Rider”) to pay for the domestic prints and advertising costs for the motion picture Deal (“Blue Rider Loan”) and arranged that the revenues due from Metro-Goldwyn-Mayer Studios Inc. (“MGM”) to us for the distribution of that motion picture be assigned to Blue Rider Financial as partial security for that loan. To date the revenues paid to us from MGM have not been sufficient to repay the Blue Rider Loan. We have therefore entered into an accommodation agreement with Blue Rider to redeem the loan due for \$2,200,000, less approximately \$812,000 of collections that have been received by Blue Rider to date from MGM. We expect this indebtedness will be repaid from proceeds due from MGM on or before December 31, 2011.

On August 30, 2010, the Group issued an aggregate of \$470,000 Convertible Debt to qualified investors that mature on February 28, 2011. The Convertible Debts bear interest at a rate of 15.0% per annum and could be converted into the Group’s ordinary shares beginning on the date which is one hundred twenty (120) days following the issuance of the Convertible Debt, at the conversion rate of \$3.75 per share, subject to certain changes.

On March 22, 2011 an additional 300,000 convertible notes were issued to Runway Investments Ltd on the same terms as above. At the same time the original notes were extended to July 31, 2011.



All \$770,000 of these notes were extended on May 24, 2011, to September 30, 2011, and the conversion terms were changed as follows:

- The Scarborough note's principal and interest convert into common stock now at \$0.50 per share.
- For extending the maturity date until December 31, 2011, Sendero and Runway will reduce their conversion price to \$0.60 per share.
- For extending the maturity date until September 30, 2011, Agua Alta will reduce its conversion price to \$0.75 per share.
- The average conversion price of the three remaining notes is \$0.64 per share.

\$225,000 Scarborough notes were converted to 507,000 shares on July 29, 2011.

\$170,000 Agua Alta and \$75,000 Sendero options were converted on October 19, 2011 into 1,786,374 shares.

On June 10, 2011, The Group borrowed \$150,000 from Isaac Capital Group (“ICG”) in the form of a convertible note. The loan is for six months with interest at 15% per annum. ICG will have the right to convert the Loan at any time into shares at a conversion price of 60% of the volume weighted average sale price on NASDAQ of the shares for the 10 trading days prior to the closing of the loan. There is also a closing fee of 15,000 shares on closing of the Loan. (These shares have not yet been issued).

We issued a \$150,000 convertible note which was due in March 2011, and a \$50,000 convertible note which was due in June 2011 to Asher Enterprise Inc. These notes are convertible into our ordinary shares at a discount to the volume weighted average price of our common shares on conversion. These convertible notes have now been converted.

We had entered into an agreement with BRG Investments, LLC (“BRG”), an affiliate of Fletcher Asset Management, for the investment by BRG of up to \$30,000,000 in preferred stock of Seven Arts and the formation of a joint venture to, among other things, produce and distribute motion pictures and make investments.

BRG purported to cancel the agreement in May 2011.

Seven Arts settled this issue on October 5, 2011, whereon the Company arranged a mutually acceptable settlement of its dispute with Fletcher Asset Management arising out of an investment agreement purported terminated by Fletcher as we announced on June 7, 2011 in a press release. In the settlement with Fletcher, the Company waived all claims against Fletcher. Fletcher agreed to acquire and did acquire 250,000 shares of our common stock at a price of \$1.00 per share. Fletcher received a warrant to buy an additional 100,000 shares at \$1.00, Fletcher has the right within six months to buy an additional 250,000 shares of our common stock based on a volume weighted average price but no less than \$1.00 or more than \$1.50, and if it buys these shares, Fletcher will receive an additional warrant to buy an additional 100,000 shares of our common stock on the same terms as the warrant we have issued. Seven Arts intends to use the proceeds of this transaction to partially fund its next motion picture production in Louisiana entitled Schism, written and to be directed by Adam Gierasch, the director of Autopsy and Night of the Demons, two recent releases by the Company.

Management believes that, as a result of the proceeds derived from a proposed offering, and based on historical revenues generated from the licensing of the distribution rights on our motion pictures, we will have sufficient working capital to operate for the next twelve months. In particular,

- (a) the indebtedness to Palm will be satisfied by a debt to equity conversion,
- (b) the indebtedness to Trafalgar from future conversion of our common shares and
- (c) the indebtedness to Blue Rider from the distribution revenues due from MGM on the motion picture Deal.

During the year ended June 30, 2011, the Group utilized cash flow from operating activities of approximately \$0.5 million. This was attributable to the Group’s net profit from operations of \$1,461,555 and is offset by following:

- Amortization and depreciation expense of \$14,000,
- Amortization, write-off, and impairment of capitalized film costs of \$2,843,000,
- EBT interest receivable of \$(72,000)
- Ordinary shares issued in exchange for interest and fees of \$2,977,000
- Bad debt expense of \$234,000

- Forgiveness of debt and interest by lenders of (\$4,459,000),
- Changes in the operating assets and liabilities of (\$2,526,000).

The Group used minimal cash in investing activities for the fiscal year ended June 30, 2011.

The Group used approximately \$0.2 million in financing activities for the year ended June 30, 2011 .

We currently borrow funds for the financing of each of our motion pictures from several banks and other production lenders. There can be no assurances given that the Group will be able to borrow funds to finance our motion pictures in the future. We are currently seeking a revolving credit facility for the financing of our future motion picture productions.

## 5.C. Research and Development, Patents and Licenses, etc.

NA

## 5.D. Trend Information.

The Group is aware of no trends that could materially affect the Group's business.

## 5.E. Off-Balance Sheet Arrangements.

The Group has no Off-Balance Sheet Arrangements.

## 5.F. Tabular Disclosure of Contractual Obligations (as of June 30, 2011):

|                                  | Total         | Payments Due By Period |              |              |                         |
|----------------------------------|---------------|------------------------|--------------|--------------|-------------------------|
|                                  |               | Less Than<br>1 Year    | 1-3<br>Years | 3-5<br>Years | More<br>Than 5<br>Years |
| Bank and Other Production        |               |                        |              |              |                         |
| 1. Loans (1)                     | \$ 10,890,000 | \$ 10,890,000          |              |              |                         |
| Post Production Facility Line of |               |                        |              |              |                         |
| 2. Credit + Mortgage(2)          | 1,603,500     | 1,603,500              |              |              |                         |
| Armadillo Investments plc/EBT    |               |                        |              |              |                         |
| 3. (3)                           | 1,000,000     | 1,000,000              |              |              |                         |
| Trafalgar Capital Special        |               |                        |              |              |                         |
| 4. Investment Fund (4)           | 490,000       | 490,000                |              |              |                         |
| 5. Lion House                    | 263,000       | 263,000                |              |              |                         |
| 6. Sums Due To Producers (5)     | 503,000       | 503,000                |              |              |                         |
| Convertible Debenture (no        |               |                        |              |              |                         |
| 7. redemption date) (6)          | 3,432,500     |                        |              | \$ 3,432,500 |                         |
| 8. Convertible debentures (7)    | 853,000       | 853,000                |              |              |                         |
| 9. Isaac Capital Group (8)       | 148,000       | 148,000                |              |              |                         |
| Total                            | \$ 19,183,000 | \$ 15,750,500          |              | \$ 3,432,500 |                         |

- (1) The current bank and production loans include (i) approximately \$7,702,000 owed to Palm Finance for three motion pictures produced by us and (ii) \$3,200,000 in special purpose financing arranged for six motion pictures produced by us owed to Palm Finance, for production of the motion picture Nine Miles Down.
- (2) Seven Arts Pictures Louisiana LLC ("SAPLA"), a subsidiary of SAP Inc. (one of our affiliates and a company controlled by Peter Hoffman, our Chief Executive Officer), entered into a Credit Agreement with Advantage Capital Community Development Fund, L.L.C. ("Ad Cap") dated October 11, 2007 for the acquisition and improvement of a production and post production facility located at 807 Esplanade Avenue in New Orleans, Louisiana. The aggregate borrowing amount under this facility was \$3,700,000, all of which was drawn down as of April 30, 2010. In November 2010 Palm Finance Inc ("Palm") acquired this mortgage for \$1,000,000 and agreed to extend a construction facility of \$1,850,000 to complete the facility. As of June 2011, \$603,500 of this amount had been drawn down. We expect this facility will be completed for a cost not to exceed \$1,850,000. We have guaranteed the indebtedness to Palm for the \$1,000,000 and ultimately the additional \$1,850,000. We do not anticipate the use of any material amount of our working capital to complete and operate this facility, and we expect to realize substantial film production, film infrastructure, historic rehabilitation and other state and federal tax credits and other tax incentives from the acquisition, renovation, and operation of this property as a post

production facility. Management believes that expenditures by SAPLA for this facility would generate approximately \$4,000,000 in Louisiana Film Infrastructure tax credits, approximately \$3,000,000 in Louisiana State Rehabilitation tax credits and \$3,000,000 in Federal Historic Preservation tax credits.

- (3) We have guaranteed an additional £1,000,000, ( plus interest at 10% from July 1, 2011) due from the EBT to Armadillo. This liability will be met by the EBT from the funds that we advance to it from the proceeds of a future offering. The second and third payments to Armadillo were due in April and October 2009, and the EBT did not make those payments. In February 2,011 150,000 new shares were pledged to Armadillo in repayment for them extending the repayment date of the £1,000,000 to June 30, 2011.
- (4) A portion of the loan due to Trafalgar Capital Special Investment Fund was advanced by us to the Seven Arts Employee Benefit Trust (“EBT”) for the partial acquisition of the Preference Shares owned by Armadillo Investments plc (“Armadillo”). The loan to Trafalgar came due on June 30, 2009 and we have made a partial payment of \$1,000,000 on September 2, 2009. On June 22, 2010, we entered into an amended agreement with Trafalgar for an extension of the due date of the convertible debentures to December 31, 2010, and the issuance of 340,000 shares in July 2010. This agreement has been further extended, in January 2011, to March 31, 2011 for the issuance of another 425,000 shares against the loan principal.
- (5) Includes estimated amounts due to producers of motion pictures. As of June 30, 2011, \$503,000 had been accrued.
- (6) The outstanding Debentures have a face value of £1,750,000 (approximately \$3,432,500 at the exchange rate prevailing at the time of the financing) and are convertible into an aggregate of 280,000 ordinary shares. There is no due date or required due date on our Debentures. The Debentures rank junior to all our indebtedness and senior only to our ordinary or preference shares and they are included as a part of Shareholders’ Equity as there was no stated redemption date.

(7) a) On August 30, 2010, the Group issued an aggregate of \$470,000 Convertible Debt to qualified investors that mature on February 28, 2011. The Convertible Debts bear interest at a rate of 15.0% per annum and could be converted into the Group's ordinary shares beginning on the date which is one hundred twenty (120) days following the issuance of the Convertible Debt, at the conversion rate of \$3.75 per share, subject to certain changes.

b) On March 22, 2011 an additional 300,000 convertible notes were issued to Runway Investments Ltd on the same terms as above. At the same time the original notes were extended to July 31, 2011.

c) All \$770,000 of these notes were extended on May 24, 2011 to September 30, 2011 but the conversion terms were changed as follows:

The Scarborough note's principal and interest to convert into common stock its at \$0.50 per share.

For extending the maturity date until December 31, 2011, Sendero and Runway will reduce their conversion price to \$0.60 per share.

For extending the maturity date until September 30, 2011, Agua Alta will reduce its conversion price to \$0.75 per share.

The average conversion price of the three remaining notes is \$0.64 per share.

d) \$225,000 of the Scarborough notes were converted to 507,000 shares on July 29, 2011.

e) \$170,000 Aqua notes and \$75,000 Sendero notes were converted to 1,786,374 shares on October 19 2011.

f) The Company has evaluated these convertible notes for embedded derivative features and has determined that no derivative liability exists.

(8) On June 10, 2011, the Group borrowed \$150,000 from Isaac Capital Group ("ICG") in the form of a convertible note. The loan is for six months with interest at 15% per annum. ICG will have the right to convert the Loan at any time into shares at a conversion price of 60% of the volume weighted average sale price on NASDAQ of the shares for the 10 trading days prior to the closing of the loan. There is also a closing fee of 15,000 shares on closing of the Loan.(These shares have not yet been issued).

## Critical Accounting Policies

### Basis of Consolidation

The Company consolidates its subsidiaries in accordance with Accounting Standards Codification ("ASC") 810, "Business Combinations", and specifically ASC 810-10-15-8 which states, "The usual condition for a controlling financial interest is ownership of a majority voting interest, and, therefore, as a general rule ownership by one reporting entity, directly or indirectly, or over 50% of the outstanding voting shares of another entity is a condition pointing toward consolidation." The Company does not have any variable interest or special purpose entities.

The consolidated financial statements include the financial statements of Seven Arts Pictures Plc ("PLC"), and its wholly owned subsidiaries, Seven Arts Filmed Entertainment Limited ("SAFE Ltd"), Seven Arts Filmed Entertainment (UK) Limited, Cinematic Finance Limited and Cinematic Finance (Equicap) Ltd, herein referred to as (the "Group", the

“Company” or “Seven Arts”).

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|   | Years<br>Ended<br>June 30,<br>2011 and<br>2010 |   |
|---|--|---|
| Seven Arts Pictures Plc.  | 100  | % |
| Seven Arts Filmed Entertainment Limited                             | 100  | % |
| Seven Arts Filmed Entertainment (UK) Limited (formed March 6, 2008) | 100  | % |
| Cinematic Finance Limited (formed February 14, 2008)                | 100  | % |
| Cinematic Finance (Equicap) Ltd (formed February 27, 2009)          | 100  | % |

The Group acquired SAFCO's in May 2009. SAFCO's refers to 17 companies formed by investors in the Zeus transaction. The Group intends to liquidate the SAFCO's under the applicable laws of the United Kingdom upon obtaining full control of the books, records and operation of the SAFCO's. The Group does not anticipate any material assets or liabilities related to the SAFCO's except the contingent liability for VAT on the Zeus transaction described in notes 12 below. The SAFCO's results have not been and will not be consolidated as the Group does not have control.

All significant intercompany balances and transactions have been eliminated on consolidation.

#### Significant Accounting Policies

The Company's management selects accounting principles generally accepted in the United States of America and adopts methods for their application. The application of accounting principles requires the estimating, matching and timing of revenue and expense. It is also necessary for management to determine, measure and allocate resources and obligations within the financial process according to those principles. The accounting policies used conform to generally accepted accounting principles which have been consistently applied in the preparation of these financial statements.

The financial statements and notes are representations of the Company's management which is responsible for their integrity and objectivity. Management further acknowledges that it is solely responsible for adopting sound accounting practices, establishing and maintaining a system of internal accounting control and preventing and detecting fraud. The Company's system of internal accounting control is designed to assure, among other items, that 1) recorded transactions are valid; 2) valid transactions are recorded; and 3) transactions are recorded in the proper period in a timely manner to produce financial statements which present fairly the financial condition, results of operations and cash flows of the Company for the respective periods being presented.

#### Basis of Accounting

The Company prepares its financial statements on the accrual basis of accounting and in accordance with Generally Accepted Accounting Principles of the United States of America ("US GAAP"). All intercompany balances and transactions are eliminated. Management believes that all adjustments necessary for a fair presentation of the results of the years ended June 30, 2011 and 2010, respectively, have been made.

The Group has also engaged in various transactions under which it has received cash proceeds from the transfer of tax credits or other tax benefits associated with its motion picture productions. Any such proceeds are generally treated as a reduction in the production costs of the applicable motion picture.

- a) To the extent such tax benefit proceeds would exceed the capitalized cost of the film or represent fee income not applied to production cost, such proceeds are accounted for as producers' fees income where relevant producers



contracts are in place.

- b) To the extent that the Group were to receive benefits from tax advantaged investments relating to:
  - i. a picture that has not commenced production by a particular date and that investment is forfeited such that the Group has no further obligations to the investor (See note 1.3)
  - ii. third party productions taken on by the Group as sales agent/distributor then such benefits are also recorded as producer fees income

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## Revenue Recognition

Revenues earned by the Group can be classified into two categories:

1. Film revenues: earned from the exploitation of our new productions, back catalogue and third party productions taken on as sales agent.
2. Fee-related revenues: Producer's fees income earned by the Group on productions controlled by the Group is earned when the Group is entitled to receive under a binding agreement a fixed sum irrespective of the distribution revenue from that picture.

## Film Revenue

The Group recognizes revenue from the sale (minimum guarantee or non-refundable advances) or licensing arrangement (Royalty agreement) of a film in accordance with ASC 605-15 "Revenue Recognition". Revenue will be recognized only when all of the following criteria have been met:

- a) Persuasive evidence of a sale or licensing arrangement with a customer exists.
- b) The film is complete and, in accordance with the terms of the arrangement, has been delivered or is available for immediate and unconditional delivery. (i.e. the "notice of delivery" (NOD) has been sent and there is a master negative available for the customer)
- c) The license period of the arrangement has begun and the customer can begin its exploitation, exhibition, or sale.
  - d) The arrangement fee is fixed or determinable.
  - e) Collection of the arrangement fee is reasonably assured.

A written agreement with clients (purchase order, letter, contract, etc.,) indicating the film name, territory and period is required for the recognition of revenue. Revenue is recognized when the performance criteria in the contracts have been met. The customer generally confirms agreement by their signature on the contract.

Minimum guarantee revenue (i.e. non-refundable advances) is recognized as and when the film is available for delivery to the respective territories. Cash deposits received on the signing of the contracts are recorded as deferred income until the film is available for delivery (as described above) at which point the deposit revenue is recognized. The Group does not recognize any revenues relating to minimum guarantee on any motion picture or amortization expenses on that picture until United States theatrical release if it has agreed with the licensees that delivery or payment of minimum guarantee will be delayed for any material period of time to permit such a theatrical release.

Royalty revenue which equates to an agreed share of gross receipts of films is recognized as income as and when the Group is notified of the amounts by the customers through their royalty reports.

## Fee-related revenues

Many countries make tax credits available to encourage film production in the territory. Seven Arts benefits from tax credits in:

- a) the UK and several other European territories for their European productions
- b) Canada for their Canadian productions
- c) Louisiana for their US productions
- d) Tax preferred financing deals



In the majority of circumstances these tax credits are treated as a reduction in the capitalized costs of the film assets they are financing. However, to the extent such tax benefit proceeds would

- a) exceed the capitalized cost of the film or;
- b) represent fee income not applied to production cost, such proceeds are accounted for as producers' fees income where relevant producers contracts are in place.

In addition, to the extent that the Group was to receive benefits from tax advantaged investments relating to

- a) a picture that has not commenced production by the investment agreement closing date that investment is forfeited such that the Group has no further obligations to the investor
- b) third party productions taken on by the Group as sales agent/distributor then such benefits are also recorded as producer fees income

One of the risks for the investor associated with these tax advantaged investments is that a particular picture will not start production within the investment agreement period therefore giving no asset value to their slate of investments. The contract with the Group will generally state that there is no recourse to the Group and associated companies as this is one of the many risks of the film industry that the investors are made aware of on signing the investment agreements. Therefore, when a picture has not commenced production by the investment agreement closing date that investment is forfeited and the Group has no further obligations to the investors. These financing schemes are part of the general operations of the Group in its role of producer. Revenues in the year ended June 30, 2011 however did not include fee income derived from a structured film and distribution cost financing with UK investors. It did include additional producer fee of \$570,029 associated with films produced in Louisiana. In 2010, the Group recognized revenue of \$2,650,794 of fee income as described and producer's fees of \$1,792,125.

#### Investments

Investments are held at the lower of cost or net realizable value, and reviewed annually for any impairment charges. As of June 30, 2011 the Group has no outstanding investments.

#### Film Costs

Film costs include the unamortized costs of completed films which have been produced by the Group or for which the Group has acquired distribution rights, libraries acquired as part of acquisitions of companies and films in progress and in development. For films produced by the Group, capitalized costs include all direct production and financing costs, capitalized interest and production overhead.

Costs of acquiring and producing films are amortized using the individual-film-forecast method, whereby these costs are amortized and participations and residuals costs are accrued in the proportion that current year's revenue bears to management's estimate of ultimate revenue at the beginning of the current year expected to be recognized from the exploitation, exhibition or sale of the films. Generally, 80% or more of a film's costs are amortized within three years of the picture's initial release.

Ultimate revenue includes estimates of revenue to be earned over a period not to exceed ten years following the date of initial release. Film costs are stated at the lower of amortized cost or estimated fair value. Individual film costs are reviewed on a title-by-title basis, when an event or change in circumstances indicates that the fair value of a film is less than its unamortized cost. The fair value of the film is determined using management's future revenue and cost estimates and a discounted cash flow approach. Impairment is recorded in the amount by which the unamortized costs exceed the estimated fair value of the film. Estimates of future revenue involve measurement uncertainty and it is

therefore possible that reductions in the carrying value of investment in films may be required as a consequence of changes in management's future revenue estimates.

Films are included in the general "library" category when initial release dates are at least three years prior to the acquisition date.

Films in progress include the accumulated costs of productions which have not yet been completed. Films in development include costs of acquiring film rights to books, stage plays or original screenplays and costs to adapt such projects. Such costs are capitalized and, upon commencement of production, are transferred to production costs. Projects in development are written off at the earlier of the date they are determined not to be recoverable or when abandoned.

## Property & Equipment

Equipment is carried at the cost of acquisition or construction and depreciated over the estimated useful lives of the assets. Costs associated with repair and maintenance are expensed as incurred. Costs associated with improvements which extend the life, increase the capacity or improve the efficiency of our property and equipment are capitalized and depreciated over the remaining life of the related asset. Gains and losses on dispositions of equipment are reflected in operations. Depreciation and amortization are provided using the straight-line method over the estimated useful lives of the assets, which are 2 to 5 years.

## Income Taxes

The Company has adopted ASC 740-10 “Income Taxes”, which requires the use of the liability method in the computation of income tax expense and the current and deferred income taxes payable.

The Group is not part of any consolidated return filed in the United States.

## Inflation

Management believes that inflation has not had a material effect on the Group’s operations to date.

## Related Party Transactions

For a description of the Group’s related party transactions see the section of this report 7.B entitled “Related Party Transactions.”

## ITEM 6. DIRECTORS, SENIOR MANAGEMENT, AND EMPLOYEES

### 6.A. Directors and Senior Management

Table No. 9  
Directors and Senior Management  
October 21, 2011  
Table No. 1  
Directors

| Name           | Position           | Age | Date First Elected or Appointed | Date of Expiration of Current Term (1) |
|----------------|--------------------|-----|---------------------------------|--|
| Hubert Gibbs   | Chairman, Director | 52  | April 9, 2010                   | November 15, 2014                      |
| Peter Hoffman  | CEO, Director      | 62  | September 2, 2004               | November 15, 2014                      |
| Kate Hoffman   | COO, Director      | 34  | February 26, 2008               | November 15, 2013                      |
| Anthony Hickox | Director           | 44  | October 15, 2007                | November 15, 2012                      |
| Elaine New     | Director           | 51  | January 11, 2007                | November 15, 2012                      |
| Daniel Reardon | Director           | 51  | November 1, 2010                | November 15, 2012                      |
| Robert Kaiser  | Director           | 57  | September 1, 2011               | November 15, 2012                      |

(1) Directors serve for three years.

The Directors served in their respective capacities since their election and/or appointment and will serve until the next Annual General Meeting or until a successor is duly elected, unless the office is vacated in accordance with the Articles of Association.



The senior management serves at the pleasure of the Board of Directors.

No director and/or senior management had been the subject of any order, judgment, or decree of any governmental agency or administrator or of any court or competent jurisdiction, revoking or suspending for cause any license, permit or other authority of such person or of any corporation of which he or she is a director and/or senior management, to engage in the securities business or in the sale of a particular security or temporarily or permanently restraining or enjoining any such person or any corporation of which he or she is an officer or director from engaging in or continuing any conduct/practice/employment in connection with the purchase or sale of securities, or convicting such person of any felony or misdemeanor involving a security or any aspect of the securities business or of theft or of any felony.

The experience and qualifications of the directors and senior management for at a minimum the last five years are as follows:

The Honorable Hubert Gibbs has been our Chairman and one of our directors since April 9, 2010. After graduating from Oxford University in 1981, Mr. Gibbs started his career as an editor, reader and translator at Quartet Books UK. Subsequently he worked as a stock market analyst with Banque Bruxelles Lambert and then as an independent communications entrepreneur responsible for starting up various companies including Instlang.com which was sold to market leader SDL in 1999. Most recently Mr. Gibbs has been involved in financing and producing independent films, including *As Good as Dead*, and *The Killing Jar*. Mr. Gibbs managed the family estate, Tyntesfield until it was taken over by the National Trust in 2002.

Peter Hoffman has been our Chief Executive Officer and one of our directors since September 2004 and is also our founder. Mr. Hoffman took over as Chairman on December 31, 2009 following the death of previous chairman Anthony Bryan but resigned that position on election of Hubert Gibbs as Chairman. Under Mr. Hoffman's direction, we and our predecessors have produced and or distributed over thirty features since our inception including: *Johnny Mnemonic*, *Never Talk To Strangers*, *9 ½ Weeks II* and *Shattered Image*. As our CEO, his responsibilities include, among others, the selection and production of motion pictures, strategic planning, business development, operations, financial administration, accounting, and reporting to the Board of Directors. Mr. Hoffman was previously President and CEO of Carolco Pictures. He was directly involved at Carolco in the production of a large slate of independent motion pictures, including *Terminator 2*, *Basic Instinct*, *Total Recall*, and *Rambo III*. Mr. Hoffman is a graduate of the Yale Law School and has participated as a lawyer and executive in numerous financial and tax-preferred financings for more than twenty-five years. Mr. Hoffman is the father of Kate Hoffman, our Chief Operating Officer and our Executive Director.

Kate Hoffman has been our Chief Operating Officer and a director since February 2008. As our COO, her responsibilities include supervising the production of motion pictures and licensing and delivering our motion pictures to third parties. She began her career at the age of 17 as an intern for Hollywood casting directors, Mary Vernieu and Risa Gramon-Garcia. Ms. Hoffman then worked for film agent Mort Viner at International Creative Management until his retirement when she joined our predecessors in 1998. She has managed the development, production and delivery of films including *The Believer*, *No Good Deed*, *Stander*, and *Asylum*. In addition to her production responsibilities, Ms. Hoffman is responsible for international distribution, acquisitions and film financing. Ms. Hoffman is the daughter of Peter Hoffman, our Chief Executive Officer and a Director.

Anthony Hickox has been a director since October 2007. He is a film director, writer and producer. Mr. Hickox wrote and directed his first film, *Waxworks* at the age of 21. Mr. Hickox was involved in the production of or direction of *Sundown*, *Warlock: Armageddon*; *Children of the Corn*, *Turn of the Screw*; *Carnival of Souls*, and *Hellraiser 3: Hell on Earth*.



Elaine New was our Chief Financial Officer and a director from January 2007 until July 31, 2009 and remains an executive director. She is Cambridge University educated and is a Price Waterhouse (London) qualified Chartered Accountant. Elaine has been in the media industry for the last ten years as Finance Director of Metrodome Group plc, a UK film distributor. Ms. New was previously engaged as Financial Controller of Harrods International, helping to establish an airport retailing arm, and as Commercial Director of Outfit, a new division of Sears Womenswear Ltd that she helped to create in the latter part of the 1990s. Ms. New was on the Executive Committee of The Quoted Companies Alliance for almost three years helping represent small to mid-cap companies listed both on AIM and the main list of The London Stock Exchange.

Daniel Reardon has been a director since October, 2010. Dan Reardon is a highly successful entrepreneur with a strong legal background and a broad range of experience in entertainment and finance. His activities have included arranging public and private financings, initial public offerings, mergers and acquisitions and other business consulting including positions with The Albert Corporation, where he presided over the acquisition, financing, development and sales of hundreds of condominium units in the Boston area. He is a founding shareholder of four successful public companies in a variety of industries ranging from mining to biotechnology Pan Africa Mining Corp. and Sacre-Coeur Minerals Ltd. Both are Canadian companies traded on the TSX Venture Exchange (Toronto). Mr. Reardon has an extensive background in real estate tax incentive financing programs. He developed and structured tax incentive programs for owners of historic properties for the Architectural Trust in Washington, DC. Mr. Reardon administers several hundred million of incentives annually through the Federal Preservation Tax Incentive Program. His knowledge and expertise of tax incentive programs has been presented before the US Congress to discuss tax incentives and their economic benefits. He also served as CFO for Concrete Film Ventures, which financed several independent, feature film projects, raised venture capital through limited partnerships, and secured substantial lines of credit from media banks successfully using off balance sheet receivable Presale and Gap financing on the following feature films: LEGACY starring David Hasselhoff, MY BROTHER THE PIG starring Scarlet Johansson and Eva Mendes, THE PAVILION starring Richard Chamberlain, and CHANGING HEARTS starring Faye Dunaway. Currently Dan is Executive Producing LUNATIC AT LARGE an original story by Stanley Kubrick based on a treatment by Jim Thompson Starring Scarlett Johansson and Sam Rockwell.

Robert Kaiser is currently and has been since 2007 Chairman and Chief Executive Officer of CLST Holdings, the remaining public company of Cellstar Inc. whose assets were sold in 2007. Mr. Kaiser held several executive positions, including chairman and chief executive officer of Cellstar from 2002 to 2007, an international logistics and distribution company in the communication industry with sales in excess of \$2 billion. Mr. Kaiser was formerly the Chief Executive Officer of Mobile Star and SkyTel/Worldcom from 1996 to 2001. Mr. Kaiser was also the Chief Financial Officer of Southwestern Bell Mobile Systems from 1986-1996.

## 6.B. Compensation

### Cash Compensation

Since February 15, 2009, our compensation policies with respect to our Directors and executive officers are established, administered, and the subject of periodic review by our Independent Directors in accordance with the NASDAQ Marketplace Rules. Total compensation accrued and/or paid (directly and/or indirectly) to the Directors and senior management during the fiscal year ended June 30, 2011 was \$894,838. We have a Compensation Committee, consisting of Mr. Gibbs, Mr. Hickox, and Mr. Reardon, all three Independent Directors, that reviews and approves all employee compensation and bonuses.

Table No. 10  
Officer and Director Compensation

| Name          | Annual Compensation |       |                    | Long-Term Compensation                                       |  |                  |                           |
|---------------|---------------------|-------|--------------------|--|--|------------------|---------------------------|
|               | Salary              | Bonus | Other Compensation | Awards<br>Securities<br>Under<br>Option/<br>SAR's<br>Granted | Shares/<br>Units<br>Subject to<br>Resale<br>Restrictions | LTIP<br>Pay outs | All Other<br>Compensation |
|               | (\$)                | (\$)  | (\$)               | (#)  | (\$)   | (\$)             | (\$)                      |
| Peter Hoffman | \$ 500,000          | -     | -                  | -  | -  | -                | -                         |

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|                               |         |   |   |   |   |   |   |
|-------------------------------|---------|---|---|---|---|---|---|
| Elaine New                    | 269,826 | - | - | - | - | - | - |
| Kate Hoffman                  | 92,158  | - | - | - | - | - | - |
| Other Directors as<br>a Group | 33,853  | - | - | - | - | - | - |

Stock Options.

Seven Arts intends to grant stock options to Directors, Senior Management and employees as an Unapproved Share Option Scheme authorized under United Kingdom law. The Group may grant options worth up to £ 120,000 to any employee at the date of grant and grant up to £ 3,000,000 for all employees at the date of grant. See Table No. 11 for information about stock options outstanding.

Table No. 11  
Stock Option Grants from Inception to June 30, 2011

| Name   | Number of Options Granted | % Of Total Options Granted on Grant Date | Exercise Price per Share | Grant Date | Expiration Date | Mkt. Value of Securities Underlying Options on Date of Grant |
|--|---------------------------|--|--------------------------|------------|-----------------|--|
| Michael Garstin                                  | 20,000                    | 100 %                                    | \$ 1.54                  | 6/1/2008   | 6/1/2011        | \$ 1.80  |
| Michael Arata(1)                                 | 2,000                     | 100 %                                    | \$ 1.54                  | 6/1/2008   | 6/1/2011        | \$ 1.80  |
| Tony Hickox(3)                                   | 2,000                     | 100 %                                    | \$ 2.29                  | 2/7/2007   | 2/7/2010        | \$ 2.29  |
| Julia Verdin(3)                                  | 2,000                     | 100 %                                    | \$ 2.29                  | 2/7/2007   | 2/7/2010        | \$ 2.29  |
| Elaine New(3)                                    | 2,000                     | 100 %                                    | \$ 2.29                  | 2/7/2007   | 2/7/2010        | \$ 2.29  |
| Chris Bialek(2)                                  | 2,000                     | 100 %                                    | \$ 2.29                  | 2/7/2007   | 2/7/2010        | \$ 2.29  |
| Philip Kendall                                   | 4,000                     | 100 %                                    | \$ 1.46                  | 9/30/2008  | 9/29/2011       | \$ 1.15  |
| Other Employees                                  | 12,000                    | 100 %                                    | \$ 1.55                  | 11/7/08    | 11/7/11         | \$ 1.75  |
| <b>Total Granted</b>                             | <b>46,000</b>             |  |                          |            |                 |  |
| Exercised during fiscal Year ended June 30, 2009 | (2,000 )                  |  |                          |            |                 |  |
| Exercised during fiscal Year ended June 30, 2010 | (2,000 )                  |  |                          |            |                 |  |
| Cancelled during fiscal Year ended June 30, 2010 | (6,000 )                  |  |                          |            |                 |  |
| Cancelled during fiscal Year ended June 30, 2011 | (20,000 )                 |  |                          |            |                 |  |
| <b>Total Outstanding</b>                         | <b>16,000</b>             |  |                          |            |                 |  |

(1) On November 5, 2008 Michael Arata exercised 2,000 of these options.

(2) On December 1, 2009 Chris Bialek exercised all 2,000 of these options.

(3) Options issued to employees totaling 6,000 were cancelled during fiscal year ended June 30, 2010.

(4) Options issued to Michael Garstin expired during fiscal year ended June 30 2011.

In addition, we have granted stock options in the following amounts to the following persons in connection with financing services provided by them:

| Name  | Number of Options Granted | Exercise Price Per Share | Market Value of Securities on Date of Grant | Grant Date    | Expiration Date |
|---|---------------------------|--------------------------|---|---------------|-----------------|
| Blue Rider Finance/<br>Robert Oppenheim(1)          | 10,000                    | \$ 1.125                 | \$ 1.463                                    | Jan. 22, 2008 | Jan. 23, 2011   |
| Trafalgar Capital<br>Specialized Investment Fund(2) | 32,000                    | \$ 1.013                 | \$ 1.463                                    | Jan. 31, 2008 | Jan. 30, 2013   |
| Trafalgar Capital<br>Specialized Investment Fund(2) | 12,000                    | \$ 1.013                 | \$ 1.988                                    | Oct. 30, 2008 | Oct. 30, 2013   |

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|  |           |         |    | March 1 | Feb 28  |
|--|-----------|---------|----|---------|---------|
| Bobby Meyers   | 20,000    | \$ 2.00 | \$ | 2011    | 2013    |
| National Financial                                   | 100,000   | \$ 1.00 | \$ | Sept 21 | Sept 20 |
| Total Granted  | 174,000   |         |    | 2010    | 2013    |
| Exercised during the fiscal year ended June 30, 2009 | (2,500 )  |         |    |         |         |
| Cancelled during the fiscal year ended June 30, 2009 | (44,000 ) |         |    |         |         |
| Cancelled during the fiscal year ended June 30, 2011 | (7,500)   |         |    |         |         |
| Total Outstanding                                    | 120,000   |         |    |         |         |

(1) On October 21, 2008 Robert Oppenheim exercised 12,500 options.

(2) We terminated all 44,000 stock options granted to Trafalgar in October 2008 in return for 6,800 restricted ordinary shares.

Langley's remaining Debentures have a face value of £1,750,000 (approximately \$3,432,500 at the exchange rate prevailing at the time of the financing) and they have an option to convert into a maximum aggregate of 280,000 ordinary shares. There is no due date or required due date on our Debentures. The Debentures rank junior to all our indebtedness and senior only to our ordinary or preference shares and they are included as a part of Shareholders' Equity.

#### Change of Control Compensation.

We have now and have had in all periods described no plans or arrangements in respect of compensation received, or that may be received, by our executive officers to compensate such officers in the event of termination of employment (as a result of resignation, retirement, change of control) or a change of responsibilities following a change of control, where the value of such compensation exceeds US\$60,000 per senior manager other than those set out in Peter Hoffman's Employment Agreement. Pursuant to the Employment Agreement, if we terminate Peter Hoffman without cause, we shall be obliged to pay SAP Inc. a lump sum of approximately \$1,500,000.

#### Other Compensation.

No senior management director received "other compensation" in excess of the lesser of US\$25,000 or 10% of such officer's cash compensation, and senior management and Directors as a group did not receive other compensation which exceeded \$25,000 times the number of persons in the group or 10% of the compensation.

#### Bonus/Profit Sharing/Non-Cash Compensation.

Except for the stock options discussed above, we have no material bonus or profit sharing plans pursuant to which cash or non-cash compensation is or may be paid to some of our directors or senior management, except that our Board has adopted a bonus plan substantially in the following form:

1. Compensation Committee will recommend amount of bonus pool each year, which will be 10% of pre-tax profits for the prior fiscal year. The CEO and the Compensation Committee will decide recipients of project-related awards and amounts.
2. In future years, comparisons will be made to peer groups in the motion picture industry.
3. There will be two types of annual bonuses:
  - (a) Those related to the overall management of our Group
  - (b) Those related to performance on specific projects
4. Managers in bonus pool:
  - (a) Peter Hoffman (Chairman/CEO)
  - (b) Kate Hoffman (COO)
  - (c) Elaine New
5. Management bonuses as follows:

|                       | CEO | Management | Project<br>Related |
|-----------------------|-----|------------|--------------------|
| Group Results         | 40% | 25%        | 15%                |
| Individual Objectives | 10% | 30%        | 50%                |
| Subjective            | 20% | 20%        | 25%                |
| Share Performance     | 30% | 25%        | 10%                |

6. Individual objects for Management will be agreed by the Board.

7. Criteria include individual contributions to our overall profits.

#### Seven Arts Employee Benefit Trust

The Group employed Smith and Williamson Trustees Jersey Ltd to establish the Seven Arts Employee Benefit Trust (“EBT”) to acquire 3,000,000 of the Group’s preference shares from Armadillo Investments Plc. in a transaction described in Item 7.B Related Party Transactions below.

EBT is governed by a Trust Deed that Seven Arts entered into with the trustee. The Group has the right after approval of the audit committee to restrict the Trust’s right to vote its shares of the Group to prevent the Trust from taking control of the Group and the right to remove the Trustees under certain circumstances for the same purpose. The Group has no interest in the profits or losses of the Trust on the Group’s shares and does not control the actions of the Trustees in the sale or use of these shares.

All cash and ordinary shares owned by EBT are held by EBT for the benefit of Seven Arts’ employees. Any distributions by EBT will be approved by the trustees and are expected to be made to the Group’s executive management as part of the Group’s bonus plan described above.

#### Pension/Retirement Benefits

No funds were set aside or accrued by Seven Arts as of June 30, 2011 to provide pension, retirement or similar benefits for Directors or senior management.

#### 6.C. Board Practices

##### 6.C.1. Terms of Office

Refer to Item No. 6.A.1.

##### 6.C.2. Directors’ Service Contracts

SAP Inc. has an employment agreement with Peter Hoffman pursuant to which he will act as our CEO until December 31, 2013. Upon acquisition of control of our Group, we entered into a contract with the SAP Inc. to secure Mr. Hoffman’s services solely to us and our subsidiaries as our CEO. In connection with that employment agreement, we have granted Mr. Hoffman

the right to sole responsibility for creative and business decisions regarding motion pictures we develop and produce,

a right of first refusal to produce remakes, sequels or prequels of motion pictures produced by Mr. Hoffman and acquired by us or any motion picture produced by us during his employment,

an annual salary of \$500,000 per year plus bonuses, expenses and a signing option and

a right upon termination without cause to a lump sum payment of approximately \$1,500,000, an assignment of all projects in development during the term of his employment and any amounts due upon such compensation as an excise tax.

We have an employment agreement with Kate Hoffman pursuant to which she will act as our COO ad infinitum at a salary of \$85,000 (£52,000) per year plus bonuses and expenses. Ms. Hoffman's contract contains a "non-compete" clause pursuant to which she will be excluded from competing against us for 6 months following the date of her termination.

We have an employment agreement with Elaine New pursuant to which she will act as an executive director ad infinitum at a salary of \$225,000 (£150,000) per year plus bonuses and expenses. Ms. New's contract contains a "non-compete" clause pursuant to which she will be excluded from competing against us for 6 months following the date of her termination.

All of the employment agreements grant us a right to injunctive relief if the respective employee breaches the agreement. With the exception of Ms. Hoffman's and Ms. New's agreements, the employment agreements do not contain "non-compete" clauses.

#### Director Compensation

Anthony Hickox will receive approximately \$1,500 per meeting attended.

Robert Kaiser will receive \$1500 per month

#### 6.C.3. Board of Director Committees

We have an Audit Committee, which recommends to the Board of Directors the engagement of our independent auditors and reviews with the independent auditors the scope and results of our audits, our internal accounting controls, and the professional services furnished by our independent auditors. The current members of the Audit Committee are Mr. Robert Kaiser (Chair), Mr. Gibbs and Mr. Reardon. The Audit Committee did not meet separately in the fiscal period ended June 30, 2011, but will meet separately with the Group's Auditors to review the year-end financial statements and the audit process.

Our Compensation Committee (Mr. Gibbs, Mr. Hickox and Mr. Reardon) and Nominating Committee (Mr. Gibbs, Mr. Hickox and Mr. Reardon) are made up of three of our independent directors.

As of June 30, 2011, Management has determined that we are in compliance with The Combined Code of Corporate Governance of the United Kingdom, Sections A and B of which stipulate that the Remuneration Committee be comprised of at least two members and that they be non-executive and that the Nominating Committee be comprised of a majority of non-executive directors.



All Committees of the Board are organized pursuant to our Board of Directors Memorandum and resolutions of the Board of Directors. The terms of reference of each committee are based on the subject matter jurisdiction of each Committee. The Compensation Committee reviews and approves all employee compensation and bonuses. The Nomination Committee proposes candidates for election to our Board of Directors.

All meetings of each Committee are on an –ad hoc basis, decisions are made by majority vote and all decisions are reported to the full Board of Directors for approval.

## 6.D. Employees

As of June 30, 2011, Seven Arts had 13 employees and independent contractors, providing full time services. Our affiliates employ many part time employees for production of our motion pictures, but we do not engage temporary employees on any regular or material basis. We are not signatory to any labor union collective bargaining agreements, but our affiliates in the United States are signatory to the current Writer's Guild of America, Directors Guild of America and IATSE Low Budget Agreements and have in the past been signatory to the Screen Actors Guild Agreement. Our employees have ranged from a low of six to a high of fourteen over the last three fiscal years.

## 6.E. Share Ownership

As of August 31, 2011 Seven Arts had issued 6,476,344 ordinary shares of £0.25 and 13,184,000 deferred shares of £0.45 each and 2,268,120 deferred shares of £1. There were approx. 500 shareholders as of that date. On August 31, 2011 SAE Inc. issued one of its shares for each share in SAP Plc. and took on the NASDAQ listing. As of November 30, 2011 SAE Inc. had 16,475,411 shares in issue.

Table No. 12A

## Shareholdings of Directors and Senior Management

| Name of Beneficial Owner (1)          | Address of Beneficial Owner                                   | Amount of Beneficial Ownership (1) | Percent of Class |
|---------------------------------------|---|------------------------------------|------------------|
| Seven Arts Pictures Inc.(2)           | 8439 Sunset Boulevard, 4th Floor,<br>West Hollywood, CA 90069 | 23,800                             | 0.2 %            |
| All Officers and Directors as a Group |   | 16,000                             | 0.2 %            |

(1) Beneficial ownership is determined in accordance with the Rule 13d-3(a) of the Exchange Act and generally includes voting or investment power with respect to securities and includes shares underlying convertible debentures, warrants and options that have been issued, granted and have vested and not been exercised and shares underlying options that will vest within the next 60 days only in respect to any person listed in the table. Except as subject to community property laws, where applicable, the person named above has sole voting and investment power with respect to all ordinary shares shown as beneficially owned by him/her.

(2) Peter Hoffman controls approximately 70% of the voting stock of SAP Inc., and is a beneficial owner of the Group's ordinary shares held by Seven Arts Pictures Inc. This total does not include 140,000 ordinary shares pledged to ApolloMedia and over which ApolloMedia has dispositive control, 150,000 shares issued to New Moon Pictures LLC over which Armadillo has dispositive control and 23,800 shares pledged to an insurance company over which the insurance company has dispositive control.

## ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

## 7.A. Major Shareholders.

## 7.A.1.a. Holdings By Major Shareholders.

Table No. 12B lists, as of October 20, 2011, all shareholders who beneficially own 5% or more of Seven Arts' voting securities, consisting solely of ordinary shares, and the amount of Seven Arts' voting securities owned by the 5% shareholders as a group.

Table No. 12B

## Shareholdings of 5% Shareholders

| Name of Beneficial Owner (2)                | Address of Beneficial Owner                           | Amount of Beneficial Ownership(2) | Percent of Class |
|---|---|-----------------------------------|------------------|
| SAP Plc (10)                                | 136-144 New Kings Road,<br>London SW6 4LZ             | 2,000,000                         | 10.45            |
| Magna et al(8)                              | 8439 Sunset Boulevard<br>West Hollywood, CA<br>90069  | 1,600,000                         | 8.4%             |
| RELATED PARTIES                             |   |                                   |                  |
| New Moon Pictures LLC                       | 900 Royal Street New Orleans,<br>Louisiana, USA       | 150,000                           | 0.8%             |
| ApolloMedia GmbH & Co. Filmproduktion KG(5) | Candidplatz 11, 81543<br>Munich, Germany              | 140,000                           | 0.8%             |
| Peter Hoffman(3)                            | 8439 Sunset Boulevard,<br>West Hollywood, CA<br>90069 | 23,800                            | 0.1%             |
| Seven Arts Pictures Inc.                    | 8439 Sunset Blvd,<br>West Hollywood, CA<br>90069      | 163,800                           | 0.91%            |
| Lincoln Center Capital (6)                  | 8439 Sunset Boulevard,<br>West Hollywood, CA<br>90069 | 100,000                           | 0.5%             |
| Options to directors                        | 8439 Sunset Boulevard,<br>West Hollywood, CA<br>90069 | 350,000                           | 1.8%             |
| Other Employees (7)                         | 8439 Sunset Boulevard,<br>West Hollywood, CA<br>90069 | 12,000                            | 0.1%             |
| Employee Benefit Trust (4)                  | 136-144 New Kings Road,<br>London SW6 4LZ             | 200,000                           | 1.1              |

|  |   |           |      |
|--|---|-----------|------|
|  | 8439 Sunset Boulevard,<br>West Hollywood, CA<br>90069 |           |      |
| Total officers and directors as a group(9) |   | 1,139,600 | 6.0% |

Total Shareholding as at November 30, 2011 was 16,475,411 (1)

Total beneficial shareholdings at February 22, 2011 was 19,141,411 (2)

- (1) Total shareholding as at November 21, 2011 was 15,699,908.
- (2) Beneficial ownership is determined in accordance with the Rule 13d-3(a) of the Exchange Act and generally includes voting or investment power with respect to securities and includes shares underlying convertible debentures, warrants and options that have been issued, granted and have vested and not been exercised and shares underlying options that will vest within the next 60 days only in respect to any person listed in the table. Except as subject to community property laws, where applicable, the person named above has sole voting and investment power with respect to all ordinary shares shown as beneficially owned by him/her. Total shares issued as at November 30, 2011 was 16,475,411 with the balance of beneficial ownership in options and potential loan conversions.
- (3) Peter Hoffman controls approximately 70% of the voting stock of SAP Inc., and is a beneficial owner of our ordinary shares held by Seven Arts Pictures Inc. This total does not include 140,000 ordinary shares pledged to ApolloMedia and over which ApolloMedia has dispositive control nor 150,000 shares issued to New Moon Pictures LLC and pledged to Armadillo nor 23,800 shares issued to SAP Inc., and pledged to an insurance company. We intend to use the proceeds from the offering to pay a settlement amount with ApolloMedia and Armadillo (Upon the occurrence of which these 290,000 shares will be returned to us). Mr. Hoffman has voting and dispositive powers with respect to these shares.
- (4) Under the terms of the Trust Deed establishing the Seven Arts Employee Benefit Trust, EBT is to abstain from voting any of our shares that it holds unless we determine otherwise. Ben Newman has voting and dispositive powers with respect to these shares.
- (5) Represents 140,000 ordinary shares pledged by SAP Inc. and over which ApolloMedia has dispositive control. We intend to use proceeds from a proposed offering to pay a settlement amount to ApolloMedia upon which time SAP Inc. and ApolloMedia have agreed that such ordinary shares would be returned to us. Joerg Westerkamp has dispositive powers with respect to these shares and Mr. Hoffman has voting powers with respect to these shares.
- (6) Represents shares issued for services.
- (7) Represents ordinary shares underlying vested options.
- (8) Represents convertible debt acquired under s144 which is convertible into free-trading stock. As yet this debt has not been converted. Joshua Sason has voting and dispositive powers with respect to these shares.
- (9) This includes all pledged shares (140,000 pledged to Apollo, 150,000 pledged to Armadillo, ) plus SAP Inc's shares ,and other employees options.
- (10) SAE Inc issued 2,000,000 shares to SAP Plc, as part of the asset transfer to cover any liabilities left in the PLC and not assumed by SAE Inc.

7.A.1.b. Significant Changes in Major Shareholders' Holdings.

During the past three years, we have issued the following securities (including options to acquire our common stock, and debt convertible into our common stock). No underwriters were involved in these issuances. We believe that each of the following issuances was exempt from registration under the Securities Act in reliance on Regulation S under the Securities Act or pursuant to Section 4(2) of the Securities Act regarding transactions not involving a public offering.

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| Purchaser  | Date of Issuance            | Number of Securities      | Title of Securities        | Consideration |
|--|-----------------------------|---------------------------|----------------------------|---------------|
| Seven Arts Employee Benefit Trust                                  | November 2, 2008            | 400,000                   | Ordinary Shares            | (1)           |
|  | May 5, 2010                 | 80,000                    | Ordinary Shares            | (1)           |
| Langley Park Investment Trust PLC                                  | March 15, 2007              | 200,000                   | Ordinary Shares            | (2)           |
| Unique Fidelity Engineering Ltd.                                   | June 28 2007                | 6,800                     | Ordinary Shares            | \$100,000     |
|  | August 15 2007              | 100,000                   | Ordinary Shares            | \$287,000     |
| Michael Garstin  | June 1, 2008                | 20,000                    | Options                    | (3)           |
| Chris Bialek   | January 3, 2007             | 2,000                     | Options now exercised      | (3)           |
| Philip Kendall   | September 30, 2008          | 4,000                     | Options                    | (3)           |
| Michael Arata  | June 1, 2008                | 2,000                     | Options now exercised      | (3)           |
| Blue Rider nance/Robert Oppenheim                                  | January 22, 2008            |                           |                            | (4)           |
|  | October 21, 2008            | 7,500                     | Options<br>Ordinary Shares | (6)           |
| Trafalgar Capital Special Investment Fund                          | October 15, 2008            | 70,000                    | Convertible Note           | (5) (7)       |
|  | January 31, 2008            |                           | Options                    | (5) (7)       |
|  | October 30, 2008            |                           | Options                    | (5) (7)       |
|  | May 22, 2009                |                           | 6,800<br>Ordinary Shares   | (5) (7)       |
|  | June 22, 2010               |                           | 68,000<br>Ordinary Shares  | (5)           |
| January 11, 2011   |                             | 85,000<br>Ordinary Shares | (5)                        |               |
| Sendero Capital Inc, Agua Alta Inc,<br>Scarborough Investment Inc. | August 30 2010              | 94,000                    | Convertible debt           | \$470,000     |
|  | Revised<br>December 17 2010 |                           |                            |               |
| Asher Enterprises  | May 26, 2010                |                           | Convertible Debt           | \$150,000 (8) |
|  | June 15, 2010               |                           | Convertible Debt           |               |
|  | December 31, 2010           | 53,668                    | Ordinary Shares            |               |
| DC Consulting LLC  | October 8, 2010             | 5,000                     | Ordinary Shares            | (4)           |

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|   |                   |         |                 |     |
|---|-------------------|---------|-----------------|-----|
| National Financial Communications Corporation | October 8, 2010   | 6,000   | Ordinary Shares | (4) |
| Isaacs Capital LLC                            | December 17, 2010 | 70,000  | Ordinary Shares | (4) |
|   | January 27, 2011  | 120,000 | Ordinary Shares |     |
| New Moon Pictures                             | February 22, 2011 | 150,000 | Ordinary Shares | (9) |



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|                              |  |                               |   |      |
|------------------------------|--|-------------------------------|---|------|
| Palm Finance                 | March 24, 2011   | 150,000                       | Ordinary Shares                                       | (10) |
| TCA Capital Fund             | May 13, 2011   | 175,000                       | Ordinary Shares                                       | (11) |
| Eden Corporate Finance       | May 25, 2011   | 100,000                       | Ordinary Shares                                       | (12) |
| Lincoln Capital              | June 27, 2011  | 100,000                       | Ordinary Shares                                       | (13) |
| J H Darbie                   | July 14, 2011  | 10,000                        | Ordinary Shares                                       | (14) |
| Scarborough Conversions      | July 29 2011   | 507,000                       | Ordinary Shares                                       | (15) |
| Palm Finance Conversions     | August 2011  | 3,141,433                     | Ordinary Shares                                       | (16) |
| Redwood                      | September 12<br>2011                                   | 197,916                       | Ordinary shares                                       |      |
| Safron                       | November 7, 2011                                       | 1,819,557                     | Ordinary Shares                                       |      |
| Watley Group debt Conversion | August 4, 2011<br>October 25, 2011                     | 60,000<br>160,000             | Ordinary Shares<br>Ordinary Shares                    | (17) |
| 120db Conversions            | August 10, 2011<br>September, 2011<br>October 24, 2011 | 250,000<br>250,000<br>250,000 | Ordinary Shares<br>Ordinary Shares<br>Ordinary Shares | (18) |
| Goldstrand                   | September 2011   | 2,090,000                     | Ordinary Shares                                       | (19) |
| Goldstrand                   | October 13, 2011                                       | 1,035,000                     | Ordinary shares                                       |      |
| Watley Group                 | September 26,<br>2011                                  | 250,000                       | Ordinary shares                                       |      |
| Fletcher                     | October 4, 2011  | 250,000                       | Ordinary Shares                                       | (20) |
| Sendero/Agua convertible     | October 21, 2011                                       | 1,786,374                     | Ordinary Shares                                       | (21) |
| Goldstrand                   | November 10,<br>2011                                   | 150,000                       | Ordinary Shares                                       | (22) |
| Directors                    | October 14, 2011                                       | 350,000                       | Options   | (23) |
| SAP Plc.                     | January 27, 2011                                       | 2,000,000                     | Ordinary Shares                                       | (24) |

- (1) We issued 400,000 ordinary shares to Seven Arts Employee Benefit Trust (EBT) upon their conversion of 2,500,000 preference shares and an additional 80,000 upon the conversion of the remaining 500,000 preference shares. The EBT has subsequently sold /transferred to creditors of the Group all but 266,667 shares and paid the funds received over to the Group in reduction of the Group's loan to the EBT. All sales/transfers of shares are carried out at fair market value.
- (2) We issued 200,000 shares to Langley Park Investment Trust PLC in exchange for the conversion of £1,250,000 of a convertible debenture. We believe that Langley have disposed of some of their shares and currently have a balance of 51,525 shares.
- (3) We issued these options to employees and consultants as part of a compensation and incentive program.
- (4) We issued these shares in connection with financing services provided by these persons.
- (5) On October 15, 2008 the Group borrowed £1,000,000 from Trafalgar Capital Special Investment Fund ("Trafalgar"). A portion of this loan the Group advanced to the EBT for it to use as the first installment for the acquisition of all the Preference Shares owned by Armadillo. On September 2, 2009 the Group repaid Trafalgar \$1,000,000 (about £698,934) as a partial payment against this loan, with the remaining balance subject to repayment in cash or convertible to the ordinary shares of the Group at the conversion terms as agreed between Trafalgar and the Group. On June 22, 2010 an amended agreement was entered into with Trafalgar for an extension of the due date of the convertible debentures to December 31, 2010, and the Group agreed to issue 68,000 ordinary shares to settle a portion of the debt. Trafalgar agreed to reduce the loan amount from the proceeds it received from selling the 68,000 ordinary shares. The transaction was consummated subsequent to the date of the financial statements and all of the 68,000 shares have been sold in the market before December 31, 2011.. Subsequent to June 30, 2010, a further amended agreement was entered into with Trafalgar for an extension of the due date of the convertible debentures to March 31, 2011, and the Group agreed to issue 85,000 ordinary shares to settle a portion of the debt (see subsequent events note 22). Trafalgar agreed to reduce the loan amount from the proceeds it receives from selling the 85,000 ordinary shares. The balance outstanding on the loan after sale of these 85,000 shares is expected to be approximately \$225,000. The per-share value is determined as the amount recovered by Trafalgar on sale thereof in the market and Trafalgar may "put" these shares to us at £1.00 per share on April 30, 2011 if not sold. We intend to pay the balance of the sum due to Trafalgar by similar conversion of our shares.
- (6) We issued 2,500 of our ordinary shares to Robert Oppenheim pursuant to the exercise of options he had to purchase our ordinary shares for £0.15 per share.
- (7) On May 22, 2009, we issued 6,800 shares to Trafalgar Capital Special Investment Fund in return for the return of the 220,000 options we had granted them to purchase our ordinary shares.
- (8) This convertible debt is convertible at a discount to market value and the shares issued. All had been converted by December 31, 2010 into 89,668 ordinary shares.
- (9) 250,000 shares were issued to New Moon Pictures who pledged them to Armadillo who in turn extended the period to repay the £1,000,000 owing by the EBT and released their lien on 66,667 shares held by the EBT.
- (10) 150,000 shares were issued to Palm Finance as loan collateral.
- (11) 175,000 shares were issued to TCA Capital Fund as surety against the loan of \$125,000 and \$50,000 in fees.
- (12) 100,000 shares were issued to Eden Corporate Finance in part payment of the loan.

- (13) 100,000 shares were issued to Lincoln Capital as a fee for marketing Pool Boys.
- (14) 10,000 shares were issued to JH Darbie as a finder's fee.
- (15) \$225,000 Scarborough convertible (including interest) was converted into 507,000 ordinary shares at its maturity date.
- (16) \$2.75 million of Palm Finance film debt was sold to Magna/Redwood who then converted part of it to 5,158,907 shares . A balance of approximately 1.6 million shares is yet to be converted. (average conversion c\$0.41)
- (17) \$152,000 debt due to Watley was converted to 220,000 shares at \$0.70/share.
- (18) Film debt due to 120db for the film Knife Edge was converted to equity.
- (19) \$535,000 of debt due to The Northern Trust/Watley was converted to equity at \$0.15/share.
- (20) The Fletcher Group bought \$250,000 restricted shares at \$1/share to settle a contract entered into with the Group in January 2011.
- (21) \$245,000 convertibles plus accrued interest were converted into 1,786,374 shares at \$0.15/share on the maturity date of the convertibles.
- (22) \$150,000 of restricted stock was sold to Goldstrand at \$1/share.
- (23) 350,000 share options were issued to all Board members (50,000 options each) at the market price on October 14, 2011.
- (24) \$2,000,000 shares were pledged by SAE Inc to SAP Plc to cover any liabilities not taken on by SAE Inc when the business transferred from Plc. to Inc. (Original date Jan 27, 2011)

7.A.1.c. Different Voting Rights.

Seven Arts' major shareholders do not have different voting rights.

7.A.2. Share Ownership.

As of August 31, 2011 Seven Arts had issued 6,611,564 ordinary shares of £0.25 and 13,184,000 deferred shares of £0.45 each and 2,268,120 deferred shares of £1. There were approx. 500 shareholders as of that date. On August 31 2011 SAE Inc. issued one of its shares for each share in SAP Plc. and took on the NASDAQ listing. As of November 30, 2011, SAE Inc. had 16,475,411 shares of common stock and 125,125 shares of preferred stock outstanding.

7.A.3. Control of the Group.

Seven Arts is a publicly owned English corporation, the shares of which are owned by U.S. residents and foreign residents. Seven Arts is not controlled by any foreign government or other person(s).

7.A.4. Change of Control of Group Arrangements

There are no arrangements, known to the Group, which may at a subsequent date result in a change of control of the Group.

7.B. Related Party Transactions

We have entered into several agreements and arrangements with Seven Arts Pictures Inc. ("SAP Inc."), an entity that owns approximately 163,800 shares of our common stock including 140,000 shares of common stock pledged to Apollo Media GmbH & Co Filmproduktion KG as set forth in Principal Shareholders and the balance is pledged to other lenders, whose majority beneficial shareholder of SAP Inc. is our Chief Executive Officer, Peter Hoffman. These transactions include:

Upon acquisition of control of our Group by SAP Inc. in September 2004, we entered into an agreement with SAP Inc. under which SAP Inc. provided the services of Peter Hoffman for the amount of his contracted salary and the Los Angeles office and staff of SAP Inc. to us at cost. Pursuant to two interGroup agreements, SAP Inc. also from time-to-time has and will own limited liability companies in the United States which distribute our motion pictures for a fee, with all profits ensuing to our benefit. These companies may also provide other services to us at no fee other than Mr. Hoffman's salary and the direct third-party costs of SAP Inc.'s Los Angeles office, all of which are reflected in our financial statements. These other services may include accounting services, audits of distribution statements, collection of accounts receivable, supervision of production of motion pictures and similar day-to-day aspects of our business. SAP Inc. has assigned to us any proceeds arising from services performed by SAP Inc. on our behalf. We have granted SAP Inc. the power and authority to enter into agreements on our behalf. SAP Inc. is not to take any actions on our behalf without our approval.

Because we do not have a working capital line of credit for movie production, (although we do have a line of credit available to our affiliate, SAPLA, to finish the restoration of the post-production facility at 807, Esplanade, New Orleans), SAP Inc. directly or through various Louisiana limited liability companies of which it is managing member, have from time-to-time made non-interest bearing advances to us or our subsidiaries, when we have been unable to collect our receivables on a timely basis or have received advances back from us. All advances have been for customary working capital purposes and the net total is \$ 2,725,974 as of June 30 2011 and \$3,021,184 as of June 30, 2010 owed to the Group. SAP Inc. has pledged an interest in its shares of the Group's stock to secure certain SAP Inc. indebtedness.



Together with SAP Inc., we entered into a settlement agreement, dated September 30, 2006, with ApolloMedia GmbH & Co. Filmproduktion KG (“ApolloMedia”) related to a dispute regarding amounts ultimately payable to ApolloMedia from distribution of the motion picture Stander and one of our subsidiaries’ assumption of indebtedness of approximately \$2,000,000 related to Stander upon acquisition of control of our Group by SAP Inc.. The Settlement Agreement fully releases us and our subsidiaries from any liability to ApolloMedia in exchange for a payment of \$1,800,000 to be made by SAP Inc. (of which \$175,000 has been paid). In connection with the SAP Inc.’s payment obligation of the settlement amount to ApolloMedia, we issued 140,000 ordinary shares to SAP Inc. which SAP Inc. immediately pledged to ApolloMedia to secure SAP Inc.’s obligations under the settlement agreement. SAP Inc. has agreed that it will (1) return to us all ordinary shares in excess of 400,000 not necessary to satisfy SAP Inc.’s obligations to ApolloMedia and (2) deliver to us from SAP Inc.’s ordinary shares, any ordinary shares in excess of 80,000 in fact sold by SAP Inc. to satisfy the indebtedness to ApolloMedia under the settlement agreement. The shares pledged to ApolloMedia will be sold by it as necessary for ApolloMedia to derive net proceeds of \$1,625,000, and any pledged shares remaining after such sale will be returned to us.

We have entered into several agreements and arrangements with Seven Arts Pictures Louisiana LLC (“SAPLA”), an entity that is 60% beneficially owned by SAP Inc.. These transactions include:

A guarantee that we provided to SAPLA to cover its indebtedness under a Credit Agreement that SAPLA entered into with Advantage Capital Community Development Fund, L.L.C. (“Ad Cap”), dated October 11, 2007, for the acquisition and improvement of a production and post production facility located at 807 Esplanade Avenue in New Orleans, Louisiana. The aggregate borrowing amount under this facility was \$3,700,000, all of which was drawn down as of April 30, 2010. In November 2010 Palm Finance Inc (“Palm”) acquired this mortgage secured on the facility for \$1,000,000 and agreed to extend a construction facility of \$1,850,000 to complete the facility. We have guaranteed the indebtedness to Palm and have not included it in our total indebtedness. We expect this facility will be completed for a cost not to exceed \$1,850,000 on or before December 31, 2011. We do not anticipate the use of any material amount of our working capital to complete and operate this facility, and we expect to realize substantial film production, film infrastructure, historic rehabilitation and other state and federal tax credits and other tax incentives from the acquisition, renovation, and operation of this property as a post production facility. In particular SAPLA has submitted audited expense reports which would generate approximately \$4,000,000 in Louisiana Film Infrastructure tax credits \$3,000,000 in Louisiana State Rehabilitation tax credits and \$3,000,000 in Federal Historic Preservation tax credits.

A distribution agreement that we entered into with SAPLA later assigned by SAPLA to Seven Arts Pictures Louisiana (Equicap) LLC (“SAPLA Equicap”) pursuant to which we granted SAPLA the right to distribute our motion pictures in return for a distribution fee of 20% of the revenues generated from these films, SAPLA and SAPLA Equicap is obligated under the interGroup agreements described above to pay and has permitted us to retain 100% of all such distribution fees.

By reason of the transactions set forth above, we have paid and received the following sums for the following transactions with companies controlled by or related to Mr. Hoffman for each of the last two fiscal years.

TABLE OF RELATED PARTY BALANCES AS AT PERIOD END

|                        | Fiscal<br>Year<br>Ended | Fiscal Year<br>Ended |
|------------------------|-------------------------|----------------------|
|                        | 6/30/10                 | 6/30/11              |
| Related Party Balances |                         |                      |
| Opening Balance        | \$2,048,134             | \$3,021,183          |
| Movement in the period | 973,050                 | (295,209 )           |

|                 |             |             |
|-----------------|-------------|-------------|
| Closing Balance | \$3,021,184 | \$2,725,974 |
|-----------------|-------------|-------------|

## MOVEMENT IN RELATED PARTY BALANCES YEAR ON YEAR

| Transaction (1)                                 | Fiscal Year<br>Ended<br>6/30/10 | Fiscal<br>Year Ended<br>6/30/11 |
|---|---------------------------------|---------------------------------|
| Payment of General and Administrative Costs (2) | \$(1,986,438)                   | \$(2,356,214)                   |
| Payment of Film Costs                           | (124,448 )                      | (37,935 )                       |
| Payment for Shares Pledged                      | 185,438                         | 1,046,610                       |
| Loans to Us                                     | 828,258                         | 552,330                         |
| Equicap   | 1,358,155                       | -                               |
| Grant of Distribution Rights to SAPLA           | 712,086                         | 500,000                         |
| Total Movement                                  | \$973,050                       | \$(295,209 )                    |

(1) Positive numbers (without brackets) represent payments by us to Mr. Hoffman or his affiliates, including his salary, and negative numbers (in brackets) represent payments by Mr. Hoffman or his affiliates to us.

(2) General and administrative costs include salaries of employees providing services for our benefit, office costs, insurance premiums and rent, paid by Seven Arts Pictures, Inc.

We have secured an \$8,300,000 loan (the "Arrowhead Loan") owed by Seven Arts Future Flow I ("SFF"), an entity that is beneficially owned by SAP Inc., with liens on twelve motion pictures. SFF borrowed these funds from Arrowhead Target Fund Ltd. ("Arrowhead") in February 2006, at an interest rate of 15% per annum. Our purpose was to obtain these funds to retire certain motion picture production loans then outstanding and for general corporate purposes. Although the loan is secured by certain assets of Seven Arts Future Flows I, LLC, the Group is not required to repay the Arrowhead Loan from any of our other assets or revenues. Arrowhead is now collecting directly all sums receivable by us with respect to these motion pictures, and has appointed a new servicing agent for these motion pictures with the result that we no longer control the licensing of these motion pictures. (see "Management's Discussion and Analysis of Financial Condition and Results of Operations – Liquidity and Capital Resources" for a description of the Arrowhead Loan).

The Seven Arts Employee Benefit Trust ("EBT") currently owns approximately 200,000 of our outstanding ordinary shares (see "Management Compensation – Seven Arts Employee Benefit Trust" for a description of EBT). We advanced a loan at a nominal rate of interest of totaling approximately £2,300,000 to EBT consisting of approximately £1,500,000 cash and 1,600,000 ordinary shares of Armadillo Investments plc ("Armadillo"). On October 30, 2008, the Seven Arts Employee Benefit Trust acquired 3,000,000 of our convertible preference shares from Armadillo for £1,500,000, payable in three equal installments of £500,000 each on execution, and six months and twelve months thereafter, and for a return to Armadillo of 1,600,000 ordinary shares of Armadillo. We have guaranteed the remaining two payments aggregating approximately £1,000,000 at current exchange rates due to Armadillo, but have not yet advanced these sums to EBT which is therefore in default on both payments. In February 2011 the Group issued 150,000 shares to New Moon LLC who pledged these shares to Armadillo who in turn extended the repayment period of the £1,000,000 to June 30, 2011. We will advance this amount to EBT from the proceeds of this offering and EBT will in turn pay this amount to Armadillo, thereby fully settling the amounts due. The additional advance to EBT will increase our total advance to approximately £2,300,000 ("Trust Loan"). On November 20, 2008, EBT converted 2,500,000 of these preference shares into 400,000 of our ordinary shares. In May 2010 the EBT converted the balance of 500,000 preference shares into 80,000 of our ordinary shares.

Together with SAP Inc. we have guaranteed a \$4,000,000 loan of December 17, 2007 between Palm Finance Corporation and Gone To Hell Ltd., a Group controlled by our Chief Operating Officer and Director Kate Hoffman. The loan was made exclusively to finance our motion picture Nine Miles Down and is secured by the distribution rights to that motion picture. The loan carries an annual rate of interest of 15% and became due on June 30, 2009. We have entered into a forbearance agreement with Palm extending the due date of this loan to December 31, 2011.

We entered into a loan and security agreement dated January 15, 2009 in the amount of \$750,000 as a borrower together with SAP Inc. and certain limited liability companies controlled by SAP Inc. in connection with the production of our motion picture Night of the Demons ("NOTD"). The loan was made to finance NOTD and is secured by the distribution rights to NOTD. The loan bears an annual rate of interest of ten percent (10%) per annum. The loan became due on or about March 31, 2010 and is being repaid from distribution revenues of NOTD.

We engage as an employee and director, Kate Hoffman, who is the daughter of Peter Hoffman, our Chief Executive Officer.



ITEM 8. FINANCIAL INFORMATION

The consolidated financial statements for the fiscal years ended June 30, 2011 and 2010, as required under Item No. 17 are attached hereto and found immediately following the text of this annual report. The audit report of The Hall Group CPAs for the fiscal years ended June 30, 2011 and 2010, is included therein immediately preceding the financial statements.

#### 8.A.7. Legal/Arbitration Proceedings

##### Fireworks Litigation

The Group prevailed in a motion for summary adjudication on February 10, 2011 in an action against CanWest Entertainment and two of its affiliates (“CanWest”) confirming the Group’s ownership of five motion pictures “Rules of Engagement”, “An American Rhapsody,” “Who Is Cletis Tout,” “Onegin,” and “The Believer”, (the “Copyrights”). The Group has filed an action in England against Content Media Corporation (“Content”) and Paramount Picture Corp. (“Paramount”) to recover the Copyrights and substantial damages for the use of the copyrighted works after their purported acquisition from CanWest. The Group may incur up to \$200,000 in legal expenses to pursue this claim but expects to recover those fees from Content.

##### Jones Film

The Group, its subsidiary Seven Arts Filmed Entertainment Limited, and a related party, Seven Arts Pictures Inc. (“SAP INC”), were the subject of an arbitration award of approximately \$900,000 against them for legal fees and interest thereon relating to an ongoing dispute regarding a participation in the motion picture entitled 9 ½ Weeks II, even though the arbitration found no additional sums due to the complaining party, and potential loss of further distribution rights in this motion picture. The Federal District Court enforced this arbitration award, and the Group is seeking relief from that decision. The Group has accrued for the liability in the amount of \$800,000 including approximately \$100,000 of accrued interest at June 30, 2011. The remaining interest, costs and fees has been guaranteed by SAP Inc., a related party.

##### • Parallel Action

On June 28, 2011, Seven Arts Pictures Plc. (“PLC”) filed an action in the High Court of England against Parallel Media LLC (“Parallel”) to collect sums due to PLC with respect to acquisition of distribution rights in Russia to four motion pictures and to confirm Parallel’s obligations under both a signed and unsigned investment agreement with respect to the motion picture project Winter Queen. On the same day Parallel filed a petition to wind up and liquidate PLC in the Companies Courts of England based on its claim of repayment of \$1,000,000 of investment made by Parallel in Winter Queen. PLC is no longer part of the Company. On September 19, 2011, Parallel filed a new action against PLC and SAE in the Superior Court of California, asserting the same claims as in the winding up petition and seeking to enjoin the proposed administration proceedings in England. A request for a preliminary injunction was denied by the Superior Court.

##### • HMRC Investigation

On July 19, 2011 Officers of Her Majesty’s Revenue & Customs (“HMRC”) attended the offices of Seven Arts Pictures Plc. (the “Company”) in London. Documents were retained appertaining to arrangements involving the subscription for shares in a number of companies which had lost value, resulting in subscribers making claims to tax relief.

The Company’s participation in these transactions was limited to the Company’s predecessor’s transfer of rights to certain motion pictures to the investors in return for their investments in the production and release costs of those pictures and making available the provision of loans to fund a portion of those investments. The Company received no tax benefits from the transactions, which were made on arms-length terms. The Company believes that it is not a subject of the HMRC investigation.

In connection with the transactions, the Company did not make any representations or warranties to any party, including the investors, regarding any potential tax benefits related to the transactions. Prior to the closing of the

transactions the investors obtained and made available to the Company, an opinion of prominent Queen's counsel, specializing in United Kingdom tax laws, that the transactions were permitted and acceptable under the terms of the applicable United Kingdom revenue laws. The Company remains confident that the transactions were permitted and acceptable under the terms of the applicable United Kingdom revenue laws.

HMRC has requested interviews with three officers of the Company to discuss whether those officers were involved in the arrangements for subscription of shares in the relevant companies. The Company is fully cooperating with the investigation. The Company believes there is no basis for any claim of responsibility of any of its officers or employees. Based on facts currently known by the Company, there is no need for it to record a contingent liability in its financial statements in connection with the investigation or the related transactions.

#### Arrowhead Target Fund

Seven Arts Future Flow I (“SFF”), a limited liability Group owned by SAP Inc., one of the Group’s controlling shareholders and a Group controlled by Mr. Hoffman, obtained financing from the Arrowhead Target Fund, Ltd. (“Arrowhead”) of approximately \$8,300,000 (the “Arrowhead Loan”). The Group secured the Arrowhead Loan with liens on 12 motion pictures that generated revenues of \$820,026 in the fiscal year ended June 30, 2009, \$2,739,800 in the fiscal year ended March 31, 2008. The Group’s only liability is to repay the Arrowhead Loan from the proceeds of the film assets pledged against the Arrowhead Loan. The Group is not required to repay the Arrowhead Loan from any of its other assets or revenues. SAE’s subsidiary, SAFE Ltd., was the collateral agent of the film assets.

The Arrowhead Loan became due in February 2009 and SFF has not paid the outstanding principle and interest due. Arrowhead has the right to foreclose on the pledged film assets, but has not done so at the present time. SFF has received a default notice to this effect and as a result Arrowhead is now collecting directly all sums receivable by the Group with respect to these motion pictures, and has appointed a new servicing agent for these motion pictures with the result that the Group no longer controls the licensing of these motion pictures. Failure to repay or refinance the Arrowhead Loan could result in a material disposition of assets through the loss of the Group’s rights to the twelve motion pictures and related loss of revenues in amounts that are difficult to predict.

As a result of the foregoing, the Group has removed all assets accounts relating to the twelve motion pictures pledged to Arrowhead and has removed the corresponding limited recourse indebtedness from the Group’s consolidated balance sheet at fiscal year ended June 30, 2009, due to the fact that the loan was a limited recourse loan and the Group had no further obligations to Arrowhead beyond the pledged film assets.

Arrowhead has made a claim against the Group by reason of monies the Group has collected from distribution of these motion pictures and not paid to Arrowhead based on the Group’s interpretation of the transactional contracts. The Group has accounted for the collections from the Arrowhead titles films as accrued liabilities in its consolidated financial statements.

Arrowhead filed an action on September 22, 2010 which seeks recovery from the Group of the monies which the Group has retained under its interpretation of the relevant agreements with Arrowhead. In addition, Arrowhead makes substantial additional claims against the Group, Mr. Hoffman and Seven Arts Pictures Inc. regarding claimed breaches of the terms of the operative agreements, including failure to properly account, failure to turn over materials, failure to remit monies collected, and similar matters. The claims against the Group for these breaches of warranties for damages are \$8,300,000 although Arrowhead states no basis for this amount.

The Group had moved to dismiss the action against all defendants other than Seven Arts Future Flows I LLC, which is not part of the Group. On August 9, 2011, the New York Supreme Court granted the Group’s motion and dismissed all defendants except Seven Arts Filmed Entertainment Limited in its capacity as a collateral agent, which is not a material element of Arrowhead claim. The Group continues to believe that Arrowhead’s claims against the Group are without substantial merit

#### Arrowhead Capital Partners – AGC Loan

The Group and several affiliates were named as defendants in an action by Arrowhead Capital Partners Ltd filed in the Supreme Court of New York County of New York State purportedly served on May 24, 2010, seeking to collect \$1,000,000 plus interest (the “ACG Loan”) due to Arrowhead Consulting group LLC (“ACG”) as well as foreclosure on the collateral granted as part of the Cheyne Loan described above in NOTE 10 under “Film and Production Loans”. The ACG Loan is fully subordinated to repayment of the Cheyne Loan, which has not been repaid, and a subsidiary of the

Group has been assigned all Cheyne's rights under the subordination provision of the Cheyne Loan. As a result Management does not believe that ACG has the right to maintain this action to collect any monies or to foreclose on any collateral pursuant to the Cheyne Loan. The Group intends to vigorously defend against this action and has filed a motion for summary judgement to dismiss this action

#### Silverback – Hungarian co-producer

The Group has obtained a final judgment from the Queen’s Bench in England for approximately \$300,000 erroneously converted to fees by a Hungarian co-producer on the motion picture *Nine Miles Down*. The Group is seeking to collect these fees back through enforcement by Hungarian courts and currently a bailiff has been appointed to collect the monies due in Hungary. The incorrectly appropriated fees have been included in the film asset in prior years. Capitalised film costs will be reduced upon collection of these fees.

#### Stonewood/Nine Miles Down

A settlement agreement for \$250,000 has been reached with the liquidators of *Gone to Hell* (“GTH”) the production company for *Nine Miles Down*. The main beneficiaries of the GTH liquidation are Stonewood; owned by the director of GTH and SAP INC for an action it took against the liquidator for interfering in the free distribution of the film. The debt to the liquidation is fully insured, but only to the amount that is not payable back to SAP INC and Stonewood as they are the insured parties. The Group has guaranteed the legal costs of this action to make sure it releases the distribution rights to the movie. The Group has accounted for the legal expenses incurred related to this litigation by capitalizing them into film assets in the value of \$200,000 as of June 30, 2011, due to the fact that these are direct expenditures that are direct costs to this particular film.

#### Zeus VAT

The Group believes that the accrual of the VAT input refund or output VAT tax with respect to the Zeus transaction is highly uncertain. Her Majesty’s Customs and Revenue (“HMRC”) raised issues regarding the Zeus transaction as early as May, 2008, and has made no determination regarding any of the inputs or outputs of VAT with respect to the Zeus transaction through today. The situation is still unresolved in that HMRC has not made a VAT refund to the 17 companies formed by investors in the Zeus transaction (“SAFCO’s”) of the output VAT tax charged by Seven Arts on the supplies made for the SAFCO’s and declared on the Group’s VAT return filed in 2008 and in that HMRC has taken no steps to enforce the collection of the output VAT tax as declared by the Group, as an internal “hold” has been placed on collection by HMRC. Until and unless this interest is lifted, HMRC will take no action to enforce the collection of the VAT output tax declared by the Group. The amount of VAT at issue is approximately £23,000,000 (\$35,000,000) which would be both the amount owed by the Group to HMRC and the amount due to the Group from the SAFCO’s as their refund from HMRC. The collection department of HMRC has stopped the collection of the VAT due from the Group, and to date no notices of interest have been received. The Group does not expect any penalties or fees will result from the VAT related to the Zeus transaction, accordingly no accrual of interest or penalties have been accrued as of June 30, 2011.

The Group acquired the SAFCO’s as part of the Zeus transaction described above in May, 2009. The SAFCO’s are not consolidated into the Group as the Group still does not have control of the bank accounts and the accounting records. The Group has instructed counsel to liquidate the SAFCO’s under the applicable laws of the United Kingdom.

One of the Group’s affiliates filed an action against Zeus Partners Limited and two of its executives for indemnity in relation to Value Added Tax due with respect to the Zeus Transaction. The purpose of this action is to protect the Group’s rights with respect to any potential liability to the Group with respect to Value Added Tax arising out of the Zeus Transaction.

#### Director’s Service Contracts

SAP INC. has an employment agreement with Peter Hoffman pursuant to which he will act as the Group’s CEO until December 31, 2013. Upon acquisition of control of Group, it entered into a contract with SAP INC. to secure Mr.

Hoffman's services solely to the Group as CEO. In connection with that employment agreement, Mr. Hoffman has been granted

- the right to sole responsibility for creative and business decisions regarding motion pictures we develop and produce,
- a right of first refusal to produce remakes, sequels or prequels of motion pictures produced by Mr. Hoffman and acquired by the Group or any motion picture produced by the Group during his employment,
  - an annual salary of \$500,000 per year plus bonuses, expenses and a signing option and
- a right upon termination without cause to a lump sum payment of approximately \$1,500,000, an assignment of all projects in development during the term of his employment and any amounts due upon such compensation as an excise tax.

The Group has an employment agreement with Kate Hoffman pursuant to which she will act as COO ad infinitum at a salary of \$85,000 (£52,000) per year plus bonuses and expenses. Ms. Hoffman's contract contains a "non-compete" clause pursuant to which she will be excluded from competing against the Group for 6 months following the date of her termination.

The Group has an employment agreement with Elaine New pursuant to which she will act as an executive director and CFO ad infinitum at a salary of \$225,000 (£150,000) per year plus bonuses and expenses. Ms. New's contract contains a "non-compete" clause pursuant to which she will be excluded from competing against the Group for 6 months following the date of her termination.

All of the employment agreements grant us a right to injunctive relief if the respective employee breaches the agreement. With the exception of Ms. Hoffman's and Ms. New's agreements, the employment agreements do not contain "non-compete" clauses.

- Acquisition of Big Jake Music

On September 29, 2011, the Company entered into a definitive agreement to acquire all of the capital stock of Big Jake Music ("BJM"), a newly formed record and multi-media entertainment company, for \$5,000,000 of convertible preferred stock, convertible into common stock at a premium to the market price at closing, and which is subject to restricted holding periods. BJM will also release soundtracks of Seven Arts films, including *Night of the Demons* (a film released in October 2010) and *The Pool Boys* (a film released in October 2011).

- Creditors Liquidation of SAP Plc.

The Company was placed into compulsory liquidation on November 8, 2011 by the English Companies Court. The Company's CEO, Mr. Peter Hoffman, as a director of PLC had sought an administration order but this request was denied by the Courts as a result of inter alia the opposition of Parallel Pictures LLC ('Parallel'). The creditors are likely to be invited to appoint a licensed insolvency practitioner as liquidator. The role of a liquidator is to realize a company's assets for the benefit of the creditors and shareholders. Mr. Hoffman expects that the liquidator and PLC will pursue its substantial claims against Parallel and its defenses to Parallel's claims. Parallel has claimed in the proceedings in England and the United States that the Asset Transfer Agreement between the Company and PLC was 'fraudulent' and may seek additional compensation or guarantees from Company. Management believes that the Asset Transfer Agreement is a valid agreement for value and not subject to attack and that Parallel will not prevail in its claims. Management believes it has the support of its creditors to resist these claims by Parallel which are disputed by the Company and as a result Parallel will not obtain any relief from the courts on this issue.



- 807 Esplanade Guarantee

Seven Arts Pictures Louisiana LLC, a related party of the Company, entered into a Credit Agreement with Advantage Capital Community Development Fund LLC dated October 11, 2007, for the acquisition and improvement of a production and post production facility located at 807 Esplanade Avenue in New Orleans, Louisiana for aggregate principal advances of up to \$3,700,000. This agreement was guaranteed by the Company's predecessor. Approximately \$3,700,000 has been drawn under the terms of this Credit Agreement, as of June 30, 2011. The Company has also guaranteed this amount.

There is a guarantee of a \$1,000,000 note due to Armadillo by the Employee Benefit Trust resulting from the purchase back of the Seven Arts preferred shares from Armadillo.

#### Investigation into Claim for Tax Credits (SAPLA)

The US Attorney in New Orleans is investigating claims for Louisiana film infrastructure tax credits including such tax credits to be claimed by an affiliate of the Company, Seven Arts Pictures Louisiana LLC. This investigation appears to include investigation as to whether certain expenses claimed by this affiliate were improper or fraudulent. All such claimed expenses were audited by independent auditors in Louisiana and reviewed by counsel. None of these expenses or credits have been included in the Company's financial statements for any period. Management believes that this investigation will have no material adverse effect on the Company's operations or the total tax credits to be received by the Company's affiliates, but could result in charges against current or former employees of this affiliate based on prior audits, including Mr. Hoffman.

#### Asset Transfer Agreement

As of June 10, 2010 the Group proposed to enter an Asset Transfer Agreement, as amended on December 15, 2010, to transfer all of the assets of Seven Arts Pictures Plc. ("PLC") (including ownership of SAFE, Ltd.) to Seven Arts Entertainment Inc. ("SAE"), in exchange for assumption by SAE of certain indebtedness and for one share of common stock of SAE for each ordinary share of PLC which is expected to be distributed subject to a future Registration Statement to be filed by the Group. This transfer was agreed to by the shareholders at the Extraordinary General Meeting on June 11, 2010. The purpose of this transfer was to eliminate the Company's status as a foreign private issuer and to assume compliance with all obligations of a domestic issuer under all applicable state and Federal securities laws. (See NOTE 20 - Subsequent Events).

Effective at the opening of trading on September 1, 2011, Seven Arts Entertainment Inc. ("Seven Arts" or "SAE") was substituted for the NASDAQ listing of Seven Arts Pictures PLC (the "Company"). On that date, each of the Company's ordinary shares was exchanged for one share of common stock of SAE, which commenced trading on NASDAQ as the successor to the Company's NASDAQ listing. SAE's new CUSIP number is 81783N102 and its trading symbol will remain SAPX.

#### ITEM 9. THE OFFER AND LISTING

N/A

##### 9.A. Ordinary Share Trading Information

Our ordinary shares have traded in the past five years on several different markets. Starting in February of 2009, our shares have been quoted on the NASDAQ Capital Market under the symbol "SAPX". Starting in March of 2008 and continuing until February 12, 2009, our shares have been quoted on the Over-the-Counter Bulletin Board under the

symbol “SAPxf”. Our ordinary shares traded on the Alternative Investment Market in London, England from September 2004 until February 2007 under the symbol “SAPP”. Our ordinary shares were listed on the PLUS Market in London, England starting in April 2007 under the symbol “SAP P”. We notified our shareholders of our decision to de-list our ordinary shares on the PLUS Market on February 25, 2009 and this de-listing was approved by the shareholders at an extraordinary general meeting on March 16, 2009 and the de-listing was effective on March 24, 2009.

Table No. 13 A lists the high, low and closing sales prices on the NASDAQ Capital Market for the past years, Table No. 13 B lists the high, low and closing sales prices on the AIM for the previous six months, last ten fiscal quarters, and last two fiscal years, and Table No. 13 C lists the high, low and closing prices on the PLUS Market for the months of May 2007 through October 2008. Table No. 13 D lists the high, low and closing prices of the Over-The-Counter Bulletin Board for the months of March through October, 2008.

## 9.A.4 Price Information

Table No. 13 A  
NASDAQ Capital Market  
Ordinary Shares Trading Activity  
(Numbers quoted post reverse-split May 2011)

| Period                      | High<br>(dollars) | Low<br>(dollars) | Price at<br>Period End<br>(dollars) |
|-----------------------------|-------------------|------------------|-------------------------------------|
| <b>Month Ended</b>          |                   |                  |                                     |
| November 30, 2011           | \$ 0.43           | \$ 0.38          | \$ 0.38                             |
| October 31, 2011            | \$ 0.67           | \$ 0.46          | \$ 0.50                             |
| September 30, 2011          | \$ 0.40           | \$ 0.25          | \$ 0.35                             |
| August 31, 2011             | \$ 0.89           | \$ 0.65          | \$ 0.68                             |
| July 31, 2011               | \$ 2.59           | \$ 2.00          | \$ 2.08                             |
| June 30, 2011               | \$ 1.44           | \$ 1.13          | \$ 1.19                             |
| May 31, 2011                | \$ 2.82           | \$ 2.82          | \$ 2.82                             |
| April 30, 2011              | \$ 2.24           | \$ 2.11          | \$ 2.11                             |
| March 31, 2011              | \$ 2.13           | \$ 1.65          | \$ 1.95                             |
| February 28, 2011           | \$ 4.00           | \$ 3.82          | \$ 4.00                             |
| January 31, 2011            | \$ 3.75           | \$ 3.51          | \$ 3.75                             |
| December 31, 2010           | \$ 5.35           | \$ 4.36          | \$ 5.05                             |
| November 30, 2010           | \$ 3.59           | \$ 3.00          | \$ 3.46                             |
| October 31, 2010            | \$ 4.20           | \$ 3.91          | \$ 4.20                             |
| September 30, 2010          | \$ 4.60           | \$ 4.45          | \$ 4.60                             |
| August 31, 2010             | \$ 5.30           | \$ 5.24          | \$ 5.30                             |
| July 31, 2010               | \$ 6.75           | \$ 6.30          | \$ 6.75                             |
| June 30, 2010               | \$ 8.25           | \$ 6.45          | \$ 7.95                             |
| May 31, 2010                | \$ 9.10           | \$ 7.75          | \$ 8.75                             |
| April 30, 2010              | \$ 11.35          | \$ 10.10         | \$ 10.25                            |
| March 31, 2010              | \$ 15.00          | \$ 13.45         | \$ 14.65                            |
| February 28, 2010           | \$ 11.25          | \$ 10.10         | \$ 11.25                            |
| January 31, 2010            | \$ 15.00          | \$ 13.50         | \$ 13.50                            |
| December 31, 2009           | \$ 13.66          | \$ 10.40         | \$ 12.70                            |
| November 30, 2009           | \$ 16.75          | \$ 15.03         | \$ 15.15                            |
| October 31, 2009            | \$ 24.15          | \$ 20.50         | \$ 24.000                           |
| September 30, 2009          | \$ 25.55          | \$ 24.75         | \$ 25.55                            |
| August 31, 2009             | \$ 20.25          | \$ 18.75         | \$ 18.75                            |
| July 31, 2009               | \$ 14.95          | \$ 13.05         | \$ 13.05                            |
| June 30, 2009               | \$ 19.75          | \$ 18.00         | \$ 19.75                            |
| May 31, 2009                | \$ 30.00          | \$ 25.00         | \$ 30.00                            |
| April 30, 2009              | \$ 33.00          | \$ 33.00         | \$ 33.00                            |
| March 31, 2009              | \$ 34.50          | \$ 34.50         | \$ 34.50                            |
| February 28, 2009 (1)       | \$ 28.00          | \$ 27.50         | \$ 27.50                            |
| <b>Fiscal Quarter Ended</b> |                   |                  |                                     |
| September 30, 2011          | \$ 0.40           | \$ 0.25          | \$ 0.35                             |
| June 30, 2011               | \$ 1.44           | \$ 1.13          | \$ 1.19                             |

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|                          |          |          |          |
|--------------------------|----------|----------|----------|
| March 31, 2011           | \$ 2.13  | \$ 1.65  | \$ 1.95  |
| December 31, 2010        | \$ 5.35  | \$ 4.36  | \$ 5.05  |
| September 30, 2010       | \$ 4.60  | \$ 4.45  | \$ 4.60  |
| June 30, 2010            | \$ 8.25  | \$ 6.45  | \$ 7.95  |
| March 31, 2010           | \$ 15.00 | \$ 13.45 | \$ 14.65 |
| December 31, 2009        | \$ 13.66 | \$ 10.40 | \$ 12.70 |
| September 30, 2009       | \$ 25.55 | \$ 24.75 | \$ 25.55 |
| June 30, 2009            | \$ 19.75 | \$ 18.00 | \$ 19.75 |
| March 31, 2009 (1)       | \$ 34.50 | \$ 34.50 | \$ 34.50 |
| <b>Fiscal Year Ended</b> |          |          |          |
| June 30, 2011            | \$ 1.44  | \$ 1.13  | \$ 1.19  |
| June 30, 2010            | \$ 8.25  | \$ 6.45  | \$ 7.95  |
| June 30, 2009            | \$ 19.75 | \$ 18.00 | \$ 19.75 |

(1) Seven Arts began trading on the NASDAQ Capital Market on February 13, 2009.

Table No. 13 B

Alternative Investment Market  
Ordinary Shares Trading Activity  
-Sales-

(Numbers quoted post reverse-split May 2011)

| Period                          | High<br>(pence)   | Low<br>(pence)    | Price at<br>Period End<br>(pence) |
|---------------------------------|-------------------|-------------------|-----------------------------------|
| Month Ended 3/31/07 (1)         | 1.48              | 1.43              | 1.48                              |
| Month Ended 2/28/07             | 1.48              | 1.43              | 1.48                              |
| Month Ended 1/31/07             | 1.75              | 1.43              | 1.43                              |
| Month Ended 12/31/06            | 1.58              | 1.53              | 1.53                              |
| Month Ended 11/30/06            | 2.28              | 1.55              | 1.55                              |
| Month Ended 10/31/06            | 2.48              | 1.28              | 2.28                              |
| Month Ended 9/30/06             | 2.08              | .50               | 1.68                              |
| Fiscal Year Ended 3/31/2007 (1) | 1,238             | 250               | 738                               |
| Fiscal Year Ended 3/31/2006     | 500               | 312.5             | 312.5                             |
| Fiscal Year Ended 3/31/2005     | 875               | 475               | 475                               |
| Fiscal Year Ended 3/31/2004     | 1,687.50          | 437.50            | 875                               |
| Fiscal Year Ended 3/31/2003     | Not<br>Applicable | Not<br>Applicable | Not<br>Applicable                 |

(1) The information for the 2007 fiscal year only includes data from April 1, 2006 to February 19, 2007 as our ordinary shares ceased trading on the AIM Market on February 19, 2007.

Table No. 13 C  
PLUS Market  
Ordinary Shares Trading Activity  
-Sales-

(Numbers quoted post reverse-split May 2011)

| Period                               | High<br>(pence) (1) | Low<br>(pence) (1) | Price at<br>Period End<br>(pence) (1) |
|--------------------------------------|---------------------|--------------------|---------------------------------------|
| Month ended 3/31/09 (to 3/24/09) (1) | 725                 | 475                | 725                                   |
| Month ended 2/28/09                  | 525                 | 525                | 525                                   |
| Month ended 1/31/09                  | 538                 | 525                | 525                                   |
| Month ended 12/31/08                 | 588                 | 538                | 538                                   |
| Month ended 11/30/08                 | 663                 | 588                | 588                                   |
| Month ended 10/31/08                 | 713                 | 613                | 663                                   |
| Month ended 9/30/08                  | 713                 | 487.5              | 646.5                                 |
| Month ended 8/31/08                  | 488                 | 288                | 336                                   |
| Fiscal Quarter Ended                 |                     |                    |                                       |
| December 31, 2008                    | 713                 | 538                | 538                                   |
| September 30, 2008                   | 713                 | 287.5              | 712.5                                 |
| Ended June 30, 2008                  | 538                 | 513                | 513                                   |
| Ended March 31, 2008                 | 488                 | 463                | 463                                   |

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|                            |       |       |        |
|----------------------------|-------|-------|--------|
| Ended December 31, 2007    | 638   | 513   | 513    |
| Ended September 30, 2007   | 613   | 563   | 613    |
| Ended June 30, 2007        | 638   | 738   | 738    |
| <b>Fiscal Period Ended</b> |       |       |        |
| June 30, 2008              | 637.5 | 287.5 | 336.25 |

(1) The approximate UK pound/US dollar exchange rate as of December 31, 2008 was 1:1.5.

(2) The Group's shares ceased trading on the PLUS Market on March 24, 2009.

Table No. 13 D

OTC BB Market  
 Ordinary Shares Trading Activity  
 -Sales-  
 (Numbers quoted post reverse-split May 2011)

| Period                                | High     | Low      | Price at<br>Period End |
|---------------------------------------|----------|----------|------------------------|
| Month Ended 02/11/09 (see Table 13 A) | \$ 33.75 | \$ 26.25 | \$ 31.25               |
| Month Ended 01/31/09                  | \$ 62.50 | \$ 20.00 | \$ 32.50               |
| Month Ended 12/31/08                  | \$ 46.75 | \$ 36.25 | \$ 40.00               |
| Month Ended 11/30/08                  | \$ 48.00 | \$ 27.50 | \$ 48.00               |
| Month Ended 10/31/08                  | \$ 46.25 | \$ 29.00 | \$ 44.90               |
| Month Ended 9/30/08                   | \$ 28.75 | \$ 11.25 | \$ 28.75               |
| Month Ended 8/31/08                   | \$ 12.50 | \$ 2.75  | \$ 12.50               |
| Month Ended 7/31/08                   | \$ 10.00 | \$ 3.75  | \$ 3.75                |
| Month Ended 6/30/08                   | \$ 12.50 | \$ 9.00  | \$ 11.50               |
| Month Ended 5/31/09                   | \$ 11.50 | \$ 9.00  | \$ 9.00                |
| Month Ended 4/30/08                   | \$ 12.50 | \$ 9.00  | \$ 9.00                |
| Month Ended 3/31/08                   | \$ 10.50 | \$ 10.00 | \$ 10.50               |
| Fiscal Quarter Ended 9/30/08          | \$ 28.75 | \$ 2.75  | \$ 28.75               |
| Fiscal Quarter Ended 6/30/08          | \$ 12.50 | \$ 9.00  | \$ 11.50               |
| Fiscal Quarter Ended 3/30/08          | \$ 10.50 | \$ 10.00 | \$ 10.50               |

(1) Seven Arts ceased trading on the Over-the-Counter Bulletin Board on February 11, 2009.

(2) The information for the 2008 fiscal year only includes data from March 2008 through to June 2008 as our ordinary shares only began trading on the Over-the-Counter Bulletin Board in March 2008.

#### 9.A.5. Ordinary and Preferred Share Description

##### Registrar/Ordinary Shares Outstanding/Shareholders

The authorized share structure consists of 20,527,360 ordinary shares par value of £0.25 each, 20,527,360 ordinary shares of £1.00 each, 13,184,000 deferred shares of £0.45 each and 6,000,000 convertible redeemable preference shares of £1.00 each. All the shares of ordinary stock of the Group are of the same class and, once issued, rank equally as to dividends, voting powers, and participation in assets.

As of the date of this Form 20-F, 16,475,411 shares of common stock of SAE, Inc. (the successor entity) are issued and outstanding and 125,125 preferred shares are issued and outstanding.

Interwest Transfer Group, 1981 Murray Holladay Road, Suite 100, Salt Lake City, UT 84117 is the registrar and transfer agent for the common shares.

##### Stock Options and Warrants

Refer to Item No.6.E and Table No. 11 for additional information.





#### 9.A.6. Rights of Securities.

No other class of securities materially qualifies the rights of holders of ordinary shares.

#### 9.A.7. Securities Other Than Common or Ordinary Shares.

Langley Park Investment Trust PLC (“Langley”) has converted as of December 31, 2008, 1,250,000 of its convertible redeemable debentures (“Debentures”) into 200,000 ordinary shares, which are included in the ordinary shares outstanding as of December 31, 2008. Langley’s remaining Debentures have a face value of £1,750,000 (approximately \$3,432,500 at the exchange rate prevailing at the time of the financing) and are convertible into an aggregate of 280,000 ordinary shares. There is no due date or required due date on our Debentures. The Debentures rank junior to all our indebtedness and senior only to our ordinary or preference shares.

Our convertible redeemable preference shares and their terms of issuance are discussed above in Management’s Discussion and Analysis of Financial Condition and Results of Operation. All the convertible redeemed preference shares formerly owned by Armadillo Investment plc, were sold to the Seven Arts Employee Benefit Trust on October 30, 2008 as indicated in Certain Related Transactions. On November 20, 2008, EBT converted 2,500,000 of these preference shares into 400,000 ordinary shares and on May 25, 2010 the EBT converted the remaining 500,000 preference shares into 80,000 ordinary shares. . There were no preferred shares outstanding at June 30, 2011.

#### 9.C. Stock Exchanges Identified

Seven Arts’ ordinary shares have traded in the past five years on several different markets. Starting in February of 2009, the Group’s shares have been quoted on the NASDAQ Capital Market under the symbol “SAPX”. Starting in March of 2008 and continuing until February 12, 2009, the Group’s shares had been quoted on the Over-the-Counter Bulletin Board under the symbol “SAPxf”. Seven Arts’ ordinary shares traded on the Alternative Investment Market in London, England from September 2004 until February 2007 under the symbol “SAPP”. The Group’s ordinary shares were listed on the PLUS Market in London, England starting in April 2007 under the symbol “SAPP”. Seven Arts notified the Group’s shareholders of the decision to de-list the Group’s ordinary shares from the PLUS Market on February 25, 2009 and this de-listing was approved by the shareholders at an extraordinary general meeting on March 16, 2009 and the de-listing was effective on March 24, 2009.

### ITEM 10. ADDITIONAL INFORMATION

#### 10.A. Share Capital

N/A

##### 10.A.1. Authorized/Issued Capital

N/A

10.A.2. Shares Not Representing Capital

N/A

10.A.3. Shares Held By Group.

N/A

10.A.4. Stock Options/Share Purchase Warrants

N/A

10.A.5. Stock Options/Share Purchase Warrants

N/A

10.A.6. History of Share Capital

N/A

10.A.7. Resolutions/Authorizations/Approvals

N/A

10.B. Articles of Association

Seven Arts was incorporated as Glasgow Park Investments PLC on 24 August 2001 under the English Group Act of 1985. Pursuant to a resolution passed at a meeting of the shareholders of the Group that was held on 11 September 2001, the Group changed its name from Glasgow Park Investments PLC to The Cabouchon Collection PLC. Pursuant to a resolution passed at a meeting of the shareholders of the Group that was held on 6 November 2003, the name of the Group was changed to Cabouchon PLC. Pursuant to a resolution passed at a meeting of the shareholders of the Group that was held on 2 September 2004, the name of the Group was changed to Seven Arts Pictures PLC.

There are no restrictions on the business the Group may carry on in the Articles of Association attached hereto as Exhibit "1," as amended at an Extraordinary General Meeting of shareholders held on 10 March 2008. Also included in Exhibit "1" is the Group's Board Memorandum on Financial Reporting Procedure presented to the Board of Directors on 9 January, 2007, as amended.

Under Article 124 of the Group's Articles of Association, a director or senior officer must declare its interest in any existing or proposed contract or transaction with the Group and such director is not allowed to vote on any transaction or contract with the Group in which has a disclosable interest, unless the interest arises in accordance with certain circumstances as set forth in the Group's Articles of Association. A director may hold any office or place of profit with the Group in conjunction with the office of director, and no director shall be disqualified by his office from contracting with the Group. A director or his firm may act in a professional capacity for the Group and he or his firm shall be entitled to remuneration for professional services. A director may become a director or other officer or employee of, or otherwise interested in, any corporation or firm in which the Group may be interested as a shareholder or otherwise. The director shall not be accountable to the Group for any remuneration or other benefits received by him.

Article 99 of the Group's Articles addresses the duties of the directors. Directors must manage or supervise the management of the business and affairs of the Group and have the authority to exercise all such powers which are not required to be exercised by the shareholders, or as governed by the Companies Act of 1985. Article 100 addresses Committees of the Board of Directors. Directors may, by resolution, create and appoint an executive committee consisting of the director or directors that they deem appropriate. The committees established by the Group are the Audit Committee (currently Mr. Garstin, Ms. New, and Ms. Verdin), Nomination Committee (currently Ms. Hoffman, Mr. Hickox and Ms. Verdin) and Compensation Committee (currently Mr. Gibbs, Mr. Hickox, and Mr. Reardon).

Directors may also by resolution appoint one or more other committees. These committees may be delegated any of the directors' powers except the power to fill vacancies on the board of directors, the power to remove a director, the power to change the membership or fill vacancies on any committee of the directors, the power to appoint or remove officers appointed by the directors, and make any delegation subject to the conditions set out in the resolution or any subsequent directors' resolution. The quorum necessary for the transaction of the business of the directors may be fixed by the directors and if not so fixed shall be two directors.

Under Article 104, the board may exercise all the powers of the Group to borrow money, to guarantee, to indemnify, to mortgage or charge its undertaking, property, assets (present and future) and uncalled capital, and to issue debentures and other securities whether outright or as collateral security for any debt, liability or obligation of the Group or any third party.

A director need not be a shareholder of the Group, and there are no age limit requirements pertaining to the retirement or non-retirement of directors. The directors are entitled to the remuneration for acting as directors, if any as the directors may from time to time determine. If the directors so decide, the remuneration of directors, if any, will be determined by the shareholders. That remuneration may be in addition to any salary or other remuneration paid to any officer or employee of the Group as such who is also a director. The Group must reimburse each director for the reasonable expenses that he or she may incur in and about the business of the Group. If any director performs any professional or other services for the Group that in the opinion of the directors are outside the ordinary duties of a director, or if any director is otherwise specially occupied in or about the Group's business, he or she may be paid remuneration fixed by the directors, or, at the option of that director, fixed by ordinary resolution and such remuneration may be either in addition to, or in substitution for, any other remuneration that he or she may be entitled to receive.

Article 161 of the Group's Articles of Association provides for the mandatory indemnification of directors, senior officers, former directors, and alternate, as well as their respective heirs and personal or other legal representatives, or any other person, to the greatest extent permitted by the New Act. The indemnification includes the mandatory payment of expenses. The directors may cause the Group to purchase and maintain insurance for the benefit of eligible parties.



The rights, preferences and restrictions attaching to each class of the Group's shares are as follows:

The authorized share structure consists of 20,527,360 ordinary shares par value of £0.25 each, 13,184,000 deferred shares of £0.45 each, 20,527,360 deferred shares of £1.00 each and 6,000,000 convertible redeemable preference shares of £1.00 each. All the shares of ordinary stock of the Group are of the same class and, once issued, rank equally as to dividends, voting powers, and participation in assets. Holders of ordinary stock are entitled to one vote for each share held of record on all matters to be acted upon by the shareholders. Holders of ordinary stock are entitled to receive such dividends as may be declared from time to time by the Board of Directors, in its discretion, out of funds legally available therefore.

Upon liquidation, dissolution or winding up of the Group, holders of ordinary stock are entitled to receive pro rata the assets of Group, if any, remaining after payments of all debts and liabilities and the satisfaction of preferred shareholders, if any. No shares have been issued subject to call or assessment. There are no pre-emptive or conversion rights and no provisions for redemption or purchase for cancellation, surrender, or sinking or purchase funds.

Subject to the Companies Act of 1985, the Group may alter its authorized share structure by ordinary and/or special resolution. These ordinary and/or special resolutions may:

- (1) create one or more classes or series of shares or, if none of the shares of a series of a class or series of shares are allotted or issued, eliminate that class or series of shares;
- (2) increase, reduce or eliminate the maximum number of shares that the Group is authorized to issue out of any class or series of shares or establish a maximum number of shares that the Group is authorized to issue out of any class or series of shares for which no maximum is established;
- (3) grant authority to the Directors to allot ordinary shares in the capital of the Group in accordance with Sections 80 and 95 of the Companies Act 1985. At the General Meeting held on 10 March 2008 the Directors of the Group were authorities to issue a total of 35,000,000 ordinary shares in the Group. The authority granted expires at the conclusion of the Annual General Meeting to be held in 2009.
- (4) subdivide or consolidate all or any of its unissued, or fully paid issued, shares;
- (5) if the Group is authorized to issue shares of a class or shares with par value;
  - (a) decrease the par value of those shares; or
  - (b) if none of the shares of that class of shares are allotted or issued, increase the par value of those shares;
- (6) alter the identifying name of any of its shares; or
- (7) otherwise alter its share or authorized share structure when required or permitted to do so.

The Group may by special resolution:

- (1) create special rights or restrictions for, and attach those special rights or restrictions to, the shares of any class or series of shares, whether or not any or all of those shares have been issued; or
- (2) vary or delete any special rights or restrictions attached to the shares of any class or series of shares, whether or not any or all of those shares have been issued.

An Annual General Meeting shall be held once every calendar year at such time (not being more than 15 months after holding the last preceding Annual Meeting) and place as may be determined by the Directors. The Directors may, as they see fit, to convene an extraordinary general meeting. An extraordinary general meeting, if requisitioned in accordance with the Companies Act of 1985, shall be convened by the Directors or, if not convened by the Directors, may be convened by the requisitionists as provided in the Companies Act of 1985.

There are no limitations upon the rights to own securities.

There are no provisions that would have the effect of delaying, deferring, or preventing a change in control of the Group.

There is no special ownership threshold above which an ownership position must be disclosed.

#### 10.C. Material Contracts

The only material contracts are the Employment Agreements for the services of Peter Hoffman described in Item 6 No. 2C above, the agreements embodying the redeemable convertible preference shares and debentures referred to in Item 4 No. A above, and the contracts attached as Exhibits hereto and in previous Form 20-FR/A filings by the Group.

#### 10.D. Exchange Controls

The United Kingdom has no system of exchange controls. There are no United Kingdom restrictions on the repatriation of capital or earnings of an English public Group to non-resident investors. There are no laws in the United Kingdom or exchange restrictions affecting the remittance of dividends, profits, interest, royalties and other payments to non-resident holders of Seven Arts' securities.

Restrictions on Share Ownership by UK citizens: There are no limitations under the laws of English or in the organizing documents of Seven Arts on the right of foreigners to hold or vote securities of Seven Arts.

#### 10.E. Taxation

The following summary of the material United Kingdom income tax consequences are stated in general terms and are not intended to be advice to any particular shareholder. Each prospective investor is urged to consult his or her own tax advisor regarding the tax consequences of his or her purchase, ownership and disposition of ordinary shares. The tax consequences to any particular holder of ordinary shares will vary according to the status of that holder as an individual, trust, corporation or member of a partnership, the jurisdiction in which that holder is subject to taxation, the place where that holder is resident and, generally, according to that holder's particular circumstances. This summary is applicable only to holders who are resident in the United States, have never been resident in United Kingdom, deals at arm's length with the Group, hold their ordinary shares as capital property and who will not use or hold the ordinary shares in carrying on business in the United Kingdom. Special rules, which are not discussed in this summary, may apply to a United States holder that is an issuer that carries on business in the United Kingdom and

elsewhere.

Management urges each holder to consult his own tax advisor with respect to the income tax consequences applicable to him in his own particular circumstances.

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## UNITED KINGDOM INCOME TAX CONSEQUENCES

### Disposition of Ordinary Stock.

The summary below is restricted to the case of a holder (a "Holder") of one or more ordinary shares ("Ordinary Shares") who for the purposes of the United Kingdom inland revenue acts ("Tax Acts") is a non-resident of the United Kingdom, holds his Ordinary Shares as capital property and deals at arm's length with the Group.

### Dividends

The UK does not require any tax to be withheld from the payment of dividends to holders of ordinary shares.

### Disposition of Ordinary Shares

The UK does not impose any tax on investors disposing shares in a UK Group, unless those investors are either UK tax resident or operate through a UK permanent establishment which holds the shares.

## UNITED STATES FEDERAL INCOME TAX CONSEQUENCES

The following is a discussion of material United States Federal income tax consequences, under the law, generally applicable to a U.S. Holder (as defined below) of ordinary shares of the Group. This discussion does not cover any state, local or foreign tax consequences.

The following discussion is based upon the sections of the Internal Revenue Code of 1986, as amended ("the Code"), Treasury Regulations, published Internal Revenue Service ("IRS") rulings, published administrative positions of the IRS and court decisions that are currently applicable, any or all of which could be materially and adversely changed, possible on a retroactive basis, at any time. In addition, the discussion does not consider the potential effects, both adverse and beneficial, or recently proposed legislation which, if enacted, could be applied, possibly on a retroactive basis, at any time. The discussion is for general information only and it is not intended to be, nor should it be construed to be, legal or tax advice to any holder or prospective holder of ordinary shares of the Group. Each holder and prospective holder of ordinary shares of the Group is advised to consult their own tax advisors about the federal, state, local, and foreign tax consequences of purchasing, owning and disposing of ordinary shares of the Group applicable to their own particular circumstances.

### U.S. Holders

As used herein, a "U.S. Holder" includes a holder of ordinary shares of the Group who is a citizen or resident of the United States, a corporation created or organized in or under the laws of the United States or of any political subdivision thereof, an estate whose income is taxable in the United States irrespective of source or a trust subject to the primary supervision of a court within the United States and control of a United States fiduciary as described in Section 7701(a)(30) of the Code. This summary does not address the tax consequences to, and U.S. Holder does not include, persons subject to special provisions of Federal income tax law, such as tax-exempt organizations, qualified retirement plans, financial institutions, insurance companies, real estate investment trusts, regulated investment companies, broker-dealers, non-resident alien individuals, persons or entities that have a "functional currency" other than the U.S. dollar, shareholders who hold ordinary shares as part of a straddle, hedging or conversion transaction, and shareholders who acquired their ordinary shares through the exercise of employee stock options or otherwise as compensation for services. This summary is limited to U.S. Holders who own ordinary shares as capital assets. This summary does not address the consequences to a person or entity holding an interest in a shareholder or the consequences to a person of the ownership, exercise or disposition of any options, warrants or other rights to acquire ordinary shares.





#### Distribution on Ordinary Shares of the Group

U.S. Holders receiving dividend distributions (including constructive dividends) with respect to ordinary shares of the Group are required to include in gross income for United States Federal income tax purposes the gross amount of such distributions equal to the U.S. dollar value of such distributions on the date of receipt (based on the exchange rate on such date), to the extent that the Group has current or accumulated earnings and profits, without reduction for any U.K. income tax withheld from such distributions. Such U.K. tax withheld may be credited, subject to certain limitations, against the U.S. Holder's United States Federal Income tax liability or, alternatively, individuals may be deducted in computing the U.S. Holder's United States Federal taxable income by those individuals who itemize deductions. (See more detailed discussion at "Foreign Tax Credit" below). To the extent that distributions exceed current or accumulated earnings and profits of the Group, they will be treated first as a return of capital up to the U.S. Holder's adjusted basis in the ordinary shares and thereafter as gain from the sale or exchange of the ordinary shares. Dividend income will be taxed at marginal tax rates applicable to ordinary income while preferential tax rates for long-term capital gains are applicable to a U.S. Holder which is an individual, estate or trust. There are currently no preferential tax rates for long-term capital gains for a U.S. Holder which is a corporation.

In the case of foreign currency received as a dividend that is not converted by the recipient into U.S. dollars on the date of receipt, a U.S. Holder will have a tax basis in the foreign currency equal to its U.S. dollar value on the date of receipt. Generally any gain or loss recognized upon a subsequent sale or other disposition of the foreign currency, including the exchange for U.S. dollars, will be ordinary income or loss.

Dividends paid on the ordinary shares of the Group will not generally be eligible for the dividends received deduction provided to corporations receiving dividends from certain United States corporations. A U.S. Holder which is a corporation may, under certain circumstances, be entitled to a 70% deduction of the United States source portion of dividends received from the Group (unless the Group qualifies as a "foreign personal holding Group" or a "passive foreign investment Group", as defined below) if such U.S. Holder owns shares representing at least 10% of the voting power and value of the Group. The availability of this deduction is subject to several complex limitations which are beyond the scope of this discussion.

Under current Treasury Regulations, dividends paid on the Group's ordinary shares, if any, generally will not be subject to information reporting and generally will not be subject to U.S. backup withholding tax. However, dividends and the proceeds from a sale of the Group's ordinary shares paid in the U.S. through a U.S. or U.S. related paying agent (including a broker) will be subject to U.S. information reporting requirements and may also be subject to the 31% U.S. backup withholding tax, unless the paying agent is furnished with a duly completed and signed Form W-9. Any amounts withheld under the U.S. backup withholding tax rules will be allowed as a refund or a credit against the U.S. Holder's U.S. federal income tax liability, provided the required information is furnished to the IRS.

#### Foreign Tax Credit

For individuals whose entire income from sources outside the United States consists of qualified passive income, the total amount of creditable foreign taxes paid or accrued during the taxable year does not exceed \$300 (\$600 in the case of a joint return) and an election is made under section 904(j), the limitation on credit does not apply.

A U.S. Holder who pays (or has withheld from distributions) U.K. income tax with respect to the ownership of ordinary shares of the Group may be entitled, at the option of the U.S. Holder, to either a deduction or a tax credit for such foreign tax paid or withheld. Generally, it will be more advantageous to claim a credit because a credit reduces United States Federal income taxes on a dollar-for-dollar basis, while a deduction merely reduces the taxpayer's income subject to tax. This election is made on a year-by-year basis and applies to all foreign income taxes (or taxes in lieu of income tax) paid by (or withheld from) the U.S. Holder during the year. There are significant and complex limitations which apply to the credit, among which is the general limitation that the credit cannot exceed the proportionate share of the U.S. Holder's United States income tax liability that the U.S. Holder's foreign source income

bears to his/her or its worldwide taxable income in the determination of the application of this limitation. The various items of income and deduction must be classified into foreign and domestic sources. Complex rules govern this classification process. In addition, this limitation is calculated separately with respect to specific classes of income such as “passive income”, “high withholding tax interest”, “financial services income”, “shipping income”, and certain other classifications of income. Dividends distributed by the Group will generally constitute “passive income” or, in the case of certain U.S. Holders, “financial services income” for these purposes. The availability of the foreign tax credit and the application of the limitations on the credit are fact specific and management urges holders and prospective holders of ordinary shares of the Group to consult their own tax advisors regarding their individual circumstances.

#### Disposition of Ordinary Shares of the Group

A U.S. Holder will recognize gain or loss upon the sale of ordinary shares of the Group equal to the difference, if any, between (i) the amount of cash plus the fair market value of any property received, and (ii) the shareholder’s tax basis in the ordinary shares of the Group. Preferential tax rates apply to long-term capital gains of U.S. Holders, which are individuals, estates or trusts. This gain or loss will be capital gain or loss if the ordinary shares are capital assets in the hands of the U.S. Holder, which will be a short-term or long-term capital gain or loss depending upon the holding period of the U.S. Holder. Gains and losses are netted and combined according to special rules in arriving at the overall capital gain or loss for a particular tax year. Deductions for net capital losses are subject to significant limitations. For U.S. Holders, which are not corporations, any unused portion of such net capital loss may be carried over to be used in later tax years until such net capital loss is thereby exhausted, but individuals may not carry back capital losses. For U.S. Holders, which are corporations (other than corporations subject to Subchapter S of the Code), an unused net capital loss may be carried back three years from the loss year and carried forward five years from the loss year to be offset against capital gains until such net capital loss is thereby exhausted.

#### Other Considerations

In the following circumstances, the above sections of the discussion may not describe the United States Federal income tax consequences resulting from the holding and disposition of ordinary shares of the Group.

#### Foreign Personal Holding Group

If at any time during a taxable year more than 50% of the total combined voting power or the total value of the Group's outstanding shares is owned, actually or constructively, by five or fewer individuals who are citizens or residents of the United States and 60% (50% after the first tax year) or more of the Group's gross income for such year was derived from certain passive sources (e.g. from interest income received from its subsidiaries), the Group would be treated as a "foreign personal holding Group." In that event, U.S. Holders that hold ordinary shares of the Group would be required to include in gross income for such year their allocable portions of such passive income to the extent the Group does not actually distribute such income.

The Group does not believe that it currently has the status of a "foreign personal holding Group". However, there can be no assurance that the Group will not be considered a foreign personal holding Group for the current or any future taxable year.

#### Foreign Investment Group

If 50% or more of the combined voting power or total value of the Group's outstanding shares are held, actually or constructively, by citizens or residents of the United States, United States domestic partnerships or corporations, or estates or trusts other than foreign estates or trusts (as defined by the Code Section 7701(a)(31), and the Group is found to be engaged primarily in the business of investing, reinvesting, or trading in securities, commodities, or any interest therein, it is possible that the Group might be treated as a "foreign investment Group" as defined in Section 1246 of the Code, causing all or part of any gain realized by a U.S. Holder selling or exchanging ordinary shares of the Group to be treated as ordinary income rather than capital gains.

#### Passive Foreign Investment Group

As a foreign corporation with U.S. Holders, the Group could potentially be treated as a passive foreign investment Group ("PFIC"), as defined in Section 1297 of the Code, depending upon the percentage of the Group's income which is passive, or the percentage of the Group's assets which is held for the purpose of producing passive income.

Certain United States income tax legislation contains rules governing PFICs, which can have significant tax effects on U.S. shareholders of foreign corporations. These rules do not apply to non-U.S. shareholders. Section 1297 (a) of the Code defines a PFIC as a corporation that is not formed in the United States and, for any taxable year, either (i) 75% or more of its gross income is "passive income", which includes interest, dividends and certain rents and royalties or (ii) the average percentage, by fair market value (or, if the Group is a controlled foreign corporation or makes an election, by adjusted tax basis), of its assets that produce or are held for the production of "passive income" is 50% or more. The taxation of a US shareholder who owns stock in a PFIC is extremely complex and is therefore beyond the scope of this discussion. Management urges US persons to consult with their own tax advisors with regards to the impact of these rules.

#### Controlled Foreign Corporation

A Controlled Foreign Corporation (CFC) is a foreign corporation more than 50% of whose stock by vote or value is, on any day in the corporation's tax year, owned (directly or indirectly) by U.S. Shareholders. If more than 50% of the voting power of all classes of stock entitled to vote is owned, actually or constructively, by citizens or residents of the United States, United States domestic partnerships and corporations or estates or trusts other than foreign estates or trusts, each of whom own actually or constructively 10% or more of the total combined voting power of all classes of stock of the Group could be treated as a "controlled foreign corporation" under Subpart F of the Code. This classification would affect many complex results, one of which is the inclusion of certain income of a CFC, which is

subject to current U.S. tax. The United States generally taxes United States Shareholders of a CFC currently on its pro rata shares of the Subpart F income of the CFC. Such United States Shareholders are generally treated as having received a current distribution out of the CFC's Subpart F income and are also subject to current U.S. tax on its pro rata shares of the CFC's earnings invested in U.S. property. The foreign tax credit described above may reduce the U.S. tax on these amounts. In addition, under Section 1248 of the Code, gain from the sale or exchange of shares by a U.S. Holder of ordinary shares of the Corporation which is or was a United States Shareholder at any time during the five-year period ending with the sale or exchange is treated as ordinary income to the extent of earnings and profits of the Group (accumulated in corporate tax years beginning after 1962, but only while the shares were held and while the Group was "controlled") attributable to the shares sold or exchanged. If a foreign corporation is both a PFIC and a CFC, the foreign corporation generally will not be treated as a PFIC with respect to the United States Shareholders of the CFC. This rule generally will be effective for taxable years of United States Shareholders beginning after 1997 and for taxable years of foreign corporations ending with or within such taxable years of United States Shareholders. The PFIC provisions continue to apply in the case of PFIC that is also a CFC with respect to the U.S. Holders that are less than 10% shareholders. Because of the complexity of Subpart F, a more detailed review of these rules is outside of the scope of this discussion.

The amount of any backup withholding will not constitute additional tax and will be allowed as a credit against the U.S. Holder's federal income tax liability.

Filing of Information Returns

Under a number of circumstances, United States Investor acquiring shares of the Group may be required to file an information return with the Internal Revenue Service Center where they are required to file their tax returns with a duplicate copy to the Internal Revenue Service Center, Philadelphia, PA 19255. In particular, any United States Investor who becomes the owner, directly or indirectly, of 10% or more of the shares of the Group will be required to file such a return. Other filing requirements may apply, and management urges United States Investors to consult their own tax advisors concerning these requirements.

10.G. Statement by Experts

NA

10.H. Document on Display

NA

10.I. Subsidiary Information

No disclosure required

ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Group believes no disclosures regarding market risk are required because the Group owns no market risk sensitive investments. The Group does enter into license agreements often denominated in dollars and its financial statements are calculated in British pounds sterling, which may result in variations in the value of dollar denominated license agreements. See Table 4 for recent movements in the dollar/pound sterling exchange rate. The Group adjusts its licensing requests to reflect currency exchange in the various foreign territories in which it licenses distribution rights.

ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES

12.A. Debt Securities

N/A

12.B. Warrants and Rights

N/A

12.C. Other Securities

N/A

12.D. American Depository Shares

N/A



PART II

ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES

N/A

ITEM 14. MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS

N/A

ITEM 15. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Disclosure controls and procedures are controls and other procedures that are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934, as amended (the "Exchange Act") is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in the reports that we file under the Exchange Act is accumulated and communicated to our management, including our principal executive and financial officers, as appropriate to allow timely decisions regarding required disclosure.

The Group's management, under the supervision and with the participation of the Group's Chief Executive Officer and Chief Financial (and principal accounting) Officer, carried out an evaluation of the effectiveness of the design and operation of the Group's disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) of the Exchange Act) as of June 30, 2011. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Group's disclosure controls and procedures were ineffective as of the end of the period covered by this report in that the Group had one material weakness in its internal control over financial reporting, described below under "Management's Report on Internal Control over Financial Reporting."

Management's Report on Internal Control over Financial Reporting

A Group's internal control over financial reporting is a process designed by, or under the supervision of, a public Group's principal executive and principal financial officers, or persons performing similar functions, and effected by the board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Generally Accepted Accounting Principles of the United States of America ("US GAAP") including those policies and procedures that: (i) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Group, (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with US GAAP, and that receipts and expenditures are being made only in accordance with authorizations of management and directors of the Group, and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Group's assets that could have a material effect on the financial statements.



Management is responsible for establishing and maintaining adequate internal control over financial reporting. Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has assessed the effectiveness of our internal control over financial reporting as of June 30, 2011. In making this assessment, our management used the criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”).

During this evaluation, the Group identified a material weakness in its internal control over financial reporting. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis. The identified material weakness consists of, as of the end of the period covered by this report, limited resources and limited number of employees, and the need for additional personnel to prepare financial information in a timely manner under US GAAP standards for timely compliance with the Group’s reporting obligations under the Exchange Act.

This annual report does not include an attestation report of the Group’s independent registered public accounting firm regarding internal control over financial reporting. Management’s report was not subject to attestation by the Group’s independent registered public accounting firm.

#### Plan for Remediation of Material Weaknesses

To mitigate the current limited resources and limited employees, we rely heavily on direct management oversight of transactions, along with the use of legal and accounting professionals. As we grow, we expect to increase our number of employees and engage outsourced accounting professionals, which will enable us to implement adequate segregation of duties within the internal control framework.

These control deficiencies could result in a misstatement of account balances that would result in a reasonable possibility that a material misstatement to our consolidated financial statements may not be prevented or detected on a timely basis. Accordingly, we have determined that these control deficiencies as described above together constitute a material weakness.

In light of this material weakness, we performed additional analyses and procedures in order to conclude that our consolidated financial statements for the fiscal year ended June 30, 2011 included in this Annual Report on Form 20-F were fairly stated in accordance with US GAAP. Accordingly, management believes that despite our material weaknesses, our consolidated financial statements for the fiscal year ended June 30, 2011 are fairly stated, in all material respects, in accordance with US GAAP.

#### Limitations on Effectiveness of Controls and Procedures

Our management, including our Chief Executive Officer and Chief Financial Officer, does not expect that our disclosure controls and procedures or our internal controls will prevent all errors and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Group have been detected. These inherent limitations include, but are not limited to, the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events and there can be no assurance that any design will

succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

## Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Rule 13a-15 or 15d-15 under the Exchange Act that occurred during the period ended June 30, 2011 that have materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## ITEM 16. RESERVED

## ITEM 16A. AUDIT COMMITTEE FINANCIAL EXPERT

The Group's Board of Directors has determined that the Group has one financial expert serving on its Audit Committee, Robert Kaiser. Mr. Kaiser is independent under NASDAQ listing standards. Mr. Kaiser's professional qualifications are set forth in response to Item 6.

## ITEM 16B. CODE OF ETHICS

The Group has not adopted a code of ethics that applies to its principal executive officer, principal financial officer, principal accounting officer or controller or persons performing similar functions. The Group believes that the Board Memorandum on Financial Reporting Procedure (included as Exhibit 1) establishes the standards of conduct applicable to these officers of the Group.

## ITEM 16C. PRINCIPAL ACCOUNTING FEES AND SERVICES

The Group engaged The Hall Group, CPAs, an independent registered public accounting firm on August 8, 2011 to replace RBSM LLP, an US-based independent registered accounting firm. The following table shows the aggregated fees billed by our principal accountant, The Hall Group CPAs for the audit and other services provided during and for the fiscal years ended June 30, 2011 and 2010, and the aggregated fees billed by RBSM LLP during the fiscal years ended June 30, 2011 and 2010. In addition to auditing the fiscal year ended June 30, 2011, The Hall Group CPAs were also engaged to audit our fiscal year ended June 30, 2010 in accordance with US GAAP. Previous filings presented the year ended June 30, 2010 in accordance with International Financial Reporting Standards ("IFRS").

|                        | June 30,   |            |
|------------------------|------------|------------|
|                        | 2011       | 2010       |
| Audit Fees (a)         | \$ 149,978 | \$ 228,558 |
| Audit Related Fees (b) | -          | -          |
| Tax Fees (c)           | 45,880     | -          |
| All Other Fees (d)     | 222,317    | 228,558    |
| Total                  | \$ 418,175 | \$ 228,558 |

- (a) Audit fees consist of fees billed for professional services rendered during the fiscal year ended June 30, 2011 as well as the review of the Group's December 31, 2010's interim unaudited consolidated financial statements and services that are normally provided in connection with statutory and regulatory filings or engagements. We engaged our principal accountant, The Hall Group CPAs in August 2011 and there was no professional services rendered prior to such date by them.
- (b) Audit related fees – The Group has not been billed by our principal accountant, The Hall Group CPAs for audit related fees other than the audit fees disclosed in (a) since engaged in August 2011.

- (c) Tax Fees - The Group has not been billed by our principal accountant, The Hall Group CPAs for tax fees since engaged in July 2010 through June 30, 2011.
- (d) All Other Fees - The Group has not been billed by our principal accountant, The Hall Group CPAs for all other fees since engaged in August 2011.
- (e) The aggregated fees billed by RBSM LLP during the fiscal year ended June 30, 2010 for professional services rendered (audit-related work, SEC Filing, NASDAQ and AIM compliance work) to the Group in connection with audit related work of \$141,584 and SEC filings, NASDAQ and AIM compliance work of \$323,704, which totaled to \$465,288.

The Group's Audit Committee approved the engagement of The Hall Group CPAs based on pre-approval policies and procedures which did not delegate either the Audit Committee or Board's responsibilities to management. The policies and procedures include approval of a fee estimate, discussion of the key accounting policies of the Group, review of the auditor's professional qualifications and agreement on application of International Financial Reporting Standards.

(f). Independent Contractors

Not applicable

#### ITEM 16D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES

The Group now has three independent directors on its Audit Committee as required by NASDAQ Rule 5605(c) and Exchange Act Rule 10A-3. Hubert Gibbs; Dan Reardon and Robert Kaiser are all considered independent directors by the Board of Directors (“Board”). Robert Kaiser is considered by the Board to be the financial expert on the audit committee.

The Group has already determined that it is in compliance with The Combined Code of Corporate Governance of the United Kingdom (the governing code of companies in the Group’s home country), Section A and B of which stipulate that the Audit Committee be comprised of at least two members and that they be independent “non-executive” directors.

#### ITEM 16E. PURCHASES OF EQUITY SECURITIES BY SEVEN ARTS/AFFILIATED PURCHASERS

In February 2011 the Group issued 150,000 shares to New Moon LLC who pledged these shares to Armadillo who in turn extended the repayment period of the £1,000,000 to June 30, 2011. We will advance this amount to EBT from the proceeds of this offering and EBT will in turn pay this amount to Armadillo, thereby fully settling the mounts due.

Peter Hoffman, the CEO of Seven Arts, holds 23,800 shares pledged to an insurance company over which the insurance company has dispositive control.

#### ITEM 16.F. CHANGE IN REGISTRANT CERTIFYING ACCOUNTANT

##### Previous Independent Registered Public Accounting Firm

In April, 2011 (the “Dismissal Date”) the Group notified RBSM LLP (“RBSM”) that it was dismissed as the Group’s independent registered public accounting firm. The decision to dismiss RBSM as the Group’s independent registered public accounting firm was approved by the Group’s Board of Directors in April, 2011. The reports of RBSM on the Group’s consolidated financial statements for the year ended June 30 2010 did not contain an adverse opinion or disclaimer of opinion, and such reports were not qualified or modified as to uncertainty, audit scope, or accounting principle.

The Group provided RBSM with a copy of this disclosure and was requested to furnish a letter addressed to the Securities & Exchange Commission stating whether or not it agrees with the above statements. This letter was supplied.

##### New Independent Registered Public Accounting Firm

On August 8, 2011 (the “Engagement Date”), the Group engaged The Hall Group CPAs (“Hall”) as its independent registered public accounting firm for the Group’s fiscal year ended June 30, 2011. The decision to engage Hall as the Group’s independent registered public accounting firm was approved by the Group’s Board of Directors. Subsequently, Hall was engaged to audit the fiscal year ended June 30, 2010 in accordance with US GAAP. Previous filings had included June 30, 2010 as reported in IFRS.

During the fiscal years ended June 30, 2010 and 2009 and through the Engagement Date, the Group has not consulted with Hall regarding either:

(1) the application of accounting principles to any specified transaction, either completed or proposed, or the type of audit opinion that might be rendered on the Group’s financial statements, and neither a written report was provided to the Group nor oral advice was provided that Hall concluded was an important factor considered by the Group in

reaching a decision as to the accounting, auditing or financial reporting issue; or

(2) any matter that was either the subject of a disagreement (as defined in paragraph (a)(1)(iv) of Item 304 of Regulation S-K and the related instructions thereto) or a reportable event (as described in paragraph (a)(1)(v) of Item 304 of Regulation S-K).

#### ITEM 16. G. CORPORATE GOVERNANCE

The Group believes its corporate governance practices are consistent with those required by the United Kingdom Companies Acts, the requirements applicable to the Group as English companies.

NASDAQ rules provide that foreign private issuers may follow home country practice in lieu of the NASDAQ corporate governance standards subject to certain exceptions and except to the extent that such exemptions would be contrary to US federal securities laws. The Group received an exemption from the Board independence requirement at the time of initial listing and is relying on home country practice in lieu of NASDAQ rules in that the Group has an equal number of independent directors to directors who are part of management or otherwise not treated under NASDAQ rules as independent. The Group believes it otherwise complies with NASDAQ rules.

## PART III

## ITEM 17. FINANCIAL STATEMENTS

## ITEM 18. FINANCIAL STATEMENTS

The financial statements as required under Item No. 18 are attached hereto and found immediately following the text of this annual report. The audit report of The Hall Group CPAs, our Independent Registered Public Accounting Firm, is included herein immediately preceding the audited financial statements.

## ITEM 19. EXHIBITS

## Exhibit

| No.    | Description  |
|--------|--|
| 1.1    | Form of Underwriting Agreement**   |
| 2.1    | Asset Acquisition Agreement dated as of July 1, 2010 between Seven Arts Entertainment Inc. and Seven Arts Pictures Plc*  |
| 3.1    | Articles of Association*   |
| 3.1.2  | Articles of Incorporation of Seven Arts Entertainment Inc.*  |
| 3.2    | By-Laws and Board Memorandum of Seven Arts (incorporated by reference to Exhibit 2 to Amendment No. 12 to our Registration Statement on Form 20-F filed on December 12, 2008)  |
| 3.2.2  | By-Laws of Seven Arts Entertainment Inc.*  |
| 4.1    | Specimen Ordinary Share Certificate*   |
| 4.2    | Langley Debentures*  |
| 10.1   | Form of Lock-Up Agreement**  |
| 10.2   | Employment Agreement for Peter Hoffman*  |
| 10.2.2 | Restated Employment Agreement for Peter Hoffman*   |
| 10.2.3 | Employment Agreement Amendment for Peter Hoffman*  |
| 10.3   | Employment Agreement for Michael Garstin*  |
| 10.4   | Subscription Agreement, dated 2004, between Seven Arts Pictures plc and Langley Park Investments plc*  |
| 10.5   | Subscription Agreement, dated August 2004, between Cabouchon plc and Armadillo Investments plc*  |
| 10.6   | Loan and Security Agreement, dated as of February 15, 2006, among Arrowhead Target Fund Ltd. Seven Arts Future Flows I, LLC, Seven Arts Filmed Entertainment Limited, and Seven Arts Pictures Inc.*  |
| 10.7   | Master Agreement, dated December 2006, among Cheyne Specialty Finance Fund L.P. and Arrowhead Consulting Group LLC and Seven Arts Pictures PLC, Seven Arts Filmed Entertainment, Ltd., Seven Arts Pictures, Inc., Seven Arts Future Flows I and affiliates*      |
| 10.8   | Subscription Agreement, dated March 6, 2007, between Seven Arts Pictures plc and Unique Fidelity Engineering Limited*  |
| 10.9   | Credit Agreement, dated October 11, 2007, between Seven Arts Louisiana, LLC and Advantage Capital Community Development Fund, L.L.C.*  |
| 10.10  | Assignment Agreement, dated April 22, 2008, among Cheyne Specialty Finance Fund L.P., Seven Arts Filmed Entertainment Limited, Peter Hoffman, Seven Arts Pictures plc, Seven Arts Future Flows I LLC and other parties affiliated with Seven Arts Pictures plc.* |
| 10.11  | Stock Sale Agreement, dated October 2008, between Seven Arts Pictures plc, Smith & Williamson Trustees (Jersey) Limited and Armadillo Investments Ltd.*  |
| 10.12  | Convertible Loan Agreement, dated October 15, 2008, between Seven Arts Pictures plc and Trafalgar Capital Specialized Investment*  |
| 10.13  | Bridging Loan Agreement, dated January 31, 2008, between Seven Arts Pictures plc and Trafalgar Capital Specialized Investment*   |

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- 10.14 Guarantee and Debenture, dated January 31, 2008, from Seven Arts Pictures plc and Seven Arts Filmed Entertainment Limited to Trafalgar Capital Specialized Investment\*
- 10.15 Intercompany Agreement, dated November 1, 2004, between Seven Arts Pictures plc and Seven Arts Pictures, Inc.\*
- 10.16 Letter Agreement, dated September 2, 2004, Regarding the Intercompany Agreement between Seven Arts Pictures plc and Seven Arts Filmed Entertainment Limited\*
- 10.17 Distribution Agreement, between Seven Arts Filmed Entertainment Limited and Seven Arts Louisiana LLC\*
- 10.18 Trust Deed, dated October 21, 2008, establishing The Seven Arts Pictures Employee Benefit Trust between Seven Arts Pictures plc and Smith & Williamson Trustees (Jersey) Limited\*
- 10.19 Loan Agreement, dated October 2008, relating to between The Seven Arts Pictures Employee Benefit Trust between Seven Arts Pictures plc and Smith & Williamson Trustees (Jersey) Limited\*
- 10.20 Operating Agreement, dated November 21, 2008, relating to The Seven Arts Pictures Employee Benefit Trust between Seven Arts Pictures plc and Smith & Williamson Trustees (Jersey) Limited\*
- 10.21 Loan Agreement, dated December 17, 2007, between Palm Finance Corporation and Gone to Hell Limited\*
- 10.22 Loan Agreement, dated May 7, 2007 among Palm Finance Corporation and affiliates of Seven Arts Pictures plc\*
- 10.23 Restated Intercompany Agreement between Seven Arts Pictures Inc. and Seven Arts Entertainment Inc.\*
- 10.24 Subscription Agreement, dated August 30, 2010 and revised December 17, 2010 and February 9, 2011, between Seven Arts Pictures plc and Agua Alta LTD
- 10.25 Subscription Agreement, dated August 30, 2010 and revised December 17, 2010 and February 9, 2011, between Seven Arts Pictures plc and Scarborough Limited
- 10.26 Subscription Agreement, dated August 30, 2010 and revised December 17, 2010 and February 9, 2011, between Seven Arts Pictures plc and Sendero Capital Inc.
- 12.1 Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith)
- 13.1 Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith)
- 20.1 Notice of Extraordinary General Meeting of Shareholders of Seven Arts Pictures Plc.\*
- 21.1 List of Subsidiaries (incorporated by reference to the organizational chart of Seven Arts Pictures plc included in this Form 20-F on page 31)

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\* Filed as an exhibit to Amendment No. 4 to Registration Statement on Form F-1 on September 27, 2010 and incorporated herein by reference.

\*\* To be filed at a future date.



SIGNATURES

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

Seven Arts Pictures Plc.

Date: December 21, 2011

By: /s/ Peter Hoffman  
Name: Peter Hoffman  
Title: Chief Executive Officer  
and Principal Financial Officer

SEVEN ARTS PICTURES PLC.  
CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE YEARS ENDED JUNE 30, 2011 AND 2010

Contents

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Audit Committee and  
Board of Directors  
Seven Arts Pictures Plc.  
London, UK

We have audited the accompanying consolidated balance sheets of Seven Arts Pictures Plc. and its subsidiaries, as of June 30, 2011 and 2010 and the related consolidated statements of operations and comprehensive income (loss), shareholders' equity and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Group's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We have conducted our audits of these financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States of America). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Group is not required to have, nor were we engaged to perform, an audit of management's assertion about the effectiveness of the Group's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above, present fairly, in all material respects, the consolidated financial position of Seven Arts Pictures Plc. and its subsidiaries as of June 30, 2011 and 2010 and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The Hall Group, CPAs  
Dallas, Texas

December 19, 2011

## SEVEN ARTS PICTURES PLC.

CONSOLIDATED BALANCE SHEETS  
AS OF JUNE 30, 2011 AND 2010

|  | 2011                 | 2010                 |
|--|----------------------|----------------------|
| <b>ASSETS</b>  |                      |                      |
| <b>CURRENT ASSETS:</b>   |                      |                      |
| Cash and cash equivalents  | \$ 8,785             | \$ 26,818            |
| Trade receivables, net of allowance of \$669,396 and \$532,996   | 431,891              | 1,478,400            |
| Due from related parties, net  | 2,725,974            | 3,021,184            |
| Other receivables and prepayments  | 1,620,895            | 263,150              |
| <b>Total Current Assets</b>  | <b>4,787,545</b>     | <b>4,789,552</b>     |
| <b>FILM COSTS</b> , net of accumulated amortization of \$8,497,211 and \$5,653,477, respectively                         | <b>23,133,560</b>    | <b>23,808,869</b>    |
| <b>PROPERTY AND EQUIPMENT</b> , net of accumulated depreciation of \$94,910 and \$90,968, respectively                   | <b>24,540</b>        | <b>26,389</b>        |
| <b>TOTAL ASSETS</b>  | <b>\$ 27,945,645</b> | <b>\$ 28,624,810</b> |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>  |                      |                      |
| <b>CURRENT LIABILITIES:</b>  |                      |                      |
| Bank overdraft   | \$ 987               | \$ -                 |
| Accounts payable   | 2,569,275            | 2,304,009            |
| Accrued liabilities  | 2,382,916            | 2,414,963            |
| Participation and residuals  | 503,187              | 480,357              |
| Other loans  | 1,755,250            | 1,534,591            |
| Film and production loans  | 10,890,430           | 16,766,689           |
| Deferred income  | 407,763              | 1,460,230            |
| VAT payable  | 1,477,584            | 1,463,497            |
| <b>Total current liabilities</b>   | <b>19,987,392</b>    | <b>26,424,336</b>    |
| <b>TOTAL LIABILITIES</b>   | <b>19,987,392</b>    | <b>26,424,336</b>    |
| <b>SHAREHOLDERS' EQUITY</b>  |                      |                      |
| Convertible redeemable preference shares, £1.00 par value, 6,000,000 shares authorized; no shares issued and outstanding |                      |                      |
| Ordinary stock, £0.25 par value, 20,527,360 shares authorized; 2,643,131 and 1,495,460 shares issued and outstanding     | 1,121,208            | 641,126              |
| Deferred stock, £0.45 par value, 13,184,000 shares authorized; 13,184,000 and 13,184,000 shares issued and outstanding   | 11,636,594           | 11,636,594           |
| Deferred stock, £1.00 par value, 2,268,120 and 1,495,460   |                      |                      |

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|   |                      |                      |
|---|----------------------|----------------------|
| shares issued and outstanding                         | 3,876,745            | 2,564,504            |
| Additional paid in capital                            | 11,118,198           | 9,248,415            |
| Convertible debentures                                | 3,432,450            | 3,432,450            |
| Receivable from Employee Benefit Trust                | (1,237,417 )         | (2,121,458 )         |
| Accumulated deficit                                   | (19,952,188)         | (21,413,746)         |
| Translation reserve                                   | (2,037,337 )         | (1,787,411 )         |
| Shareholders' equity                                  | 7,958,253            | 2,200,474            |
| <b>TOTAL LIABILITIES AND SHAREHOLDERS'<br/>EQUITY</b> | <b>\$ 27,945,645</b> | <b>\$ 28,624,810</b> |

The accompanying notes are an integral part of these consolidated financial statements.

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## SEVEN ARTS PICTURES PLC.

CONSOLIDATED STATEMENTS OF OPERATIONS AND  
OTHER COMPREHENSIVE INCOME  
FOR THE YEARS ENDED JUNE 30, 2011 AND 2010

|   | Year Ended<br>June 30, |              |
|---|------------------------|--------------|
|   | 2011                   | 2010         |
| Revenue                                   |                        |              |
| Film revenue                              | \$2,758,359            | \$1,974,516  |
| Fee related revenue - related party       | 570,029                | 4,442,919    |
| Total revenue                             | 3,328,388              | 6,417,435    |
| Cost of sales                             |                        |              |
| Amortization and impairment of film costs | 2,843,734              | 1,770,650    |
| Other cost of sales                       | 604,262                | 628,326      |
| Cost of sales                             | 3,447,996              | 2,398,976    |
| Gross profit/(loss)                       | (119,608 )             | 4,018,459    |
| Operating expenses                        |                        |              |
| General and administrative expenses       | 1,852,303              | 2,619,205    |
| Bad debt expense                          | 234,429                | 319,344      |
| Total operating expenses                  | 2,086,732              | 2,938,549    |
| Income (loss) from operations             | (2,206,340)            | 1,079,910    |
| Non-operating income (expense)            |                        |              |
| Other income                              | 4,458,621              | 533,874      |
| Interest expense                          | (829,878 )             | (2,199,844)  |
| Interest income                           | 71,681                 | 110,409      |
| Total non-operating income (expense)      | 3,700,424              | (1,555,561)  |
| Profit (loss) before taxes                | 1,494,084              | (475,651 )   |
| Change in debt derivative                 | (32,530 )              | -            |
| Provision for income tax (benefit)        | -                      | -            |
| Net income (loss)                         | \$1,461,554            | \$(475,651 ) |
| Comprehensive income (loss):              |                        |              |
| Net income (loss)                         | 1,461,554              | (475,651 )   |
| Foreign exchange translation gain (loss)  | (249,926 )             | 420,963      |
| Comprehensive income (loss)               | \$1,211,628            | \$(54,688 )  |

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|   |           |           |
|---|-----------|-----------|
| Weighted average number of ordinary shares used in the profit (loss) per share calculation: |           |           |
| Basic   | 1,888,712 | 1,402,720 |
| Diluted   | 1,888,712 | 1,402,720 |
|   |           |           |
| Basic profit (loss) per share   | \$0.77    | \$(0.34 ) |
| Diluted profit (loss) per share   | \$0.77    | \$(0.34 ) |

The accompanying notes are an integral part of these consolidated financial statements.

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## SEVEN ARTS PICTURES PLC.

CONSOLIDATED STATEMENTS OF DEFICIENCY IN STOCKHOLDERS' EQUITY  
 FOR THE YEARS ENDED MARCH 31, 2008, JUNE 30, 2008, JUNE 30, 2009, JUNE 30, 2010 and JUNE 30, 2011

|   | £1 Conv, Redeem Pref<br>Shares |            | Non Red Conv Loans |             | Common Stock |           | Deferred Stock 2 |             | Defer |
|---|--------------------------------|------------|--------------------|-------------|--------------|-----------|------------------|-------------|-------|
|   | Shares                         | GBP        | Shares             | USD         | Shares       | USD       | Shares           | USD         | Share |
| Balance, June<br>30, 2009   | 500,000                        | £1,539,800 | 1,750,000          | \$3,432,450 | 1,385,460    | \$599,684 | 1,385,460        | \$2,398,736 | 13,1  |
| Chris Bialek<br>options-Oct 27,<br>09                                     |                                |            |                    |             | 2,000        | 807       | 2,000            | 3,230       |       |
| Adjust payable<br>by SAP Inc on<br>above @ par<br>value                   |                                |            |                    |             | 8,000        | 3,230     | 8,000            | 12,918      |       |
| Receiveable<br>from SAP Inc<br>on above<br>transaction                    |                                |            |                    |             |              |           |                  |             |       |
| Translation Adj<br>- Dec 09   |                                |            |                    |             |              |           |                  |             |       |
| Tfr Share<br>options M<br>Garstin to loan<br>2 Dec 08 pd<br>\$200,000     |                                |            |                    |             |              |           |                  |             |       |
| Eden loan<br>100,000 shres<br>@ 25p Dec 09                                |                                |            |                    |             | 20,000       | 7,481     | 20,000           | 29,924      |       |
| Pref Share<br>Conversion -<br>EBT (£0.25 per<br>share)                    | (500,000)                      | (748,100 ) |                    |             | 80,000       | 29,924    | 80,000           | 119,696     |       |
| 23/4/10 EBT -<br>60,000 @<br>\$2.285 exc<br>\$1.5793/£1<br>shares to Eden |                                |            |                    |             |              |           |                  |             |       |
| 8/6/10 EBT -<br>122,000 @<br>\$1.7 exc                                    |                                |            |                    |             |              |           |                  |             |       |



\$1.457/£1  
shares to Inc

Interest charged  
to EBT

Interest  
reversed to  
EBT

Transfer  
balance of  
Redeem to Sh  
Prem

(791,700 )

Profit & Loss -  
June 30, 2010

Translation  
adjustment

Balance, June  
30, 2010

-

£-

1,750,000

\$3,432,450

1,495,460

641,126

1,495,460

\$2,564,504

\$13,1

Asher &  
Trafalgar  
shares Dec 10

267,522

126,850

267,522

507,400

EBT shares  
sold

Translation  
adjustment

Trafalgar, Isaac  
& New Moon  
shares Feb

355,138

142,497

355,138

569,988

Correction to  
AsherTrafalgar  
2010

(5,987 )

Palm Finance  
shares Mar

150,000

60,210

150,000

240,840

TCA & Eden  
shares May

275,011

110,385

J Shapiro  
shares June

100,000

40,140

EBT shares  
sold

Net loss

Translation  
adjustment

Balance, June  
30, 2011

-

£-

1,750,000

\$3,432,450

2,643,131

\$1,121,208

2,268,120

\$3,876,745

13,1

The accompanying notes are an integral part of these consolidated financial statements.

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## SEVEN ARTS PICTURES PLC.

CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED JUNE 30, 2011 AND 2010

|   | 2011               | 2010                |
|---|--------------------|---------------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>  | <b>\$1,461,554</b> | <b>\$(475,651 )</b> |
| Net income/ (loss)  |                    |                     |
| Adjustments to reconcile net income (loss)<br>to net cash provided by (used in) operating activities: |                    |                     |
| Depreciation of property and equipment  | 14,026             | 13,884              |
| Amortization of film cost   | 2,022,783          | 1,575,093           |
| Impairment of film cost   | 820,951            | 195,557             |
| Write off of previously capitalized film assets   | -                  | 244,640             |
| Forgiveness of debt   | (1,000,000)        | (150,000 )          |
| Forgiveness of interest by lender   | (3,458,621)        | (383,874 )          |
| (Increase)/reduction of EBT interest receivable   | (71,966 )          | 178,904             |
| Write-off of other receivables and prepayments  | -                  | 572,509             |
| Ordinary shares issuance in exchange for I/R fees and to repay loans                                  | 2,977,208          | 257,159             |
| Bad debt expense and provision for doubtful accounts  | 234,429            | 319,345             |
| Write-off of previously accrued participations  | -                  | (215,250 )          |
| Change in operating assets and liabilities  |                    |                     |
| Trade receivables   | 812,080            | (218,659 )          |
| Due to and due from related parties, net  | 969,570            | (907,699 )          |
| Capitalized film assets   | (2,168,426)        | (2,470,299)         |
| Other receivables and prepayments   | (1,357,745)        | (66,008 )           |
| Accounts payable  | 233,219            | 541,212             |
| Other current liabilities   | 36,919             | 2,205,483           |
| Deferred income   | (1,052,464)        | 96,620              |
| Net cash provided by operating activities   | 473,517            | 1,312,966           |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>  |                    |                     |
| Purchase of property and equipment  | (12,177 )          | (2,808 )            |
| Net cash (used in) investing activities   | (12,177 )          | (2,808 )            |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>  |                    |                     |
| Proceeds from/(repayment of) participation equity/investment<br>and notes payable                     | (230,434 )         | (1,353,958)         |
| Issuance of common stock for cash   | -                  | 23,818              |
| Net cash (used in) financing activities   | (230,434 )         | (1,330,140)         |
| Effect of exchange rate changes on cash and cash equivalents  | (249,926 )         | 18,007              |
| <b>NET (DECREASE) IN CASH &amp; CASH EQUIVALENTS</b>  | <b>(19,020 )</b>   | <b>(1,975 )</b>     |
| <b>CASH &amp; CASH EQUIVALENTS, BEGINNING OF YEAR</b>   | <b>26,818</b>      | <b>28,793</b>       |
| <b>CASH &amp; CASH EQUIVALENTS, END OF YEAR</b>   | <b>\$7,798</b>     | <b>\$26,818</b>     |

## SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION

## Cash paid during the year or period for:

|              |            |              |
|--------------|------------|--------------|
| Interest     | \$ 149,326 | \$ 1,173,528 |
| Income taxes | \$-        | \$-          |

## NON CASH INVESTING AND FINANCING TRANSACTIONS:

|  |              |              |
|--|--------------|--------------|
| Accounts receivable applied against loan set off         | \$-          | \$ 475,374   |
| Production loan settled by shares owned by EBT           | \$-          | \$ 133,661   |
| Reclassification of share premium to accrued liabilities | \$-          | \$ 221,142   |
| Related party advances settled by shares owned by EBT    | \$ 164,500   | \$ 212,800   |
| Interest of loan payable capitalized on film assets      | \$ 50,262    | \$ 429,142   |
| Accrued interest included in loan payable amount         | \$ 2,244,903 | \$ 1,946,705 |
| Share based compensation expense                         | \$ 87,026    | \$-          |

The accompanying notes are an integral part of these consolidated financial statements.

SEVEN ARTS PICTURES, PLC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE YEARS ENDED JUNE 30, 2011 AND 2010

NOTE 1 - NATURE OF ACTIVITIES AND SIGNIFICANT ACCOUNTING POLICIES

Nature of Activities, History and Organization

Seven Arts Pictures, Plc. (herein referred to as “PLC” or collectively as “the Group”, “the Company”, or “Seven Arts”), was founded in 2002 as an independent motion picture production and distribution company engaged in the development, acquisition, financing, production, and licensing of theatrical motion pictures for exhibition in domestic (i.e., the United States and Canada) and foreign theatrical markets, and for subsequent worldwide release in other forms of media, including home video and pay and free television. The Company currently owns interests in 33 completed motion pictures, subject in certain instances to the prior financial interests of other parties.

The consolidated financial statements include the financial statements of Seven Arts Pictures Plc. (“PLC”), and its wholly owned subsidiaries, Seven Arts Filmed Entertainment Limited (“SAFE Ltd”), Seven Arts Filmed Entertainment (UK) Limited, Cinematic Finance Limited and Cinematic Finance (Equicap) Ltd, herein referred to as (the “Group”, the “Company” or “Seven Arts”). See below for detail on consolidated entities.

On June 11, 2010, Seven Arts Entertainment, Inc. (“SAE”), a Nevada Corporation, was formed and became a 100% owned subsidiary of Seven Arts Pictures Plc. The Company entered into an Asset Transfer Agreement, as amended on January 27, 2011 and again on August 31, 2011, to transfer all of the assets with a cost basis from PLC to SAE, in exchange for assumption by SAE of certain indebtedness and for one share of common stock of SAE for each ordinary share of PLC which have been distributed to shareholders. Additionally, 2,000,000 shares of SAE were issued to PLC in order to satisfy any remaining obligations. This transfer was approved by the PLC shareholders at an Extraordinary General Meeting on June 11, 2010. The purpose of this transfer was to eliminate our status as a foreign private issuer and to assume compliance with all obligations of a domestic issuer under all applicable state and Federal securities laws. Our intention in executing this transaction was to redomicile our business in the United States of America with no change in the economic interests of our shareholders.

As of January 27, 2011, net assets with a book value totaling approximately \$7,200,000 plus convertible debentures with no redemption date, which are accounted for as equity, were transferred to SAE in accordance with the asset transfer agreement.

On August 31, 2011, NASDAQ approved the substitution of one share of SAE stock for the Company's NASDAQ listing, effective at the opening of trading on September 1, 2011. On that date, each of the Company's ordinary shares were exchanged for one share of common stock of SAE, and commenced trading on NASDAQ as the successor to the Company's NASDAQ listing. This transaction was approved by the Company's shareholders at the Company's Extraordinary General Meeting on June 11, 2010.

SAE's authorized capital consists of 50,000,000 shares of stock, \$.01 par value per share, of which the board of directors has approved 25,000,000 shares as common stock. As of September 1, 2011, there were 6,476,344 shares of common stock outstanding, all of which are fully paid and non-assessable. Each outstanding share of common stock entitles the holder thereof to one vote per share on matters submitted to a vote of stockholders.

SAE is now a United States issuer and commenced regular quarterly reporting for the first quarter ended September 30, 2011.

On November 8, 2011, PLC, was placed into involuntary creditors liquidation under English law (See NOTE 16 – Commitments and Contingencies). Certain indebtedness of PLC remained with PLC and will be subject to administration or payment in those administration proceedings. In accordance with the asset transfer agreement, PLC has been issued 2,000,000 shares of common stock of SAE in order to satisfy these obligations.

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## Basis of Consolidation

The Company consolidates its subsidiaries in accordance with Accounting Standards Codification (“ASC”) 810, “Business Combinations”, and specifically ASC 810-10-15-8 which states, “The usual condition for a controlling financial interest is ownership of a majority voting interest, and, therefore, as a general rule, ownership by one reporting entity, directly or indirectly, or over 50% of the outstanding voting shares of another entity is a condition pointing toward consolidation.” The Company does not have any variable interest or special purpose entities.

The consolidated financial statements include the financial statements of Seven Arts Pictures Plc (“PLC”), and its wholly owned subsidiaries, Seven Arts Filmed Entertainment Limited (“SAFE Ltd”), Seven Arts Filmed Entertainment (UK) Limited, Cinematic Finance Limited and Cinematic Finance (Equicap) Ltd, herein referred to as (the “Group”, the “Company” or “Seven Arts”).

The accompanying consolidated financial statements include the accounts of Seven Arts Pictures Plc. (“SAP Plc.”) and its wholly owned subsidiaries as follows:

|  | Years<br>Ended<br>June 30,<br>2011 and<br>2010 |   |
|--|--|---|
| Seven Arts Pictures Plc.                     | 100  | % |
| Seven Arts Filmed Entertainment Limited      | 100  | % |
| Seven Arts Filmed Entertainment (UK) Limited | 100  | % |
| Cinematic Finance Limited                    | 100  | % |
| Cinematic Finance (Equicap) Ltd              | 100  | % |

The Group acquired SAFCO’s in May 2009. SAFCO’s refers to 17 companies formed by investors in the Zeus transaction (as described in NOTE 16). The Group intends to liquidate the SAFCO’s under the applicable laws of the United Kingdom upon obtaining full control of the books, records and operation of the SAFCO’s. The Group does not anticipate any material assets or liabilities related to the SAFCO’s except the contingent liability for VAT on the Zeus transaction. The SAFCO’s results have not been and will not be consolidated as the Group does not have control.

All significant intercompany balances and transactions have been eliminated on consolidation.

## Significant Accounting Policies

The Company’s management selects accounting principles generally accepted in the United States of America and adopts methods for their application. The application of accounting principles requires the estimating, matching and timing of revenue and expense. The accounting policies used conform to generally accepted accounting principles which have been consistently applied in the preparation of these financial statements.

The financial statements and notes are representations of the Company’s management which is responsible for their integrity and objectivity. Management further acknowledges that it is solely responsible for adopting sound accounting practices, establishing and maintaining a system of internal accounting control and preventing and detecting fraud. The Company’s system of internal accounting control is designed to assure, among other items, that 1) recorded transactions are valid; 2) valid transactions are recorded; and 3) transactions are recorded in the proper period in a timely manner to produce financial statements which present fairly the financial condition, results of operations and cash flows of the Company for the respective periods being

presented.

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## Basis of Accounting

The Company prepares its financial statements on the accrual basis of accounting and in accordance with Generally Accepted Accounting Principles of the United States of America ("US GAAP"). All material intercompany balances and transactions are eliminated. Management believes that all adjustments necessary for a fair presentation of the results of the years ended June 30, 2011 and 2010, respectively, have been made.

The Group has also engaged in various transactions under which it has received cash proceeds from the transfer of tax credits or other tax benefits associated with its motion picture productions. Any such proceeds are generally treated as a reduction in the production costs of the applicable motion picture.

- a) To the extent such tax benefit proceeds would exceed the capitalized cost of the film or represent fee income not applied to production cost, such proceeds are accounted for as producers' fees income where relevant producers contracts are in place.
- b) To the extent that the Group were to receive benefits from tax advantaged investments relating to:
  - i. a picture that has not commenced production by a particular date and that investment is forfeited such that the Group has no further obligations to the investor or
  - ii. third party productions taken on by the Group as sales agent/distributor, then such benefits are also recorded as producer fees income.

## Revenue Recognition

Revenue earned by the Group can be classified into two categories:

1. Film revenue: Revenue is earned from the exploitation of new productions, back catalogue and third party productions taken on as sales agent.
2. Fee-related revenue: Producer's fees income earned by the Group on productions controlled by the Group is earned when the Group is entitled to receive, under a binding agreement a fixed sum irrespective of the distribution revenue from that picture.

## Film Revenue

The Group recognizes revenue from the sale (minimum guarantee or non-refundable advances) or licensing arrangement (Royalty agreement) of a film in accordance with ASC 605-15 “Revenue Recognition”. Revenue will be recognized only when all of the following criteria have been met:

- a) Persuasive evidence of a sale or licensing arrangement with a customer exists.
- b) The film is complete and, in accordance with the terms of the arrangement, has been delivered or is available for immediate and unconditional delivery. (i.e. the “notice of delivery” (NOD) has been sent and there is a master negative available for the customer)
- c) The license period of the arrangement has begun and the customer can begin its exploitation, exhibition, or sale.
  - d) The arrangement fee is fixed or determinable.
  - e) Collection of the arrangement fee is reasonably assured.

A written agreement with clients (purchase order, letter, contract, etc.) indicating the film name, territory and period is required for the recognition of revenue. Revenue is recognized when the performance criteria in the contracts have been met. The customer generally confirms agreement by their signature on the contract.

Minimum guarantee revenue (i.e. non-refundable advances) is recognized as and when the film is available for delivery to the respective territories. Cash deposits received on the signing of the contracts are recorded as deferred income until the film is available for delivery (as described above) at which point the deposit revenue is recognized. The Group does not recognize any revenues relating to minimum guarantee on any motion picture as well as amortization expense on that picture until United States theatrical release if it has agreed with the licensees that delivery or payment of minimum guarantee will be delayed for any material period of time to permit such a theatrical release.

Royalty revenue which equates to an agreed share of gross receipts of films is recognized as income as and when the Group is notified of the amounts by the customers through their royalty reports.

## Fee-related Revenues

Many countries make tax credits available to encourage film production in their territory. Seven Arts benefits from tax credits in:

- a) the UK and several other European territories for their European productions
- b) Canada for their Canadian productions
- c) Louisiana for their US productions
- d) Tax preferred financing deals

In the majority of circumstances, these tax credits are treated as a reduction in the capitalized costs of the film assets they are financing. However, to the extent such tax benefit proceeds would:

- a) exceed the capitalized cost of the film or
- b) represent fee income not applied to production cost, such proceeds are accounted for as producers' fees income where relevant producer's contracts are in place.

In addition, to the extent that the Group was to receive benefits from tax advantaged investments relating to:

- a) a picture that has not commenced production by the investment agreement closing date, that investment is forfeited such that the Group has no further obligations to the investor or
- b) third party productions taken on by the Group as sales agent/distributor, then such benefits are also recorded as producer fees income

One of the risks for the investor associated with these tax advantaged investments is that a particular picture will not start production within the investment agreement period therefore giving no asset value to their slate of investments. The contract with the Group will generally state that there is no recourse to the Group and associated companies as this is one of the many risks of the film industry that the investors are made aware of on signing the investment agreements. Therefore, when a picture has not commenced production by the investment agreement closing date that investment is forfeited and the Group has no further obligations to the investors. These financing schemes are part of the general operations of the Group in its role as producer. Revenues in the year ended June 30, 2011 however did not include fee income derived from a structured film and distribution cost financing with UK investors. It did include additional producer fee of \$570,029 associated with films produced in Louisiana. In 2010, the Group recognized \$2,650,794 of fee income as described and, in addition, producer's fees of \$1,792,125.

#### Investments

Investments are held at the lower of cost or net realizable value, and reviewed annually for any impairment charges. As of June 30, 2011 the Group has no outstanding investments.

#### Film Costs

Film costs include the unamortized costs of completed films which have been produced by the Group or for which the Group has acquired distribution rights, libraries acquired as part of acquisitions of companies and films in progress and in development. For films produced by the Group, capitalized costs include all direct production and financing costs, capitalized interest and production overhead.

Costs of acquiring and producing films are amortized using the individual-film-forecast method, whereby these costs are amortized and participations and residuals costs are accrued in the proportion that current year's revenue bears to management's estimate of ultimate revenue at the beginning of the current year expected to be recognized from the exploitation, exhibition or sale of the films. Generally, 80% or more of a film's costs are amortized within three years of the picture's initial release.

Ultimate revenue includes estimates of revenue to be earned over a period not to exceed ten years following the date of initial release. Film costs are stated at the lower of amortized cost or estimated fair value. Individual film costs are reviewed on a title-by-title basis, when an event or change in circumstances indicates that the fair value of a film is less than its unamortized cost. The fair value of the film is determined using management's future revenue and cost estimates and a discounted cash flow approach. Impairment is recorded in the amount by which the unamortized costs exceed the estimated fair value of the film. Estimates of future revenue involve measurement uncertainty and it is

therefore possible that reductions in the carrying value of film costs may be required as a consequence of changes in management's future revenue estimates.

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Films are included in the general “library” category when initial release dates are at least three years prior to the acquisition date.

Films in progress include the accumulated costs of productions which have not yet been completed. Films in development include costs of acquiring film rights to books, stage plays or original screenplays and costs to adapt such projects. Such costs are capitalized and, upon commencement of production, are transferred to production costs. Projects in development are written off at the earlier of the date they are determined not to be recoverable or when abandoned.

#### Property & Equipment

Equipment is carried at the cost of acquisition or construction and depreciated over the estimated useful lives of the assets. Costs associated with repair and maintenance are expensed as incurred. Costs associated with improvements which extend the life, increase the capacity or improve the efficiency of our property and equipment are capitalized and depreciated over the remaining life of the related asset. Gains and losses on dispositions of equipment are reflected in operations. Depreciation and amortization are provided using the straight-line method over the estimated useful lives of the assets, which are two to five years.

#### Income Taxes

The Company has adopted ASC 740-10 “Income Taxes”, which requires the use of the liability method in the computation of income tax expense and the current and deferred income taxes payable.

The Group is not part of any consolidated return filed in the United States.

#### Foreign Currency Transactions and Comprehensive Income

The accounts are presented in United States Dollars (“USD”), the functional currency of the main operating company, SAFE Ltd. The functional currency of the holding company SAP Plc. and other entities located in the UK is in Pounds Sterling (“GBP”). The books of the foreign entities are converted to USD at each reporting period date.

The Group translates the foreign currency transactions and balances into USD using the year or reporting period end or average exchange rates. Assets and liabilities of the foreign entities are translated at exchange rates as of the balance sheet date. Revenues and expenses are translated at average rates in effect for the periods presented. The cumulative translation adjustment is included in the translation reserve within shareholders’ equity (deficit). Foreign currency transaction gains and losses arising from exchange rate fluctuations on transactions denominated in a currency other than the functional currency are included in the consolidated results of operations.

Where possible, the Group seeks to match USD income with USD expenditures. To date the Group has not hedged any transactional currency exposure but will keep such exposures under review and where appropriate may enter into such transactions in future.

Relevant exchange rates used in the preparation of the financial statements are as follows for the years ended June 30, 2011 and 2010 (GBP per one USD):

|   | June 30, 2011 |        |
|---|---------------|--------|
| Balance sheet period end exchange rate:   | GBP           | 1.6056 |
| Average exchange rate for the year ended: | GBP           | 1.5655 |
|   | June 30, 2010 |        |
| Balance sheet period end exchange rate:   | GBP           | 1.4962 |
| Average exchange rate for the year ended: | GBP           | 1,5721 |

#### Derivative Instruments and Hedging Activities

The Group's policy is not to use derivative or hedging financial instruments for trading or speculative purposes, except certain embedded derivatives derived from certain conversion features or reset provision attached to the convertible debentures as described in NOTE 12.

#### Earnings Per Share

Basic earnings (loss) per share are computed by dividing net income (loss) by the weighted average number of common shares outstanding for the period. Diluted earnings (loss) per share include the effects of any outstanding options, warrants and other potentially dilutive securities. For the periods presented, there were no potentially dilutive securities outstanding, therefore basic earnings per share equals diluted earnings per share. Basic and diluted earnings per share ("EPS") are based on weighted-average common shares and exclude shares that would have an anti-dilutive effect. In accordance with ASC 260-10-45-19, the Company did not consider any potential common shares in the computation of diluted EPS as of June 30, 2011 and 2010, due to the loss from continuing operations, as they would have an anti-dilutive effect on EPS.

#### Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. The most significant estimates made by management in the preparation of the financial statements relate to ultimate revenue and costs of its films which are used in the amortization and impairment of film costs, estimates for allowances, option pricing for options and warrants issued and income taxes. Accordingly, actual results could differ from those estimates.

#### Recently Issued Accounting Pronouncements

The Company does not expect the adoption of recently issued accounting pronouncements to have a significant impact on the Company's results of operations, financial position or cash flow.

#### Accounts Receivable

Receivables are recognized at the initial amount of the invoice. As a result of the nature of the Group's activities, accounts receivables are generally of a short-term nature. However, any receivable whose recovery date was beyond one year would be measured at its present value. The Group does not charge interest on late payment of trade receivables and loans.

Reserve for doubtful accounts represent a provision charged to reflect management's best estimate of the likelihood that certain of the Group's accounts receivable may not ultimately be collected. This provision is based on historical experience and relevant facts and information regarding collectability at the time and will be adjusted up or down over time with the benefit of actual results.

Any receivable outstanding is only written off after management has deemed the receivable to be uncollectible, under the terms of the agreement and/or based on the financial conditions of the customers at each reporting period. As of June 30, 2011 and 2010 the Group had an allowance for bad debts and doubtful accounts of \$310,796 and \$532,996, respectively, to cover any future uncollectible receivables. The Group determines its allowance by considering a number of factors, including the length of time receivables are past due, the Group's previous loss history, the customer's current ability to pay its obligation to the Group, and the condition of the general economy and the industry as a whole.

Substantially all of the trade receivables at face value as reflected in the consolidated financial statements are pledged as security for borrowings by the Group.

#### Accounts Payable

All operating trade payables (including notes payable and accrued supplier invoices) relate to the purchase of goods and services. These payables are due within and or less than one year. However any payable whose due date was more than one year would be measured at its present value. The Group did not have any such long-term accounts payable during the periods presented.

#### Fair Value of Financial Instruments

The carrying amount of cash, trade accounts receivable, other accounts receivable, receivables due from and payable to related parties, trade accounts payable, other accounts payable and accrued expenses, as well as short-term debt, approximate their corresponding estimated fair values due to the short-term maturity and revolving nature of these financial assets and liabilities. Cash and cash equivalents are recognized at fair value considering quoted market prices if available for the same or similar instruments. Long-term debt is based on estimated market prices for similar instruments, considering interest rates currently available in connection with bank loans with similar terms and due dates.

#### Share Based Payments

The Company accounts for share based payments using a fair value based method whereby compensation cost is measured at the grant date based on the value of the services received and is recognized over the service period. The Company uses the Black-Scholes pricing model to calculate the fair value of options and warrants issued. In calculating this fair value, there are certain assumptions used such as the expected life of the option, risk-free interest rate, dividend yield, volatility and forfeiture rate. The use of a different estimate for any one of these components could have a material impact on the amount of calculated compensation expense.





## Cash and Cash Equivalents

The cash and cash equivalents of the Group consisted of cash balances held on deposit with banks, of which \$8,767 is denominated in USD and \$(968) denominated in GBP, as of June 30, 2011. These deposits earn interest at the relevant bank interest rates, which are all floating rates of interest. These annual interest rates ranged from 2.8% to 8.8% for the fiscal year ended June 30, 2011, and 3.1% to 8.8% for the fiscal year ended June 30, 2010.

## NOTE 2 - REVENUE

Revenue earned by the Group can be classified into two categories: film revenues and fee-related revenues (see NOTE 1).

Film revenues consist of minimum guarantees from distributors, royalties earned either collected or receivable, and other fees or income associated with the sale of the Group's motion pictures.

Film revenue by geographical areas is as follows:

|                        | June 30,<br>2011 | June 30,<br>2010 |
|------------------------|------------------|------------------|
| Europe                 | \$969,077        | \$110,285        |
| North America          | 1,113,074        | 1,714,271        |
| South America          | 378,763          | 24,000           |
| Africa and Middle East | 39,416           | -                |
| Asia                   | 209,030          | 91,942           |
| Australia              | 48,999           | 34,018           |
| Total                  | \$2,758,359      | \$1,974,516      |

All fee-related revenues for the years ended June 30, 2011 and 2010 were generated in North America, and through a related party (as described below).

Fee related revenues in the period ended June 30, 2011 consisted of:

- a) Producer's fees of \$70,097 resulting from excess tax credits received on Night of the Demons. This item was collected by Seven Arts Pictures Louisiana LLC who will pay it over to the Group under the agreement between the Group and SAPLA.
- b) \$500,000 of fees relating to Esplanade Pictures based in Louisiana.

Fee related revenues in the period ended June 30, 2010 consisted of:

- a) \$2,650,794 of fee income derived from the Equicap transactions, a structured finance transaction with UK investors who invested in certain third party motion pictures distributed by the Group. The fee items related to the Equicap transactions were contractually entered with Seven Arts Pictures Louisiana LLC ("SAPLA"), a related party who is acting on behalf of the Group but collected and recorded by the Group under the Group's agreement with SAPLA as fee income.

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- b) Producer's fees of \$637,397 resulting from excess tax credits received on Night of the Demons. This item was collected by SAPLA and will be paid over to the Group under the agreement between the Group and SAPLA.
- c) Producer's fees income of \$1,154,728 resulting from excess tax credits received on American Summer (Pool Boys) and Autopsy. This will be collected by SAPLA and will be paid over to the Group under the Group's agreement with SAPLA.

All of the Group's revenues and profits before taxes in each year are derived from the financing, production and distribution of films.

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## NOTE 3 – NET INTEREST EXPENSE

The following presents the Group's interest expense and interest income for the years ended June 30, 2011 and 2010:

|                                      | June 30,<br>2011    | June 30,<br>2010     |
|--------------------------------------|---------------------|----------------------|
| Interest expense                     |                     |                      |
| Production loans interest paid       | \$(184,661 )        | \$(1,490,924)        |
| Corporate loans interest paid        | (607,267 )          | (672,004 )           |
| Bank interest paid                   | (37,950 )           | (36,916 )            |
| <b>Total interest paid</b>           | <b>\$(829,878 )</b> | <b>\$(2,199,844)</b> |
| Interest income                      |                     |                      |
| Interest received                    | \$368               | \$110,365            |
| Bank interest received               | 71,313              | 44                   |
| <b>Total interest received</b>       | <b>\$71,681</b>     | <b>\$110,409</b>     |
| <b>Net interest (expense)/income</b> | <b>\$(758,197 )</b> | <b>\$(2,089,435)</b> |

## NOTE 4 – OTHER INCOME RELATED TO CANCELTION OF INDEBTEDNESS

The Group recorded of \$4,458,621 of other income for the year ended June 30, 2011 related to the cancellation of indebtedness arising from:

- a) The release of a loan of \$1,788,904 from Arrowhead (See NOTE 11) which is subordinated to the Cheyne debt of \$6,500,000 which was assigned to Seven Arts in 2008. Management does not believe that forecast income will be sufficient to repay the primary loan; therefore the subordinated loan will also not be repaid.
- b) Forgiveness of accrued interest of \$2,669,717, which was accrued through June 30, 2010, on the Palm Finance loans.

During the year ended June 30, 2010, the Company recorded a \$150,000 gain on the cancellation of indebtedness arising from a settlement with Kismet releasing a loan of \$150,000. Also during 2010, 120dB agreed to a cash settlement of \$323,000 in full and final settlement of the outstanding loan for Knife Edge. The Group recorded a \$383,874 gain on the cancellation of indebtedness related to this settlement. Total other income related to cancellation of indebtedness was \$533,874 for the year ended June 30, 2010.

## NOTE 5 – INCOME TAXES

The Company has adopted ASC 740-10, “Income Taxes”, which requires the use of the liability method in the computation of income tax expense and the current and deferred income taxes payable (deferred tax liability) or benefit (deferred tax asset). Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized.

During the year ended June 30, 2011 the Company had a net income of \$1,461,554 decreasing the deferred tax asset approximately \$496,928 at the statutory tax rate of 34%. Deferred tax assets at June 30, 2011 and 2010 consisted of the following:

|                                     | Year ended<br>June 30,<br>2011 | Year ended<br>June 30,<br>2010 |
|-------------------------------------|--------------------------------|--------------------------------|
| Net operating loss carry forwards   | \$ 10,422,664                  | \$ 11,579,923                  |
| Capital loss carry forwards         | 5,398,529                      | 5,398,529                      |
| Total carry forwards                | 15,821,193                     | 16,978,452                     |
| Tax rate of 34%                     | 34%                            | 34%                            |
| Total long-term deferred tax assets | 5,379,206                      | 5,772,673                      |
| Less: valuation allowance           | (5,379,206)                    | (5,772,673)                    |
| Net long-term deferred tax assets   | \$ -                           | \$ -                           |

The net deferred tax asset generated by the loss carry forward has been fully reserved and will expire in 2019 through 2030. The realization of deferred tax benefits is contingent upon future earnings and, therefore, is fully reserved at June 30, 2011 and 2010.

The following represents the effect of timing differences on the Group's tax expense or benefit for the years ended June 30, 2011 and 2010:

|  | Year ended<br>June 30,<br>2011 | Year ended<br>June 30,<br>2010 |
|--|--------------------------------|--------------------------------|
| Current tax charge/(benefit)   | \$ -                           | \$ -                           |
| Factors affecting the tax charge for the year:   |                                |                                |
| Income/(loss) before taxes   | 1,461,554                      | (475,651)                      |
| Income/(loss) before taxes multiplied by the standard rate of UK corporation tax of June 30 2011 at 27.5% (June 2010 at 28%) | 401,927                        | (133,182)                      |
| Effects of:  |                                |                                |
| Non deductible expenses  | 47,606                         | 42,000                         |
| Excess of amortization over tax deductions   | (14,158)                       | (14,416)                       |
| Non-qualifying depreciation  | 782,027                        | 495,782                        |
| Excess of capital allowances over depreciation   | (1,182)                        | (824)                          |
| Movement in tax losses   | (714,322)                      | (727,311)                      |
| Film tax profit adjustment   | (501,898)                      | 337,951                        |
| Current tax expense/(benefit)  | \$ -                           | \$ -                           |

As of June 30, 2011, the Group had operating losses of approximately \$10,422,664 to carry forward against future operating profits.

As of June 30, 2011, the Group had capital losses of approximately \$5,398,529 to carry forward against future capital profits.

The net deferred tax asset generated by the loss carry forwards has been fully reserved and will expire in 2019 through 2030. The realization of deferred tax benefits is contingent upon future earnings and is fully reserved at June 30, 2011 and 2010.

## NOTE 6 – EARNINGS PER SHARE

Basic net income/(loss) per share is based upon the weighted average number of common shares outstanding for the period presented and all shares amounts have been adjusted to reflect the Group's two separate 5:1 reverse stock splits. Diluted earnings per share is based on the assumption that all dilutive convertible shares and stock warrants were converted or exercised. Warrants are assumed to be exercised at the beginning of the period (or at the time of issuance, if later), and as if funds obtained thereby were used to purchase common stock at the average market price during the period. At June 30, 2011, the Company had a total of 2,217,872 common stock equivalents outstanding, including options, warrants and convertible debentures. All common stock equivalents for the year ended June 30, 2010 are anti-dilutive due to the net loss incurred.

Basic and diluted earnings per share ("EPS") are based on weighted-average common shares and generally exclude shares that would have an anti-dilutive effect. In accordance with ASC 260-10-45-19, the Group did not consider any potential common shares in the computation of diluted EPS as of June 30, 2011 or for June 30, 2010, due to the loss from continuing operations. For the year ended June 30, 2011, 329,160 anti-dilutive shares were excluded from the EPS calculation, which would have been considered dilutive if the Company did not have a loss from operations.

The following is a reconciliation of the number of shares (denominator) used in the basic and diluted earnings per share computations for the years ended June 30, 2011 and 2010:

|                            | 2011   |                     | 2010   |                     |
|----------------------------|--|---------------------|--|---------------------|
|                            | Weighted<br>Average<br>Shares<br>Outstanding | Per Share<br>Amount | Weighted<br>Average<br>Shares<br>Outstanding | Per Share<br>Amount |
| Basic earnings per share   | 1,888,712                                    | \$0.77              | 1,402,720                                    | \$(0.34 )           |
| Diluted earnings per share | 1,888,712                                    | \$0.77              | 1,402,720                                    | \$(0.34 )           |

Basic and diluted net income (loss) per share is calculated based on the weighted average common shares outstanding for the period presented and all have been adjusted to reflect the Group's 5:1 reverse stock splits which occurred on December 31, 2008 and May 12, 2011.

## NOTE 7- EMPLOYEE BENEFIT TRUST

The Group established the Seven Arts Employee Benefit Trust ("EBT") for the purpose, among others, of acquiring 3,000,000 of the Group's preferred shares from Armadillo Investments Plc. ("Armadillo"). EBT is governed by a Trust Deed that the Group entered into with the trustees. Under the Trust Deed, the Trustees have absolute control over the Trust although the Group may recommend options to the trustees. The Group has the right after approval of the audit committee to restrict the Trust's right to vote its shares of the Group to prevent the Trust from taking control of the Group and the right to remove the Trustees under certain circumstances for the same purpose.

The Group has no interest in the profits or losses of the Trust on the Group's shares and does not control the actions of the Trustees in the sale or use of these shares. The Group has no control or significant influence on the EBT. All cash and ordinary shares owned by EBT are held by EBT for the benefit of the Group's United Kingdom employees.

On October 30, 2008, EBT reached an agreement to acquire these preference shares for £1,500,000 plus the return of 1,600,000 of Armadillo's ordinary shares. On that date the Group advanced £500,000 as the first of three equal installments together with 1,600,000 shares of Armadillo Investments Plc. The EBT acquired 3,000,000 of the Group's convertible preferred shares from Armadillo. Seven Arts has guaranteed the remaining two payments due to Armadillo aggregating £1,000,000, but has not yet advanced these payments to EBT, so EBT is in default on both payments due to Armadillo. On November 20, 2008, EBT converted 2,500,000 of these preferred shares into 2,000,000 of the Group's ordinary shares. On June 30, 2010, the EBT converted the remaining 500,000 preferred shares to 400,000 ordinary shares.

The EBT originally pledged 266,667 ordinary shares to Armadillo to secure the sum due to Armadillo, which the pledge will be terminated when the EBT pays the £1,000,000 to Armadillo. As of February 9, 2011, 150,000 shares of the Group were issued to New Moon Pictures LLC who then pledged the shares to Armadillo Investments Ltd who in turn have:

- a) extended the terms of the repayment of the £1,000,000 due from the EBT to June 30, 2011; and
- b) reduced their lien over the 266,667 shares currently held by the EBT to 200,000 shares.

At June 30, 2011, the loan receivable from EBT amounted to £643,084 (\$1,107,134) and the EBT owned 200,000 shares (or approximately 7.6% of the Group's outstanding ordinary shares as at June 30, 2011) all of which are pledged to Armadillo Investments Ltd.

#### NOTE 8 - FILM COSTS

The following presents the Group's film costs as of June 30, 2011 and 2010:

|  | June 30,<br>2011 | June 30,<br>2010 |
|--|------------------|------------------|
| Film costs - beginning balance           | \$23,808,869     | \$22,902,513     |
| Additional costs incurred                | 2,168,425        | 2,677,006        |
| Third party investments/ tax credits     | -                | -                |
| Amortization of film costs during period | (2,843,734)      | (1,770,650)      |
| Film costs as of June 30, 2011           | \$23,133,560     | \$23,808,869     |

The net book value of all films as of June 30, 2011 includes \$17,917,287 relating to films released since April, 2007 and \$5,216,272 relating to pictures in development.

Over 98% of the Group's pictures released before April 2007 have been fully amortized and therefore have a net book value of zero as of June 30, 2011.

Capitalized film costs are reviewed for impairment at least twice a year and whenever events or changes in circumstances indicate that the carrying amounts of such assets may not be recoverable. Determination of recoverability is based on an estimate of future cash flows resulting from the use of the asset, and its eventual disposition. Measurement of an impairment loss for the assets is based on the fair value of the asset as estimated using a discounted cash flow model. An impairment charge of \$ 820,951 was recognized during the year ended June 30, 2011 and \$195,557 for the year ended June 30, 2010.

## NOTE 9 – PROPERTY AND EQUIPMENT

The Group's property and equipment as of June 30, 2011 and 2010:

|                                    |           |
|------------------------------------|-----------|
| Net book value as of June 30, 2009 | \$40,112  |
| Additions                          | 2,808     |
| Depreciation charge for the period | (13,884 ) |
| Exchange differences               | (2,647 )  |
| Net book value as of June 30, 2010 | 26,389    |
| Additions                          | 12,177    |
| Depreciation charge for the period | (14,026 ) |
| Exchange differences               | -         |
| Net book value as of June 30, 2011 | \$24,540  |

## NOTE 10 – FILM AND PRODUCTION AND CORPORATE LOANS

The following presents that Company's film and production and corporate loans as of June 30, 2011 and 2010:

|                         | June 30,<br>2011<br>(USD) | June 30,<br>2010<br>(USD) |
|-------------------------|---------------------------|---------------------------|
| Current                 |                           |                           |
| Film & production loans | \$10,890,430              | \$16,766,689              |
| Corporate loans         | 1,755,250                 | 1,534,591                 |
| Current                 | \$12,645,680              | \$18,301,280              |



## Film and Production Loans

Film and production loans arose from the financing of motion pictures and are secured with an interest in the associated motion pictures. Detail of these production loans is presented below.

A loan of \$8,300,000 was advanced to Seven Arts Future Flows I LLC ("SFF"), a subsidiary of Seven Arts Pictures Inc., ("SAP, Inc.) a related party, on a non-recourse basis by Arrowhead Ltd. ("Arrowhead") and was secured by a pledge of Seven Arts Filmed Entertainment Limited's distribution rights in twelve designated pictures owned by SFF for the period of the loan. During the period ended June 30, 2009, Arrowhead made the decision to take control over the distribution rights to these pictures. Since the Group no longer controls the licensing of these motion pictures, it has removed all investment in the cost of these pictures as well as receivables from its assets and has removed the non-recourse indebtedness and accrued interest from its liabilities as of June 30, 2009. This resulted in the recognition of \$5,601,683 of "Other income" in the period ended June 30, 2009 relating to the cancellation of indebtedness.

Arrowhead filed an action on September 22, 2010, which seeks recovery from the Group of the monies which the Group has retained under its interpretation of the relevant agreements with Arrowhead. In addition, Arrowhead makes substantial additional claims against the Group, Mr. Hoffman and Seven Arts Pictures Inc. regarding claimed breaches of the terms of the operative agreements, including failure to properly account, failure to turn over materials, failure to remit monies collected, and similar matters. The claims against the Group for these breaches of warranties for damages are \$8,300,000 although Arrowhead states no basis for this amount.

The Group had moved to dismiss the action against all defendants other than Seven Arts Future Flows I LLC, which is not part of the Group. On August 9, 2011, the New York Supreme Court granted the Group's motion and dismissed all defendants except SAFE Ltd. in its capacity as a collateral agent, which is not a material element of Arrowhead claim. The Group continues to believe that Arrowhead's claims against the Group are without substantial merit.

Management has accounted for the monies collected and not remitted from the Arrowhead titles as accrued liabilities in the Group's books and records as of June 30, 2011.

An original loan of \$7,500,000 was taken from Cheyne Specialty Finance Fund LLP (\$6,500,000) senior debt and Arrowhead Consulting Group Limited (\$1,000,000) -subordinated debt. The Cheyne portion of the loan was acquired by SAFE Ltd for payment of \$6,500,000 in April 2008, leaving a balance owed by the Group of \$1,000,000 due to Arrowhead Consulting Group Limited but subordinated to the collection of \$6,500,000 plus interest from certain pictures after June 30, 2008. The \$1,000,000 balance of the loan is secured with all of the income over and above the \$6,500,000 plus interest from six films ( Deal, Noise, Pool Hall Prophets, A Broken Life, Mirror Wars and Boo ) as well as with a secondary security interest in certain film library assets (behind Arrowhead) and a first security interest in 321,400 shares of the Group owned by Seven Arts Pictures Inc. The Group is in litigation with the liquidator of Arrowhead Consulting Group regarding the \$1,000,000 plus accrued interest and it believes this debt will never be paid due to its subordination to the senior loan.

A security interest in favor of Palm Finance Corporation ("Palm") was lodged at Companies House (the United Kingdom's registrar of companies) in January 2008, by the Group to cover loans made by Palm to finance the films Nine Miles Down, The Pool Boys and Autopsy. The Group entered into two senior financing loan and security agreements with Palm Finance Corp ("Palm") to finance the production costs of The Pool Boys, Autopsy and Nine Miles Down dated May 7, 2007 and December 17, 2007. These loans are secured by the revenues to be collected from these motion pictures. The revenues so far collected have been insufficient to repay the majority of these loans, primarily as result of management's decision to delay the release of these films. The original principal amount of the Palm loan for The Pool Boys and Autopsy are \$5,500,000 including \$700,000 of accrued interest, and for Nine Miles Down was \$4,000,000 including \$750,000 of accrued interest. In November 2010, the Group entered into a new

financing agreement with Palm extending the due date of these loans to December 31, 2011.

The lender agreed to write-off the accrued interest as of June 30, 2011, giving rise to forgiveness of debt income of \$2,669,717. The outstanding balances on these loans as at June 30, 2011 were \$4,910,052 (Pool Boys/Autopsy) and \$3,176,018 (Nine Miles Down).

Subsequent to June 30, 2011, the lender sold \$2,750,000 of its debt and converted 50% of the monies received to Series A preference shares in SAE Inc. (See NOTE 13 – Subsequent Events.)

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On August 27, 2007, the Group borrowed \$1,650,000 from Blue Rider Financial (“Blue Rider”) to pay for the domestic prints and advertising costs for the motion picture “Deal” (“Blue Rider Loan”) and arranged that the revenues due from Metro-Goldwyn-Mayer Studios Inc. (“MGM”) to the Group for the distribution of that motion picture be assigned to Blue Rider Financial as partial security for that loan. To date the revenues paid to the Group from MGM have not yet been sufficient to repay the Blue Rider Loan. The Group has therefore entered into an accommodation agreement with Blue Rider to redeem the loan due for \$2,200,000, less approximately \$812,000 of collections that have been received by Blue Rider to date from MGM. We expect this indebtedness will be repaid from proceeds due from MGM on or before December 31, 2011.

#### Corporate loans

##### Trafalgar Loan

On October 15, 2008 the Group borrowed £1,000,000 from Trafalgar Capital Special Investment Fund (“Trafalgar”). A portion of this loan the Group advanced to the EBT for it to use as the first installment for the acquisition of all the Preferred Shares owned by Armadillo. On September 2, 2009 the Group repaid Trafalgar \$1,000,000 (approximately £698,934) as a partial payment against this loan, with the remaining balance subject to repayment in cash or convertible to the ordinary shares of the Group at the conversion terms as agreed between Trafalgar and the Group. On June 22, 2010 an amended agreement was entered into with Trafalgar for an extension of the due date of the convertible debentures to December 31, 2010, and the Group agreed to issue 340,000 ordinary shares to settle a portion of the debt. Trafalgar agreed to reduce the loan amount from the proceeds it receives from selling the 340,000 ordinary shares. All of the 340,000 shares were sold in the market before December 31, 2010. A further amended agreement was entered into with Trafalgar for an extension of the due date of the convertible debentures to March 31, 2011, and the Group issued 425,000 ordinary shares to settle a portion of the debt. Trafalgar agreed to reduce the loan amount from the proceeds it receives from selling the 425,000 ordinary shares. The per-share value is determined as the amount recovered by Trafalgar on sale thereof in the market and Trafalgar may “put” these shares to the Group at £1.00 per share on April 30, 2011 if not previously sold. This put option was not exercised by Trafalgar.

##### Asher Loan

In May, June and September 2010, the Group issued an aggregate of \$200,000 Convertible Promissory Notes to Asher Enterprises, Inc. (“Asher Notes”) that were to mature on March 11, 2011, March 17, 2011 and June 24, 2011, respectively. The Asher Notes bore interest at a rate of 8% per annum and were convertible into the Group’s ordinary shares beginning on the date which is one hundred twenty (120) days following the issuance of the Asher Notes, at the holder’s option, at the conversion rate of 60% of the market price of the lowest three trading prices of the Group’s ordinary shares during the ten-day period ending one trading day prior to the date of the conversion notice is sent by the note holders via facsimile.

The Group has identified the embedded derivatives related to the Asher Notes. These embedded derivatives included certain conversion features and reset provision. The accounting treatment of derivative financial instruments requires that the Group record fair value of the derivatives as of the inception date of Asher Notes and to fair value as of each subsequent reporting date. At the inception of the Asher Notes, the Group determined a fair value of \$178,187 on the embedded derivative. The fair value of the embedded derivative was determined using the Black Scholes Option Pricing Model based on the following assumptions:

| Assumption      | Amount        |
|-----------------|---------------|
| Dividend yield: | 0.0%          |
| Volatility      | 133% ~ 142%   |
| Risk free rate: | 0.25% ~ 0.37% |

During the year ended June 30, 2011, the Company issued an aggregate of 53,668 shares of common stock in full settlement of the \$100,000 Convertible Promissory Note dated May 2010 and related interest. In addition, the Company paid remaining two Convertible Promissory Notes an aggregate of \$120,000 in cash. As such, the Company recorded amortization of \$178,187 as debt discount for the year ended June 30, 2011 and \$32,530 loss on change in fair value of debt derivative.

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Convertible Notes issued August 30, 2010

On August 30, 2010, the Group issued an aggregate of \$470,000 Convertible Debt to qualified investors that matures on February 28, 2011. The Convertible Debts bear interest at a rate of 15.0% per annum and could be converted into the Group's ordinary shares beginning on the date which is one hundred twenty (120) days following the issuance of the Convertible Debt, at the conversion rate of \$3.75 per share, subject to certain changes, and are convertible at the option of the Group.

- a) On March 22, 2011 an additional \$300,000 of convertible notes were issued to Runway Investments Ltd on the same terms as above. At the same time the original notes were extended to July 31, 2011.
- b) All \$770,000 of these notes were extended on May 24, 2011 to September 30, 2011, and the conversion terms were changed as follows:

The Scarborough note's principal and interest will convert into common stock at \$0.50 per share.

For extending the maturity date until December 31, 2011, Sendero and Runway will reduce their conversion price to \$0.60 per share.

For extending the maturity date until September 30, 2011, Agua Alta will reduce its conversion price to \$0.75 per share.

The average conversion price of the three remaining notes is \$0.64 per share.

- c) \$225,000 of the Scarborough notes were converted to 507,000 shares on July 29, 2011, subsequent to year-end.
- d) \$170,000 of the Agua Alta and \$75,000 of the Sendero notes were converted into 1,786,374 shares on October 19, 2011.

## Isaac Capital Group

On June 10, 2011, the Group borrowed \$150,000 from Isaac Capital Group (“ICG”) in the form of a convertible note. The loan is for 6 months with interest at 15% per annum. ICG will have the right to convert the Loan at any time into shares at a conversion price of 60% of the volume weighted average sale price on NASDAQ of the shares for the 10 trading days prior to the closing of the loan. There is also a closing fee of 15,000 shares on closing of the Loan. (These shares have not yet been issued).

The maturity dates and interest rates applicable to the Group’s funded indebtedness and third party guarantees are as follows:

| Lender  | Amount outstanding |               | Applicable interest rate   | Status                |
|---|--------------------|---------------|--|-----------------------|
|   | June 30, 2011      | June 30, 2010 |  |                       |
| <b>Film and Production Loans</b>              |                    |               |  |                       |
| Arrowhead Consulting Group                    | \$ -               | \$ 1,788,904  | 19-23% Variable  | Subordinated          |
| Palm Finance Corporation                      | 4,910,052          | 6,575,881     | 18% Fixed  | Forbearance agreement |
| Palm Finance Corporation                      | 3,176,018          | 4,243,835     | 18% Fixed  | Forbearance agreement |
| Blue Rider Finance Inc.                       | 813,742            | 1,599,813     | 22.5% per annum plus 4% of outstanding indebtedness for each 30 days period the indebtedness remains outstanding after December 15, 2008 | Due on demand         |
| 120dB Film Finance LLC                        | 323,000            | 219,000       | No stated interest rate  | Due on demand         |
| Cold Fusion Media Group LLC                   | 582,510            | 920,410       | 10% Fixed  | Due on demand         |
| Parallel Media                                | 1,469,108          | 1,418,846     | No stated interest rate  | Due on demand         |
| Pledged Shares                                | (384,000 )         | -             |  |                       |
| Film and Production Loans                     | \$ 10,890,430      | \$ 16,766,689 |  |                       |
| <b>Corporate Loans</b>                        |                    |               |  |                       |
| Trafalgar Capital Specialized Investment Fund | \$ 490,412         | \$ 1,176,608  | 9% Fixed   | Forbearance agreement |
| Asher Enterprise, Inc.                        | -                  | 150,000       | 8% Fixed   |                       |

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|                     |               |               |           |  |
|---------------------|---------------|---------------|-----------|--|
|                     |               |               |           | Due on March 11, 2011 and March 17, 2011 |
| Lion House          | 263,234       | 207,983       | 30% Fixed | In default                               |
| Scarborough/Runway  | 853,384       | -             | 15% fixed | Due September 30, 2011                   |
| Isaac Capital Group | 148,220       | -             | 15% fixed | Due December 10, 2011                    |
| Corporate Loans     | \$ 1,755,250  | \$ 1,534,591  |           |  |
| Total Loans         | \$ 12,645,680 | \$ 18,301,280 |           |  |

The loan amounts as of June 30, 2011 and 2010, includes accrued interest of \$2,233,994 and \$5,238,407, respectively.

## NOTE 11 - SHAREHOLDERS' EQUITY

The following presents the Company's authorized, issued and outstanding shares, by class as of June 30, 2011 and 2010:

|   | June 30,<br>2011 | June 30,<br>2010 |
|---|------------------|------------------|
| <b>Authorized</b>   |                  |                  |
| 6,000,000, £1 convertible, redeemable preference shares for all periods.                        | 11,337,600       | 11,337,600       |
| 20,527,360 ordinary shares at £ 0.25 par value each for all periods.                            | 9,055,719        | 9,055,719        |
| 20,527,360 deferred shares at £1.00 par value each for all periods                              | 36,222,876       | 36,222,876       |
| 13,184,000 deferred shares at £0.45 par value each for all periods                              | 11,636,594       | 11,636,594       |
|   | 68,252,789       | 68,252,789       |
| <b>Issued and outstanding</b>   |                  |                  |
| £1.00 convertible, redeemable preference shares   | -                | -                |
| 2,643,131 ordinary shares at £.25 par value as of June 30, 2011, 1,495,460 as of June 30, 2010; | \$ 1,121,208     | \$ 641,126       |
| 2,268,120 deferred shares of £1 as of June 30, 2011, 1,495,460 as of June 30, 2010;             | 3,876,745        | 2,564,504        |
| 13,184,000 deferred shares of £0.45 each for all periods.                                       | 11,636,594       | 11,636,594       |
|   | \$ 16,634,547    | \$ 14,842,224    |

**Convertible Redeemable Preferred Shares**

During the year ended March 31, 2005, Seven Arts issued approximately £3,000,000 of convertible redeemable preferred shares to Armadillo Investments Plc ("Armadillo") in return for 3,000,000 ordinary shares from Armadillo, valued at \$5,668,800.

- a) The convertible redeemable preferred shares held by Armadillo were acquired by the Seven Arts Employee Benefit Trust ("EBT") on October 30, 2008 and 2,500,000 of the preferred shares were converted into 2,000,000 of the Seven Arts Pictures Plc ordinary shares on November 20, 2008.
- b) The remaining 500,000 convertible preferred shares owned by the EBT were converted into 400,000 ordinary shares of Seven Arts Pictures Plc on June 30, 2010. As of June 30, 2011 and 2010, there were no convertible redeemable preferred shares outstanding.



The terms attached to the convertible redeemable preferred shares include:

- a. no dividends,
- b. a liquidation preferred,
- c. conversion rights into ordinary shares, and
- d. redemption rights only in the event of certain defaults by Group

#### Ordinary Shares

On May 9, 2011, the shareholders approved a 5:1 reverse split and then the division of the new share into £0.25 ordinary share and £1.00 deferred share. All per share amounts in the financial statements have been retroactively adjusted to the earliest period presented for the effect of this reverse split.

In the year ended June 30, 2011, the Group issued an aggregate of 1,147,671 shares of ordinary stock comprised of:

- a) 342,000 shares issued to consultants in exchange for services rendered
- b) 153,000 shares issued to Trafalgar Capital Specialized Investment Fund pursuant to an amended loan agreement and 100,000 issued to Eden Corporate Finance in part payment of their debt
- c) 53,668 shares issued to Asher Enterprises in exchange for conversion of notes payable in the aggregate amount of \$200,000.
- d) Pledges of stock issued to SAP Inc (23,800 shares) for an insurance policy, New Moon LLC (150,000 shares) pledged against Armadillo's debt, Palm Finance (150,000 shares) and TCA (175,000 shares) pledged against a loan of \$125,000 given to the Company in March 2011 (See NOTE 12)

See NOTE 20 – Subsequent Events, for details of shares issued subsequent to June 30, 2011.

In the year ended June 30, 2010, the Group issued an aggregate of 110,000 shares of ordinary stock comprised of:

- a) 80,000 shares issued to the EBT on conversion of 500,000 convertible preferred shares. The EBT conversion resulted in an addition of \$149,620 to the share capital account and \$1,390,180 to the additional paid in capital account and a reduction of \$1,539,800 in the carrying value of the preferred shares in the capital account.
- b) 2,000 share options were converted to 10,000 ordinary shares by a former employee. As the excess 8,000 ordinary shares were issued in error, a related party (SAP Inc.) has promised to advance and pledge 8,000 of its shares of Seven Arts Pictures Plc to the Group until it can arrange for the cancellation of these shares and replace with the correct shares to be issued and sent to the former employee. As of June 30, 2010, the Group had not received these cancelled shares.
  - c) 20,000 shares were issued to Eden Finance to cover loan, interest and fees in April 2010.

## Deferred Shares

The Group's deferred shares issued prior to March 31, 2007 have essentially no rights for participation with income or assets of the Group other than their existing rights under ordinary share ownership. The Group has the right to purchase back and cancel the deferred shares. These shares were issued when the ordinary stock par value was reduced from £0.50 to £0.05 per share (i.e. for every £0.50 per share held the shareholder received one £0.05 ordinary share and one £0.45 deferred share.). The Group has no current plans to retire this deferred stock. The stock is treated as part of the nominal share capital valued at £0.45 per share.

The second category of deferred shares was issued on May 12, 2011 after the 5:1 reverse split when five ordinary shares with £0.25 par values were combined into one share of £1.25 par value share and then the resulting share subdivided into one ordinary share of £0.25 and one deferred share of £1.00. These shares have essentially no rights for participation with income or assets of the Group other than their existing rights under ordinary share ownership. The Group has the right to purchase back and cancel the deferred shares. The stock is treated as part of the nominal share capital valued at £1.00 per share.

## NOTE 12 - CONVERTIBLE DEBENTURES WITH NO REDEMPTION DATE

|                        | As of<br>June 30,<br>2011 | As of<br>June 30,<br>2010 |
|------------------------|---------------------------|---------------------------|
| Convertible debentures | \$3,432,450               | \$3,432,450               |

During the year ended March 31, 2005, Seven Arts issued £3,000,000, of convertible debt to Langley Park Investment Trust Plc ("Langley") in return for 3,000,000 ordinary shares in Langley valued at approximately \$5,204,000. Langley converted £1,250,000 of its convertible debenture into 1,000,000 ordinary shares in Seven Arts Pictures Plc. on March 15, 2007. The remaining £1,750,000 (\$3,432,450) of convertible debentures are convertible into a maximum of 1,400,000 ordinary shares at 4:1 conversion.

The original Langley agreement stated that the debentures were convertible at 2:1 when the original share price was £0.5 and above, increasing to 4:1 if the original share price was £0.25 or less. After the 5:1 reverse split the conversion parameters became 2:1 at £2.5 and above and 4:1 at £1.25 and below. The Group also agreed to grant Langley options to acquire the number of ordinary shares as is equal to the difference, if a positive amount, between (a) the number of ordinary shares into which the original amount of debt would have been convertible at a conversion price of £0.5, less (b) the aggregate number of the ordinary shares into which the original amount of debt has actually been converted at the date of conversion. The exercise price of the option shall be the fixed conversion price of £0.5. As of June 30, 2011, there were no such options granted.

The Convertible debentures bear no interest, are entitled to a liquidation preferred ahead of ordinary and preferred shareholders, are convertible into ordinary shares. There is no due date or required due date on the Group's Debentures. The Debentures rank junior to all the Group's indebtedness and senior only to its ordinary and preferred shares; accordingly these debentures have accounted for as equity transactions.

## NOTE 13 - DERIVATIVES AND OTHER FINANCIAL INSTRUMENTS

## Financial instruments

The Group's financial instruments comprise cash balances, items such as trade receivables and trade payables that arise directly from its operations, convertible loan notes, convertible redeemable preference shares and loans taken out from banks and other third parties. Financial instruments such as investments in, and advances to, subsidiary undertakings including short-term receivables and payables have been offset in the consolidation.

The Group relies on loans taken out from banks and other third parties to fund its investment in the production of motion pictures and to minimize the liquidity risk that it faces. The strategy in relation to these loans is to minimize the interest rate and to maximize the flexibility of repayment terms. The reliance on loans to provide finance is clear from the significant balances included within loans payables at the period end and the extent to which favorable terms have been achieved on these loans is indicated in the disclosures below.

The main risks arising from the Group's financial instruments are foreign currency risk, interest rate risk, liquidity risk, credit risk and price risk.

## Foreign currency risk

The Group receives distribution income from overseas, normally in US Dollars. Consequently, its trade receivables are largely denominated in US Dollars. It also maintains a significant part of its cash in US Dollars. The Group's exposure to exchange rate fluctuations is currently deemed to be low, since the majority of its liabilities are also denominated in US Dollars. Therefore, the Group does not hedge against this risk.

Transactions in GB Pounds are in the opinion of Management either immaterial or outside the ordinary course of business and therefore there is no policy for mitigation of risks associated with conversion of GBP to USD.

An analysis of the monetary assets of the Group as of June 30, 2011, showing the amount denominated in each currency, is as follows:

|                             | GBP                 | USD                  | Total                |
|-----------------------------|---------------------|----------------------|----------------------|
| Trade receivables           | \$ -                | \$ 431,891           | \$ 431,891           |
| Prepayments                 | 1,369,399           | 231,843              | 1,601,242            |
| <b>Assets</b>               | <b>\$ 1,369,399</b> | <b>\$ 663,734</b>    | <b>\$ 2,033,133</b>  |
| Trade payables              | \$ 1,964,776        | \$ 604,499           | 2,569,275            |
| Accrued liabilities         | 371,051             | 2,011,865            | 2,382,916            |
| Participation and residuals | -                   | 503,187              | 503,187              |
| Corporate loans             | 1,766,158           | -                    | 1,766,158            |
| Film and production loans   | -                   | 10,949,675           | 10,949,675           |
| Deferred income             | -                   | 311,880              | 311,880              |
| Taxes payable               | 366,237             | -                    | 366,237              |
| <b>Liabilities</b>          | <b>\$ 4,468,222</b> | <b>\$ 14,381,106</b> | <b>\$ 18,849,328</b> |



#### Liquidity risk

Management monitors liquidity risk regularly by way of preparing cash flow forecasts and ensuring that adequate loan facilities are in place prior to the commencement of principle photography for any film.

#### Credit risk

The Group has a large number of customers, primarily sub-distributors who are located all over the world. Certain of these customers are large and well-known companies and these are not generally regarded as presenting a credit risk. However, certain of the smaller customers are considered to be a potential credit risk, and the Group manages such risk to the extent possible by maintaining regular contact with those customers who owe the Group money.

#### Economic dependence

During the year ended June 30, 2011, revenue from two major customers approximated \$714,681 and \$149,000, or 26% and 5%, respectively, of film revenues. Accounts receivable due from these two customers approximated \$0 and \$0, respectively, of the total accounts receivable at June 30, 2011.

During the year ended June 30, 2010, revenue from two major customers approximated \$1,020,000 and \$518,000, or 52% and 26%, respectively, of film revenues. Accounts receivable due from these two customers approximated \$212,000 and \$518,000, or 14% and 35%, respectively, of the total accounts receivable at June 30, 2010.

During the year ended June 30, 2011, 100% of fee related revenue in the amount of \$570,029 was generated through SAPLA, all of which has been paid to the Group.

During the year ended June 30, 2010, 100% of fee related revenues in the amount of \$4,442,919 was generated through SAPLA, \$3,288,191 of which has been paid to the Group (see note 2). Overall receivable due from SAPLA (including SAPLOU Equicap) through the related parties accounts was approximately \$2,473,000 at June 30, 2010, and reflected in Due From Related Parties.

There was no supplier in any of the periods reported who accounted for more than 10% of the Company's expenditures during the years ended June 30, 2011 and 2010.

## Price risk

The Group manages the risk of goods and services being obtained at a higher than necessary price by ensuring that all purchases above a certain value are authorized by a Director prior to the purchase order being placed.

Production and corporate loans are included in the Group's balance sheet as financial liabilities. Production loans of \$10,890,430 as of June 30, 2011 are all denominated in US Dollars; corporate loans of \$1,755,250 are denominated in both USD and GBP. The bank overdraft in June 30, 2011 was denominated in Pounds Sterling.

The analysis of notes payable is as follows:

|  | Year ended<br>June 30,<br>2011 | Year ended<br>June 30,<br>2010 |
|--|--------------------------------|--------------------------------|
| Fixed and variable rate - production and corporate loans | \$ 10,826,572                  | \$ 16,663,434                  |
| No stated interest - production loans                    | 1,819,108                      | 1,637,846                      |
| Total financial liabilities                              | \$ 12,645,680                  | \$ 18,301,280                  |

The fixed rate financial liabilities have fixed interest rates for the entire term of each loan. The weighted average interest rate of these fixed rate liabilities on the production loans was 11.0% for the year ended June 30, 2011 and 12.2% for the year ended June 30, 2010.

Those loans where no interest was payable were all loans made to fund the production of motion pictures that were repayable from the proceeds of each motion picture in accordance with a defined payment schedule. The period over which these loans are repayable, therefore, depends on the performance of each motion picture.

The financial assets of the Group are cash balances held on deposit with banks. As of June 30, 2011, the Group had only nominal cash balances. Such deposits earn interest at the relevant bank interest rates, which are generally fixed.

The fair value of all the financial assets and liabilities of the Group are considered to be equal to their stated value due to the short-term nature.

The Group has recorded the fair value of the derivative liabilities at fair value with changes in the value of the derivatives accounted for as gain or loss on derivative liabilities. As described in Note 12, as of June 30, 2011, the Group measured fair value of its derivative liabilities at approximately \$0, using unobservable, Level 3 inputs.

## NOTE 14 – SHARE BASED PAYMENTS

The Group accounts for share based payments in accordance with ASC 718 (“Accounting for Stock Compensation”) using a fair value based method whereby compensation cost is measured at the grant date based on the value of the services received and is recognized over the service period. The Company uses the Black-Scholes pricing model to calculate the fair value of options and warrants issued. In calculating this fair value, there are certain assumptions used such as the expected life of the option, risk-free interest rate, dividend yield, volatility and forfeiture rate. The use of a different estimate for any one of these components could have a material impact on the amount of calculated compensation expense.

The numbers of stock options granted by the Group, by period, are as follows:

|                                    | Year Ended<br>June 30,<br>2011 | Year Ended<br>June 30,<br>2010 |
|------------------------------------|--------------------------------|--------------------------------|
| Outstanding at beginning of period | 43,500                         | 51,500                         |
| Granted                            | 120,000                        | -                              |
| Exercised                          |                                | (2,000 )                       |
| Cancelled or expired               | (27,500 )                      | (6,000 )                       |
| Outstanding at end of period       | 136,000                        | 43,500                         |

120,000 and 0 options were issued during the years ended June 30, 2011 and 2010, respectively.

The following presents the inputs used by the Group in the Black Scholes valuation model for the new options issued in the periods presented:

|                                  | Year Ended<br>June 30,<br>2011 | Year Ended<br>June 30,<br>2010 |
|----------------------------------|--------------------------------|--------------------------------|
| Risk-free interest rate          | 5 %                            | 5 %                            |
| Expected option lives (in years) | 3 years                        | 3 years                        |
| Expected volatility for options  | 207%-238 %                     | 207%-238 %                     |
| Expected dividend yield          | 0 %                            | 0 %                            |
| Forfeiture rate                  | 0 %                            | 0 %                            |

All shares are vested upon the grant date the Group recognized share-based compensation expense of \$ 87,026 and \$0 in the years ended June 30, 2011 and 2010. There was no income tax benefit recognized in the statements of operations for share-based compensation arrangements during any periods presented herein. Under standard applicable UK tax rules, the Group is not entitled to any tax benefit for such share-based compensation arrangements.

The weighted average exercise price of the share options outstanding at June 30, 2011 is \$1.97 per share. The weighted average remaining exercise period of these options is approximately 12 months.

## Employee options

| Range of Exercise Prices | Number of Shares Outstanding | Options Outstanding                                 |  | Options Exercisable          |  |
|--------------------------|------------------------------|---|--|------------------------------|--|
|                          |                              | Weighted Average Remaining Contractual Life (years) | Weighted Average Exercise Price of Outstanding Options | Number of Shares Exercisable | Weighted Average Exercise Price of Exercisable Options |
| \$7.30                   | 4,000                        | 0.17  | 7.30   | 4,000                        | 7.30   |
| \$7.70                   | 12,000                       | 0.35  | 7.70   | 12,000                       | 7.70   |

## Non-employee options

| Range of Exercise Prices | Number of Shares Outstanding | Options Outstanding                                 |  | Options Exercisable          |  |
|--------------------------|------------------------------|---|--|------------------------------|--|
|                          |                              | Weighted Average Remaining Contractual Life (years) | Weighted Average Exercise Price of Outstanding Options | Number of Shares Exercisable | Weighted Average Exercise Price of Exercisable Options |
| \$2.00                   | 20,000                       | 1.6   | \$2.00   | 20,000                       | \$2.00   |
| \$1.00                   | 100,000                      | 2.3   | \$1.00   | 100,000                      | \$1.00   |

## NOTE 15 – RELATED PARTY TRANSACTIONS

## Employment Agreement

The Group engaged Kate Hoffman as an employee and director, who is the daughter of Peter Hoffman, the Chief Executive Officer. The Group has an employment agreement with Kate Hoffman pursuant to which she will act as Chief Operating Officer ad infinitum at a current salary of £52,000 (\$85,000) per year plus bonuses and expenses. Ms. Hoffman's contract contains a non-compete clause whereby she is excluded from competing against the Group for 6 months following the date of her termination. She currently does not have any share options or shares in the Group.



#### Affiliated and Related Party Agreements

Upon acquisition of control of the Group by Seven Arts Pictures Inc. ("SAP Inc.") in September 2004, Seven Arts Pictures Plc. entered into an agreement with Seven Arts Pictures Inc. under which Seven Arts Pictures Inc. provided the services of Peter Hoffman for the amount of his contracted salary as well as the direct costs of the Los Angeles office and staff of Seven Arts Pictures Inc. SAP Inc. is a related party by virtue of it being majority owned by Peter Hoffman, the Group's Chief Executive Officer and Director, and his wife, Susan Hoffman.

Certain affiliates controlled by Mr. Hoffman are entitled to be reimbursed by the Group for general overhead incurred by each to conduct business for the Group. Amounts are approved by the Group and then to be reimbursed for certain third party costs on motion pictures controlled by the Group and to be indemnified for loss costs or damages arising from the conduct of the Group's business if approved by the Group. The Group has the right to control through management all material decisions of all affiliates controlled by Mr. Hoffman to the extent such decisions have any material effect on the Group's business or results of operations.

Peter Hoffman controls several companies that are not part of the Group but from which it obtains or transfers distribution rights or other assets related to the business and which control production of the motion pictures. The agreements with Mr. Hoffman, and the companies controlled by him; provide that all revenues related to the Group's business payable to Mr. Hoffman or any of these related party companies is due to the Group, except Mr. Hoffman's salary, bonus and stock ownership.

Pursuant to an inter Group agreement, SAP Inc. also, from time to time, holds ownership of limited liability corporations in the United States, with all distribution rights and profits thereof being due to SAFE Ltd. In addition, they also provide other services for PLC and SAFE Ltd. At no fee other than Mr. Hoffman's salary and the direct third party costs of the Los Angeles office. These other services are any reasonable requests of the management of the Group including accounting services, audits of distribution statements, collection of accounts receivable, supervision of production of motion pictures and similar day-to-day aspects of the Group's business.

SAP Inc. has, from time to time, made non-interest bearing advances to the Group and SAFE Ltd, when the Group has not been able to collect amounts due from third party receivables in time to meet payments required to creditors. Any such advances that have been made by SAP. Inc. have been made solely for working capital purposes.

Pursuant to the inter Group agreements, the Group earned \$551,672 from distribution of the Group's motion pictures during the year ended June 30, 2011. The Group is obligated to pay these funds to SAPLA which is a Louisiana limited liability company controlled by SAP Inc. SAP Inc. would then be obligated to return the funds to the Group. These obligations have been offset in the Group's books of account and the Group has recorded the amounts earned as described above.

The Group has from time to time made and received advances from and to Seven Arts Pictures Inc., Seven Arts Future Flow I LLC and various Louisiana limited liability companies referred to above, where the advances from and to these related parties do not bear interest. The balances of these combined accounts as of June 30, 2011 were \$2,725,974 and \$3,021,184 on June 30, 2010.

## Apollo Media

Together with SAP Inc, the Group entered into a settlement agreement, dated September 30, 2006, with ApolloMedia GmbH & Co. Film produktion KG (“ApolloMedia”) related to a dispute regarding amounts ultimately payable to ApolloMedia from distribution of the motion picture Stander and one of our subsidiaries’ assumption of indebtedness of approximately \$2,000,000 related to Stander. The Settlement Agreement fully releases the Group from any liability to ApolloMedia in exchange for a payment of \$1,800,000 to be made by SAP Inc (of which \$175,000 has been paid). In connection with the SAP Inc’s payment obligation of the settlement amount to ApolloMedia, the Group issued 700,000 ordinary shares to SAP Inc. which SAP Inc immediately pledged to ApolloMedia to secure SAP Inc’s obligations under the settlement agreement. SAP Inc has agreed that it will (1) return to the Group all ordinary shares in excess of 400,000 not necessary to satisfy SAP Inc’s obligations to ApolloMedia and (2) deliver to the Group from SAP Inc’s ordinary shares, any ordinary shares in excess of 400,000 in fact sold by SAP Inc to satisfy the indebtedness to ApolloMedia under the settlement agreement. The shares pledged to ApolloMedia will be sold by Apollo as necessary for ApolloMedia to derive net proceeds of \$1,625,000, (\$1,800,000 less \$175,000) and any pledged shares remaining after such sale will be returned to the Group.

## Relationship with Seven Arts Pictures Louisiana LLC (“SAPLA”)

The Group license distribution rights to pictures controlled by them to its affiliate, SAPLA which perform distribution services for their motion pictures. All fees payable to SAPLA are subject to the agreements with Mr. Hoffman and his affiliates described above.

The Company entered into a distribution agreement with SAPLA (subsequently assigned by SAPLA to Seven Arts Pictures Louisiana (Equicap) LLC (“SAPLA Equicap”)) pursuant to which the Group granted SAPLA the right to distribute motion pictures in return for a distribution fee of 20% of the revenues generated from these films, SAPLA and SAPLA Equicap are obligated under the related party agreements described above to pay and has permitted the Group to retain 100% of all such distribution fees.

SAPLA entered into a Credit Agreement with Advantage Capital Community Development Fund LLC dated October 11, 2007 for the acquisition and improvement of a production and post-production facility located at 807 Esplanade Avenue in New Orleans, Louisiana for aggregate principal advances of up to \$3,700,000. This agreement was guaranteed by the Group. Approximately \$3,700,000 has been drawn under the terms of this Credit Agreement, as of June 30, 2011 and 2010.

The Group has entered into a new financing agreement with Palm Finance in November 2010 to refinance the existing indebtedness secured by our production and post-production facility in New Orleans, Louisiana under which Palm has acquired the existing credit facility of \$3,700,000 plus accrued interest of our affiliate SAPLA for \$1,000,000 and agreed to advance an additional \$1,800,000 to complete renovation and construction of this facility. Palm’s advance and interest at the rate of 15% per annum are due and payable within five years and are secured by the property at 807 Esplanade Avenue in New Orleans (“Property”) and Louisiana film infrastructure and historical rehabilitation credits, as well as Federal historical rehabilitation credits (“Credits”) associated with the Property. As part of this agreement the Group has entered into an agreement with Palm extending the due date of the loans on American Summer, Autopsy and Nine Miles Down to December 31, 2011.

Upon commencement of business of SAPLA’s production and post-production facility in New Orleans, Louisiana, SAPLA and an affiliate, Seven Arts Filmed Entertainment LLC (“SAFE LA”) will be the lessee of those facilities and under the related party agreement all profits of SAFE LA if any will be returned to the Group under the agreements with Mr. Hoffman and his affiliates.



#### Investigation into Claim for Tax Credits (SAPLA)

The US Attorney in New Orleans is investigating claims for Louisiana film infrastructure tax credits including such tax credits to be claimed by an affiliate of the Group, Seven Arts Pictures Louisiana LLC. This investigation appears to include investigation as to whether certain expenses claimed by this affiliate were improper or fraudulent. All such claimed expenses were audited by independent auditors and reviewed by counsel. None of these expenses or credits have been included in the Group's financial statements for any period. Management believes that this investigation will have no material adverse effect on the Group's operations or the total tax credits to be received by the Group's affiliates, but could result in charges against current or former employees of this affiliate based on prior audits, including Mr. Hoffman.

#### Loan to Gone to Hell from Palm Finance

Together with SAP Inc, the Group guaranteed a \$4,000,000 loan on December 17, 2007 between Palm Finance Corporation ("Palm") and Gone To Hell Ltd., a company controlled by the Chief Operating Officer and Director Kate Hoffman, in exchange for the distribution rights to the movie, Nine Miles Down. The loan was made exclusively to finance the motion picture Nine Miles Down and is secured by the distribution rights to that motion picture. The loan carries an annual rate of interest of 15% and became due on June 30, 2009. The Group has entered into a forbearance agreement with Palm in extending the due date of this loan to December 31, 2011.

#### Loan from Cold Fusion

The Group entered into a loan and security agreement dated January 15, 2009 for \$750,000, together with SAP Inc. and certain limited liability companies controlled by SAP Inc. in connection with the production of the motion picture Night of the Demons ("NOTD"). The Group guaranteed the loan in exchange for the distribution rights to the picture. The loan was made to the Group to finance NOTD and is secured by the distribution rights to NOTD. The loan bears interest of ten percent (10%) per annum. The loan became due on March 31, 2010 and is being repaid from distribution revenues of NOTD. At June 30, 2011, the balance due to Cold Fusion amounted to \$582,510 including unpaid accrued interest.

#### Employee Benefit Trust

The Group engaged Smith and Williams Trustees (Jersey) Limited to set up an Employee Benefit Trust ("EBT") in December, 2008. The Trust is a significant shareholder of the Group and controlled by the Trustees. The EBT entered into an agreement to purchase the 3,000,000 convertible preferred shares held by Armadillo Investment Trust ("Armadillo") for £1,500,000, to be paid in three equal installments of £500,000, and the return of the 1,600,000 ordinary shares in Armadillo owned by the Group, valued at £800,000 for an aggregate purchase price of £2,300,000. The agreed upon purchase price was to be loaned to the EBT by the Group at a nominal interest rate and, to date, the Group has advanced £500,000 as the first of three equal installments, together with the 1,600,000 ordinary shares of Armadillo, valued at £800,000 in the Group's books, to the EBT which has paid them over to Armadillo. The Group has guaranteed the EBT's remaining debt of £1,000,000 representing the second and third installments, but has not yet advanced these amounts. The EBT has repaid £582,604 (\$1,039,946) of the £1,300,000 in the year ended June 30, 2011 by selling ordinary shares owned by the EBT to creditors of the Group. The Group charged interest of \$44,822 to the EBT during the year ended June 30, 2011. The total balance due from the EBT to the Group as at June 30, 2011 was \$1,237,417.

## NOTE 16 – COMMITMENTS AND CONTINGENCIES

### Acquisition of Big Jake Music

On September 29, 2011, the Company entered into a definitive agreement to acquire all of the capital stock of Big Jake Music ("BJM"), a newly formed record and multi-media entertainment company, for \$5,000,000 of convertible preferred stock, convertible into common stock at a premium to the market price at closing, and which is subject to restricted holding periods. BJM will also release soundtracks of Seven Arts films, including Night of the Demons (a film released in October 2010) and The Pool Boys (a film released in October 2011).

### Creditors Liquidation of SAP Plc.

PLC was placed into compulsory liquidation on November 8, 2011 by the English Companies Court. The Company's CEO, Mr. Peter Hoffman, as a director of PLC had sought an administration order but this request was denied by the Courts as a result of inter alia the opposition of Parallel Pictures LLC ('Parallel'). The creditors are likely to be invited to appoint a licensed insolvency practitioner as liquidator. The role of a liquidator is to realize a company's assets for the benefit of the creditors and shareholders. Mr. Hoffman expects that the liquidator and PLC will pursue its substantial claims against Parallel and its defenses to Parallel's claims. Parallel has claimed in the proceedings in England and the United States that the Asset Transfer Agreement between the Company and PLC was 'fraudulent' and may seek additional compensation or guarantees from Company. Management believes that the Asset Transfer Agreement is a valid agreement for value and not subject to attack and that Parallel will not prevail in its claims. Management believes it has the support of its creditors to resist these claims by Parallel which are disputed by the Company and as a result Parallel will not obtain any relief from the courts on this issue.

### 807 Esplanade Guarantee

Seven Arts Pictures Louisiana LLC, a related party of the Company, entered into a Credit Agreement with Advantage Capital Community Development Fund LLC dated October 11, 2007, for the acquisition and improvement of a production and post-production facility located at 807 Esplanade Avenue in New Orleans, Louisiana for aggregate principal advances of up to \$3,700,000. This agreement was guaranteed by the Company's predecessor. Approximately \$3,700,000 has been drawn under the terms of this Credit Agreement, as of June 30, 2011. The Company has also guaranteed this amount.

There is a \$1,000,000 guarantee of a note due to Armadillo by the Employee Benefit Trust resulting from the purchase back of the Seven Arts preferred shares from Armadillo.

### Fireworks Litigation

The Group prevailed in a motion for summary adjudication on February 10, 2011 in an action against CanWest Entertainment and two of its affiliates ("CanWest") confirming the Group's ownership of five motion pictures "Rules of Engagement", "An American Rhapsody," "Who Is Cletis Tout," "Onegin," and "The Believer", (the "Copyrights"). The Group has filed an action in England against Content Media Corporation ("Content") and Paramount Picture Corp. ("Paramount") to recover the Copyrights and substantial damages for the use of the copyrighted works after their purported acquisition from CanWest. The Group has also filed suits against Content and Paramount in the United States for collateral damage for copyright infringement against Paramount for use of copyright. The Group may incur up to \$200,000 in legal expenses to pursue this claim but expects to recover those fees from Content.



#### Jones Film

The Group, its subsidiary Seven Arts Filmed Entertainment Limited, and a related party, SAP Inc, were the subject of an arbitration award of approximately \$900,000 against them for legal fees and interest thereon relating to an ongoing dispute regarding a participation in the motion picture entitled 9 ½ Weeks II, even though the arbitration found no additional sums due to the complaining party, and potential loss of further distribution rights in this motion picture. The Federal District Court enforced this arbitration award, and the Group is seeking relief from that decision. The Group has accrued for the liability in the amount of \$800,000 including approximately \$100,000 of accrued interest as of June 30, 2011. The remaining interest, costs and fees have been guaranteed by SAP Inc., a related party.

#### Arrowhead Target Fund

Seven Arts Future Flow I (“SFF”), a limited liability Group owned by SAP Inc., one of the Group’s controlling shareholders and a Group controlled by Mr. Hoffman, obtained financing from the Arrowhead Target Fund, Ltd. (“Arrowhead”) of approximately \$8,300,000 (the “Arrowhead Loan”). The Group secured the Arrowhead Loan with liens on 12 motion pictures that generated revenues of \$820,026 in the year ended June 30, 2009, \$2,739,800 in the year ended March 31, 2008. The Group’s only liability is to repay the Arrowhead Loan from the proceeds of the film assets pledged against the Arrowhead Loan. The Group is not required to repay the Arrowhead Loan from any of its other assets or revenues.

The Arrowhead Loan became due in February 2009 and SFF has not paid the outstanding principle and interest due. Arrowhead has the right to foreclose on the pledged film assets, but has not done so at the present time. SFF has received a default notice to this effect and as a result Arrowhead is now collecting directly all sums receivable by the Group with respect to these motion pictures, and has appointed a new servicing agent for these motion pictures with the result that the Group no longer controls the licensing of these motion pictures. Failure to repay or refinance the Arrowhead Loan could result in a material disposition of assets through the loss of the Group’s rights to the twelve motion pictures and related loss of revenues in amounts that are difficult to predict.

As a result of the foregoing, the Group has removed all assets accounts relating to the twelve motion pictures pledged to Arrowhead and has removed the corresponding limited recourse indebtedness from the Group’s consolidated balance sheet at fiscal year ended June 30, 2009, due to the fact that the loan was a limited recourse loan and the Group had no further obligations to Arrowhead beyond the pledged film assets.

Arrowhead filed an action on September 22, 2010 which seeks recovery from the Group of the monies which the Group has retained under its interpretation of the relevant agreements with Arrowhead. In addition, Arrowhead makes substantial additional claims against the Group, Mr. Hoffman and Seven Arts Pictures Inc. regarding claimed breaches of the terms of the operative agreements, including failure to properly account, failure to turn over materials, failure to remit monies collected, and similar matters. The claims against the Group for these breaches of warranties for damages are \$8,300,000 although Arrowhead states no basis for this amount.

The Group had moved to dismiss the action against all defendants other than Seven Arts Future Flows I LLC, which is not part of the Group. On August 9, 2011, the New York Supreme Court granted the Group’s motion and dismissed all defendants except Seven Arts Filmed Entertainment Limited in its capacity as a collateral agent, which is not a material element of Arrowhead claim. The Group continues to believe that Arrowhead’s claims against the Group are without substantial merit.

#### Arrowhead Capital Partners – AGC Loan

The Group and several affiliates were named as defendants in an action by Arrowhead Capital Partners Ltd filed in the Supreme Court of New York County of New York State purportedly served on May 24, 2010, seeking to collect \$1,000,000 plus interest (the “ACG Loan”) due to Arrowhead Consulting group LLC (“ACG”) as well as foreclosure on the collateral granted as part of the Cheyne Loan described above in NOTE 12 under “Production Loans”. The ACG Loan is fully subordinated to repayment of the Cheyne Loan, which has not been repaid, and a subsidiary of the Group has been assigned all Cheyne’s rights under the subordination provision of the Cheyne Loan. As a result Management does not believe that ACG has the right to maintain this action to collect any monies or to foreclose on any collateral pursuant to the Cheyne Loan. The Group intends to vigorously defend against this action and has filed a motion for summary judgement to dismiss this action.

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#### Silverback – Hungarian co-producer

The Group has obtained a final judgment from the Queen’s Bench in England for approximately \$300,000 erroneously converted to fees by a Hungarian co-producer on the motion picture Nine Miles Down. The Group is seeking to collect these fees back through enforcement by Hungarian courts and currently a bailiff has been appointed to collect the monies due in Hungary. The incorrectly appropriated fees have been included in the film asset in prior years. Capitalized film costs will be reduced upon collection of these fees.

#### Stonewood/Nine Miles Down

A settlement agreement for \$250,000 has been reached with the liquidators of Gone to Hell (“GTH”) the production company for Nine Miles Down. The main beneficiaries of the GTH liquidation are Stonewood; owned by the director of GTH and SAP INC for an action it took against the liquidator for interfering in the free distribution of the film. The debt to the liquidation is fully insured but only to the amount that is not payable back to SAP INC and Stonewood as they are the insured parties. The Group has guaranteed the legal costs of this action to make sure it releases the distribution rights to the movie. The Group has accounted for the legal expenses incurred related to this litigation by capitalizing them into film assets in the value of \$200,000 as of June 30, 2011, due to the fact that these are direct expenditures to this particular film.

#### Zeus VAT

The Group believes that the accrual of the VAT input refund or output VAT tax with respect to the Zeus transaction is highly uncertain. Her Majesty’s Customs and Revenue (“HMRC”) raised issues regarding the Zeus transaction as early as May, 2008, and has made no determination regarding any of the inputs or outputs of VAT with respect to the Zeus transaction through today. The situation is still unresolved in that HMRC has not made a VAT refund to the 17 companies formed by investors in the Zeus transaction (“SAFCO’s”) of the output VAT tax charged by Seven Arts on the supplies made for the SAFCO’s and declared on the Group’s VAT return filed in 2008 and in that HMRC has taken no steps to enforce the collection of the output VAT tax as declared by the Group, as an internal “hold” has been placed on collection by HMRC. Until and unless this interest is lifted, HMRC will take no action to enforce the collection of the VAT output tax declared by the Group. The amount of VAT at issue is approximately £23,000,000 (\$35,000,000) which would be both the amount owed by the Group to HMRC and the amount due to the Group from the SAFCO’s as their refund from HMRC. The collection department of HMRC has stopped the collection of the VAT due from the Group, and to date no notices of interest have been received. The Group does not expect any penalties or fees will result from the VAT related to the Zeus transaction, accordingly no accrual of interest or penalties have been accrued as of June 30, 2011.

The Group acquired the SAFCO’s as part of the Zeus transaction described above in May, 2009. The SAFCO’s are not consolidated into the Group as the Group still does not have control of the bank accounts and the accounting records. The Group has instructed counsel to liquidate the SAFCO’s under the applicable laws of the United Kingdom.

One of the Group’s affiliates filed an action against Zeus Partners Limited and two of its executives for indemnity in relation to Value Added Tax due with respect to the Zeus Transaction. The purpose of this action is to protect the Group’s rights with respect to any potential liability to the Group with respect to Value Added Tax arising out of the Zeus Transaction.

#### Investigation into Claim for Tax Credits (SAPLA)

The US Attorney in New Orleans is investigating claims for Louisiana film infrastructure tax credits including such tax credits to be claimed by an affiliate of the Group, Seven Arts Pictures Louisiana LLC. This investigation appears

to include investigation as to whether certain expenses claimed by this affiliate were improper or fraudulent. All such claimed expenses were audited by independent auditors in Louisiana and reviewed by counsel. None of these expenses or credits have been included in the Group's financial statements for any period. Management believes that this investigation will have no material adverse effect on the Group's operations or the total tax credits to be received by the Group's affiliates, but could result in charges against current or former employees of this affiliate based on prior audits, including Mr. Hoffman.

#### Director's Service Contracts

SAP Inc. has an employment agreement with Peter Hoffman pursuant to which he will act as the Group's Chief Executive Officer ("CEO") until December 31, 2013. Upon acquisition of control of Group, it entered into a contract with SAP Inc. to secure Mr. Hoffman's services solely to the Group as CEO. In connection with that employment agreement, Mr. Hoffman has been granted:

- the right to sole responsibility for creative and business decisions regarding motion pictures we develop and produce,
- a right of first refusal to produce remakes, sequels or prequels of motion pictures produced by Mr. Hoffman and acquired by the Group or any motion picture produced by the Group during his employment,
  - an annual salary of \$500,000 per year plus bonuses, expenses and a signing option and
- a right upon termination without cause to a lump sum payment of approximately \$1,500,000, an assignment of all projects in development during the term of his employment and any amounts due upon such compensation as an excise tax.

The Group has an employment agreement with Kate Hoffman pursuant to which she will act as Chief Operating Officer ad infinitum at a salary of \$85,000 (£52,000) per year plus bonuses and expenses. Ms. Hoffman's contract contains a "non-compete" clause pursuant to which she will be excluded from competing against the Group for 6 months following the date of her termination.

The Group has an employment agreement with Elaine New pursuant to which she will act as an executive director and Chief Financial Officer ad infinitum at a salary of \$225,000 (£150,000) per year plus bonuses and expenses. Ms. New's contract contains a "non-compete" clause pursuant to which she will be excluded from competing against the Group for 6 months following the date of her termination.

All of the employment agreements grant us a right to injunctive relief if the respective employee breaches the agreement. With the exception of Ms. Hoffman's and Ms. New's agreements, the employment agreements do not contain "non-compete" clauses.

#### Parallel Action

On June 28, 2011, PLC filed an action in the High Court of England against Parallel Media LLC ("Parallel") to collect sums due to PLC with respect to acquisition of distribution rights in Russia to four motion pictures and to confirm Parallel's obligations under both a signed and unsigned investment agreement with respect to the motion picture project Winter Queen. On the same day Parallel filed a petition to wind up and liquidate PLC in the Companies Courts of England based on its claim of repayment of \$1,000,000 of investment made by Parallel in Winter Queen. On September 19, 2011, Parallel filed a new action against PLC and SAE in the Superior Court of California, asserting the same claims as in the winding up petition and seeking to enjoin the proposed administration proceedings in England. A request for a preliminary injunction was denied by the Superior Court.

#### HMRC Investigation

On July 19, 2011 Officers of Her Majesty's Revenue & Customs ("HMRC") attended the offices of PLC in London. Documents were retained appertaining to arrangements involving the subscription for shares in a number of companies which had lost value, resulting in subscribers making claims to tax relief.

PLC's participation in these transactions was limited to the transfer of rights to certain motion pictures to the investors in return for their investments in the production and release costs of those pictures and making available the provision of loans to fund a portion of those investments. PLC received no tax benefits from the transactions, which were made on arms-length terms. PLC believes that it is not a subject of the HMRC investigation.

In connection with the transactions, PLC did not make any representations or warranties to any party, including the investors, regarding any potential tax benefits related to the transactions. Prior to the closing of the transactions the investors obtained and made available to the Company, an opinion of prominent Queen's counsel, specializing in United Kingdom tax laws, that the transactions were permitted and acceptable under the terms of the applicable United Kingdom revenue laws. PLC remains confident that the transactions were permitted and acceptable under the terms of the applicable United Kingdom revenue laws.

#### Asset Transfer Agreement

On June 11, 2010, Seven Arts Entertainment, Inc. ("SAE"), a Nevada Corporation, was formed and became a 100% owned subsidiary of Seven Arts Pictures Plc. The Company entered into an Asset Transfer Agreement, as amended on January 27, 2011 and again on August 31, 2011, to transfer all of the assets with a cost basis from PLC to SAE, in exchange for assumption by SAE of certain indebtedness and for one share of common stock of SAE for each ordinary share of PLC which have been distributed to shareholders. Additionally, 2,000,000 shares of SAE were issued to PLC in order to satisfy any remaining obligations. This transfer was approved by the PLC shareholders at an Extraordinary General Meeting on June 11, 2010. The purpose of this transfer was to eliminate our status as a foreign private issuer and to assume compliance with all obligations of a domestic issuer under all applicable state and Federal securities laws. Management's intention in executing this transaction was to redomicile the business with no change in the economic interests of the shareholders.

Effective at the opening of trading on September 1, 2011, Seven Arts Entertainment Inc. ("Seven Arts" or "SAE") was substituted for the NASDAQ listing of Seven Arts Pictures PLC (the "Company"). On that date, each of the Company's ordinary shares was exchanged for one share of common stock of SAE, which commenced trading on NASDAQ as the successor to the Company's NASDAQ listing. SAE's new CUSIP number is 81783N102 and its trading symbol will remain SAPX.

#### Guarantees and Pledges

##### Guarantee of the Advantage Capital Loan

SAPLA, a related party of the Group, entered into a Credit Agreement with Advantage Capital Community Development Fund LLC dated October 11, 2007 for the acquisition and improvement of a production and post-production facility located at 807 Esplanade Avenue in New Orleans, Louisiana for aggregate principal advances of up to \$3,700,000. This agreement was guaranteed by the Group. Approximately \$3,700,000 has been drawn under the terms of this Credit Agreement, as of June 30, 2011. The Group has guaranteed this amount.



Guarantee of the £1,000,000 due to Armadillo by the EBT

As discussed in NOTE 1, PLC is a guarantor on the £1,000,000 due to Armadillo by the EBT.

#### NOTE 17 – OPERATING LEASE COMMITMENTS

During the years ended June 30, 2011 and 2010, the Group had no operating lease commitments. Both office facilities are operating under month to month agreements. Rent expense is approximately \$4,500 a month for the Los Angeles office and \$6,500 a month in London.

#### NOTE 18 – FAIR VALUE OF FINANCIAL INSTRUMENTS

Cash, accounts receivable, accounts payable and other accrued expenses and other current assets and liabilities are carried at amounts which reasonably approximate their fair values because of the relatively short maturity of those instruments.

ASC 820, “Fair Value Measurements and Disclosures”, establishes a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under ASC 820 are described as follows:

Level 1 - Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Company has the ability to access.

Level 2 - Inputs to the valuation methodology include:

- quoted prices for similar assets or liabilities in active markets;
- quoted prices for identical or similar assets or liabilities in inactive markets;
- inputs other than quoted prices that are observable for the asset or liability;
- inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3 - Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset or liability’s fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

The preceding method described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Company believes its valuation method is appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the

reporting date. As of June 30, 2011 and 2010, all of the Company's assets and liabilities were considered current and due to the short maturity the carrying amounts are considered to approximate fair value.

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#### NOTE 19 – RECENT ACCOUNTING PRONOUNCEMENTS

In May 2011, the FASB issued guidance intended to achieve common fair value measurements and related disclosures between U.S. GAAP and international accounting standards. The amendments primarily clarify existing fair value guidance and are not intended to change the application of existing fair value measurement guidance. However, the amendments include certain instances where a particular principle or requirement for measuring fair value or disclosing information about fair value measurements has changed. This guidance is effective for the periods beginning after December 15, 2011, and early application is prohibited. The Company will adopt these amendments on January 1, 2012; however, the requirements are not expected to have a material effect.

#### NOTE 20 – SUBSEQUENT EVENTS

On June 11, 2010, Seven Arts Entertainment, Inc. (“SAE”), a Nevada Corporation, was formed and became a 100% owned subsidiary of Seven Arts Pictures Plc. The Company entered into an Asset Transfer Agreement, as amended on January 27, 2011 and again on August 31, 2011, to transfer all of the assets with a cost basis from PLC to SAE, in exchange for assumption by SAE of certain indebtedness and for one share of common stock of SAE for each ordinary share of PLC which have been distributed to shareholders. Additionally, 2,000,000 shares of SAE were issued to PLC in order to satisfy any remaining obligations. This transfer was approved by the PLC shareholders at an Extraordinary General Meeting on June 11, 2010. The purpose of this transfer was to eliminate our status as a foreign private issuer and to assume compliance with all obligations of a domestic issuer under all applicable state and Federal securities laws. Management’s intention in executing this transaction was to redomicile the business with no change in the economic interests of the shareholders.

As of January 27, 2011, net assets with a book value totaling approximately \$7,200,000 plus convertible debentures with no redemption date, which are accounted for as equity, were transferred to SAE in accordance with the asset transfer agreement.

On August 31, 2011, NASDAQ approved the substitution of one share of SAE, Inc. stock for the Company's NASDAQ listing, effective at the opening of trading on September 1, 2011. On that date, each of the Company's ordinary shares were exchanged for one share of common stock of SAE, and commenced trading on NASDAQ as the successor to the Company's NASDAQ listing. This transaction was approved by the Company’s shareholders at the Company’s Extraordinary General Meeting on June 11, 2010.

SAE’s authorized capital consists of 50,000,000 shares of common stock, \$.01 par value per share, of which the board of directors has allocated 25,000,000 shares as common stock. As of September 1, 2011, there were 6,476,344 shares of common stock outstanding. Each outstanding share of common stock entitles the holder thereof to one vote per share on matters submitted to a vote of stockholders.

SAE will be a United States issuer and commenced regular quarterly reporting for the first quarter ended September 30, 2011.



#### Issuance of New Shares or Options

Subsequent to June 30, 2011, an aggregate of 13,832,280 ordinary shares were issued, and accordingly there were 16,475,411 shares of the Group's issued and outstanding ordinary shares as of November 30, 2011.

The shares issued subsequent to June 30, 2011 include 10,000 shares issued to consultants in exchange for services rendered. \$400,000 restricted shares were sold for cash.

Certain debt securities were partially converted into 11,422,000 ordinary shares at an average per-share price of \$0.42.

The issuance of the converted debt was made pursuant to the exemption from registration provided pursuant to Section 4(2) of the Securities Act. Management believed that such exemption was available because (i) no advertising or general solicitation was employed in offering the debt securities, (ii) the offering and sale thereof were made solely to an accredited investor, and (iii) transfer of the debt securities was restricted in accordance with the requirements of such Act. More than one year passed between the issuance of the converted debt and its conversion into ordinary shares. In accordance therewith, the resale of such shares was exempt from the registration thereof pursuant to the exemption provided by Rule 144.

The debt that was converted to equity included \$2,750,000 from Palm Finance, \$350,000 from 120dB Film and \$725,000 of convertible debt, including \$500,000 from Whatley and \$225,000 from Eden.

Palm Finance reinvested \$1,250,000 back into SAE, Inc. (PLC's successor entity) by acquiring 125,125 shares of Series A (\$10 par) preferred stock in November 2011.

On October 14, 2011, the Board of Directors of SAE Inc. were each issued 50,000 options at the market price of \$0.44 a share.

On November 21, 2011 SAE, Inc. issued 2,000,000 shares to PLC in accordance with the asset transfer agreement approved by shareholders on June 11, 2011.

#### Letter of Intent Regarding David Michery

On November 7, 2011, the Company signed a letter of intent to acquire the music assets of David Michery for 10,000,000 shares of preferred stock subject to due diligence and Board approval.

#### Creditors Liquidation of SAP Plc.

PLC was placed into compulsory liquidation on November 8, 2011, by the English Companies Court. PLC's CEO, Mr. Peter Hoffman, as a director of PLC had sought an administration order but this request was denied by the Courts as a result of inter alia the opposition of Parallel Pictures LLC ('Parallel'). The creditors are likely to be invited to appoint a licensed insolvency practitioner as liquidator. The role of a liquidator is to realize a company's assets for the benefit of the creditors and shareholders. Mr. Hoffman expects that the liquidator and PLC will pursue its substantial claims against Parallel and its defenses to Parallel's claims. Parallel has claimed in the proceedings in England and the United States that the Asset Transfer Agreement between SAE and PLC was 'fraudulent' and may seek additional compensation or guarantees SAE Inc. Management believes that the Asset Transfer Agreement is a valid agreement for value and not subject to attack and that Parallel will not prevail in its claims. Management believes it has the support of its creditors to resist these claims by Parallel which are disputed by SAE Inc. and PLC and as a result Parallel will not obtain any relief from the courts on this issue.

Certain indebtedness of PLC remained with PLC under the asset transfer agreement and will be subject to liquidation or payment in these liquidation proceedings. PLC has been issued 2,000,000 shares of common stock of the Company in order to satisfy these obligations.

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#### Issue of Promissory Note to RBSM LLP

On September 4, 2011, SAE Inc. issued a promissory note to RBSM LLP (“RBSM”), the Group’s prior registered accounting firm. The note guarantees that SAE Inc. will pay RBSM \$150,000 on or before the six month anniversary of the note. The note bears interest of 7% per annum but this will be waived if the note is paid off within the six months. On maturity of the note if the principal and interest have not been paid in full then RBSM can convert the note into freely trading common shares with an issue price of 75% of the weighted average closing bid price per common share during the 10 days preceding the maturity date. In accordance therewith, the resale of such shares will be exempt from the registration thereof pursuant to the exemption provided by Rule 144.

#### Arrowhead Action

The Arrowhead Target Fund filed an action on September 22, 2010 which seeks recovery from the Group for amounts which the Group has retained under its interpretation of the relevant agreements with Arrowhead. In addition, Arrowhead makes substantial additional claims against the Group, Mr. Hoffman and Seven Arts Pictures Inc. regarding claimed breaches of the terms of the operative agreements, including failure to properly account, failure to turn over materials, failure to remit monies collected, and similar matters. The claims against the Group for these breaches of warranties for damages are \$8,300,000 although Arrowhead states no basis for this amount.

The Group had moved to dismiss the action against all defendants other than Seven Arts Future Flows I LLC, which is not part of the Group. On August 9, 2011, the New York Supreme Court granted the Group’s motion and dismissed all defendants except Seven Arts Filmed Entertainment Limited in its capacity as a collateral agent, which is not a material element of Arrowhead claim. The Group continues to believe that Arrowhead’s claims against the Group are without substantial merit, and nothing has been accrued in the financial statements related to this claim.

#### HMRC Investigation

On July 19, 2011 Officers of Her Majesty’s Revenue & Customs (“HMRC”) attended the offices of Seven Arts Pictures plc (the “Company”) in London. Documents were retained appertaining to arrangements involving the subscription for shares in a number of companies which had lost value, resulting in subscribers making claims to tax relief.

The Company’s participation in these transactions was limited to the Company’s transfer of rights to certain motion pictures to the investors in return for their investments in the production and release costs of those pictures and making available the provision of loans to fund a portion of those investments. The Company received no tax benefits from the transactions, which were made on arms-length terms. The Company believes that it is not a subject of the HMRC investigation.

In connection with the transactions, the Company did not make any representations or warranties to any party, including the investors, regarding any potential tax benefits related to the transactions. Prior to the closing of the transactions the investors obtained and made available to the Company, an opinion of prominent Queen’s counsel, specializing in United Kingdom tax laws, that the transactions were permitted and acceptable under the terms of the applicable United Kingdom revenue laws. The Company remains confident that the transactions were permitted and acceptable under the terms of the applicable United Kingdom revenue laws.

HMRC has requested interviews with three officers of the Company to discuss whether those officers were involved in the arrangements for subscription of shares in the relevant companies. The Company is fully cooperating with the investigation. The Company believes there is no basis for any claim of responsibility of any of its officers or employees. Based on facts currently known by the Company, there is no need for it to record a contingent liability in its financial statements in connection with the investigation or the related transactions.

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#### Board of Directors

The Board of Directors of SAE Inc. is the existing six members of the Board of Directors of the Company, plus the addition of Robert Kaiser as a Board Member and Chairman of SAE's Audit Committee. SAE will have four members of its Board who are independent as defined by NASDAQ.

#### Parallel Action

On June 28, 2011, Seven Arts Pictures plc ("PLC") filed an action in the High Court of England against Parallel Media LLC ("Parallel") to collect sums due to PLC with respect to acquisition of distribution rights in Russia to four motion pictures and to confirm Parallel's obligations under both a signed and unsigned investment agreement with respect to the motion picture project Winter Queen. On the same day Parallel filed a petition to wind up and liquidate PLC in the Companies Courts of England based on its claim of repayment of \$1,000,000 of investment made by Parallel in Winter Queen. That winding up petition will not be heard until some unspecified date after October 10, 2011. PLC is no longer part of the Group and will file for administration under the laws of England, which management of PLC believes will be granted and which will result in the denial of Parallel's winding up petition. The disputes between PLC and Parallel will then be resolved in this administration under English law and should not affect the results of operations of the Group. On September 19, 2011, Parallel filed a new action against PLC and Seven Arts Entertainment Inc. ("SAE") in the Superior Court of California, asserting the same claims as in the winding up petition and seeking to enjoin the proposed administration proceedings in England. A request for a preliminary injunction was denied by the Superior Court. PLC will move to dismiss this action since all the operative agreements between PLC and Parallel include a clause requiring exclusive jurisdiction of all litigation in the courts of England. PLC expects this motion to dismiss will be granted.

#### Fletcher Joint Venture

The Group entered into an agreement with BRG Investments, LLC ("BRG"), an affiliate of Fletcher Asset Management ("Fletcher") for the investment by BRG of up to \$30,000,000 in preferred stock of the Group and the formation of a joint venture to, among other things, produce and distribute motion pictures and make investments.

BRG purported to cancel the agreement in May 2011.

On October 5, 2011, the Company arranged a mutually acceptable settlement of its dispute with Fletcher arising out of an investment agreement purported terminated by Fletcher as was announced in a press release on June 7, 2011. In the settlement with Fletcher, the Company waived all claims against Fletcher. Fletcher agreed to acquire, and did acquire, 250,000 shares of the Company's common stock at a price of \$1.00 per share. Fletcher received a warrant to buy an additional 100,000 shares at \$1.00, Fletcher has the right within six months to buy an additional 250,000 shares of the Company's common stock based on a volume weighted average price but no less than \$1.00 or more than \$1.50, and if it buys these shares, Fletcher will receive an additional warrant to buy an additional 100,000 shares of our common stock on the same terms as the warrant we have issued. Seven Arts intends to use the proceeds of this transaction to partially fund its next motion picture production in Louisiana entitled Schism, written and to be directed by Adam Gierasch, the director of Autopsy and Night of the Demons, two recent releases by the Company.

#### Legal Action by Arrowhead Target Fund

The Arrowhead Target Fund has filed an action on September 22, 2010, which seeks recovery from the Group of the monies which the Group has retained under its interpretation of the relevant agreements with Arrowhead. In addition, Arrowhead makes substantial additional claims against the Group, Mr. Hoffman and Seven Arts Pictures Inc. regarding claimed breaches of the terms of the operative agreements, including failure to properly account, failure to turn over materials, failure to remit monies collected, and similar matters. The claims against the Group for these breaches of warranties for damages are \$8,300,000 although Arrowhead states no basis for this amount. The Group does not believe there is any basis to the Arrowhead claims except with respect to the monies withheld by the Group based on its interpretation of the applicable agreements. The Group intends to aggressively defend these claims but is currently in settlement discussions with Arrowhead regarding the reacquisition of the 12 motion pictures subject to the Arrowhead transaction. However, the ultimate outcome of these claims cannot be determined at this time, and nothing has been accrued related to these claims.

#### New Office Lease in Los Angeles

On December 1, 2011, SAE Inc. entered into an agreement for office space in Los Angeles. The lease is for 60 months at a monthly rate of approximately \$9,500. The office space and expense will be shared with related parties; however, SAE Inc. is joint and severally liable.