Baronsmead VCT 3 plc

2005
Summary annual report
for the year ended
31 December 2005

Investment Objective

Baronsmead VCT 3 is a tax efficient listed company which aims to achieve long-term capital growth and generate tax free dividends for private investors.

Investment Policy

To establish a diverse portfolio comprising:

- Larger unquoted companies, typically as lead investor and alongside institutional investors, which do not offer the same tax benefits to their shareholders as a VCT.
- Technology-enabled companies.

Buy-back Policy

Purchases of shares will be made within guidelines established from time to time by the Board. This power will be exercised only if in the opinion of the Board a repurchase would be in the interests of shareholders as a whole. Historically the repurchase price has represented an approximate 10 per cent discount to Net Asset Value per share.

Dividend Policy

The Board wishes to sustain average annual dividends of 4.5p per ordinary share, but this depends primarily on the level of realisations achieved and it cannot be guaranteed. There will be variations in the amount of dividends paid year on year. Since launch the average annual tax-free dividend paid to Shareholders has been 3.9p per share (equivalent to a pre-tax return of 5.7p per share for a higher rate taxpayer.

Dividend Reinvestment

The Directors offer to Shareholders the opportunity to reinvest their dividends by subscribing for new shares in the Company. The Dividend Reinvestment Scheme enables Shareholders to increase their shareholding without incurring dealing costs, issue costs or stamp duty. These shares should qualify for the VCT tax reliefs that are applicable to subscriptions for new shares and form part of each Shareholder's current annual limit of £200,000 for investing in VCTs.

Financial Highlights*

- Net asset value ('NAV') increased by 15.1 per cent to 119.31p per ordinary share before deduction of annual dividends.
- After ordinary dividends totalling 5.5p per share, for the year, the NAV is 113.81p at 31 December 2005.
- An ordinary interim dividend of 2p per share was paid on 28 September 2005 and a final ordinary dividend of 3.5p per share will be paid on 20 March 2006, subject to shareholder approval.
- Since launch in 2001, the total return to ordinary shareholders is 46.4 per cent (based on quoted investments valued at mid-market price).
- The C share fundraising closed on 3 January 2006, fully subscribed and raising over £22m of net proceeds.

*The Net Asset Values stated above are based on revised UK GAAP in that quoted investments are valued at bid price. However, dividends payable by the Company have been recognised in the accounting period to which they related and not in the accounting period in which they are paid . This is a departure from revised UK GAAP.

Financial Summary

	31 December 2005	31 December (as restated) 2004	% change
Ordinary Share – capital values‡			
Net asset value	**119.31p**	103.68p	15.1%
Share price	**100.50p**	92.50p	8.6%
Discount (against NAV per share, revised UK GAAP)	**14.3%**	13.0%	
Net asset value total return since launch†	**46.4%**	27.5%	
Total assets (as per Balance Sheet)	**£39.2m**	£35.5m	

†Net asset value total return assuming gross dividends re-invested.

C Share – capital values			
Net asset value	**95.13p**		
Share price	**100.00p**		
Premium (to NAV per share, revised UK GAAP)	**5.1%**		
Total assets (as per Balance Sheet)	**£17.0m**		

The C shares were launched on 10 October 2005.

‡Reconciliation of net asset value per ordinary share	As at 31 December 2005	As at 31 December 2004
Net asset value per share (accounting policies at 31 December 2004)	**115.18p**	105.26p
Less: revaluation of investments from mid to bid prices	**(1.37p)**	(1.58p)
	113.81p	103.68p
Add: dividend declared	**3.50p**	2.70p
*Net asset value per share (revised UK GAAP)	**117.31p**	106.38p
Add: Dividend paid 28 September 2005/12 August 2004	**2.00p**	1.80p
Net asset value per share (before dividends)	**119.31p**	108.18p

	Year to 31 December 2005	Year to 31 December 2004
Dividends		
Revenue dividends per ordinary share	**2.00p**	1.20p
Capital dividend per ordinary share	**3.50p**	3.30p

*The introduction of Revised UK GAAP for accounting periods commencing 1 January 2005 has resulted in the following changes to the Company's net asset value:

In accordance with FRS25/26 quoted investments are now valued at bid instead of mid.

In accordance with FRS21, dividends payable by the Company are now recognised in the period in which they are paid.

Five Year Record

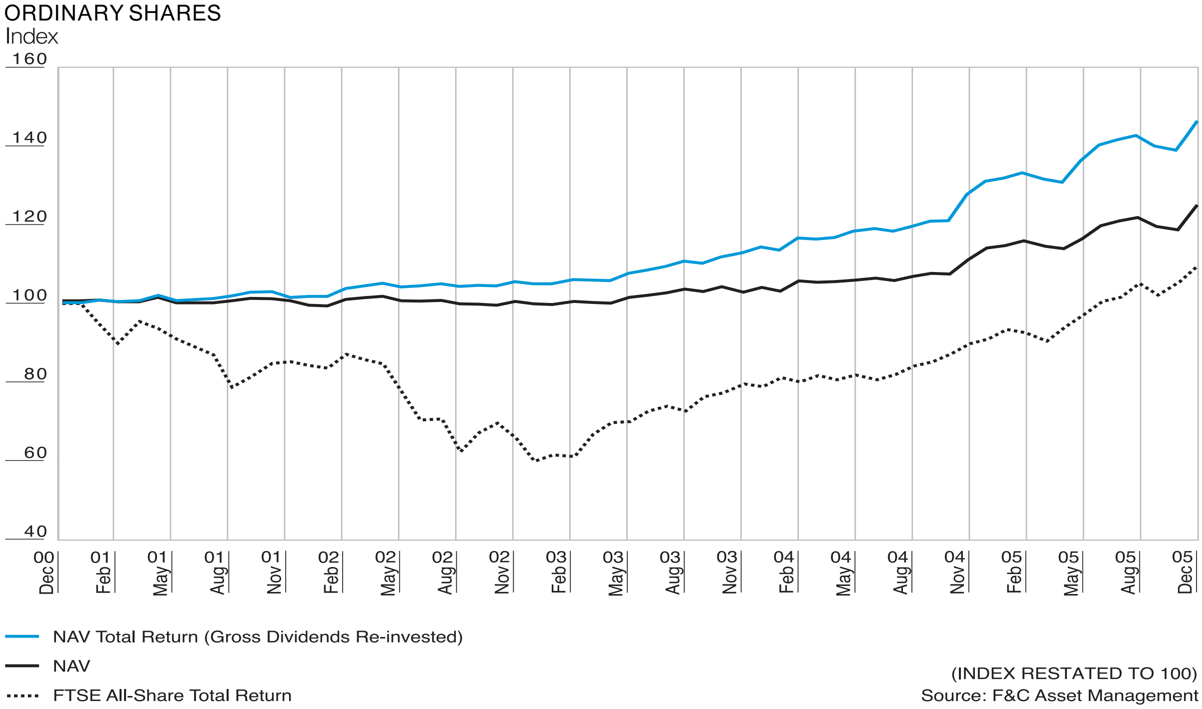
Performance Record – ordinary shares

At 31 December	Shareholders' funds £'000	Net asset value per share p	Net asset value total return* %	Share price p	Discount (note 1) %	Revenue dividend per Ordinary share p	Capital dividend per Ordinary share p
2001	31,069	93.85	101.21	88.00	(6.2)	2.30	–
2002	32,050	94.85	105.35	85.50	(9.9)	2.80	–
2003	32,994	97.15	112.66	90.00	(7.4)	2.20	2.00
2004 (revised UK GAAP)	35,488	106.38	127.52	92.50	(13.0)	1.20	3.30
2005 (revised UK GAAP)	39,226	117.31	146.38	100.50	(14.3)	2.00	3.50

*Source: F&C Asset Management plc.

Note 1 – (Discount)/premium is the difference between Baronsmead VCT 3's quoted price and its underlying net asset value.

Baronsmead VCT 3 NAV and NAV Total Return (based on middle market price) since launch against the FTSE All-Share Index Total Return



Cash Returned to Shareholders

The Board is also aware that shareholders are concerned that the original capital subscribed into Baronsmead VCT 3 has been maintained. The table below shows the cash returned to shareholders, including their income tax reclaimed on subscription.

Year subscribed	Subscription price p	Income tax reclaim p	Net cash equivalent p	Cumulative dividends paid p	Net annual yield* %	Gross annual yield† %
2001	100	20.0	80.0	19.3	4.9	7.3

Note 1 – The cash returns could be higher for those shareholders who were able to defer a capital gain on subscription and the net sum invested may be less.
*Net annual yield represents the cumulative dividends paid expressed as a percentage of the net cash invested.
†The gross equivalent yield if the dividends had been subject to higher rate (40% income tax).

Chairman's Statement

I am delighted to present this fifth annual report and particularly welcome the new C shareholders to the Company. The total return for ordinary shareholders has particularly benefited from the increase in value of the unquoted investments.

The C share fundraising during autumn 2005 proved popular with both new and existing 'Baronsmead' shareholders as it is estimated that we had a 30 per cent share of all the VCT capital being raised during the period that we were open.

Mark Cannon Brookes
Chairman

Results

In the year to 31 December 2005, the Net Asset Value (NAV) per ordinary share increased by 15.1 per cent from 103.68p to 119.31p before dividends. The 2p interim dividend was paid in September 2005 and the proposed final dividend of 3.5p is payable on 20 March 2006. After dividend payments, which are tax-free for qualifying shareholders, the NAV per ordinary share at the year end is 113.81p.

This level of dividends is possible through the successful realisation of profits from across the portfolio. AssA was sold outright to a third party and the refinancing of Americana also generated a sizeable gain over original cost.

From our launch in 2001, the Managers have had the incentive to grow the value of the portfolio such that any performance fee only becomes payable once the total return exceeds 40 per cent and thereafter rises at 8 per cent simple per annum. The results for the year to 31 December 2005 trigger a performance fee of £159,000 (excluding VAT) which is based on the Managers receiving 20 per cent of the total return in excess of this trigger level.

The C share offer raised net proceeds of £22.5 million and from this pool of capital the first three investments were made in Green Issues, Autoclenz Holdings and Appian Technology. The first C share dividend will be paid in September 2006 out of any surplus from net revenue. The NAV per C share was 95.13p at 31 December 2005.

Long Term Performance

The record of total returns generated and net yield paid to ordinary shareholders is set out on page 2 of this report. This performance compares well against other VCTs and the FTSE All-Share index. Since launch the total return (based on quoted investments being valued at mid-market price) for founder shareholders is 46 per cent, net of all costs. This level of return is calculated by combining the growth in NAV with reinvested dividends per ordinary share of 19.3p.

When compared to the five Generalist VCTs launched at the same time, your Company has a total return in excess of the average and is also over 37 per cent ahead of the FTSE All-Share Index which is a broad UK comparator for equity investments.

This record also shows how over the last five years the share price has moved. On average we seek to maintain a 10 per cent discount to NAV. However, at certain times of the year, prior to publication of financial results and payment of dividends this discount may fluctuate. The bid price for the second half of the year exceeded 100p and many of the 2.1 million shares sold by ordinary shareholders were at close to this level.

The Portfolio

In the year under review, 16 new investments were made and two investments sold taking the net portfolio to 61 companies. There were six new unquoted and ten AiM investments totalling £8.0 million. The average size of each unquoted investment was significantly larger at £880,000 than the AiM investments of £270,000.

Chairman's Statement

Six VCT tests relating to the running of Baronsmead VCT 3 have to be, and were, met for each day of the year to 31 December 2005. The most visible of these tests is that more than 70 per cent of the portfolio has been invested in qualifying investments beyond the first three accounting periods from when new share capital was subscribed. At the year end, over 87 per cent of the capital raised (net of launch costs) prior to 31 December 2003 was invested in VCT qualifying investments.

The relative health of portfolio companies is measured quarterly in terms of profitability as well as other non-financial benchmarks. At the year end, 80 per cent of the portfolio companies were reporting higher or steady profits. In the last quarter there had been some softening in the trading of investee companies.

The sale of the investment in AssA was reported in the autumn fact sheet and generated a return of 2.5x cost over the two-year period that the investment was held prior to the sale to Carter & Carter. Since the year end, Language Line has also been sold at 2.1x cost to a similar US company and generated a profit of £600,000. However, the largest gain came from the refinancing of Americana, which returned a profit of £2.9 million in November 2005.

The change in NAV of the C shares, in the first year, is only likely to be from the change in bid share price of new AiM shareholdings as the residual portfolio will be a high proportion in cash and fixed interest securities. Unquoted investment are rarely revalued from their cost during this first period under BVCA guidelines.

Change in Fund Manager Ownership

On 1 July 2005, a recently formed Limited Liability Partnership (ISIS EP LLP) assumed the existing business and operations of ISIS Equity Partners plc, managing over £500 million of private equity assets, including the management contract of the Company. The relationship between F&C Asset Management plc and ISIS EP LLP remains strong as the status moves from being a subsidiary to that of a partnership. The Board was consulted regarding this change and was fully supportive. The Board retains its confidence in the management team which remains in place and now enjoys the added motivation provided by the change of ownership.

Your Investment Managers role as active investors with unquoted portfolios was recognised by an award in 2005 (EVCA/Real Deals) for the best growth capital transaction in Europe made by ISIS Equity Partners relating to a 2000 investment in Fat Face. This investment held between 2000 to 2005 predated our Company but did involve the first two Baronsmead VCTs.

Meeting Shareholders Needs

C Share Fundraising

Shareholders approved the C share fundraising at the fourth AGM in March 2005 and the extension of the life of your Company from 2008 to 2013. The prospectus issued in September was well received by commentators, advisers and their clients resulting in the offer for 2005/06 being fully subscribed one month ahead of schedule. Over 35 per cent of existing shareholders across the 4 Baronsmead VCTs subscribed to the fundraising.

Tax Reliefs

The current rate of income tax relief is 40 per cent and is available until 5 April 2006. The Government remains committed to ensuring the long term sustainability and success of the VCT market and will announce the future level of VCT reliefs at Budget 2006. The intervening period will allow further analysis of trends in the VCT market and continued dialogue with key stakeholders.

Shareholder Communication

Your Board has a policy of full and open disclosure to shareholders, many of whom have previously expressed longer-term investment horizons when surveyed in the past. Your Board are minded to survey shareholders, once more, so that we can understand your priorities for the future and whether existing shareholder policies need to be reconsidered.

Existing shareholders subscribed for 0.5 million new shares at an average price of 110p per ordinary share under the Dividend Reinvestment Scheme. A further 1.7 million shares were issued, under the Offer for Subscription – ‘‘Top Up’’, during March/April 2005 at an average price of 113p. This latter scheme is in abeyance as it is currently not cost effective following the introduction of the EU Prospectus Directive on 1 July 2005.

Dividend Policy

The Board has agreed that it wishes to sustain an annual dividend policy of 4.5p per ordinary share. This takes into account that the Board's aim is to maintain an NAV at 100p or more per ordinary share. The ability to meet these twin objectives will depend significantly on the level and timing of profitable realisations and the underlying value of the portfolio. The Board therefore wishes to build a buffer of reserves, which will enable this policy to be continued once the current C shares are converted into ordinary shares in early 2008.

The total dividends paid and proposed for 2005 are 5.5p per ordinary share and are in excess of the stated policy. To date the average paid to founder shareholders has been 3.9p per year. For those qualifying founder shareholders who obtained income tax relief of 20 per cent on subscription, the net annual yield is 4.9 per cent. For a higher rate taxpayer the equivalent yield rises to 7.3 per cent.

Chairman's Statement

Co-Investment Scheme

The co-investment scheme for executive members of the Managers to invest in unquoted transactions was announced to shareholders in November 2004 and was explained in more detail in the fact sheet issued after the 30 September 2005 quarter end. The rationale remains to expand the existing skills and capacity of the Manager's team. In its first year of this scheme coming into force, 21 members of ISIS EP LLP have invested £74,950 in all the six unquoted investments where the Manager was the lead investor.

A full review of the Company's website www.baronsmeadvct3.co.uk is being undertaken and shareholders may experience problems in obtaining certain literature. If you experience such difficulty, please contact either the Investment Manager or Company Secretary who will be more than happy to assist.

Outlook

At the end of our first five years, a firm base has been established for future growth with over £60 million of net assets and a portfolio of 61 companies. Our priority in the coming years is to sustain this progress and the investment performance.

We now have over 3,500 ordinary and C shareholders and our task as a Board is to ensure that we meet and better your expectations in the longer term. I look forward to welcoming as many shareholders as possible at the AGM on 16 March 2006 at 11.00 a.m. at the offices of ISIS EP LLP, Exchange House, Primrose Street, London EC2A 2NY. There will be a number of presentations followed by a light buffet lunch and shareholder workshop finishing by 2.30 pm.

Mark Cannon Brookes

Chairman

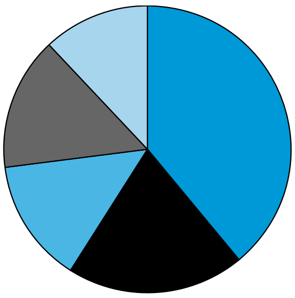
8 February 2006

Portfolio Analysis

Portfolio by Sector . . .

Company Investments (excluding cash and fixed interest portfolio)

Sector Analysis as at 31 December 2005

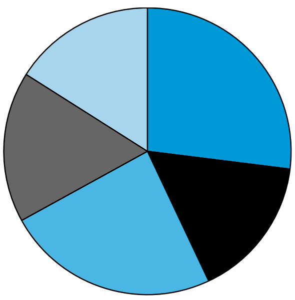


Business services	**39%**
Media	**20%**
Consumer	**15%**
IT support services	**14%**
Healthcare	**12%**

. . . and by Asset Classification

Total Assets less Current Liabilities

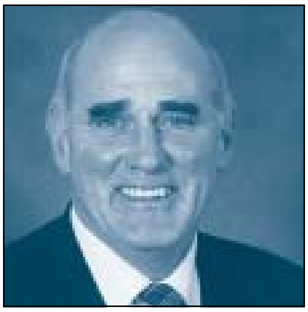
Market Analysis as at 31 December 2005



AiM/FTSE SmallCap	**27%**
Unquoted – ordinary and preference shares	**16%**
Fixed interest	**24%**
Unquoted – loan stock	**17%**
Net current assets	**16%**

Manager's Review

The portfolio has achieved good aggregate gains during the last year including some notable realisations from two unquoted investments, Americana and AssA.



David Thorp
Investment Manager

Gerard Kelly
Finance Manager

Rhonda Nicoll
Company Secretary

New Investment

The total portfolio grew to 61 companies during the year to 31 December 2005, with new investment of £8.5 million split between unquoted and AiM-traded investees. The first three investments, for the C share pool, were made in Green Issues, Autoclenz Holdings and Appian Technology and allotted by the Board under prescribed rules relating to the level of 'free cash' in the respective pools of capital. Further rounds of investment were made in Domantis and Xention subsequent to the first round of investments led by Medical Venture Managers.

Portfolio Performance and Realisations

The value of the unquoted portfolio advanced by some £5.0 million with steady growth in value by most and a significant gain by Americana. A provision of £0.4 million was made against the investment in Hawksmere. Spaform, already valued at nil in 2004, went into administration in autumn 2005.

The refinancing of Americana released profits of £2.9 million, representing 5.5 times the cost of the investment in August 2003. A small shareholding has been retained. The sale of AssA and Language Line, the latter after the year end, generated another £1.7 million increase in value during 2005 following their respective trade sales. Both of these investments illustrate the role of an active investor in orchestrating changes at Board level as the companies needed to resolve commercial problems and then grow.

The AiM-traded portfolio was slightly behind last years valuation. The new investments made in 2005 opening strongly as well as a significant rise in the share price of Begbies Traynor where some top slicing profits were taken. Conversely, there were a number of down grades where companies like Air Music and Media and Real Food Group were involved in corporate acquisitions that did not settle down as expected. We can learn from such experiences

Realisations in year to 31 December 2005		First investment date	Cost £'000	Proceeds £'000	Multiple return
Americana	Refinancing	August 2003	56	2,924	5.5†*
AssA	Trade sale	September 2003	1,268	2,392	2.5*
Begbies Traynor Group	Market sale	September 2004	110	253	2.3
Huveaux	Market sale	March 2003	18	39	2.2
Medal Entertainment & Media	Market sales	August 2002	36	72	2.0
Business Direct Group	Market sale	August 2004	64	114	1.8
Murgitroyd Group	Market sales	November 2001	182	256	1.4
Vectura Group	Market sale	April 2001	270	335	1.2
FDI	Trade sale	March 2002	685	776	1.1

*includes interest received
†original cost included loan stock redeemed in December 2004

Manager's Review

and where possible try to influence the Boards of these companies as to how they can undertake increased levels of due diligence in making acquisitions.

The technology portfolio consists of 10 shareholdings where the main value growth came from Vectura and its transaction announced with Novartis in April 2005. Overall, this part of the portfolio showed little net gain in the year.

Net realised profits from the sale of unquoted and AiM investments totalled £4.1 million and £0.4 million respectively.

Andrew Garside joined ISIS in April 2005 after 14 years at 3i and is responsible for new investment activity for VCT investments across the London, Birmingham and Manchester Offices. A new Leeds office is planned for 2006. Henrietta Marsh also joined in 2005 taking day-to-day responsibility for the AiM portfolio within your Company. She has a combination of private equity investing and Small Cap quoted fund management while at 3i over 14 years.

Andrew has become a member of the Investment Committee for all VCT unquoted investment decisions. This committee comprises six members of the Manager led by a non-executive chairman. Investment and divestment decisions for the AiM portfolio remain with David Thorp and Wol Kolade, Managing Partner of ISIS EP LLP.

Investor Relations

Although the move to Computershare as registrars took place in July 2004, it has taken time for the electronic systems to settle down and in particular produce the annual statement of the record of individual shareholders share and dividend histories. Once this IT platform is sound we can move to the next stage of electronic shareholder services, which will necessarily take several years as shareholders increasingly embrace the advantages of such communication and hopefully dialogue.

The Company Secretary, Rhonda Nicoll and David Thorp as fund manager can both respond to shareholder queries. Gerard Kelly can also be contacted as he has responsibility for financial control and planning, which is an essential part of the management of VCTs so that the VCT legislation is met at all times and there is adherence to high compliance standards.

Outlook

As Managers we have strived to improve our investment skills and private equity disciplines over the last year. The intention is to continue to build the portfolio and generate value from these investments.

David Thorp
Investment Manager
ISIS EP LLP
8 February 2006

Company	Location	Sector	Activity	Investment Cost (£'000) C shares	Investment Cost (£'000) Ordinary shares
New unquoted investments					
AssA *	Washington	Business services	Work place training		11
Boldon James	Crewe	IT	Secure messaging software		687
Credit Solutions	Carshalton	Business services	Credit management		1,032
Domantis *	Cambridge	Healthcare	Drug discovery		245
Green Issues	Reading	Media	PR for construction	399	99
Independent Living Services	Alloa	Healthcare	Domiciliary care		624
Kafevend	Crawley	Consumer	Vending services		1,247
Reed & Mackay	London	Business services	Travel management		1,211
Xention *	Cambridge	Healthcare	Drug discovery		246
				399	**5,402**
AiM-traded investments					
Accuma Group	Manchester	Consumer	Insolvency services		108
Appian Technology	Buckinghamshire	IT	High technology proprietary products	102	23
Autoclenz Holdings	Derbyshire	Consumer	Car valeting	320	80
Debtmatters Group	Manchester	Consumer	Insolvency services		219
Driver Group	Lancashire	Business services	Construction industry services		347
Eg Solutions	Staffordshire	IT	Financial services software		375
Fishworks	Bath	Consumer	Fishmongers & fish restaurants		128
Hamsard Group	Warrington	IT	Software for security networks		375
InterQuest Group	London	Business services	IT recruitment		323
Talarius	London	Consumer	'Quicksilver' amusement shops		313
				422	**2,291**
				821	**7,693**
Total investments in year				**£8,514**	

Ten Largest Investments

by Current Value at 31 December 2005

The Art Group Limited *London*

First Investment: October 2003
Cost: £1,281,000
Valuation: £2,547,000
Valuation Basis: Discounted price earnings

The Art Group is a market leading publisher of art content on cards, posters and canvas prints sold to retailers in over 50 countries such as IKEA and Habitat. It raised £4.5m to support a management buy-out.

Among its artists under licence is Jack Vettriano to which it has exclusive rights to market globally.

Year ended 31 December	**2004**	2003
	£ million	£ million
Sales	**26.4**	18.3
Profit before tax	**1.4**	2.0
Retained profit	**0.6**	1.3
Net assets	**2.5**	1.4

Martin Audio Limited *High Wycombe*

First Investment: August 2003
Cost: £786,000
Valuation: £2,053,000
Valuation Basis: Discounted price earnings

Martin Audio designs, assembles and markets high performance speaker systems for use in the concert and public entertainment markets, in the UK and overseas. It raised £3m of capital to support a management buy-out.

85 per cent of turnover is exported and in the last five years distribution agreements were signed covering a total of 22 countries.

Year ended 30 June	**2004**	2003
	£ million	£ million
Sales	**11.4**	9.5
Profit before tax	**1.1**	1.0
Retained loss	**(0.8)**	–
Net assets	**0.9**	1.3

RLA Group Media Limited *Bournemouth*

First Investment: December 2002
Cost: £1,105,000
Valuation: £1,904,000
Valuation Basis: Discounted price earnings

RLA is a regional marketing services agency, predominantly servicing national and multinational brands selling through local outlets. £2.4m was raised in December 2002 to fund a replacement capital deal.

The original investment was in RLA Media Limited. The business RLA Media was transferred entirely into RLA Group Limited on 27 April 2005. The financials for RLA Media Limited are shown as they are a more relevant reflection of the business owned. Amongst its clients RLA includes the VAG Group.

Year ended 31 May	**2004**	2003*
	£ million	£ million
Sales	**10.6**	4.5
Profit before tax	**1.7**	0.4
Retained profit	**0.6**	0.1
Net assets	**3.5**	2.9

*for the period from 19 November 2002 to 31 May 2003

Vectura Group *Chippenham*

First Investment: April 2001
Cost: £771,000
Valuation: £1,295,000
Valuation Basis: Bid price

Vectura is a small, but rapidly growing drug formulation and drug delivery company. The role of drug delivery is to encapsulate a drug into an appropriate system that is acceptable for human use. The Company raised three rounds of capital between April 2001 and November 2002. Vectura floated on AiM in July 2004.

Year ended 31 March	**2005**	2004
	£ million	£ million
Sales	**4.5**	2.9
Loss before tax	**(8.8)**	(9.0)
Retained loss	**(7.7)**	(8.1)
Net assets	**21.7**	6.4

Kafevend Limited *Crawley*

First Investment: October 2005
Cost: £1,247,000
Valuation: £1,247,000
Valuation basis: Cost

Kafevend is a leading drinks vending machine service provider to the SME market. £5 million was invested in October 2005 to fund a management buy-out.

Kafevend employs over 70 people and operates from five sites across the UK.

Year ended 30 September	**2004**	2003
	£ million	£ million
Sales	**10.7**	10.2
Profit before tax	**1.7**	1.7
Retained profit	**1.6**	1.1
Net assets	**11.2**	9.7

Ten Largest Investments

Reed & Mackay Limited *London*

First Investment: November 2005
Cost: £1,211,000
Valuation: £1,211,000
Valuation basis: Cost

Reed & Mackay is a provider of business travel management services to professional services firms and corporates. £5.0 million was raised to fund a replacement capital deal.

Year ended 30 March	2005	2004
	£ million	£ million
Sales	**8.9**	8.5
Profit before tax	**2.6**	1.9
Retained profit	**1.6**	1.3
Net assets	**6.4**	4.8

Begbies Traynor Group *Manchester*

First Investment: October 2004
Cost: £414,000
Valuation: £1,202,000
Valuation basis: Bid price

Begbies Traynor Group is the UK's leading independent insolvency, corporate and rescue and recovery specialist. The Company joined AiM in September 2004 raising £5.4 million.

BTG covers the UK with 24 offices and 147 professionals.

Year ended 30 April	2005	2004
	£ million	£ million
Sales	**24.7**	22.0
Profit before tax	**1.9**	3.0
Retained loss	**1.0**	1.0
Net assets	**25.2**	1.1

Language Line Limited *London*

First Investment: August 2003
Cost: £660,000
Valuation: £1,142,000
Valuation Basis: Offer

Language Line is the UK's leading provider of telephone interpretation and translation solutions predominately to the public sector. In August 2003, £7.2 million was raised for a management buy-out.

Since the year end, this company was sold at 2.1x cost to a similar US company.

Year ended 31 December	2004	2003
	£ million	£ million
Sales	**8.7**	5.3
Profit before tax	**0.9**	1.9
Retained profit	**0.6**	1.3
Net assets	**1.2**	2.4

Boldon James Limited *Crewe*

First Investment: June 2005
Cost: £687,000
Valuation: £1,118,000
Valuation basis: Discounted price earnings

Boldon James is a provider of secure messaging and connectivity software solutions. Boldon James' products are primarily supplied into the defence and intelligence sectors via global system integrators such as EDS and Fujitsu.

Year ended 31 December	2004	2003
	£ million	£ million
Sales	**4.8**	4.8
(Loss)/profit before tax	**(0.2)**	0.2
Retained (loss)/profit	**(0.2)**	0.2
Net liabilities	**(0.5)**	(0.3)

kidsunlimited Limited *Wilmslow*

First Investment: August 2003
Cost: £481,000
Valuation: £1,061,000
Valuation Basis: Discounted price earnings

kidsunlimited is a major UK provider of day care facilities for children under five years old. The company operates a combination of owned nurseries and those located within the workplace. It raised £4.95 million to fund expansion and a share reorganisation.

Since investment in 2001, the number of places for children has grown from 2,077 to 4,086 across 46 sites.

Year ended 30 April	2004	2003
	£ million	£ million
Sales	**16.8**	13.8
Loss before tax	**(1.3)**	(1.3)
Retained loss	**(1.3)**	(1.3)
Net liabilities	**(3.6)**	(2.3)

Investment Portfolio

Company	Nature of Business	Cost Ord £'000	Cost C £'000	Valuation Ord £'000	Valuation C £'000	% of Total Assets Less Current Liabilities Ord £'000	% of Total Assets Less Current Liabilities C £'000	% of Equity held by Baronsmead VCT 3 plc	% of Equity held by Other Funds*
Unquoted									
The Art Group	Media	1,281	–	2,547	–	6.5	–	7.0	24.3
Martin Audio	Business services	786	–	2,053	–	5.2	–	13.0	33.6
RLA Group	Media	1,105	–	1,904	–	4.9	–	14.2	34.8
Kafevend	Consumer markets	1,247	–	1,247	–	3.2	–	15.4	49.6
Reed & Mackay	Business services	1,211	–	1,211	–	3.1	–	9.5	30.5
Language Line	Business services	660	–	1,142	–	2.9	–	6.0	62.0
Boldon James	IT support services	687	–	1,118	–	2.9	–	9.0	29.0
kidsunlimited	Business services	481	–	1,061	–	2.7	–	4.1	46.9
Americana	Consumer markets	443	–	1,039	–	2.6	–	1.0	10.0
Credit Solutions	Business services	1,032	–	1,032	–	2.6	–	8.6	26.4
SLR Holdings	Business services	494	–	993	–	2.5	–	2.8	24.4
Domantis	Healthcare	601	–	705	–	1.8	–	1.3	1.0
Independent Living Services	Healthcare	624	–	624	–	1.6	–	8.9	28.6
Occam	Business services	420	–	576	–	1.5	–	3.6	31.4
Green Issues	Media	99	399	99	399	0.3	2.3	9.5	40.0
Country Artists	Consumer	448	–	402	–	1.0	–	5.3	54.7
Xention Discovery	Healthcare	377	–	400	–	1.0	–	2.5	1.2
Oxxon Pharmaccines	Healthcare	250	–	–	–	–	–	0.8	0.8
Hawksmere	Business services	766	–	–	–	–	–	10.5	34.5
Spaform	Consumer	866	–	–	–	–	–	13.5	36.5
Total unquoted		**13,878**	**399**	**18,153**	**399**	**46.3**	**2.3**		
AiM									
Vectura Group	Healthcare	771	–	1,295	–	3.3	–	1.5	1.9
Begbies Traynor Group	Business services	414	–	1,202	–	3.1	–	1.1	3.0
Huveaux	Media	541	–	947	–	2.4	–	1.5	2.7
IDOX	IT support services	600	–	720	–	1.8	–	2.8	4.3
Colliers CRE	Business services	470	–	634	–	1.6	–	1.2	2.4
Eg Solutions	IT support services	375	–	631	–	1.6	–	3.1	9.2
Murgitroyd Group	Business services	319	–	627	–	1.6	–	3.2	6.4
Debtmatters Group	Consumer markets	219	–	567	–	1.5	–	1.4	4.1
Jelf Group	Business services	393	–	563	–	1.4	–	3.6	10.1
Interactive Prospect Targeting	Business services	253	–	520	–	1.3	–	1.0	3.0
Talarius	Consumer markets	313	–	475	–	1.2	–	0.8	2.5
Zoo Digital Group	IT support services	584	–	472	–	1.2	–	1.8	3.0
Hamsard Group	IT support services	375	–	456	–	1.2	–	2.1	6.2
Autoclenz Holdings	Consumer markets	80	320	80	320	0.2	1.9	3.1	9.2
Sanderson Group	IT support services	387	–	387	–	1.0	–	1.9	5.5
WIN	IT support services	263	–	358	–	0.9	–	1.4	3.9
Driver Group	Business services	347	–	306	–	0.8	–	2.0	6.2
Real Good Food Company	Consumer markets	540	–	300	–	0.8	–	0.6	1.7
Adventis Group	Media	281	–	296	–	0.8	–	3.0	7.8
Medal Entertainment & Media	Media	299	–	279	–	0.7	–	3.3	5.0
Air Music & Media Group	Media	575	–	250	–	0.6	–	1.6	2.9
Prologic	IT support services	310	–	248	–	0.6	–	4.1	10.9
Quadnetics Group	Business services	296	–	246	–	0.6	–	0.7	1.8
NeuTec Pharma	Healthcare	79	–	230	–	0.6	–	0.2	0.2
InterQuest Group	Business services	323	–	223	–	0.6	–	2.3	6.8
Accuma Group	Consumer	108	–	198	–	0.5	–	0.5	1.5
Blooms of Bressingham	Consumer markets	320	–	192	–	0.5	–	1.0	1.0
Stagecoach Theatre Arts	Consumer markets	419	–	180	–	0.5	–	4.6	4.6
Polaron	IT support services	296	–	172	–	0.4	–	1.4	3.4
Business Direct Group	Business services	457	–	164	–	0.4	–	2.6	5.0
Fishworks	Consumer markets	128	–	155	–	0.4	–	1.2	3.6
Cardpoint	Business services	92	–	126	–	0.3	–	0.2	0.4
Appian Technology (commenced trading on 4/1/06)	IT support services	23	102	23	102	0.1	0.6	2.2	6.7
Universe Group	IT support services	158	–	121	–	0.3	–	1.1	2.8
VI Group	IT support services	300	–	98	–	0.3	–	3.7	10.5
Xpertise Group	Business services	296	–	92	–	0.2	–	2.6	4.4
Scott Tod	Business services	421	–	80	–	0.2	–	2.3	5.9
MKM Group	Business services	284	–	29	–	0.1	–	1.5	3.8
Micap	Healthcare	325	–	27	–	0.1	–	1.1	2.0
Capcon Holdings	Business services	137	–	14	–	–	–	1.7	3.4
Total AiM		**13,171**	**422**	**13,983**	**422**	**35.7**	**2.5**		
FTSE SmallCap									
Ardana	Healthcare	619	–	610	–	1.6	–	1.0	0.8
Total FTSE SmallCap		**619**	**–**	**610**	**–**	**1.6**	**–**		
Interest bearing securities									
UK Treasury 4.5% 07/03/07		1,440	9,031	1,455	9,033	3.7	53.1		
Money Market OEIC		3,344	–	3,344	–	8.6	–		
Total interest bearing securities		**4,784**	**9,031**	**4,799**	**9,033**	**12.3**	**53.1**		
Total investments		**32,452**	**9,852**	**37,545**	**9,854**	**95.9**	**57.9**		
Net current assets		**–**		**1,681**	**7,168**	**4.1**	**42.1**		
Total assets less current liabilities		**–**		**39,226**	**17,022**	**100.0**	**100.0**		

A provision of £1,928,000 has been made against unquoted investments as at 31 December 2005 (31 December 2004 – £1,288,000).
*Other funds managed by the same investment managers, ISIS EP LLP.

Board of Directors

as at 31 December 2005

Mark Cannon Brookes (Chairman)

(age 66) is a director of Smith & Williamson Investment Management. The NCL group has £7 billion of investments under management. He is chairman of CG Asset Management Limited and is also a director of ISIS UK Select Trust plc and a number of other companies, mostly overseas.

Andrew Karney
(age 63) was deputy chairman and a shareholder of Language Line Limited in which Baronsmead VCT 3, was until recently, an investor. He is also a director of The Guardian Media Group plc, Guardian Newspapers Limited and a number of unquoted companies. Previously he was a director of Integrated Micro Products plc, a founder director of Cable London plc and an executive director of Logica plc.

Gillian Nott
(age 60) was until March 1999 chief executive of ProShare (UK) Limited. She was a director of the Financial Services Authority for 6 years to November 2004 and is on the board of a number of investment trusts at Merrill Lynch, Witan and Martin Currie. Previously she worked for the BP Group where she managed their venture capital portfolio. She is also chairman of Baronsmead VCT plc and a director of Baronsmead VCT 2 plc and was recently appointed deputy chairman of the AITC.

Robert Owen
(age 60) is a business consultant to developing companies and a director of Baronsmead VCT 4 plc. Previously he was a senior manager at Coutts and Co, responsible for the overall running of the venture capital investment portfolio.

As a fully listed Company, Baronsmead VCT 3 is required to comply with the Combined Code relating to its Corporate Governance. This Code requires the Company to be headed by an effective Board of Directors who lead and control the Company's affairs.

The Directors of a VCT and investment managers are required under the listing and continuing obligations of the London Stock Exchange to have sufficient and satisfactory experience in the management of a portfolio of unquoted investments of the size and type in which the VCT proposes to invest.

Summary Financial Statement

This summary financial statement has been prepared voluntarily by the Directors in accordance with the relevant requirements of section 251 of the Companies Act 1985. It does not contain sufficient information to allow a full understanding of the results and state of affairs of the Company. For further information, the full Annual Financial Statements, the Auditor's Report on those financial statements and the Directors' Report should be consulted. A copy of the Annual Report, which may be obtained free of charge from the Company Secretary, will be delivered to the Registrar of Companies after the Annual General Meeting. KPMG Audit Plc have reported on the Company's statutory accounts for the year ended 31 December 2005. This report was unqualified and contained no statement under section 237(2) and (3) of the Companies Act 1985.

Summary Directors' Report

Results and Dividends

The Directors submit the Report and Accounts of the Company for the year ended 31 December 2005.

These financial statements have been prepared under UK Generally Accepted Accounting Practice (UK GAAP). A number of new UK Financial Reporting Standards have been introduced as part of the UK convergence programme with International Accounting Standards. The changes affecting the Company relate to FRS 26 Financial Instruments: Measurement and FRS 21 Events after the Balance Sheet Date. A reconciliation of these changes is set out in Notes 1 and 2.

A review of the Company's business during the year is contained in the Chairman's Statement and Manager's Review.

A final dividend of 3.5p per ordinary share payable on 20 March 2006 to shareholders on the register on 17 February 2006 has been proposed.

Principal Activity and Status

The Company is registered as a Public Limited Company under the Companies Act 1985. The Directors have managed and intend to continue to manage the Company's affairs in such a manner as to comply with Section 842AA of the Income and Corporation Taxes Act 1988 and the Company has received approval as a Venture Capital Trust from HM Revenue & Customs for the year to 31 December 2004.

Issue and Buy-Back of Shares

Ordinary shares

During the year the Company issued 2,142,660 Ordinary Shares and raised net proceeds of £2,348,000. The Company bought back for cancellation 725,000 Ordinary Shares during the year at a cost of £712,000 (2004: 1,485,000 shares at a cost of £1,340,000). Since the Company's AGM held on 23 March 2005, the Company has bought back 1,340,000 Ordinary Shares to be held in Treasury at a cost of £1,333,000. These shares will be re-issued at Net Asset Value or above.

C share issue

Pursuant to the C share offer issued during September 2005, the Company issued 17,894,064 C shares and raised net proceeds of £17,011,000. Under the terms of the C shares as set out in the Securities Note dated 14 September 2005, the C shares will convert into ordinary shares on the earlier of at least 70 per cent of new funds being invested in qualifying holdings or 31 December 2007.

Since 31 December 2005, the Company issued a further 6,105,708 C shares bringing the total issued share capital to 23,999,772 C shares. The Offer closed on 3 January 2006.

Directors

Biographies of the Directors are shown on page 11.

Mark Cannon Brookes whose biography appears on page 11 retires by rotation at the fifth Annual General Meeting of the Company and, being eligible, offers himself for re-election.

The Board confirms that following performance evaluations, the performance of Mark Cannon Brookes continues to be effective and demonstrates commitment to his role as Chairman; the Board believes that it is therefore in the best interest of shareholders that he is re-elected.

As any further increase in Directors' remuneration would result in the current maximum permitted under the Articles of Association being exceeded, a resolution to increase the maximum aggregate sum to which the Directors would be entitled as remuneration to £100,000 (currently £50,000 adjusted for RPI) will be proposed at the Annual General Meeting.

This amendment is proposed to allow for a progressive increase in total Directors' remuneration over time in line with inflation and market practice.

The Directors who held office during the year, and their interests in the Ordinary Shares of the Company, were:

	31 December 2005 Ordinary 10p Shares	**31 December 2005 C 50p Shares**	31 December 2004 Ordinary 10p Shares
Mark Cannon Brookes	**116,983**	**20,700**	112,128
Andrew Karney	**33,295**	**41,200**	23,098
Gillian Nott	**16,118**	**10,350**	15,450
Robert Owen	**10,709**	**–**	10,709

There have been no changes in the holdings of the Directors between 31 December 2005 and 8 February 2006.

No Director has a service contract with the Company.

Corporate Governance

Arrangements to ensure the appropriate level of corporate governance have been put in place by the Board, which it believes are appropriate to a venture capital trust. The Company, except as disclosed below, complies with the provisions of the revised Combined Code on Corporate Governance issued by the Financial Reporting Council in July 2003 ('the Combined Code').

Since all Directors are non executive, the Company is not required to comply with the provisions of the revised Code in respect of the Directors' remuneration, except in so far as they relate specifically to non-executive Directors.

The Board consists solely of non-executive Directors of which Mark Cannon Brookes is Chairman and Andrew Karney is Senior Independent Director. All Directors are considered by the Board to be independent of the Company's Manager. New Directors will receive an induction from the Manager on joining the Board, and all Directors receive other relevant training as necessary.

The full Corporate Governance Statement is set out in the Annual Report for the year ended 31 December 2005.

Relations with Shareholders

The Company welcomes the views of shareholders and places great importance on communication with its shareholders. The Chairman

Summary Financial Statement

and other Directors are available to meet shareholders if required. The Annual General Meeting of the Company provides a forum, both formal and informal, for investors to meet and discuss issues with Directors and Managers of the Company. Details of the resolutions to be proposed at the Annual General Meeting on 16 March 2006 can be found in the Notice of Meeting on pages 21 and 22.

Management

ISIS EP LLP ('the Manager') manages the investments for the Company. The Manager will also provide or procure the provision of secretarial, administrative and custodian services to the Company. The management agreement may be terminated at any date by either party giving twelve months' notice of termination. Under the management agreement, the Manager receives a fee of 2.5 per cent per annum of the net assets relating to the Ordinary Shares and 2.0 per cent per annum of the net assets relating to the C Shares. In addition, the Manager receives an annual administration fee subject to a maximum of £100,000 excluding VAT (adjusted for the movement in RPI). Annual running costs are capped at 3.5 per cent of the net assets of the Company (excluding any performance fee payable to the Manager and irrecoverable VAT), any excess being refunded by the Manager by way of an adjustment to its management fee.

It is the Board's opinion that the continuing appointment of ISIS EP LLP on the terms agreed is in the best interests of shareholders as a whole.

Performance Incentive

The Manager may become entitled to receive a performance fee from the Company calculated by reference to the increase (if any) in the net asset value of the Company, calculated on the assumption that any dividends paid by the Company are re-invested by way of subscription for further shares (the 'Total Return').

No performance fee will be paid unless and until the Total Return on net proceeds of the Offers exceeds 8 per cent per annum (simple) over the period from the issue of shares under the 2001/2002 Offers to the end of the relevant accounting period. To the extent that the Total Return to the end of an accounting period exceeds this threshold, a performance fee (plus VAT) will be paid to the Manager of 20 per cent of the excess. The first performance fee will not be paid to the Manager unless and until the Total Return on the net proceeds of the Offers exceeds 40 per cent. In addition, the amount of any performance fee due which is paid in respect of an accounting period shall not exceed 5 per cent of the net asset value of the Company at the end of the year.

To take account of the proceeds from the 'C' Share Offer which will be held initially in cash and fixed interest securities, an annual threshold of only 2 per cent for the period to 31 December 2007 (simple) will apply to the funds raised under the Offer after which the existing arrangement described above will be applied. The performance fee will be capped at 5 per cent of the 'C' Share pool of assets.

In the event that the Company purchases shares or raises new capital, the threshold returns required in order for the Manager to earn a performance fee will be adjusted so that the Manager's entitlement is unaffected by the purchase or new capital raising.

Co-investment Scheme

The Co-investment Scheme requires that executive members of the Manager invest their own personal capital into five per cent of the ordinary shares of each and every unquoted investment excepting those life science transactions where ISIS is not the lead investor. By 31 December 2005, a total of £74,950 had been invested in ordinary shares of 6 unquoted investments by 21 executives.

Shares under the Scheme cannot be sold until each investment held by the four Baronsmead VCTs is sold contemporaneously. Gains for the executives will only be achieved if the Baronsmead VCTs make gains from the underlying investment. If the executive leaves before the sale of the investment, they may miss out on much of the potential value inherent in their Co-investment shares. In this way the Scheme can continue to attract, recruit, retain and incentivise members of the Manager.

Procedures are in place whereby the Board receives regular updates from the Managers regarding applicants of the Co-investment Scheme and the amounts committed by ISIS EP to each new unquoted investment. The Board will also review the Co-investment Scheme arrangements at each quarterly valuation meeting. An open dialogue is maintained between the Board and the Managers regarding the Scheme.

Auditors

PKF resigned as auditors to the Company on 28 June 2005. There are no matters in connection with their resignation which PKF wish to bring to the attention of shareholders or regulators. The Directors appointed KPMG Audit Plc as auditors to the Company and a resolution confirming their appointment will be submitted at the Annual General Meeting.

Directors' Authority to Allot Shares and to Disapply Pre-emption Rights

The authority proposed under Resolution 6 is required so that the Directors may offer existing shareholders the opportunity to add to their investment or to offer to potential shareholders an opportunity to invest in the Company in a tax efficient manner without the Company having to incur substantial costs. Any consequent modest increase in the size of the Company will, in the opinion of the Directors, be in the interests of shareholders generally and will not dilute their existing interest. Any such issues would only be made at a price greater than the net asset value per share and therefore would increase the assets underlying each Share. The issue proceeds would be available for investment in line with the Company's investment policy and may be used, in part, to purchase ordinary shares and C shares in the market.

Resolution No. 6 renews and extends (see 'Dividend Reinvestment' below) the Directors' authority to allot equity securities for cash without pre-emption rights applying in certain circumstances. This resolution would authorise the Directors, until the date falling 15 months after the date of the passing of the resolution or, if earlier, the conclusion of the next Annual General Meeting of the Company to issue Shares for cash without pre-emption rights applying by way of offer to existing shareholders, under the Dividend Reinvestment Scheme, or otherwise up to a maximum of 5,877,830 Shares (representing approximately 10 per cent of the Company's listed share capital as at 8 February 2006).

Dividend Reinvestment

The Directors offer shareholders the opportunity to reinvest their dividends by subscribing for new Ordinary Shares and C Shares in the Company.

The extension of the Directors' authority to allot equity securities for cash without pre-emption rights applying referred to above (see 'Directors' Authority to Allot Shares and to Disapply Pre-emption Rights') will enable the Directors to allot Ordinary Shares and C Shares when dividends are reinvested.

Summary Financial Statement

Directors' Authority to Purchase Shares

The current authority of the Company to make purchases of up to approximately 14.99 per cent of its issued share capital expires at the end of the Annual General Meeting and Resolution Nos. 7 and 8 seek renewal of such authority until the Annual General Meeting in 2007 (or the expiry of 15 months, if earlier). The price paid for shares will not be less than the nominal value nor more than the maximum amount determined by the rules of the UK Listing Authority at the time of purchase. This power will be exercised only if, in the opinion of the Directors, a repurchase would be in the best interests of shareholders as a whole. Any shares repurchased under this authority will either be cancelled or held in treasury for future re-sale in appropriate market conditions.

The Companies (Acquisition of Own Shares) (Treasury Shares) Regulations 2003 ('the Regulations') allow companies (such as the Company) to hold shares acquired by way of market purchase as treasury shares, rather than having to cancel them. Up to 10 per cent of each class of a Company's shares may be held in this way. Such shares may be subsequently cancelled or sold for cash.

This would give the Company the ability to re-issue treasury shares quickly and cost efficiently, and would provide the Company with additional flexibility in the management of its capital base.

Summary Directors' Remuneration Report

Directors' Fees

The Board consists solely of independent non-executive Directors and considers at least annually the level of the Board's fees, in accordance with the Combined Code on Corporate Governance. The Company Secretary provides information on comparative levels of Directors' fees to the Board in advance of each review.

The Board concluded following the review of the level of Directors' fees for the forthcoming year that the amounts should increase to £21,000 for the Chairman and £14,000 for the other Directors.

The Remuneration Committee is Mark Cannon Brookes (Chairman), Andrew Karney, Gillian Nott and Robert Owen. As the Company has no executive Directors, the Committee meets, at least annually, to determine the remuneration and terms of appointment of the Investment Manager.

Policy on Directors' Fees

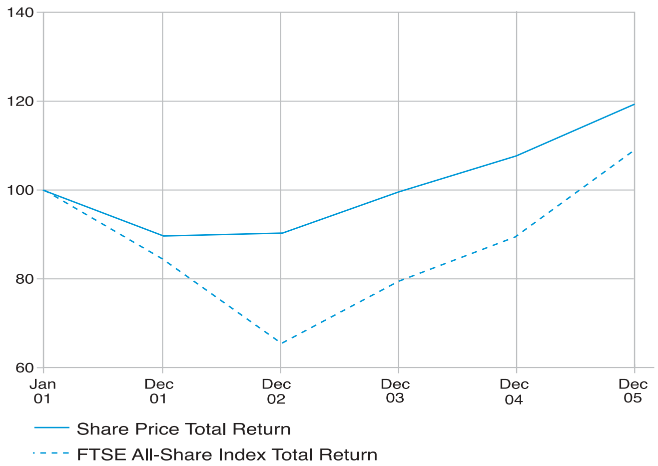
The Board's policy is that the remuneration of non-executive Directors should reflect the experience of the Board as a whole, be fair and comparable to that of other relevant venture capital trusts that are similar in size and have similar investment objectives and structures. Furthermore the level of remuneration should be sufficient to attract and retain the Directors needed to properly oversee the Company and to reflect the specific circumstances of the Company, the duties and responsibilities of the Directors and the value and amount of time committed to the Company's affairs. It is intended that this policy will continue for the year ended 31 December 2006 and subsequent years.

The fees for the non-executive Directors are determined within the limits set out in the Company's Articles of Association. The present limit is £56,720 per annum and a special resolution to increase this limit to £100,000 is included in the Notice of the Annual General Meeting, for shareholder approval. Non-executive Directors are not eligible for bonuses, pension benefits, share options, long-term incentive schemes or other benefits.

Company performance

The Board is responsible for the Company's investment strategy and performance, although the management of the Company's investment portfolio is delegated to the Manager through the investment management agreement, as referred to in the 'Report of the Directors'. The graph below compares from 29 January 2001 (the date the Company commenced trading) to 31 December 2005, the percentage change over each period in the total return (assuming all dividends are reinvested) to ordinary shareholders compared to the percentage change over each period in total shareholder return on a notional investment made up of shares of the same kinds and number as those by reference to which the FTSE All-Share Index is calculated. This index was chosen for comparison purposes, as it represents a comparable broad equity market index against which investors can measure the relative performance of the fund. An explanation of the performance of the Company is given in the Chairman's statement and Manager's review.

Share Price Total Return and FTSE All-Share Index Total Return Performance Graph



Directors' emoluments for the year (audited)

The Directors who served in the year received the following emoluments in the form of fees:

	Fees 2005 £	Fees 2004 £
Mark Cannon Brookes	**16,500**	**16,500**
Andrew Karney	**11,000**	**11,000**
Gillian Nott	**11,000**	**11,000**
Robert Owen	**11,000**	**11,000**

On behalf of the Board,

Mark Cannon Brookes
Chairman
8 February 2006

Independent Auditors' Statement

Independent Auditors' Statement to the Shareholders of Baronsmead VCT 3 plc

pursuant to section 251 of the Companies Act 1985

We have examined the summary financial statement set out on pages 16 to 20.

This statement is made solely to the Company's members, as a body, in accordance with section 251 of the Companies Act 1985. Our work has been undertaken so that we might state to the Company's members those matters we are required to state to them in such a statement and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our work, for this statement, or for the opinions we have formed.

Respective Responsibilities of Directors and Auditors

The Directors are responsible for preparing the summary annual report in accordance with applicable United Kingdom law. Our responsibility is to report to you our opinion on the consistency of the summary financial statement within the summary annual report with the full annual financial statements and the Directors' Report and the Directors' Remuneration Report, and its compliance with the relevant requirements of section 251 of the Companies Act 1985 and the regulations made thereunder. We also read the other information contained in the summary annual report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the summary financial statement.

Basis of Opinion

We conducted our work in accordance with Bulletin 1999/6 'The auditor's statement on the summary financial statement' issued by the Auditing Practices Board for use in the United Kingdom. Our report on the Company's full annual financial statements describes the basis of our audit opinion on those financial statements.

Opinion

In our opinion the summary financial statement is consistent with the full annual financial statements, the Directors' Report and the Directors' Remuneration Report of Baronsmead VCT 3 plc for the year ended 31 December 2005 and complies with the applicable requirements of section 251 of the Companies Act 1985 and the regulations made thereunder.

KPMG Audit Plc
Chartered Accountants
Registered Auditor
Edinburgh
8 February 2006

Income statement

for the year ended 31 December 2005

	Ordinary shares			C shares*			Total		
	2005 Revenue £'000	2005 Capital £'000	2005 Total £'000	2005 Revenue £'000	2005 Capital £'000	2005 Total £'000	2005 Revenue £'000	2005 Capital £'000	2005 Total £'000
Increase in fair value of investments held	–	3,793	3,793	–	2	2	–	3,795	3,795
Gain on disposal of investments	–	1,295	1,295	–	–	–	–	1,295	1,295
Income	1,461	–	1,461	92	–	92	1,553	–	1,553
Investment management fee	(278)	(1,026)	(1,304)	(14)	(42)	(56)	(292)	(1,068)	(1,360)
Other expenses	(251)	–	(251)	(27)	–	(27)	(278)	–	(278)
Profit/(loss) on ordinary activities before taxation	932	4,062	4,994	51	(40)	11	983	4,022	5,005
Tax on ordinary activities	(226)	226	–	(10)	10	–	(236)	236	–
Profit/(loss) on ordinary activities after taxation	706	4,288	4,994	41	(30)	11	747	4,258	5,005
Return per ordinary share/C share	2.09p	12.73p	14.82p	0.37p	(0.27)p	0.10p	2.06p	11.75p	13.81p

***The C Shares were launched on 10 October 2005.**

Reconciliation of Movements in Shareholders' Funds

for the year ended 31 December 2005

	2005 Ordinary Shares £'000	2005 C Shares £'000	2005 Total £'000
Opening shareholders funds' (as previously reported)	35,116	–	35,116
Less investments held at fair value changed from mid to bid basis	(528)	–	(528)
Add dividends accrued at 31 December 2004	900	–	900
Opening shareholders' funds (as restated)	35,488	–	35,488
Profit for the year	4,994	11	5,005
Deferred consideration	13	–	13
Increase in share capital in issue	303	17,011	17,314
Dividends paid	(1,572)	–	(1,572)
Closing shareholders' funds	39,226	17,022	56,248

	Ordinary shares			C shares*			Total		
	2005 Revenue £'000	2005 Capital £'000	2005 Total £'000	2005 Revenue £'000	2005 Capital £'000	2005 Total £'000	2005 Revenue £'000	2005 Capital £'000	2005 Total £'000
Dividends paid/proposed									
Final dividend for the year ended 31 December 2004 of 2.7p per ordinary share	298	596	894	–	–	–	298	596	894
Interim dividend for the year ended 31 December 2005 of 2.0p per ordinary share	169	509	678	–	–	–	169	509	678
Final dividend for the year ended 31 December 2005 of 3.5p per ordinary share	501	669	1,170	–	–	–	501	669	1,170
	968	1,774	2,742	–	–	–	968	1,774	2,742

Income statement

for the year ended 31 December 2004

	Ordinary shares		
	2004 (as restated) Revenue £'000	2004 (as restated) Capital £'000	2004 (as restated) Total £'000
Increase in fair value of investments held	–	4,029	4,029
Gain on disposal of investments	–	200	200
Income	987	–	987
Investment management fee	(248)	(745)	(993)
Other expenses	(253)	–	(253)
Profit on ordinary activities before taxation	486	3,484	3,970
Tax on ordinary activities	(76)	76	–
Profit on ordinary activities after taxation	410	3,560	3,970
Return per ordinary share	1.21p	10.49p	11.70p

Reconciliation of Movements in Shareholders' Funds

for the year ended 31 December 2004

	2004 Ordinary Shares £'000
Opening shareholders funds' (as previously reported)	32,994
Less investments held at fair value changed from mid to bid basis	(384)
Add dividends accrued at 31 December 2003	1,121
Opening shareholders' funds (as restated)	33,731
Profit for the year	3,970
Decrease in share capital in issue	(480)
Dividends paid	(1,733)
Closing shareholders' funds	35,488

	Ordinary shares		
	2004 (as restated) Revenue £'000	2004 (as restated) Capital £'000	2004 (as restated) Total £'000
Dividends paid/proposed			
Final dividend for the year ended 31 December 2003 of 3.3p per ordinary share	442	679	1,121
Interim dividend for the year ended 31 December 2004 of 1.8p per ordinary share	102	510	612
Final dividend for the year ended 31 December 2004 of 2.7p per ordinary share	298	596	894
	842	1,785	2,627

Balance Sheet

as at 31 December 2005

	2005 Ordinary Shares £'000	2005 C Shares £'000	2005 Total £'000	2004 (as restated) £'000
Fixed assets				
Investments held at fair value	**37,545**	**9,854**	**47,399**	33,696
Current assets				
Debtors	**414**	**1,828**	**2,242**	260
Cash	**1,933**	**5,815**	**7,748**	1,951
	2,347	**7,643**	**9,990**	2,211
Creditors (amounts falling due within one year)	**(666)**	**(475)**	**(1,141)**	(419)
Net current assets	**1,681**	**7,168**	**8,849**	1,792
Total assets less current liabilities	**39,226**	**17,022**	**56,248**	35,488
Capital and reserves				
Called-up share capital	**3,477**	**8,947**	**12,424**	3,335
Share premium account	**3,920**	**8,064**	**11,984**	1,786
Capital redemption reserve	**247**	**–**	**247**	175
Revaluation reserve	**5,093**	**2**	**5,095**	5,021
Profit and loss account	**26,489**	**9**	**26,498**	25,171
Equity shareholders' funds	**39,226**	**17,022**	**56,248**	35,488
Net asset value per share				
– Basic	**117.31p**	**95.13p**	**–**	106.38p

The financial statements were approved by the Board of Directors on 8 February 2006 and were signed on its behalf by:

MARK CANNON BROOKES (Chairman)

Notes to the Accounts

1. (a) Restatement of balances as at and for the year ended 31 December 2004

There have been a number of changes to financial reporting standards that have come into effect from 1 January 2005. The principal ones affecting the Company are the requirement to value quoted investments at fair value and only reflect dividends to shareholders when paid. The effect of revised UK GAAP is set out below:

	Notes	(Audited) Previously reported 31 December 2004 £'000	Effect of transition to revised UK GAAP £'000	Restated 31 December 2004 £'000
Investments	1	34,224	(528)	33,696
Current assets		2,211	–	2,211
Creditors: amounts falling due within one year	2	(1,319)	900	(419)
Total assets less current liabilities		35,116		35,488
Capital and reserves				
Called up share capital		3,335	–	3,335
Share premium		1,786	–	1,786
Capital redemption reserve		175	–	175
Revaluation reserve	1	5,549	(528)	5,021
Profit and loss account	2	24,271	900	25,171
		35,116		35,488

Notes to the reconciliation

1. Investments are designated as held at fair value under revised UK GAAP and are carried at bid prices which total their fair value of £33,696,000. Previously, under UK GAAP, they were carried at mid prices. The aggregate differences, being a revaluation downwards of £528,000, also decreases the Revaluation reserve.
2. No provision has been made for the final dividend on the ordinary shares for the year ended 31 December 2004 of £900,000. Under revised UK GAAP, dividends are not recognised until paid.

1. (b) Reconciliation of the Profit and Loss Account to the Income Statement for the year ended 31 December 2004

Under revised UK GAAP the Income Statement is the equivalent of the Profit and Loss Account reported previously.

	Notes	2004 £'000
Total transfer from reserves per the Profit and Loss Account (as previously reported)		(1,571)
Add unrealised gains on revaluation of investments	1	4,173
Add back dividends paid and proposed	2	1,512
Investments held at fair value changed from mid to bid basis at 31 December 2003	3	384
Investments held at fair value changed from mid to bid basis at 31 December 2004	3	(528)
Net profit per the Income Statement		3,970

Notes to the reconciliation

1. Unrealised gains on revaluation of investments are reflected in the Income Statement under revised UK GAAP.
2. Ordinary dividends declared and paid during the year are dealt with through the Movements in Shareholders' Funds.
3. The portfolio valuations at 31 December 2003 and 31 December 2004 are required to be valued at fair value under revised UK GAAP. These values differ from the previous valuations by £384,000 and £528,000 respectively.

Notes to the Accounts

2. Restatement of opening balances as at 31 December 2003

At 1 January 2005 the Company adopted revised UK GAAP. The following is a reconciliation of the results as at and for the year ended 31 December 2003, previously reported under UK GAAP, to the revised UK GAAP results.

	Notes	(Audited) Previously reported 31 December 2003 £'000	Effect of transition to revised UK GAAP £'000	Restated 31 December 2003 £'000
Investments	1	23,946	(384)	23,562
Current assets		11,031	–	11,031
Creditors: amounts falling due within one year	2	(1,983)	1,121	(862)
Total assets less current liabilities		32,994		33,731
Capital and reserves				
Called up share capital		3,396	–	3,396
Share premium		1,014	–	1,014
Capital redemption reserve		26	–	26
Revaluation reserve	1	1,057	(384)	673
Profit and loss account	2	27,501	1,121	28,622
		32,994		33,731

Notes to the reconciliation

1. Investments are designated as held at fair value under revised UK GAAP and are carried at bid prices which total their fair value of £23,562,000. Previously, under UK GAAP they were carried at mid prices. The aggregate differences, being a revaluation downwards of £384,000, also decreases the Revaluation reserve.
2. No provision has been made for the final dividend on the ordinary shares for the year ended 31 December 2003 of £1,121,000. Under revised UK GAAP, dividends are not recognised until paid.

Notice of Annual General Meeting

Notice is hereby given that the Annual General Meeting of Baronsmead VCT 3 plc will be held at the offices of ISIS EP LLP, Exchange House, Primrose Street, London EC2A 2NY, on 16 March 2006 at 11.00 am for the following purposes:

To consider and, if thought fit, pass the following Resolutions:

Ordinary Business

1. That the Report and Accounts for the year to 31 December 2005 be received.
2. To approve payment of a final dividend of 3.5 pence per Ordinary Share (comprising 1.5 pence revenue and 2.0 pence capital).
3. That Mark Cannon Brookes, who retires by rotation, be re-elected as a Director.
4. That the Directors' Remuneration Report for the year to 31 December 2005 be approved.
5. That KPMG Audit Plc, be appointed as Auditors and that the Directors be authorised to determine their remuneration.

Special Business

Special Resolutions

6. That :

(a) the Directors of the Company (the ''Directors'') be and are hereby empowered, pursuant to section 95(1) of the Companies Act 1985 (the ''Act'') and in addition to any existing power under section 95 of the Act, to allot equity securities for cash pursuant to the authorities given in accordance with section 80 of the Act, granted on 23 March 2005, as if section 89(1) of the Act did not apply to any such allotment, provided that this power shall be limited to the allotment of equity securities in connection with:

(i) an offer of securities, open for acceptance for a period fixed by the Directors, to holders of Ordinary Shares of 10p each and C Shares of 50p each in the Company and such other equity securities of the Company as the Directors may determine on the register on a fixed record date in proportion (as nearly as may be) to their respective holdings of such securities or in accordance with the rights attached thereto (but subject to such exclusions or other arrangements as the Directors may deem necessary or expedient to deal with fractional entitlements that would otherwise arise or with legal or practical problems under the laws of, or the requirements of any recognised regulatory body or any stock exchange in, any territory or otherwise howsoever);

(ii) the dividend reinvestment plan as more particularly described in the Report of Directors;

(iii) (otherwise than pursuant to sub-paragraphs (i) and (ii) above) up to an aggregate amount of £1,547,771;

and shall expire on the date falling 15 months after the date of the passing of this resolution or, if earlier, at the conclusion of the next Annual General Meeting of the Company, except that the Company may, before such expiry, make offers or agreements which would or might require equity securities to be allotted after such expiry; and in this resolution ''allot'' and ''allotment'' shall be construed in accordance with section 94(3A) of the act.

(b) words and expressions defined in or for the purposes of Part IV of the Act shall bear the same meanings in this resolution.

Notice of Annual General Meeting

7. That the Company is hereby generally and unconditionally authorised to make market purchases (within the meaning of section 163 of the Companies Act 1985) of Ordinary Shares of 10p each in the Company (‘‘Ordinary Shares’’), provided that:

   (a) the maximum number of Ordinary Shares hereby authorised to be purchased shall be 5,012,450;

   (b) the minimum price which may be paid for each Ordinary Share is 10p;

   (c) the maximum price which may be paid for an Ordinary Share shall be equal to the maximum amount permitted to be paid in accordance with the rules of the UK Listing Authority in force as at the date of purchase;

   (d) the authority hereby conferred shall expire at the conclusion of the Annual General Meeting of the Company in 2007 or, if earlier, on the expiry of 15 months from the passing of this resolution, unless such authority is renewed prior to such time; and

   (e) the Company may make a contract to purchase Ordinary Shares under the authority hereby conferred prior to the expiry of such authority which will or may be completed or executed wholly or partly after the expiration of such authority.

8. That the Company is hereby generally and unconditionally authorised to make market purchases (within the meaning of section 163 of the Companies Act 1985) of C shares of 50p each in the Company (‘‘C shares’’), provided that:

   (a) the maximum number of C share capital hereby authorised to be purchased shall be 3,597,560;

   (b) the minimum price which may be paid for each C share is 50p;

   (c) the maximum price which may be paid for an C share shall be equal to the maximum amount permitted to be paid in accordance with the rules of the UK Listing Authority in force as at the date of purchase;

   (d) the authority hereby conferred shall expire at the conclusion of the Annual General Meeting of the Company in 2007 or, if earlier, on the expiry of 15 months from the passing of this resolution, unless such authority is renewed prior to such time; and

   (e) the Company may make a contract to purchase C shares under the authority hereby conferred prior to the expiry of such authority which will or may be completed or executed wholly or partly after the expiration of such authority.

9. That in Article 101 of the Company’s Articles of Association, the reference to Directors’ remuneration of £50,000 (adjusted for RPI) be amended to £100,000.

By Order of the Board

Rhonda Nicoll
for F&C Asset Management plc
Secretary
80 George Street

Edinburgh EH2 3BU

8 February 2006

Pursuant to regulation 41 of the Uncertificated Securities Regulations 2001, the Company has specified that only those shareholders registered on the register of members of the Company as at 6.00 pm on 14 March 2006, or in the event that the meeting is adjourned, on the register of members 48 hours before the time of the meeting, shall be entitled to attend and vote at the meeting in respect of the number of shares registered in their name at that relevant time. Changes to entries on the register of members after 6.00 pm on 14 March 2006, or in the event that the meeting is adjourned to a later time, on the register of members 48 hours before the time of any adjourned meeting, shall be disregarded in determining the rights of any person to attend and vote at the meeting.

A member who is entitled to attend and vote at this meeting is entitled to appoint one or more proxies to attend and, on a poll, vote on his/her behalf. Such a proxy need not also be a member of the Company.

To be valid, a Proxy Card must be lodged with the Company’s Registrar, Computershare Investor Services PLC, PO Box 1075, The Pavilions, Bridgwater Road, Bristol BS99 3ZZ at least 48 hours before the meeting. A Proxy Card for use by shareholders is enclosed with this Report. Completion of the Proxy Card will not prevent a shareholder from attending the meeting and voting in person.

No Director has a contract of service with the Company.

Baronsmead VCT 3 plc

PROXY

I/We ____
(BLOCK LETTERS PLEASE)

of ____

being a member of Baronsmead VCT 3 plc, hereby appoint the Chairman of the meeting, or*

____

as my/our proxy to vote for me/us on my/our behalf at the Annual General Meeting of the Company, to be held on 16 March 2006, on the following Resolutions to be submitted to the meeting and at any adjournment thereof and at their discretion on any matter arising at such meeting.

Please indicate with an 'X' in the appropriate spaces how you wish your votes to be cast. Unless otherwise instructed, the proxy will vote as he thinks fit or abstain.

Ordinary Resolutions	For	Against	Vote Withheld
1. To receive the Report and Accounts for the year to 31 December 2005.			
2. To approve payment of a final dividend of 3.5 pence per Ordinary Share.			
3. To re-elect Mark Cannon Brookes as a Director.			
4. To approve the Directors' Remuneration Report for the year to 31 December 2005.			
5. To appoint KPMG Audit Plc as Auditors, and to authorise the Directors to determine their remuneration.			
Special Resolutions			
6. To renew the Directors' authority to disapply statutory pre-emption rights.			
7. To renew the Directors' authority to buy-in ordinary shares.			
8. To renew the Directors' authority to buy-in C shares.			
9. That the limit for Directors' remuneration be increased from £50,000 to £100,000.			

Signature ____

Dated this ______________________ day of ______________________ 2006

Notes

*You may, if you wish, in the space provided insert the name(s) of the person(s) of your choice to attend and vote at the meeting on your behalf.

In the case of a corporation, the proxy must be either under its common seal or under the hand of an officer.

In order to have effect, the proxy must be deposited at the Company's Registrars, Computershare Investor Services PLC, PO Box 1075, The Pavilions, Bridgwater Road, Bristol BS99 3ZZ at least 48 hours before the time of the meeting or any adjournment thereof together where appropriate with the power of attorney under which it is signed or a notarially certified copy of such power.

In the case of a joint holding, a proxy need only be signed by one joint holder. If more than one such joint holder lodges a proxy only that of the holder first on the Register will be counted.

Any alterations made in this proxy should be initialled.

Completion of a proxy shall not prevent a shareholder from attending the Annual General Meeting and voting in person should you decide to do so.

SECOND FOLD

BUSINESS REPLY SERVICE
Licence SWB 1002

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Computershare Investor Services PLC
PO Box 1075
The Pavilions
Bridgwater Road
Bristol BS99 3ZZ

FIRST FOLD

THIRD FOLD AND TUCK IN

Shareholder Information

Dividends

Interim dividends are paid to shareholders in September. Final dividends are paid to shareholders in March. Shareholders who wish to have dividends paid directly into their bank account rather than by cheque to their registered address can complete a Mandate Form for this purpose. Mandates can be obtained by telephoning the Company's registrar on 0870 703 0137 or by writing to them at, Computershare Investor Services PLC, PO Box 82, The Pavilions, Bridgwater Road, Bristol BS99 7NH.

Dividend Reinvestment Scheme

The Company operates a dividend reinvestment scheme to enable shareholders to buy shares using their dividends. The shares issued via this scheme are new shares and attract VCT tax reliefs for eligible investors. Details can be obtained from the Company Secretary.

Share Price

The Company's Ordinary Shares are listed on the London Stock Exchange. The mid-price of the Company's Ordinary Shares is given daily in the *Financial Times* in the Investment Companies section of the London Share Service. Share price information can also be obtained from many financial websites.

Trading Shares

The Company's Ordinary Shares can be bought and sold in the same way as any other quoted company on the London Stock Exchange via a stockbroker. The market makers for Baronsmead VCT 3 plc are:

- Teather & Greenwood (020 7426 9000)
- Winterfloods (020 7621 0004)
- UBS Warburg (020 7567 8000)

Please call the Company Secretary if you or your adviser have any questions about this process.

Financial Calendar

16 March 2006	Annual General Meeting – offices of ISIS EP LLP
20 March 2006	Final dividend paid for the year to 31 December 2005
August 2006	Announcement of interim results and posting of interim report
September 2006	Interim dividend paid
February 2007	Announcement of final results for year to 31 December 2006

VCT Workshop

A workshop for shareholders and their advisors is being held on 16 March 2006 and will be held at the office of the Investment Managers following the Annual General Meeting, which commences at 11.00 am.

Notification of Change of Address

Communications with shareholders are mailed to the registered address held on the share register. In the event of a change of address or other amendment this should be notified to the Company's registrar, Computershare Investor Services PLC, under the signature of the registered holder.

Enquiries

If shareholders have any questions or comments about their investment, please contact:

David Thorp, Investment Manager		or	Rhonda Nicoll, Company Secretary
Telephone:	020 7506 1609		0131 465 1074
Fax:	020 7601 1787		0131 225 2375
Address:	Exchange House		80 George Street
	Primrose Street		Edinburgh
	London EC2A 2NY		EH2 3BU
E-mail:	david.thorp@isisep.com		rhonda.nicoll@fandc.com

F&C Broker Support Helpline: 08457 99 22 99.

*Telephone calls may be recorded.

Registrar enquiries

Computershare Investor Services PLC contact details

Shareholder Helpline	0870 703 0137
e-mail	web.queries@computershare.co.uk
Investor Centre	www-uk.computershare.com/investor

Additional information

The information provided in this report has been produced for shareholders to be informed of the activities of the Company during the period it covers. ISIS EP LLP does not give investment advice and the naming of companies in this report is not a recommendation to deal in them.

Baronsmead VCT 3 plc is managed by ISIS EP LLP which is Authorised and regulated by the FSA. Past performance is not necessarily a guide to future performance. Stockmarkets and currency movements may cause the value of investments and the income from them to fall as well as rise and investors may not get back the amount they originally invested. Where investments are made in unquoted securities and smaller companies, their potential volatility may increase the risk to the value of, and the income from, the investment.

Corporate Information

Directors
Mark Cannon Brookes (Chairman)*
Andrew Lumsdaine Karney†
Gillian Nott OBE
Robert Richardson Owen

Secretary
F&C Asset Management plc
80 George Street
Edinburgh EH2 3BU

Registered Office and Investment Managers
ISIS EP LLP
Exchange House
Primrose Street
London EC2A 2NY

Baronsmead VCT 3 plc
Registration Number: 04115341

VCT Status Adviser
PricewaterhouseCoopers LLP
1 Embankment Place
London WC2N 6RH

Registrars and Transfer Office
Computershare Investor Services PLC
PO Box 82
The Pavilions
Bridgwater Road
Bristol BS99 7NH
Tel: 0870 703 0137

Brokers
Teather & Greenwood Limited
Beaufort House
15 St Botolph Street
London EC3A 7QR

Auditors
KPMG Audit Plc
Saltire Court
20 Castle Terrace
Edinburgh EH1 2EG

Solicitors
Norton Rose
Kempson House
Camomile Street
London EC3A 7AN

* Chairman of the Audit Committee
† Senior Independent Director

Pillans & Waddies, Edinburgh. 309845