

# SOPHEON PLC

(“Sopheon”, the “Group” or the “Company”)

## Preliminary Audited Results For The Year To 31 December 2006

Sopheon plc, the international provider of software and services that improve the financial return from innovation and product development investments, announces its results for the year ended 31 December 2006 together with an outlook for the current year. Sopheon shares are traded on AIM in London and on the Euronext Amsterdam.

### HIGHLIGHTS:

- Revenue for the year was £6.0m (2005: £4.7m) and the EBITDA result for the year was a profit of £33,000 (2005: £746,000 loss).
- Sixteen new customers were added in the year, with 20 extension orders from existing customers. By year end there were 87 companies throughout the world that had licensed our software, and the total number of individual users from within those organizations surpassed 27,000.
- We released the Accolade<sup>®</sup> Accelerators, a group of new modules which expand Accolade’s out-of-the-box capabilities in key process automation areas such as Stage-Gate<sup>®</sup> implementation, roadmapping and planning, and product portfolio management (PPM).
- Sopheon clients participating in a benchmark study by Aberdeen Group on PPM best practices ranked best-of-class in a variety of key areas including widespread process adoption, speed of portfolio management decisions, meeting cost goals and hitting deadlines.
- Revenue growth in Europe was particularly strong. Strategically we began to move beyond the specialty chemicals, materials and food & beverage markets that have historically been our targets and secured our first customers in the discrete manufacturing industries.

Barry Mence, Chairman, commented: *“Past reports to our shareholders have chronicled our progress toward profitability. With today’s announcement, we acknowledge that we achieved breakeven EBITDA for the first time. This milestone, coupled with significant strides during 2006 in virtually every area of our business, has set the stage for Sopheon’s next important phase of growth. We know that we must balance the need to drive the Company forward strategically with a continued focus on financial performance. We’re looking forward to another very promising and exciting year.”*

### FOR FURTHER INFORMATION CONTACT:

<b>Barry Mence, Chairman</b>	<b>Sopheon plc</b>	<b>Tel : + 44 (0) 1483 685 735</b>
<b>Arif Karimjee, CFO</b>		
<b>Andrew Tan</b>	<b>Hansard</b>	<b>Tel : + 44 (0) 207 245 1100</b>
		<b>+ 44 (0) 7957 203 685</b>
<b>Floor van Maaren</b>	<b>Citigate First Financial</b>	<b>Tel : + 31 (0) 205 754 010</b>

### About Sopheon

Sopheon (LSE:SPE) is an international provider of software and services that help organizations improve the business impact of product innovation. The Sopheon Accolade<sup>®</sup> system automates gate or phase-based product development processes and provides strategic decision support that allows companies to increase revenue and profits from new products. Sopheon is listed on the AIM Market of the London Stock Exchange and on the Euronext in the Netherlands. For more information, please visit [www.sopheon.com](http://www.sopheon.com).

Accolade<sup>®</sup> is a registered trademark of Sopheon plc.  
Stage-Gate<sup>®</sup> is a registered trademark of the Product Development Institute.

## **INTRODUCTION**

We achieved much in 2006. In headline terms, we grew revenues to £6.0m from £4.7m in 2005. This was underpinned by 36 license orders and extensions, taking the total number of licensed customers to 87. Full-year revenues were 30% higher than the prior year, and we achieved breakeven EBITDA (earnings before interest, tax, depreciation and amortization) for the first time in our history. Coming into 2007 we continue to enjoy high levels of activity in our sales pipeline, reinforcing our belief that we are the leading independent vendor in the market for Product Portfolio Management (PPM) solutions. This market is projected to triple in size between 2006 and 2010. Implementing a system like Accolade represents a serious commitment for any organization and this continues to weigh on our sales cycles. However, as our business matures in scale we believe that this area, which has always brought unpredictability to our revenues, will show improvement.

At the start 2006, we made a strategic decision to move beyond the chemicals, materials, and food & beverage markets that have historically been our focus. In particular, we began to pursue opportunities in non-food & beverage segments of the consumer packaged goods sector. This effort encompassed marketing programs and targeted business development activity. It led to our securing a number of new clients, exemplified by Timex, the leading watchmaker in North America, and Electrolux, the world's leading international appliance company. Leveraging our partnerships will be critical to achieving our longer term goals in this area, and we were delighted to announce our first major automobile customer, secured in collaboration with Hewlett-Packard. Geographical reach was also extended with sales for the first time in Scandinavia, France, Israel, Portugal and New Zealand. Some of these were secured through our growing reseller channel.

## **RESULTS**

Sopheon's consolidated turnover grew to £6.0m (2005: £4.7m). This overall result included a strong new sales performance by our European business, which grew revenues by 68% in the year. This was offset by a relatively flat performance in the US, accentuated by the weakening of the US dollar in global currency markets. This growth pattern is the opposite of what took place in 2005, when we experienced stronger growth in North America. Over the years we have invested heavily in maintaining a truly international footprint for our business and this is proving to be both a key differentiator in our business development and implementation efforts, and a source of balance for our revenue performance. Since the introduction of Accolade six years ago, our average annualized growth in US dollar terms continued to hold at approximately 50%.

Overall, Sopheon's revenues for 2006 were 30% higher than the preceding year. Unlike in 2005, however, revenues were evenly spread across the first and second half. Although we look forward to strong growth, we believe that our performance in any particular period will remain relatively unpredictable for some time to come. This is a function of sales cycle time and of transaction value.

## **BUSINESS MIX**

During 2006 we closed 16 new license customers and 20 extension orders from existing customers. In past statements we have noted the growing influence of larger sales, which have the potential to increase revenue volatility, but also underpin growth. Such transactions also have the effect of pulling through substantial consulting and other service opportunities due both to the more extensive nature of the implementations in question, and also to a growing trend of existing customers returning to Sopheon to support expansion efforts through additional configuration and consultancy work following the initial roll-out. During 2006, we enjoyed £0.6m of such repeat services business.

In addition to license and services revenues, our third major revenue stream is recurring maintenance income which coming into 2007 has grown to £1.7m, compared to £1.4m a year before.

In 2006 our business delivered a 37:25:38 ratio of license, maintenance, service respectively compared to 40:25:35 in the prior year. We expect our consulting revenues to continue to grow strongly and to provide another source of stability and maturity to our business. However, we believe that this will be offset as a proportion of our total revenues by the effect of license business coming through our

expanding reseller network, for which associated services work is unlikely to be performed by Sopheon. We expect maintenance to hold at approximately a quarter of our overall revenues.

As we first signaled in 2005, the higher proportion of services in our revenue mix has required us to make extensive use of subcontractor partners. This requirement has increased as the scope of deployments and the geographic spread of our customers have continued to expand. A recent example was our Accolade installation at Electrolux, where we contracted with Arthur D Little to perform the bulk of the implementation work. In spite of this we achieved an overall gross margin, measured after deducting the costs of such partners as well as our own client services resources, of 72% (2005: 73%).

## **RESEARCH & DEVELOPMENT EXPENDITURE**

During 2006, our R&D effort focused on three different areas. During the year we developed and launched the Accolade Accelerators, a group of new applications which expand Accolade's out-of-the-box capabilities in key process automation areas such as Stage-Gate<sup>®</sup> implementations, roadmapping and planning, and product portfolio management. The Accelerators feature built in best-practice content and reports that allow a company to leverage Accolade in these areas with much reduced configuration effort.

In addition, we completed the majority of the effort required to transfer our legacy healthcare protocol management system onto the Accolade platform, and our hospital clients have now started the upgrade process. Finally, we continued to invest substantial resources in developing the next release of Accolade which is due in late 2007. This release will bring a host of new features to our flagship offering, enabling Sopheon to maintain its leadership position and expand to new markets.

As a result of the above, £0.5m (2005: £0.4m) of our 2006 R&D expenditure met the criteria of IAS38 for capitalization.

## **OPERATING COSTS**

As noted in the Remuneration Report a bonus was earned by the majority of the Group's employees in respect of the 2006 performance. This has resulted in an increase in payroll costs relative to 2005 in all areas, with the principal exception of members of Sopheon's sales teams for whom incentives are tied to individual or territory results.

More specifically, if the effect of the capitalization and amortization of R&D costs is added back, we increased total R&D expenditure by £0.2m. In particular, this reflects the formation of an internal organization that we call RAD, short for Research & Application Development. The Group is chartered to work with clients to investigate and create new software applications built on the Accolade platform that would extend the utility and value of the core offering; the Accelerators described above were developed by the RAD team.

Distribution costs are slightly lower than the previous year in spite of the higher revenues. Some of this apparent reduction is attributable to the reclassification of certain employees into the RAD team; however, other than the bonus noted above both administrative and distribution costs remained tightly contained. Although we do not currently plan to increase direct sales representation in 2007, we do plan to raise investment in channel development and marketing in order to continue to drive growth.

We achieved a breakeven consolidated EBITDA position (2005: £0.75m loss). This total reflects a deduction of share based payments of £0.1m (2005: £0.2m). It excludes depreciation and amortization charges of £0.3m (2005: £0.5m) for the year. Including these items, the resultant retained loss for the year was £0.3m (2005: £1.2m) reducing the loss per ordinary share to 0.2p (2005: 0.9p).

## **FINANCING AND BALANCE SHEET**

Net assets at the end of the year stood at £1.6m (2005: £2m) and include £0.8m (2005: £0.8m) being the net book value of capitalized research and development arising from the application of IAS38. Cash resources at 31 December 2006 amounted to £1.0m (2005 - £2.0m). A surge of sales at the end of the year resulted in trade receivables of £2.5m compared to £1.7m at the end of 2005.

At the end of 2005 Sopheon renewed its €10 million equity line of credit facility with GEM Global Yield Fund Limited until December 2007, securing continued access to a source of equity-based funding over which the Company retains a substantial degree of control. The facility was not used during 2006 and over 90% of the original equity line remains untapped.

## **MARKET**

Sopheon's Accolade addresses one of the most universal challenges facing manufacturing companies today. It is the challenge of operating research and development – traditionally a black box area of business – as a repeatable process, so that results can be predicted and continuously improved. Accolade automates the innovation process, enabling companies to strengthen the alignment between their innovation strategies and product development activity, gain a clear view of the commercial potential of projects in their portfolios, and readily access other details of product innovation initiatives in progress.

Accolade belongs to a major class of software applications that concentrate on supporting Product Life-cycle Management (PLM). These solutions help companies create and execute their product strategies. ARC Advisory group states that the PLM market totalled nearly \$7 billion in 2005, and will nearly double to more than \$13 billion by the end of 2010. Sopheon is focused on Product Portfolio Management (PPM) which analysts indicate is among the fastest growing submarkets within PLM, and they expect its exceptional rate of expansion to continue. While most areas of product life cycle management concentrate on the engineering or technical challenges involved in developing and managing a product, PPM addresses the business challenges. Analysts view PPM as a strategically critical applications area. Their research has determined that adoption of PPM methodologies by cross-functional teams engaged in product development is critical to achieving business impact and success.

Most companies have tried to build their innovation processes around commonly used methodologies such as Stage-Gate<sup>®</sup>, PACE<sup>®</sup> and waterfall. But studies have shown that, when companies attempt to deploy these methodologies without automating them, they fail 48% of the time. Independent research has confirmed that Accolade users have a significant edge over other companies endeavouring to implement product portfolio management processes. In late 2006, Aberdeen Group, the IT research and advisory firm, completed a benchmarking report on PPM best-practices for which they surveyed more than 150 manufacturers. Sopheon clients participating in the study ranked best-of-class in a variety of key areas including widespread process adoption, speed of portfolio management decisions, meeting cost goals and hitting deadlines.

In 2006 we saw considerable movement in the PLM market among both established suppliers and new entrants. Many of the more established PLM vendors were involved in mergers and acquisitions. We expect that this will continue in 2007, as evidenced by the recent high-profile acquisition of UGS by Siemens. These changes are introducing some confusion in the marketplace, but they are also increasing demand. These factors will continue to challenge Sopheon to sustain its position of market leadership. Our response to this challenge is the five part strategy set out below.

## **GROWTH STRATEGY**

*Expand Within Client Base.* During 2006, we received 20 license orders from existing customers intent on extending the use of our software across their organizations. This is up from 13 extension orders in 2005, further validating that we have a sticky application with strong growth potential inside our client base. The number of Accolade end-users grew by 30% in 2006 to more than 27,000. This rapid escalation is traceable partly to the fact that, while early implementations of Accolade were on the department level, the solution is increasingly being deployed on an enterprise-wide scale. A number of our customers are using the system throughout their global operations. Accolade users can now be found in 58 countries worldwide.

*Expand Within Target Markets.* Our primary focus has been on manufacturers of chemicals, paper and, within the consumer packaged goods sector, food & beverage producers. Sopheon signed sixteen new customers in 2006, seventy-five percent of which were in our target verticals. We exited the year with 87 clients. In each of the markets we have targeted, our current level of penetration is minimal, leaving substantial room for growth. We will continue to focus on this opportunity in 2007.

*Expand Product.* In 2006, Sopheon convened its first Product Advisory Council (PAC) sessions in both North America and Europe. The PAC group is comprised of executive-level decision-makers from client companies in a mix of industries. Their input related to such areas as our product road maps and go-to-market strategies has been an extremely valuable input to the next major version of Accolade, scheduled for commercialization in late 2007.

In late 2006, Sopheon introduced a set of add-on applications for its Accolade solution. Referred to collectively as Accolade Accelerators, the new offerings are designed to enable companies to more quickly achieve the next level of maturity in the governance of their innovation processes and realize the associated higher levels of business performance.

In October of 2006, we announced that we would augment the current use of Microsoft tools within Accolade by integrating the software system with Microsoft Office Project Server 2007. Adoption of the Microsoft product will broaden and deepen aspects of Accolade's capacity to provide governance support for the product innovation process.

*Expand to New Markets.* Throughout its history, Sopheon has made ongoing, nominal investments in select new markets as a way of evaluating opportunities to leverage existing technologies and drive additional business growth. In 2006, Sopheon announced its expansion into non-food & beverage areas of the CPG (Consumer Packaged Goods) market. Today we have a growing client base in this vertical, illustrated by such industry leaders as Electrolux, Freudenberg Household Products, Nautilus, Reckitt Benckiser, and Timex. These customers include several CPG companies that operate in light discrete manufacturing. Our initial experiences in discrete will dictate the level of investment and effort we undertake towards growing in the large discrete manufacturing market – which includes the auto, defence and aerospace industries. Leveraging our partnerships will be critical to achieving our longer term goals in this area, and we were delighted to announce our first major automobile customer, secured in collaboration with Hewlett-Packard.

Sopheon continues to support its historic position as a supplier to the healthcare protocol market. Our Qualiflow<sup>®</sup> technology is used by healthcare institutions to provide doctors, nurses and other medical practitioners with procedural guidelines at the point of care. Conversion of the Qualiflow solution to operate on the Accolade platform is expected to be completed in 2007. Expansion of our protocol management market activity is on hold until this platform transition has been proven successful. Sopheon will then readdress its strategies for growing this aspect of our business.

*Expand Partnerships.* Sopheon remains committed to growing its business through partnerships. We also know that it takes time and investment to develop a strong network of partners that can add value to the Company.

The Microsoft Office Project 2007 integration initiative is the latest advance in a continuing strategic alliance between Sopheon and Microsoft. Since its inception, Sopheon's Accolade software has incorporated Microsoft products such as Microsoft Office Project Server and other components of the Microsoft Office system, focusing the capabilities of these horizontal platforms on helping manufacturers increase the business impact of new product innovation. Based on the strength and success of Sopheon's business application, the alliance between Sopheon and Microsoft has steadily grown. Sopheon has earned Microsoft's designation as a Gold Certified and "managed" partner.

In 2006, we concentrated on working with existing reseller partners to deepen their knowledge and understanding of our value proposition, the dynamics of our markets and the capabilities of our product offerings. Partner relationships resulted in Sopheon's signing its first clients in Israel, New Zealand, Portugal and Sweden, providing a critical foundation of local references to support expansion in these nascent sales territories. We were also active with our consulting partners, working together on a number of Accolade implementations in the U.S. and Europe. We expect 2007 to be a year of further collaboration and business development efforts with our partners. Plans call for a continued focus on our existing network, as well as the addition of a small number of new members.

## **PEOPLE**

Our ability to deliver value to our customers is a testament to Sopheon people in all parts of our company, many of whom have been working tirelessly for several years to build the business we have today. We thank them for their contribution to our growing success.

Sopheon's executive management team has also been in place for several years and comprises a team of five, which includes the three executive directors being Barry Mence the chairman, Andy Michuda the CEO and Arif Karimjee the CFO, in addition to Paul Heller our CTO and Huub Rutten our head of research. The Sopheon plc board includes the three executive directors, in addition to our three non-executive directors Stuart Silcock, Dan Metzger and Bernard Al who bring a wealth of knowledge and experience to our business.

## **OUTLOOK**

With the achievement of a breakeven EBITDA result, our business crossed a financial milestone during 2006. As we approach the next milestone of 100 licensees for our software, the scale and maturity for which we have been striving since the launch of Accolade six years ago is, we believe, finally coming through. This is contributing both to rising revenue stability, and to rising market recognition. As set out in more detail above, we will build on our achievements by attending to five key areas:

- Secure more business from our existing customer base
- Extend our hold in established chemicals, materials, food and beverage markets
- Expand the Accolade product in depth, functionality, integration and scalability
- Enter new vertical markets
- Develop and expand our partner network

In addition, we will carefully consider potential acquisitions that offer both strategic and operational benefits. As always, we recognize the need both to drive Sopheon forward strategically, and to stay focused on financial performance. This challenge will continue to shape our thinking in the exciting times ahead.

**SOPHEON PLC**

**CONSOLIDATED INCOME STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2006**

	<i>2006</i>	<i>2005</i>
	<i>£'000</i>	<i>£'000</i>
<b>Turnover – continuing activities</b>	<b>6,045</b>	<b>4,664</b>
Cost of sales	<u>(1,690)</u>	<u>(1,264)</u>
<b>Gross profit</b>	<b>4,355</b>	<b>3,400</b>
Distribution expenses	2,401	2,473
Research and development expenses	1,028	974
Administrative expenses	<u>1,232</u>	<u>1,175</u>
<b>Operating loss</b>	<b>(306)</b>	<b>(1,222)</b>
Investment revenue	39	53
Finance costs	<u>(36)</u>	<u>(67)</u>
<b>Loss on ordinary activities before taxation</b>	<b>(303)</b>	<b>(1,236)</b>
<b>Retained loss for the year</b>	<b><u>(303)</u></b>	<b><u>(1,236)</u></b>
Loss per share - basic and diluted	(0.2p)	(0.9p)
<b>EBITDA</b>	<b><u>33</u></b>	<b><u>(746)</u></b>

**CONSOLIDATED STATEMENT OF RECOGNISED INCOME AND EXPENSE  
FOR THE YEAR ENDED 31 DECEMBER 2006**

	<i>2006</i>	<i>2005</i>
	<i>£'000</i>	<i>£'000</i>
Exchange difference on translation of foreign operations	<u>133</u>	<u>86</u>
<b>Net income/(expense) recognised directly in equity</b>	<b>133</b>	<b>86</b>
Loss for the financial year	<u>(303)</u>	<u>(1,236)</u>
<b>Total recognised income and expense for the year (all attributable to members of the parent company)</b>	<b><u>(436)</u></b>	<b><u>(1,150)</u></b>

**SOPHEON PLC**

**CONSOLIDATED BALANCE SHEET AT 31 DECEMBER 2006**

	2006 £'000	2005 £'000
<b>Non-current assets</b>		
Property, plant and equipment	110	101
Intangible assets	848	764
Non-current receivables	10	10
	968	875
<b>Current assets</b>		
Trade and other receivables	2,484	1,741
Cash and cash equivalents	1,034	1,970
	3,518	3,711
<b>Total assets</b>	<b>4,486</b>	<b>4,586</b>
<b>Current liabilities</b>		
Short term borrowings	414	370
Trade and other payables	2,444	2,253
Obligations under finance leases	8	12
	2,866	2,635
<b>Net assets</b>	<b>1,620</b>	<b>1,951</b>
<b>Equity and reserves</b>		
Share capital	6,679	6,665
Other reserves	72,827	72,931
Profit and loss account and translation reserve	(77,886)	(77,645)
<b>Total equity (all attributable to equity holders of the parent company)</b>	<b>1,620</b>	<b>1,951</b>

**CASH FLOW STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2006**

	2006 £'000	2005 £'000
<b>Loss for the year</b>	<b>(303)</b>	<b>(1,236)</b>
Adjustments for non-cash and similar items	397	623
Movements in working capital	(596)	465
Tax and interest costs	(36)	14
<b>Net cash outflow from operating activities</b>	<b>(538)</b>	<b>(134)</b>
Investing activities	(510)	(416)
Financing activities	131	1,298
<b>(Decrease)/Increase in cash and cash equivalents</b>	<b>(917)</b>	<b>748</b>



## NOTES

### 1. Basis of preparation

The financial statements have been prepared in accordance with International Financial Reporting Standards and Interpretations issued by the International Accounting Standards Board as adopted by the European Union and those parts of the Companies Act 1985 which apply to companies preparing their financial statements under IFRS. Accounting policies have been applied consistently to all the years presented, and on the going concern basis.

### 2. Going concern.

In 2006 the Group's revenues from continuing operations were £6.0 million and it achieved a breakeven financial result on an EBITDA (earnings before interest, tax, depreciation and amortization) basis. This represented growth of 30% over the prior year. At the year end the Group reported consolidated net assets of £1.6 million and gross cash resources of £1 million. The Group has access to a \$1 million (£583,000) bank line of credit with Silicon Valley Bank, which is secured against the trade debtors of Sopheon Corporation Minnesota. At 31 December 2006, \$800,000 (£409,000) was drawn against this facility. The facilities with Silicon Valley Bank have been in place since 1999, and are renewable annually.

The directors remain positive about the direction, focus and momentum of the business and believe that this, together with the Group's existing resources provide it with adequate funding to support its activities through to the point at which they anticipate that trading will become cash generative on a sustained basis. This is in turn dependent on the Group delivering substantial sales growth.

Should this not be the case, Sopheon continues to have access to its equity line of credit facility from GEM Global Yield Fund Limited ("GEM") for an aggregate of €10 million. At the end of 2005, the facility was renewed for a further two year term expiring in December 2007. GEM's obligation to subscribe for shares is subject to certain conditions linked to the prevailing trading volumes and prices of Sopheon shares on the Euronext stock exchange. To date Sopheon has made just one call on the equity line of credit facility, raising under €1 million in March 2004, leaving over €9 million (£6 million) available.

While uncertainties remain as to the achievement of the expected sales growth and the continued availability of facilities, the directors believe that together, these factors enable the Group to continue as a going concern for the foreseeable future. The financial statements do not include the adjustments that would be required if the Group were unable to continue as a going concern.

### 3. Annual Report

The abridged financial information set out herein has been extracted from financial statements approved by the directors on 29 March 2007, and which will be delivered to the Registrar of Companies following the Company's annual general meeting. The auditors have issued an unqualified audit report, but consistent with prior years, have drawn attention to the uncertainty over going concern. This financial information does not constitute statutory accounts as defined in section 240 of the Companies Act 1985 and has been prepared on the basis of the accounting policies set out in the financial statements for the year ended 31 December 2005. The Annual Report and Financial Statements will be posted to shareholders shortly and thereafter will be available from the Company's registered office at 40 Occam Road, Surrey Research Park, Guildford, Surrey GU2 7YG.

## NOTES

### 4. Principal Accounting Policies

#### *Basis of consolidation*

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company ("subsidiaries"). Control is achieved where the Company has the power to govern the financial and operating policies of an entity and to obtain benefits from its activities. All intra-group transactions, balances, income and expenses are eliminated on consolidation.

#### *Revenue recognition*

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods and services provided in the normal course of business, net of discounts and sales related taxes. Sales of software products are recognised on delivery, and when no significant vendor obligations remain. Revenues relating to maintenance and post contract support agreements are deferred and recognised over the period of the agreements. Revenues from implementation and consultancy services are recognised as the services are performed, or in the case of milestone based or long term contracts, recognised on a percentage basis as the work is completed and any relevant milestones are met, using latest estimates to determine the expected duration and cost of the project.

#### *Leases*

Assets held under finance leases are recognised as assets of the Group at their fair value at the inception of the lease or, if lower, at the net present value of the minimum lease payments. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation. Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged to profit or loss. Rentals payable under operating leases are charged to profit or loss on a straight-line basis over the term of the relevant lease.

#### *Retirement benefit costs*

Payments to defined contribution retirement benefit plans are charged as an expense as they fall due. The Group does not operate any defined benefit retirement benefit plans.

#### *Treatment of foreign currencies for consolidation*

For the purpose of the consolidated financial statements, the results and financial position of each entity are expressed in sterling, which is the functional currency of the parent company, and the presentation currency for the consolidated financial statements. The assets and liabilities of the Group's foreign operations (including comparatives) are expressed in sterling using exchange rates prevailing on the balance sheet date. Income and expense items (including comparatives) are translated at the average exchange rates for the period. Exchange differences arising (including exchange differences on intra-group loans) are classified as equity and transferred to the Group's translation reserve. Such translation differences are recognised in profit or loss in the period in which the foreign operation is disposed of.

#### *Deferred taxation*

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences, but deferred tax assets are recognised only to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset realised. Deferred tax is charged or credited to profit or loss, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

## NOTES

### 4. Principal Accounting Policies (continued)

#### *Property, plant and equipment*

Computer equipment and fixtures and fittings are stated at cost less accumulated depreciation and any accumulated impairment losses. Depreciation is charged so as to write off the costs of assets over their estimated useful lives, using the straight-line method. Assets held under finance leases are depreciated over their expected useful lives on the same basis as owned assets, or, when shorter, over the term of the relevant lease. The gain or loss arising on the disposal or retirement of an item of property, plant and equipment is determined as the difference between the sale proceeds and the carrying amount of the asset and is recognised in profit or loss.

#### *Intangible assets - research and development expenditure*

Development expenditure on internally developed software products is capitalised if it can be demonstrated that:

- it is technically feasible to develop the product
- adequate resources are available to complete the development
- there is an intention to complete and sell the product
- the Group is able to sell the product
- sales of the product will generate future economic benefits; and
- expenditure on the product can be measured reliably

Capitalised development costs are amortized over the period over which the Group expects to benefit from selling the product developed. Development costs not satisfying the above criteria and expenditure on the research phase of internal projects are recognised in profit or loss as incurred.

#### *Share based payments*

The Group issues equity-settled share-based payments to certain employees. Equity-settled share-based payments are measured at fair value (excluding the effect of non-market-based vesting conditions) at the date of grant. The fair value determined at the date of grant is expensed on a straight-line basis over the vesting period, based on the Group's estimate of the shares that will eventually vest and adjusted for the effect of non-market-based vesting conditions. Fair value is measured by the binomial option-pricing model. The expected life used in the model had been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions and behavioral considerations.

## NOTES

### 5. Turnover

All of the Group's revenue in respect of the years ended 31 December 2006 and 2005 derived from continuing operations and from the Group's single business segment, the design, development and marketing of software products with associated implementation and consultancy services.

### 6. Share based payments

In accordance with *IFRS2 Share based Payments*, an option pricing model has been used to work out the fair value of share options granted since November 2002, with this value being charged to the profit and loss account over the expected vesting period and leading to a charge of £62,000 (2005: £143,000).

### 7. Earnings per share

The calculation of basic loss per ordinary share is based on a loss of £303,000 (2005: £1,236,000), and on 133,441,000 (2005: 131,059,000) ordinary shares, being the weighted average number of ordinary shares in issue during the year. The effect of all potential ordinary shares is antidilutive.

### 8. EBITDA

EBITDA is defined as earnings before interest, tax, depreciation and amortization and can be arrived at by adding back depreciation and amortization charges amounting to £339,000 (2005: £476,000) to the operating loss of £306,000 (2005: £1,222,000).

### 9. Intangible Assets

In accordance with *IAS 38 Intangible Assets*, certain development expenditure must be capitalised and amortised based on detailed technical criteria, rather than automatically charging such costs in the profit and loss account as they arise. This has led to the capitalization of £495,000 (2005: £427,000), and amortization of £305,000 (2005: £392,000) during the year.

### 10. Obligations under finance leases

Obligations under finance leases include £5,000 (2005: £9,000) relating to amounts due in more than one year.

### 11. Cautionary Statement

Sopheon has made forward-looking statements in this press release, including statements about the market for and benefits of its products and services; financial results; product development plans; the potential benefits of business relationships with third parties and business strategies. These statements about future events are subject to risks and uncertainties that could cause Sopheon's actual results to differ materially from those that might be inferred from the forward-looking statements. Sopheon can make no assurance that any forward-looking statements will prove correct.