Annual Report 1999

sopheon

providing the knowledge behind e-business

“ 1999 was **a year of considerable progress for Sopheon** and the year 2000 has begun well as we move towards fulfilling our objective to become **a major force** in the global market **for knowledge management solutions.** ”

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Group Profile

Founded in 1993, Sopheon is an international software product development and implementation company offering a range of proprietary business solutions in the rapidly emerging field of knowledge management, with specific focus on the healthcare, life sciences and high technology manufacturing sectors. Sopheon's business solutions are developed primarily using the company's core technology components which are geared to the rapid development of business applications, to support specific knowledge and language intensive processes and functions. Sopheon also offers systems integration and consultancy services for its software products and other complimentary products within the knowledge management and web publishing markets.

The core technologies have resulted in the development of a generic, flexible software platform that seeks to mirror the generic characteristics and structural aspects of knowledge and language intensive processes and functions, and includes capabilities geared to the creation and maintenance of content as well as its reuse, through a range of publishing techniques and applications. These can be applied and customized to specific customer requirements through a range of standardized development methodologies and tools, either by Sopheon directly or by its business partners. These business partners include consultancy firms, system integrators and other software development companies.

The group has recently announced the proposed acquisition of Teltech Resource Network Corporation, a knowledge management company based in Minneapolis, USA.

Sopheon has operations in the UK, the USA and the Netherlands and has approximately 110 employees at the present time. It is quoted on the Alternative Investment Market (AIM) of the London Stock Exchange and the EURO.NM market of the Amsterdam Exchanges.

Chairman's Statement

"1999 was a year of considerable progress for Sopheon and the year 2000 has begun well as we move towards fulfilling our objective to become a major force in the global market for knowledge management solutions."

Barry Mence
Executive Chairman

Financial highlights

In line with expectations, revenue from the core business, including the additional revenue from AppliedNet Limited which we acquired on 22 November 1999, showed an increase in turnover of 70% to £1.5 million. On an illustrative combined basis, the total revenue for AppliedNet and Sopheon for the full year 1999 was £3.6 million, also in line with expectations. Revenue for Teltech, the company proposed to be acquired by the Group, was £10.1 million for 1999 which, also based on an illustrative combined basis, would result in a revenue base for the enlarged group of £13.7 million for 1999. Sopheon losses on an EBITDA (earnings before interest, tax, depreciation and amortisation) basis were £1.7 million. We have adopted this approach for reporting on an ongoing basis in line with common industry practice on both sides of the Atlantic.

Business development

The most significant business development during 1999 was the acquisition of the UK knowledge management company, AppliedNet, which brought to the Group amongst other important elements, a strong additional customer, revenue and prospect base in the UK. With the integration of the former PolyDoc and AppliedNet organizations into the new Sopheon completed in a very smooth and expeditious manner, the Group is already starting to experience accelerated commercial results.

Amongst several other notable events, I would like to mention the recent successful launch of the new FT.com (Financial Times online news website) in which Sopheon played an important role providing software and services, as covered in a recent Financial Times newspaper article. In addition to these and other business successes, and with good progress being made in our Healthcare business and a start in Life Sciences (Pharmaceutical and Biotech), 1999 finished well and the year 2000 has started strongly in Europe. Our strategy to become the de-facto standard in healthcare knowledge management software in the Netherlands took a significant step forward in the early part of 2000 with our investment in Pro-GRAM BV, a joint venture company with three of our major healthcare clients in the Netherlands. As I have previously indicated Pro-GRAM is targeted with marketing solutions to the Dutch healthcare industry, those solutions being based on our software and the knowledge content created by teaching hospitals.

In the months since the year end we have made very substantial strides in building on these developments, as highlighted in our 3 March announcement of the proposed acquisition of Teltech Resource Network Corporation in the USA, and a now completed institutional placing for £20 million.

Our North American office in Denver has expanded rapidly with ten new staff joining in the last few months and this, together with the substantial presence of Teltech in the USA, will I believe position Sopheon exceptionally well in that market.

Product development

As discussed further in the Market and Product Overview the former PolyDoc focused on the development and provision of content management and collaborative software solutions, based on our proprietary IDP/A technology. This software was delivered as specific business solutions by industry such as QualiFlow for Healthcare, NormFlow for Manufacturing, ResearchFlow for research in Biotech and High-tech manufacturing.

Prior to acquiring AppliedNet, PolyDoc was looking to extend its software product range to incorporate software that can gather, filter and disseminate information from both internal and external sources. AppliedNet's KnowledgeAgents software not only satisfies these needs, it also profiles information automatically for distribution to individual users. Sopheon's solutions moving forward will now be drawing upon the integrated set of solutions and technology comprising both IDP/A and KnowledgeAgents software, a very powerful and currently unique offering. Recently, Doculabs (a Chicago-based software industry analyst firm) positively evaluated elements of our Sopheon technology and gave verification of our integrated product strategy.

In the immediate future our product development efforts will be focused on enhancing this integration as well as bringing the next generation of our industry-specific knowledge management business solutions to market, utilizing these new capabilities. In addition, the inclusion of Teltech's portal technology and approach into the Sopheon product set should allow the Group to significantly enhance its offering in the world of e-business and e-commerce.

Acquisition strategy

We first embarked on our acquisition strategy in 1998 with *step one* being the acquisition of Lessenger in the Netherlands, which gave us over 50 healthcare software clients and ownership of a complementary software product. *Step two* was achieved with the acquisition of AppliedNet at the end of 1999, which gave us a more substantial customer base in the UK and ownership of further complementary software. It also secured for us an established UK commercial organization with strong product development and implementation groups, which are already providing a firm base from which to further expand our business. As previously announced *step three* was targeted to be in the USA in the year 2000 with the objective of obtaining similar benefits for the Group. The proposed acquisition of Teltech in the USA, our most substantial to date, will satisfy all of our requirements for this. It will bring us a commercial organization with strong management and over 100 additional personnel, a customer base that includes half of the Fortune 500 companies, a substantial growing revenue base with a strong recurring element, and complementary technology. This together with our strong software team already in place in Denver, will give us a firm footprint into the North American market upon which to build.

A large number of our clients operate on a global basis and they expect their suppliers to operate in a similar way. This is in line with our own objective of becoming a global player in due course. Therefore *step four* of our acquisition strategy is targeted at the Pacific Rim in the year 2001. Other options are also being explored. However, the integration of Teltech and its technologies into the Group will take us through the summer and I will report to shareholders on these matters at that time.

Capital raising developments

I was pleased to announce in October last year that we had raised £8m to finance the development of the enlarged group at the same time as we acquired AppliedNet in the UK. Earlier during 1999 we also raised £0.5m to invest in Pro-GRAM BV, a joint venture company with three of our major healthcare clients in the Netherlands. I am confident that the acquisition of AppliedNet and the Pro-GRAM investment will make significant contributions to Sopheon's future.

In March 2000 I was also able to announce the raising of an additional £20 million. These funds will be used for the cash element of proposed acquisition of Teltech estimated at £10 million including costs, and to further strengthen our working capital base to accelerate our sales and marketing effort on both sides of the Atlantic. This successful institutional fund raising, which was achieved together with our brokers Durlacher, has resulted in a number of existing investors enlarging their holding in Sopheon and in a further number of top flight institutions becoming shareholders in the Group. Durlacher has used all proceeds of commissions due under the placing to subscribe for shares in Sopheon at the placing price.

I would like to welcome the new institutions to the company and to thank them for sharing our confidence in Sopheon's future. I would also like to extend this thank-you to all new and existing shareholders who have retained or acquired shares during 1999 and the beginning of 2000.

Outlook

The full integration of the AppliedNet and Teltech businesses into the Group should ensure the year 2000 will be another year of substantial progress. With a growing customer base on both sides of the Atlantic and a product and service offering that we believe has a considerable "first to market" advantage, we have confidence that we are well positioned for considerable growth in a rapidly growing market. In line with our customers' requirements and Sopheon's ambitions to become a global player in the knowledge management market, we plan to continue to accelerate our progress by acquisitions in further geographic locations as well as pursuing aggressive organic growth in each of the territories where we operate today.

Barry K. Mence
Executive Chairman
28 April 2000

Market and Product Overview

As a demand driven business, Sopheon has built expertise in areas where it perceives there are commercial opportunities now and moving forward. Sopheon's strategy is deliberately aligned to leverage existing expertise (for instance in healthcare, pharmaceuticals, biotechnology, high technology manufacturing) but also gives a customer pipeline in a number of other key verticals such as medical clinical guidelines, women's healthcare, and pharmagenomics.

As an example, healthcare, on a global basis, has reached a crossroads. Over the last 10 years the amount of electronic information stored and exchanged inside the healthcare system has rocketed. Network based IT is increasingly the method by which this sector functions. Across Europe there are numerous initiatives, which place technology at the center of the strategic development of organized healthcare. Hospitals essentially manage both their medical and non-medical processes on the basis of procedures and guidelines, which form the basis of a de-facto body of instructions.

The application of these instructions is a key element in managing the quality and efficiency of healthcare institutions and is often decisive for clinical prognoses, liability claims, and issues surrounding budgetary control. The guidelines are used for ongoing staff training, and dissemination of information as well as in compiling checklists and treatment plans by the clinicians and nurses at the bedside.

Channel Strategy and Partners

The healthcare scenario in particular has underpinned Sopheon's sales during 1998 and 1999, with a major order for Sopheon's healthcare solution, delivered through Pro-GRAM BV, a joint venture between three Dutch teaching hospitals which Sopheon has itself joined in 2000 as a 25% partner.

Outside of the Pro-GRAM channel in the Netherlands, the group has already worked with major consultancy practices in developing solutions for knowledge management. This includes KPMG and IBM. Whilst these relationships will continue to be important and welcome, there is an opportunity to fast-track the channel strategy in a more proactive manner. We believe that for the next 12-18 months a strategy of alliances with specialist, vertically oriented systems integrators or national consulting practices of complimentary software vendors is the best way forward.
This will allow us to:

- build a customer base producing revenues.
- reduce management overhead in terms of individual customers.
- move toward critical mass in building a customer base, which will make us an interesting proposition for the global systems integration companies who can provide volume sales.

The first phase of this strategy has already been implemented with the signing of an agreement with Marlow Consulting in the UK for the marketing and sales of Sopheon software into the healthcare and manufacturing sectors. In addition, in the USA we will look to aggressively leverage the proposed Teltech acquisition having previously signed up Teltech as a business partner earlier in 1999.

We are also planning discussions with a small number of software suppliers with substantial customer bases with a view to integrating modules into their offerings. Such an agreement has recently been signed with a leading Italian ERP specialist, Gruppo Formula. We have also entered into an agreement with Hiscom in the Netherlands whereby it will collaborate on medical knowledge systems, to accelerate the development of electronic patient dossiers. Hiscom is the leading medical IT supplier in the Netherlands and is increasingly marketing such solutions in other markets, in particular, the Belgium and the Scandinavian countries.

Products

The core Sopheon solutions are based on the proprietary Integrated Document Production Architecture (IDP/A), which forms the foundation of a comprehensive range of software products. In this product architecture, the key points to note are that the creation and maintenance activities are distinct from the access to published material and searching processes. International patents for IDP/A were applied for in 1996 under the Patent Cooperation Treaty process.

Prior to acquiring AppliedNet, PolyDoc was looking to extend its software product range to incorporate software that can gather, filter and disseminate information from both internal and external sources. AppliedNet's KnowledgeAgents software not only satisfied these needs, it also offered profiling of information automatically for distribution to individual users. This is described further below under Sopheon Agents™.

In addition, the period leading up to and since the acquisition of AppliedNet has seen significant progress in the branding and accessibility of the former PolyDoc software products. PolyDoc had established the XFlow suite based on its core IDP/A technology, and recent developments have made the following elements available as separate modules:

Sopheon Composer™

Authoring Support to allow the content creating community in a specific process to build an advanced, maintainable and high quality knowledge database for multiple publication purposes. This support includes advance language tools to help the writing of well-structured, linguistically correct and consistent texts. Furthermore the tools support the creation of metadata, keywords, references (links) and terminology marking. A strong element of authoring support is the so-called Terminology Checker, which supports authors and editors in checking their choice of wording against a central terminology database. Translation facilities are integrated in the environment.

Sopheon Publishing™

Publishing and Search Support to allow optimal and multiple reuse of the content, which includes historical output formats as well as web enabled access and search facilities, serving a range of "readerships". Sopheon's publishing function offers a highly communicative environment for the readerships. For example, terms in texts are highlighted and can be clicked by the reader in order to see their meaning and other background information in their original historical context. The search functionality is highly linguistic-oriented and allows the usage of thesauri and rhetorical structures as a basis for very specific and personalized reuse of content across disciplines, domains, processes and even languages. With this function Sopheon can apply any modern search technique and is able to connect with a range of search engines, though with the AppliedNet acquisition much of this technology now resides in house.

Sopheon Terms™

Terminology Management Support to enable a central function, to take care of the harmonization, storage and maintenance of the terminology of specific processes. This function is a key element of Sopheon's approach to help the process community to communicate efficiently and effectively, avoiding expensive misunderstandings. From the Terminology Database there is an output stream of data into other functions, for example, lookup dictionaries, the spell checker, the term checker, but also into the advanced search facilities (through the generation of thesauri) and into web pages. This tool is also a key element for managing the integration with other systems such as Enterprise Resource Planning (ERP) systems and specific Electronic Document Management Systems (EDMS).

Sopheon Modeler™

In order to enable the Sopheon IDP/A solutions to be rapidly customized for individual customers a set of configuration tools have come through the product development planning pipeline, and will be introduced under the name Sopheon Modeler. These tools are designed to improve the speed and ease with which both channel partners and customers can perform customization of the Sopheon IDP/A suite for their own specific requirements.

Sopheon Agents™

Sopheon Agents is designed as a central corporate knowledge base that can act as both the repository and the "broker" for information stored within the corporate memory. The product provides the ability to gather, filter, and disseminate information from both internal and external sources, while also profiling that information automatically for distribution to individual users.

Sopheon Agents allows users to define a profile on a subject that is critical to their work, defining a vocabulary of interest as this is created. That vocabulary becomes a set of triggers that are then used to identify the right information. Hunting through the corporate knowledge base, Sopheon Agents delivers information to the desktop, either via e-mail or as a special Internet page. Sopheon Agents can also make use of external information feeds and the Internet. Users can have more than one profile of interest simultaneously.

The components described above enable the delivery of applications that can be deployed in a wide variety of enterprise situations. Sopheon has developed and is developing the following range of vertical application solutions using the IDP/A technologies:

Sopheon for Life Sciences
Sopheon for Research & Development
Sopheon for Healthcare

Sopheon has several healthcare solutions.

Sopheon for Healthcare – Qualiflow™

This solution enables hospitals and healthcare organizaitons to create, maintain and publish medical protocols and healthcare quality documents. This was a major revenue contributor during 1998 and 1999, delivered through Pro-GRAM BV, the joint venture between three Dutch teaching hospitals which Sopheon has itself joined in 2000.

Sopheon for Healthcare – Lessenger™
This simple but effective document management solution supports the specific compliant version control and regulatory distribution procedures required for certification of laboratories, food processing plants, sections of the pharmacy, and other areas within the healthcare industry. Input is from standard word processors while publishing can be on paper – the appropriate headers and footers are added and distribution lists are generated automatically, or electronic – viewing either through intranet browsers or through special viewers.

Internet

Sopheon has positioned itself to benefit from developments in the Internet marketplace over the next 24 months.

At present (due to the fact that intranets and extranets are so central to the Knowledge Management proposition) the software as a matter of course allows users to reuse content from the knowledge repositories which have been created using IP, through a web interface. The next stage in the development of the business is to allow content creation to be done through a web interface. Modes of input will always be based on XML, on which Sopheon has built its content management strategy moving forward, making our products fully interoperable and reducing any possible concerns with regard to interconnectivity. From a competitive perspective this allows us to see how the market emerges without having to place a single large bet on any single vendor.

We also plan to enter the newly emerging application service (ASP) space. Knowledge management software is an ideal candidate for ASP hosting in that the commercial model for the service delivers positively on two key IT deployment concerns, return on investment and total cost of ownership.

Ongoing Developments

Sopheon's solutions moving forward will now be drawing upon the integrated set of solutions and technology comprising both the IDP/A and Sopheon Agents software, a very powerful and currently unique offering. Recently, Doculabs (a Chicago-based software industry analyst firm) positively evaluated elements of our Sopheon technology and gave verification of our integrated product strategy.

In the immediate future our product development efforts will be focused on the integration of these solutions as well as bringing the next generation of our industry-specific knowledge management business solutions to market, utilizing these new capabilities. In addition, the inclusion of Teltech's portal technology and approach into the Sopheon product set should allow the Group to significantly enhance its offering in the world of e-business and e-commerce.

A product development plan and delivery schedule is in place to continue the enhancement of the Sopheon IDP/A components and to bring the first levels of IDP/A and Sopheon Agents integrated technology to the market during Q2 and Q3 of the current year. This will be deployed through the existing industry-specific Sopheon application solutions (such as Sopheon for Healthcare) and also by the next generation of Sopheon solutions that is currently in the development planning process.

Integrated Solution Overview – Sopheon

Sopheon Modeler™

Web-based, thin client solution for creating and managing Content and Content Structures in real time.

Sopheon Terms™

Solution for Terminology Management across the Sopheon Suite. Sopheon Terms™ provides interactive navigation of Terminology Relationships, Glossaries and Dictionaries. Sopheon Terms™ is fully enabled to support authoring and terminology management across languages and content versions.

Sopheon Composer™

Content capture solution which enables Guided Authoring with Controlled Workflow across Multiple Languages. Sopheon Composer™ allows comprehensive Metadata and Keyword search across the entire knowledge base.

Sopheon Agents™

Enables gathering, filtering, and dissemination of information from a variety of external and internal sources including the Internet, Intranets, Groupware solutions, and virtually any file structures. Sopheon Agents™ provides robust search facilities with the ability to ensure that only relevant information is returned. Communities of interest and project teams can collaborate on and across content within the shared knowledge base. A staff profile is developed, enabling identification of interests, skills, and capabilities.

Sopheon Publisher™

Allows content to be automatically published to key web resources including Intranets, Portals and any e-business application. It is also an ideal solution for creating Manuals, Reports, Research Studies and any Complex Document Formats. Also included in Sopheon Publisher™ is the ability to export to other technologies such as intelligent pagers and Personal Digital Assistants (PDA's).

Vertical Solutions

Sopheon provides solutions which are tailored to the best practices and requirements of specific vertical industries. These include the following vertical solutions:

Sopheon for Healthcare

Sopheon for Healthcare is specifically designed with the challenges faced by healthcare providers in mind. Included are the following modules specifically designed to bring excellence to the point of care:

- Quality Manuals
- Managerial Policy Guidelines
- Administrative Procedures
- Laboratory Standard Operating Procedures
- Nursing Protocols
- Clinical Guidelines
- Food Procedures & Instructions
- Logistical Procedures
- Pharma Procedures

Sopheon for Life Sciences

Enterprises in the Life Sciences industries face the dilemma of increased competition, the need to reduce product development times and simultaneously embrace new technology and markets. These crucial forces will govern whether or not they are to win or lose. The real competitive advantage lies in getting more products to market, faster. Sopheon for Life Sciences is designed to collect information from the outset in a controlled and managed process, regardless of where that information is created. The created information and knowledge may be stored, published and reproduced in a variety of formats and styles. Its structured storage will allow the information to be queried and reused in many different ways throughout the extended community. By enabling collaboration, content gathering, and publishing of specialized content, Sopheon helps your company to work smarter and reduce the time taken for discovery and analysis.

Sopheon for Research & Development

Research & Development organizations face tough challenges as they seek to shorten the time it takes to bring products to market. This is accomplished in part by reducing non-productive administration time, allowing the creation of time for knowledge professionals to add greater value through innovation and creativity. This challenge is compounded by the vast mountain of information which exists on external resources. Sopheon for Research & Development enables content and knowledge collaboration across individuals, projects and communities. The result is an organization which is in touch with science and technology resources and much more.
The following is just a sampling of the list of capabilities in Sopheon for Research & Development:

- Research Reporting
- Testing Reporting
- Scientific Articles
- Best Practices
- Safety and Materials Handling
- Incident Management Procedures

Knowledge Makes All the Difference

Never before has so much information been within the reach of today's professional. With the maturity of corporate information stores, libraries, and the Web, the sheer volume and scale of these resources are just now being realized.

Where is the value in this enormous volume of information? Businesses today are valued not only by what they produce in terms of goods and services, but also the accumulated knowledge which enables their core business. It is essential for organizations to be able to have a clear understanding of the value of knowledge assets, similar to how they value assets such as capital equipment and real estate.

Consider the generation of new, original content by your organization. What happens to content which is created by your valued Knowledge Workers? Your organization should be able to continuously derive benefit from shared knowledge and create an environment for innovation. The organization should benefit from the shared knowledge base and not be limited to an individual's file stored on a local desktop. What happens when that individual leaves the company… does the knowledge walk out the door along with them? A solution is needed which supports the continuous capture of knowledge and expertise and provides the knowledge base to make it available across the organization's communities.

The ability to survive in a global environment is essential. Today's organizations are becoming decentralized and must enable knowledge assets to transcend language and geographical barriers. Sopheon was conceived in a multilingual, multinational environment in order to remove boundaries which separate knowledge from the people who need it. Only Sopheon provides knowledge solutions with core multilingual and localized content capability.

Content with Context

Simple search engines attempt scanning and categorization of such sources, but have fallen short in one key area: context. Without understanding context, one cannot make the leap from information to knowledge with meaning. The understanding of the context in which language is used is perhaps just as important as the understanding of the meaning of a simple word. Consider a simple search for the word manifold. Without knowing the context in which you want to search, you'll encounter everything from rock bands to exhaust handling products. By searching within the context of distributors of compressed medical gas brass manifolds, you find exactly what you're looking for. In a similar example, an operator at a major petrochemical plant needs to find out how to shut down a manufacturing process. Without being aware of the context of the search, perhaps that the plant is on fire, the operator may encounter information which has nothing to do with their immediate need.

What Benefits can be expected with a Sopheon solution?

Improved Business Strategy

The entire organization can have access to the critical business and technical information necessary for effective, strategic decision making. Sopheon Knowledge Solutions not only allow access to content, they provide the environment for creation of better content.

Create the Environment for Innovation

Never before has collaboration been so essential to an organization's success. Collaboration is of particular necessity in today's virtual organizations, with team members and groups working together across geographies, time zones, and languages. Sopheon allows collaboration across and within communities of interest and enables those participants to enrich the value of that content.

Faster Time to Market

Quicker access to information shortens product development cycles. Ready access to mission critical information and knowledge can shorten product development cycles by as much as 30%. This is delivered by both getting the right answers faster and also perhaps equally important: knowing what not to do, in a rapid manner.

Improved Profitability

Sopheon can deliver economies in procuring and delivering knowledge. These economies can be realized through more effective utilization of internal and external resources.

Best Practices and Process Improvement

Sopheon solutions ensure the organization captures and reuses best practices helping to reduce and eliminate redundant and unnecessary activities. By implementing best practices key knowledge workers can now focus on creativity – delivering increased productivity and innovation.

Creation of Knowledge Assets

Increasingly organizations must be able to demonstrate how they capture and quantify their intellectual assets. The value of today's leading organizations is based more upon their intellectual capital than the traditional "brick and mortar" measures. Knowledge has become your most critical asset.

Directors and advisers

Directors	Barry K. Mence	Executive Chairman
	Richard V. Maddocks	Managing Director
	Huub J.M. Rutten, Drs.	Product Research Director
	James M Macfarlane, CENG	Business Development Director
	Arif Karimjee, ACA	Finance Director
	Hans Coltof, Dr.	Non Executive Director
	Stuart A. Silcock, FCA	Non Executive Director
	Michael J. Brooke	Non Executive Director
Secretary	E.R.E. Iljitsj Wiebenga, CA (SA)	
Registered office	Stirling House, Surrey Research Park Guildford Surrey GU2 5RF	
Registered number	Registered in England and Wales:	3217859
Auditors	Ernst & Young Apex Plaza Reading RG1 1YE	
Principal bankers	Rabobank Amsterdam b.a. Wilhelminaplantsoen 124 1111 CP Diemen The Netherlands	Lloyds Bank Plc 77 High Street Southend-on Sea Essex SS1 1HT
Solicitors	Edge Ellison 18 Southampton Place London WC1A 2AJ	Nauta Dutilh Prinses Irenestraat 59 1077 WV Amsterdam The Netherlands
AIM Nominated Adviser	Brewin Dolphin Securities Limited 48 St. Vincent Street Glasgow G2 5TS	
AIM Nominated Broker	Durlacher Limited 4 Chiswell Street London EC1Y 4UP	
Registrars	Independent Registrars Group Limited Balfour House 390/398 High Road Ilford Essex IG1 1NQ	
Financial PR Consultants	Buchanan Consultants 107 Cheapside London EC2V 6DN	

Report on Directors' Remuneration

The remuneration committee of Sopheon Plc is responsible for oversight of the contract terms, remuneration and other benefits for executive directors, including performance related bonus schemes. The committee comprises the non-executive directors together with Barry Mence. The committee makes recommendations to the board, within agreed parameters, on an overall remuneration package for executive directors and other senior executives in order to attract, retain and motivate high quality individuals capable of achieving the group's objectives. The package for each director consists of a basic salary, benefits and pension contributions, together with performance related bonuses and share options for certain directors on a case by case basis. Consideration is given to pay and employment policies elsewhere in the group, especially when considering annual salary increases. In addition, the committee is in the process of taking advice from a leading firm of remuneration consultants to maximize comparability within the marketplace.

Contracts

Service contracts between the company and the executive directors are terminable on 6 months notice.

Fees for non-executive directors

The fees for non-executive directors are determined by the board. The non-executive directors are not involved in any discussions or decisions about their own remuneration.

Directors remuneration

Set out below is a summary of the fees and emoluments received by all directors during the year. Details of directors' interests in shares and options are set out in the Directors' Report.

	Basic salary and fees £	*Bonus £*	*Benefits £*	*Contributions to Pension £*	*Total 1999 £*	*Total 1998 £*
Executive directors						
B.K. Mence	67,356	-	11,808	3,000	82,164	82,730
R.V. Maddocks	78,016	-	16,115	6,876	101,007	101,841
H.J.M. Rutten	58,511	-	11,050	2,701	72,262	73,957
E.R.E.I. Wiebenga (1)	31,207	-	7,803	1,440	40,450	41,314
J.M. Macfarlane (2)	8,253	2,885	1,731	825	13,694	-
Non-executive directors						
M.J. Brooke (2)	1,000	-	-	-	1,000	-
S.A. Silcock	31,818	-	-	-	31,818	35,021
H. Coltof	6,200	-	-	-	6,200	6,300
D. Geest	-	-	-	-	-	6,272
	282,361	2,885	48,507	14,842	348,595	347,435

(1) Resigned on 1 February 2000
(2) Appointed on 22 November 1999
(3) Pension contributions are made to individual directors personal pension schemes.

The emoluments of S.A. Silcock and M.J. Brooke are paid respectively to Lawfords Limited, of which Mr Silcock is a director, and Coinshire Limited, of which Mr Brooke is a director.

Directors Report

Financial Results

The result for the year ended 31 December 1999 both before and after taxation is a loss of £2,072,000 (1998 – £1,142,000 restated) on a turnover of £ 1,510,000 (1998 – £891,000). The directors do not propose to declare a dividend.

Principal Activities

The group's principal activities during the year continued to be the development and provision of knowledge management software, solutions and services.

Review of the Business

Including revenue from AppliedNet Limited which we acquired on 22 November 1999, turnover showed an increase of 70% to £1.5 million. This included £874,000 from the former PolyDoc business, a significant proportion of which is represented by healthcare related sales as in 1998. Exceeding expectations and historic performance, a large part of the post acquisition revenues of £636,000 recorded for AppliedNet resulted from a major customer implementation that required rapid expansion of resources. On an illustrative combined basis, the total revenue for Sopheon including AppliedNet for the full year 1999 was £3.6 million. Sopheon losses on an EBITDA basis (earnings before interest, tax, depreciation and amortisation) were £1.7 million.

The North American office in Denver has expanded rapidly with ten new staff joining in the last few months.

The acquisition of AppliedNet Limited was satisfied by an issue of ordinary shares at a market price per share of 129p, which together with costs resulted in a total acquisition cost of £8,439,000. At the same date an institutional placing of shares for cash raised £7,699,000 after costs to be used to fund the development of the combined businesses. The structure of the acquisition required the share capital of the Company to be restructured such that each ordinary share of 20p was converted into one ordinary share of 5p and one deferred share of 15p, as described more fully in note 17.

Changes in accounting policies and allocations

Historically, development expenditure incurred for specific products was capitalized when its future recoverability could reasonably have been regarded as assured, and amortized in line with the expected future sales from the related product, to a maximum of 5 years. Following the acquisition of AppliedNet Limited and subsequent harmonization of group accounting policies, all such expenditure is now written off as incurred. The effect of changing this policy has been reflected by way of a prior year adjustment to the 1998 financial statements of the group. Had the previous policy been continued, the results for 1999 would have shown a reduction in losses for the year of £7,000.

Furthermore, the directors have also taken the opportunity to revise the allocation of certain costs between categories within the profit and loss account. These mainly relate to internal management and research and development activities, which have been reallocated from cost of sales to administrative expenses and is described further in note 3.

Future Developments

Sopheon will continue to build its strategy of becoming a global force in knowledge management solutions through both organic and acquisition routes. The acquisition of AppliedNet Limited in the UK has given the group new software, critical mass and a platform for expansion in Europe. The proposed acquisition of Teltech Resource Network Corporation, announced in March 2000, is expected to deliver similar benefits in the USA as well as significantly enhancing the breadth of product and service that the group can offer. Effort will continue to be directed at the integration and verticalization of the group's software assets and new product releases are planned for later in 2000. As mentioned in the Chairman's statement, the group will look for acquisition opportunities in the Pacific Rim in 2001.

Research & Development

In the area of information and language technology Sopheon continues to invest in research to ensure the group's products and core software remain at the leading edge of proven technologies. The linguistic research team in Maastricht remains a cornerstone of the group's intellectual property resource. In addition, the capability to direct effort at development activities has been increased by the acquisition of AppliedNet, which had a development team of thirteen people, as well as the ongoing expansion of Sopheon's Denver based team where there are now five development staff including Paul Heller, our Chief Technology Officer.

Core research activities include the Integrated Terminology Management Cycle (ITMC) research project being partly funded by European Union's Eureka programme. The ITMC project will draw to a close in 2000. Discussions are underway with the relevant authorities to secure participation by the group in further Eureka projects. In addition, the group has joined with other partners including Italian ERP vendor Gruppo Formula to participate in the European Union's Leveraging Operational Resource Enterprise (LORE) project.

Directors and their interests

The directors interests in the share capital of the Company (all beneficially held except those marked with an asterisk, * which are held as trustee), were as follows:

	Share Options		*Ordinary Shares*	
Director	*1999*	*1998*	*1999*	*1998*
B.K. Mence	-	-	8,337,800	8,337,800
R.V. Maddocks	400,000	400,000	25,000	25,000
H.J.M. Rutten	-	-	507,500	507,500
E.R.E.I. Wiebenga (resigned on 1 February 2000)	-	-	340,000	340,000
S.A. Silcock	-	-	192,450	192,450
S.A. Silcock*	-	-	107,010	107,010
H. Coltof	100,000	100,000	-	-
J.M. Macfarlane	-	-	1,719,716	-
M.J. Brooke	-	-	691,724	-
A. Karimjee (appointed on 1 February 2000)	100,000	-	-	-

Of the 8,337,800 Ordinary Shares mentioned above B. K. Mence beneficially owns and is the registered holder of 4,490,000 Ordinary Shares. He is, or his wife or children are, potential beneficiaries under trusts holding an aggregate of 3,847,800 Ordinary Shares of which trust directors of Lawfords Ltd., in the Isle of Man, are trustees and are registered as the holders of such shares. S.A. Silcock is a shareholder in Lawfords Ltd. in the Isle of Man. At 31 December 1998 and 1999 B K Mence also held £523,640 5% Convertible Loan Stock at par and warrants to subscribe on or before 31 December 2000 for 300,000 Ordinary Shares at £1.46 per share. If not exercised by that date the warrants shall lapse.

Both Mr Maddocks' and Mr Coltof's options have an exercise price of 20p and are exercisable at any time before 17 July 2001. Mr Karimjee's options have an exercise price of 150p and are not exercisable until 22 November 2002. Furthermore, the vesting of 50,000 of his options is linked to agreed performance criteria.

No directors exercised share options during the period. Since the year end, Mr Maddocks and Mr Coltof exercised all of their options to acquire shares in the Company. On 10 March 2000, Mr Maddocks, Mr Silcock and Mr Rutten each sold 25,000 of their shares in the Company.

On 28 July 1998, the Company issued £1,570,920 5% Convertible Loan Stock 1999 ("Convertible Loan Stock"). £523,640 of the Convertible Loan Stock was subscribed for by Barry Mence following independent shareholders' approval as required by The Panel on Takeovers & Mergers ("the Panel"). Following agreement between the Company and the Loan Stockholders, including Barry Mence, the redemption date and the conversion date for the Convertible Loan Stock has been moved from 31 July 1999 to 31 July 2000.

The midmarket share price ranged from 126p to 405p during the financial year.

Save as disclosed above, no Director (or member of his family) or connected persons within the meaning of Section 346 of the Companies Act 1985 has any interest, beneficial or non-beneficial, in the share capital of the company.

Substantial Shareholdings

The Directors are aware of the following persons who as at 28 April 2000 are interested directly or indirectly in three per cent or more of the company's issued Ordinary Shares:

Name	*No. of Ordinary Shares*	*% issued Ordinary Shares*
Brandon Limited	1,793,647	5.1
B.K. Mence (director)	8,337,800	23.7
J.M. Macfarlane (director)	1,719,716	4.9

Mr Mence's interest represents direct beneficial holdings as well as those of his family.

Share Option Schemes

Details of options granted are shown in note 17.

Creditor payment policy and practice

It is the company's policy that payments to suppliers are made in accordance with those terms and conditions agreed between the company and its suppliers, provided that all trading terms and conditions have been complied with. At 31 December 1999, the group had an average of 60 days purchases outstanding in trade creditors.

Derivatives and other financial instruments

The group's principal financial instruments comprise convertible loans, bank loans, cash and short-term deposits. The main purpose of these financial instruments is to secure funds and manage cash flow for the group's operations. The group has various other financial instruments such as trade debtors and trade creditors that arise directly from its operations. Details of financial instruments as required by FRS13 are disclosed in note 20. The disclosures exclude short term debtors and creditors.

It is, and has been throughout the period under review, the group's policy that no trading in financial instruments shall be undertaken.

The main risks arising from the group's financial instruments are interest rate risk, liquidity risk and foreign currency risk as summarized below. The board reviews and agrees policies for managing each of these risks. These policies have remained unchanged during 1998 and 1999.

Interest rate risk

On 28 July 1998, the former PolyDoc business issued £1,570,920 Convertible Loan Stock in order to fund the working capital requirements of the business. The loan stock bears an interest rate of 5% and was repayable or convertible on 31 July 1999. Following agreement between the Company and the Loan Stockholders the redemption date and the conversion date for the Convertible Loan Stock was moved from 31 July 1999 to 31 July 2000.

The former AppliedNet business had a bank loan which remains outstanding at year end and bears interest at a floating rate. The group also has overdraft facilities in UK Sterling, US Dollar and Dutch Guilder at floating rates of interest.

Where the group has significant cash resources available that are in excess of the short term needs of the business, such funds are maintained in sterling and are placed on short and medium term bank deposit at the best interest rate available.

Liquidity risk

The group's objective is to maintain a balance between continuity of funding and flexibility through the use of overdrafts and bank loans. Short term flexibility is achieved by overdraft facilities.

Foreign currency risk

As a result of having significant operating units in the USA and the Netherlands, which give rise to short term creditors, debtors and cash balances in US Dollars and Dutch Guilders, the group's balance sheet can be affected by movements in the US Dollar/Sterling and Dutch Guilder/Sterling exchange rates.

Events since the balance sheet date

Pro-GRAM investment

Since the year end, and as alluded to in previous reports, the group has committed funds of £430,000 for a 25% equity stake in ProGram BV, a company established with a number of Dutch healthcare institutions to market knowledge management solutions incorporating Sopheon's software to the Dutch healthcare industry.

£20m Placing

On 3 March 2000 the Company announced the raising of £20 million through the institutional placing of 2,500,000 ordinary shares at £8.00. These funds will be used to support the group's acquisition strategy in the USA and to further strengthen its working capital base to accelerate the sales and marketing effort on both sides of the Atlantic. Sopheon's Broker, Durlacher has used all of its proceeds of commissions due under the placing to subscribe for shares in Sopheon at the placing price. Including certain other adviser fees settled through the issue of shares at the placing price, this resulted in a further 122,500 shares being issued at the placing price pursuant to this transaction.

Proposed acquisition of Teltech

On the same date Sopheon announced that it had entered into an agreement to acquire Teltech Resource Network Corporation. The completion of the acquisition of Teltech would give Sopheon significant operations in the Netherlands, UK and the USA.

Teltech is a knowledge management and research services company based in Minneapolis, USA, which uses web technology to deliver its products and services to its customers through vertical internet portals as well as through more traditional routes. It was founded in 1984 with the current management being appointed in 1997. In early 1999, Teltech became a Sopheon business partner and the first joint software and services sales have been achieved. Currently, Teltech is experiencing good growth in revenues, having made substantial investment in the development of its knowledge portal technologies, launched into the market as Teltech.com in September 1999. Teltech has a 'blue chip' client base, which includes half of the Fortune 500 companies. In the year ended 31 December 1999, Teltech's revenues were $16.2 million (£10.1 million) and it had a loss of $0.09 million (£0.06 million). Teltech had net liabilities of $1.7 million (£1 million) at 31 December 1999.

The consideration for the Teltech acquisition is for a minimum of $20 million (£12.5 million) in new Ordinary Shares and options and $15 million (£9 million) in cash. Included in the cash element of the consideration is $1 million (£0.6 million) that would, as a result of the deal structure, be injected into the Teltech balance sheet at completion. The cash element of the proposed transaction, associated costs, and the development of the enlarged US business that would result is being funded through the £20 million placing referred to above.

Directors and employees of Teltech receiving Sopheon shares or options will undertake to retain them for 12 months and all other investors in Teltech, other than those with a minimal holding, will undertake not to dispose of any of their Sopheon shares for 6 months.

Completion of the acquisition of Teltech by Sopheon is subject to Securities and Exchange Commission approvals as well as Teltech shareholder approval, although the board of Teltech, which represents over 50% of Teltech's shares on a fully diluted basis, has already given its approval.

Other Share Issues

Since the year end 455,000 ordinary shares in Sopheon plc have been issued for £91,000 in cash to option holders exercising their options, giving rise to a premium of £68,250. Of these options, 400,000 were held by R.V. Maddocks, a director.

Auditors

A resolution to reappoint Ernst & Young as auditors will be put to the members at the Annual General Meeting.

Approved by the Board on 28 April 2000

E.R.E.I. Wiebenga
Secretary

Statement of Directors' responsibilities in respect of the accounts

Company law requires the directors to prepare accounts for each financial year which give a true and fair view of the state of affairs of the company and of the group and of the profit or loss of the group for that year. In preparing those accounts, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts;
- prepare the accounts on a going concern basis unless it is inappropriate to presume that the company will continue in business;

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and to enable them to ensure that the accounts comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Auditors' Report to the Shareholders of Sopheon plc (formerly Polydoc plc)

We have audited the accounts on pages 24 to 46 which have been prepared under the historical cost convention and the accounting policies set out on page 28.

Respective responsibilities of directors and auditors

The directors are responsible for preparing the annual report. As described on page 22, this includes responsibility for preparing the accounts in accordance with applicable United Kingdom law and accounting standards. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board and by our profession's ethical guidance.

We report to you our opinion as to whether the accounts give a true and fair view and are properly prepared in accordance with the Companies Act. We also report to you if, in our opinion, the directors' report is not consistent with the accounts, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if the information specified by law regarding directors' remuneration and transactions with the group is not disclosed.

We read the other information contained in the Annual Report and consider whether it is consistent with the audited accounts. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the accounts.

Basis of audit opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the accounts. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the accounts, and of whether the accounting policies are appropriate to the group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the accounts are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the accounts.

Opinion

In our opinion the accounts give a true and fair view of the state of affairs of the company and of the group at 31 December 1999 and of the loss of the group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Ernst & Young
Registered Auditor
Reading

28 April 2000

Group Profit and Loss Account for the Year Ended 31 December 1999

	Notes	*Continuing Operations 1999 £'000*	*Acquisitions 1999 £'000*	*Total 1999 £'000*	*Restated 1998 £'000*
TURNOVER	2	874	636	1,510	891
Cost of sales		(676)	(307)	(983)	(608)
GROSS PROFIT/(LOSS)		198	329	527	283
Sales and marketing expenses		(659)	(101)	(760)	(502)
Administrative expenses		(1,225)	(574)	(1,799)	(913)
Other operating income		16	-	16	29
OPERATING LOSS	3	(1,670)	(346)	(2,016)	(1,103)
Bank interest receivable				62	13
Interest payable and similar charges				(118)	(52)
LOSS ON ORDINARY ACTIVITIES BEFORE AND AFTER TAXATION				(2,072)	(1,142)
Loss per share - basic and diluted (pence)	8			(10.1p)	(6.1p)
LOSS ON AN EBITDA BASIS				(1,654)	(1,031)

EBITDA represents earnings before interest, tax, depreciation and amortisation.

GROUP STATEMENT OF TOTAL RECOGNIZED GAINS AND LOSSES FOR THE YEAR ENDED 31 DECEMBER 1999

	Notes	*1999 £'000*	*Restated 1998 £'000*
Loss on ordinary activities after taxation		(2,072)	(1,142)
Exchange difference on retranslation of net assets of subsidiary undertakings		(45)	47
Total recognized gains and losses relating to the year		(2,117)	(1,095)
Prior year adjustment	19	(373)	-
Total gains and losses recognized since last annual report		(2,490)	(1,095)

Group Balance Sheet at 31 December 1999

	Notes	*1999* *£'000*	*Restated* *1998* *£'000*
FIXED ASSETS			
Intangible assets	9	7,605	167
Tangible assets	10	386	203
		7,991	370
CURRENT ASSETS			
Debtors	12	1,362	127
Cash at bank and in hand	13	7,751	674
		9,113	801
CREDITORS: amounts falling due within one year	14	3,570	2,032
NET CURRENT ASSETS/(LIABILITIES)		5,543	(1,231)
TOTAL ASSETS LESS CURRENT LIABILITIES		13,534	(861)
CREDITORS: amounts falling due after more than one year	15	55	3
		13,479	(864)
CAPITAL AND RESERVES			
Called up share capital	17	4,491	3,773
Shares to be issued	18	10	15
Share premium account	18	17,960	2,213
Profit and loss account	18	(8,982)	(6,865)
Shareholders' funds (all equity interests)		13,479	(864)

Barry K. Mence
Executive Chairman
28 April 2000

Company Balance Sheet at 31 December 1999

	Notes	1999 £'000	1998 £'000
FIXED ASSETS			
Investments	11	13,211	4,777
CURRENT ASSETS			
Debtors	12	4,216	2,737
Cash at bank and in hand		6,984	95
		11,200	2,832
CREDITORS: amounts falling due within one year	14	1,955	1,613
NET CURRENT ASSETS		9,245	1,219
TOTAL ASSETS LESS CURRENT LIABILITIES		22,456	5,996
CAPITAL AND RESERVES			
Called up share capital	17	4,491	3,773
Shares to be issued	18	10	15
Share premium account	18	17,960	2,213
Profit and loss account	18	(5)	(5)
Shareholders' funds (all equity interests)		22,456	5,996

Barry K. Mence
Executive Chairman
28 April 2000

Group Statements of Cash Flows for the Year Ended 31 December 1999

	Notes	1999 £'000	Restated 1998 £'000
NET CASH OUTFLOW FROM OPERATING ACTIVITIES	3	(1,278)	(946)
RETURN ON INVESTMENTS AND SERVICING OF FINANCE			
Interest received		62	13
Interest paid		(116)	(50)
Interest element of finance lease rental payments		(2)	(2)
		(56)	(39)
CAPITAL EXPENDITURE & FINANCIAL INVESTMENT			
Payments to acquire tangible fixed assets		(52)	(52)
ACQUISITIONS AND DISPOSALS			
Purchase of subsidiary undertaking		(179)	(95)
Net cash acquired with subsidiary undertaking		389	2
		210	(93)
MANAGEMENT OF LIQUID RESOURCES			
(Increase) in short term deposits		(6,602)	(401)
NET CASH OUTFLOW BEFORE FINANCING		(7,778)	(1,531)
FINANCING			
Issue of ordinary share capital		8,265	110
New long term loan		4	1,571
Repayment of long term loan		-	(299)
Repayment of capital element of finance lease		(16)	(12)
		8,253	1,370
INCREASE/(DECREASE) IN CASH	13	475	(161)

1 Accounting Policies

Accounting convention
The accounts are prepared under the historical cost convention and in accordance with applicable accounting standards.

Basis of consolidation
The consolidated accounts include the results of the company and its subsidiary undertakings.
The results of AppliedNet Limited have been included since the date of acquisition, 22 November 1999.

Tangible fixed assets
Tangible fixed assets are stated at historical cost, less accumulated depreciation. Tangible fixed assets are depreciated on a straight line basis at rates ranging from 20% to 33% per annum on cost over their expected useful lives.

Research and development
Research and development expenditure is written off as incurred. The cost of registering patents and trademarks are written off as incurred. Subsidies received from the European Eureka funding programme are credited to the profit and loss account over the period to which they relate.

Prior year adjustment
Historically, development expenditure incurred for specific products was capitalized when its future recoverability could reasonably have been regarded as assured, and amortized in line with the expected future sales from the related product, to a maximum of 5 years. Following the acquisition of AppliedNet Limited and subsequent harmonization of group accounting policies, all such expenditure is now written off as incurred. The effect of changing this policy has been reflected by way of a prior year adjustment to the 1998 financial statements of the group.

Goodwill
Goodwill arising on consolidation is capitalized and amortized on a straight line basis over its estimated useful economic life, currently estimated at 3 to 5 years depending on circumstances. Goodwill is reviewed for impairment at the end of the first full financial year after acquisition and in other periods if events or changes in circumstances indicate that carrying values may not be recoverable. If a subsidiary, associate or business is subsequently sold or closed, any goodwill arising on acquisition that has not been amortized is taken into account in determining the profit or loss on sale or closure.

Foreign currencies
Company
Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction or at the contracted rate if the transaction is covered by a forward exchange contract. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the balance sheet date or if appropriate at the forward contract rate. All differences are taken to the profit and loss account.

Group
The assets and liabilities of the subsidiary undertakings are translated at the rate of exchange ruling at the balance sheet date. The profit and loss account is translated at the average rate of exchange. The exchange differences arising on the re-translation of subsidiary undertakings are, together with differences arising on the translation of long term intra-group funding loans which are not intended to be repaid in the foreseeable future, taken directly to reserves. All other differences are taken to the profit and loss account.

Long term contracts
Profit on long term contracts is taken as the work is carried out if the outcome can be assessed with reasonable certainty. The profit included is calculated on a prudent basis to reflect the proportion of the work carried out at the year end, by recording turnover and related costs as contract activity progresses. Turnover is calculated as that proportion of total contract value which costs incurred to date bear to total expected costs for that contract. Revenues derived from variations on contracts are recognized only when the customer has accepted them. Full provision is made for losses on all contracts in the year in which they are first foreseen.

Pensions
Sopheon contributes to the personal pension arrangements of employees, the costs of which are charged in the profit and loss account as incurred.

Leasing
Assets held under finance leases, which are leases where substantially all risks and rewards of ownership of the assets have passed to the group, are capitalized in the balance sheet and are depreciated over their useful lives. The capital elements of future obligations under financial leases are included as liabilities in the balance sheet. The interest element of the rental obligations are charged to the profit and loss account over the period of the lease and represent a constant proportion of the balance of capital repayments outstanding. Rentals payable under operation leases are charged in the profit and loss account on a straight line basis over the lease term.

2 Turnover and segmental information

Turnover (excluding valued added tax) represents the amounts derived from the group's principal activity which comprises the design, development, production and marketing of knowledge management software products together with associated implementation services. It operates within three geographical markets, the Netherlands, the United Kingdom and the United States of America.

Analysis of turnover by geographical destination

	1999 £'000	*1998 £'000*
United Kingdom	693	166
The Netherlands	777	722
United States of America	40	3
	1,510	891

Analysis of turnover and operating loss by geographical origin

	Operating loss			*Turnover*
		Restated		
	1999 £'000	*1998 £'000*	*1999 £'000*	*1998 £'000*
United Kingdom	346	-	636	-
The Netherlands	1,414	1,103	874	891
United States of America	256	-	-	-
	2,016	1,103	1,510	891

Analysis of net assets by geographical origin

	1999 £'000	*Restated 1998 £'000*
United Kingdom	8,054	-
The Netherlands	89	707
United States of America	(76)	-
Unallocated cash and loans at group level	5,412	(1,571)
	13,479	(864)

3 Operating loss

(a) This is stated after charging/(crediting):

	1999 *£'000*	*1998* *£'000*
Auditors' remuneration - audit services	34	20
Auditors' remuneration - non audit services	13	3
Research and development expenditure written off	878	815
Eureka subsidies	(315)	(304)
Foreign exchange differences	16	(29)
Depreciation of owned assets	74	63
Depreciation of assets held under finance leases	9	9
Operating lease rentals - land and buildings	103	94
Operating lease rentals - motor vehicles	84	79

During 1999 £64,000 was charged by the auditors in respect of work associated with due diligence and fund raising which has been capitalized or written off to share premium as appropriate.

The 1998 results have been restated to reflect the prior year adjustment described in note 19, whereby development costs that have been capitalized and amortized in the past are now written off as they arise. The results have also been restated whereby certain costs, mainly relating to internal research and development activities, have been reallocated from cost of sales to administration costs. Both of these changes were undertaken to bring accounting policies and disclosures into line on a group basis following the acquisition of AppliedNet Limited. Finally, in the 1998 and previous accounts, amounts disclosed as research and development costs written off included cost of sales items relating to customer led projects that were developmental in nature. The disclosures above exclude these costs.

Had the same allocation of costs been used, and had the prior year adjustment not been recorded, consolidated research and development costs would have been reported as £1,391,000 (1998 - £1,197,000) and consolidated cost of sales would have been reported as £1,383,000 (1998 - £892,000).

Reconciliation of operating loss to net cash outflow from operating activities

	1999 *£'000*	*1998* *£'000*
Operating loss	(2,016)	(1,103)
Depreciation	83	72
Amortisation	323	-
Decrease in debtors	(338)	9
Increase/(decrease) in creditors and provisions	715	30
Exchange movements	(45)	46
Net cash outflow from operating activities	(1,278)	(946)

4 Staff costs

	1999 *£'000*	*1998* *£'000*
Wages and salaries	1,231	857
Social security costs	124	74
Other pension costs	42	29
	1,397	960

The fees and emoluments of all directors were as follows:

	1999 *£'000*	*1998* *£'000*
Fees	24	19
Other emoluments	25	29
Salary	235	238
Benefits	49	47
Pension contributions	15	15
	348	348

Pension contributions are to personal defined contribution schemes and are made for five directors.
The emoluments of the highest paid director were as follows:

	1999 *£'000*	*1998* *£'000*
Basic Salary	78	79
Benefits	16	16
Pension contributions to defined contribution scheme	7	7
Total	101	102

The average monthly number of employees during the year was made up as follows:

	1999 *Number*	*1998* *Number*
Development and operations	26	21
Sales and management	14	10
	40	31

5 Interest payable and similar charges

	1999 £'000	1998 £'000
Bank loans and overdrafts	39	16
Convertible loan stock	78	34
Finance charges on finance leases	1	2
	118	52

6 Taxation

There was no tax charge for 1999 or 1998. Tax losses are available for carry forward by the Group the amount of which is under discussion with the relevant authorities in the UK and the Netherlands. In accordance with the group's policy no provision has been made for the potential deferred tax asset on these losses.

7 Loss attributable to members of the parent company

The loss dealt with in the accounts of the parent company for 1999 was £nil (1998 - £nil). Advantage has been taken of Section 230 of the Companies Act 1985 not to present a profit and loss account for the parent company.

8 Loss per ordinary share

The calculation of basic loss per ordinary share is based on a loss of £2,072,000 (1998 – £1,142,000 as restated) and 20,565,985 (1998 – 18,730,633) ordinary shares, being the weighted average number of ordinary shares in issue during the year.

The effect of all potential ordinary shares is antidilutive in 1998 and 1999.

The historic earnings per share calculations are not affected by the restructuring of share capital described in note 17 below because the total number of ordinary shares in issue did not change as a result of the restructuring.

9 Intangible fixed assets

Group only

	Goodwill £'000	Development costs £'000	Total £'000
COST			
At 1 January 1999	167	466	633
Prior year adjustment	-	(466)	(466)
Adjustment	(5)	-	(5)
Additions	7,766	-	7,766
At 31 December 1999	7,928	-	7,928
AMORTISATION			
At 1 January 1999	-	93	93
Prior year adjustment	-	(93)	(93)
Provided during the year	323	-	323
At 31 December 1999	323	-	323
NET BOOK VALUE			
At 31December 1999	7,605	-	7,605
At 31December 1998	167	373	540
Prior year adjustment	-	(373)	(373)
At 31 December 1998 (restated)	167	-	167

The prior year adjustment is discussed in note 19. The other adjustment represents reduction in contingent consideration payable for Lessenger Associates BV as described in note 11.

10 Tangible fixed assets

Group only

	Computer Equipment £'000	*Furniture & fittings £'000*	*Total £'000*
COST			
At 1 January 1999	282	117	399
Exchange adjustments	(32)	(13)	(45)
Acquired with subsidiary undertaking	324	58	382
Additions	69	2	71
At 31 December 1999	643	164	807
DEPRECIATION			
At 1 January 1999	149	47	196
Exchange adjustments	(20)	(6)	(26)
Acquired with subsidiary undertaking	158	11	169
Provided during the year	57	25	82
At 31 December 1999	344	77	421
NET BOOK VALUE			
At 31 December 1999	299	87	386
At 31 December 1998	133	70	203

The net book value of furniture and fittings above includes an amount of £18,000 (1998 – £27,000) in respect of assets held under finance leases.

11 Investments

Company	*Investment in subsidiary undertakings £'000*
COST	
At 1 January 1999	4,777
Adjustment to consideration for Lessenger (see below)	(5)
Additions	8,439
At 31 December 1999	13,211

The group acquired Lessenger Associates BV in 1998 and included in the consideration was up to a maximum of 10,000 shares to be issued at £1.46 contingent on certain conditions based on 1999 performance. These conditions were not met in full and only 7,114 shares are required to be issued, reducing the contingent consideration to £10,386.

On 22 November 1999 the group completed the acquisition of AppliedNet Limited (renamed Sopheon UK Limited) for consideration of 6,402,961 ordinary shares of Sopheon plc in respect of the entire ordinary share capital of AppliedNet and cash of £11,000 in respect of its entire preference share capital, as well as attributed costs of £168,000. The market value of Sopheon plc's ordinary shares on 27 October 1999, the date the acquisition became unconditional, was 129p. Accordingly, the total cost recorded in respect of the acquisition was £8,439,000.

Analysis of the acquisition of AppliedNet Limited:

	Book and fair value £'000
Tangible fixed assets	213
Debtors	899
Cash	389
	1,501
Creditors falling due within one year	(826)
Creditors falling due in more than one year	(2)
Net assets	673
Goodwill arising on acquisition	7,766
	8,439
Discharged by:	
Fair value of shares issued	8,260
Attributable costs	168
Cash	11
	8,439

In the view of the directors there were no fair value adjustments required. AppliedNet Limited had a loss before tax of £1,097,000 in the 15 months ended 31 December 1999 (year ended 30 September 1998 profit before tax of £208,000). There was turnover of £2,693,000 and a loss before and after tax of £1,002,000 in the period 1 October 1998 to 22 November 1999. There were no recognized gains and losses other than the loss for the period.

11 Investments (continued)

Details of the investments in which the group or company holds more than 20% of the nominal value of any class of share capital are set out below. Companies marked with an asterisk * are held via Sopheon UK Limited (formerly AppliedNet Limited).

Name of Company *Country of incorporation*	*Holding*	*Proportion of voting rights*	*Nature of Business*
Sopheon NV The Netherlands	Ordinary Shares	100%	Knowledge management software and services
Lessenger BV The Netherlands	Ordinary Shares	100%	Document management software and services
Sopheon UK Ltd United Kingdom	Ordinary Shares	100%	Knowledge management software and services
Network Managers (UK) Ltd United Kingdom*	Ordinary Shares	100%	Network management software and services
Futuretense UK Ltd United Kingdom*	Ordinary Shares	100%	Dormant
Futuretense Ltd United Kingdom*	Ordinary Shares	100%	Dormant
SageWare Europe Ltd United Kingdom*	Ordinary Shares	100%	Dormant
Applied Network Technology Ltd United Kingdom*	Ordinary Shares	100%	Employee Share Ownership Trust

12 Debtors

Group

	1999 *£'000*	*1998* *£'000*
Trade debtors	1,104	85
Other debtors	86	-
Prepayments and accrued income	172	42
	1,362	127

Company

	1999 *£'000*	*1998* *£'000*
Amounts owed by subsidiary undertakings	4,200	2,737
Other debtors	16	-
	4,216	2,737

13 Notes to Statement of Cash Flows

(a) Reconciliation of net cash flow to movement in net funds.

	1999 *£'000*	*1998* *£'000*
(Decrease)/increase in cash	475	(161)
Repayment of long term loans	4	299
New loans	(8)	-
Cash inflow from increase in debt	-	(1,571)
Repayments of capital elements of finance leases	16	12
Cash inflow/(outflow) from change in liquid resources	6,602	401
Change in net debt resulting from cash flows	7,089	(1,020)
Loans and finance leases acquired with subsidiary	(92)	-
Movement in net funds/(debt)	6,997	(1,020)
Net funds/(debt) at 1 January	(917)	103
Net funds/(debt) at 31 December	6,080	(917)

(b) Analysis of changes in net funds

	Cash at bank *£'000*	*Short term deposits/ liquid resources** *£'000*	*Term loans* *£'000*	*Convertible loan stock* *£'000*	*Finance leases* *£'000*	*Total* *£'000*
At 1 January 1999	272	402	-	(1,571)	(20)	(917)
Cashflow	475	6,602	(4)	-	16	7,089
Acquisitions	-		(86)	-	(6)	(92)
At 31 December 1999	747	7,004	(90)	(1,571)	(10)	6,080

*Short term deposits/liquid resources are included within cash at bank and in hand on the balance sheet.

14 Creditors: amounts falling due within one year

Group

	1999 *£'000*	*1998* *£'000*
Convertible loan stock 5%	1,571	1,571
Current installments due on bank loan	28	-
Obligations under finance leases	8	17
Trade creditors	619	306
Other taxes and social security costs	241	25
Accruals and deferred income	708	113
Other creditors	395	-
	3,570	2,032

The convertible loan stock carries an interest rate of 5% and was issued to the company's three largest shareholders on 31 July 1998. It was repayable or convertible into ordinary shares at a conversion price of £1.46 on 31 July 1999, at the option of the loan stockholders. On 12 April 1999, the repayment or conversion option was extended by the loan stockholders to 31 July 2000. Interest on the convertible loan stock is payable on 30 June and 31 December.

Company

	1999 *£'000*	*1998* *£'000*
Convertible loan stock 5%	1,571	1,571
Other creditors	373	-
Other taxes and social security costs	10	2
Accruals	1	40
	1,955	1,613

15 Creditors: amounts falling due after more than one year

Group

	1999 *£'000*	*1998* *£'000*
Obligations under finance leases	1	3
Bank loan	54	-
	55	3

The bank loan is a UK asset purchase facility at an implicit rate of 8.8% and is repayable in 36 equal installments from October 1999.

16 Obligations under leases

Amounts due under finance leases and hire purchase contracts:
Group only

	1999 £'000	1998 £'000
Amounts payable:		
Within one year	8	17
In two to five years	1	4
	9	21
Less finance charges allocated to future periods	-	1
	9	20

The company had no amounts due under finance leases and hire purchase contracts. At 31 December 1998 and 1999 the group had annual commitments under operating leases as set out below.

Group

	Other 1999 £'000	Land & buildings 1999 £'000	Other 1998 £'000	Land & buildings 1998 £'000
Operating leases which expire:				
within one year	64	176	26	-
in two to five years	97	51	63	100
Totals	161	227	89	100

The company had commitments under operating leases as at 31 December 1999 amounting to £12,000 (1998 - £4,000) expiring within one year and £nil expiring within two to five years (1998 - £12,000).

17 Share capital

Authorized	1999 Number	1999 £	1998 Number	1998 £
Ordinary shares of 20p each	-	-	30,000,000	6,000,000
Ordinary shares of 5p each	42,902,961	6,645,148	-	-
Deferred shares of 15p each	19,228,885	2,884,333	-	-

Allotted, called up and fully paid	1999 Number	1999 £	1998 Number	1998 £
Ordinary shares of 20p each	-	-	18,863,885	3,772,777
Ordinary shares of 5p each	32,131,846	1,606,592	-	-
Deferred shares of 15p each	19,228,885	2,884,333	-	-
	51,360,731	4,490,925	18,863,885	3,772,777

17 Share capital (continued)

On 15 October 1998, 30,000 ordinary shares were issued for cash at 20p each. On 20 October 1998 10,000 were allotted for cash to an exercising holder of share options at 20p each. On 9 December 1998 68,500 ordinary shares of 20p each were issued at £1.46 for cash and a further 40,000 ordinary shares of 20p each were issued at £1.46 as part consideration for the acquisition of Lessenger Associates BV. As described in note 11 a further 7,114 ordinary shares will be issued to the vendors of Lessenger Associates BV in connection with a contingent consideration arrangement.

An Extraordinary General Meeting of the Company held on 28 July 1998, approved the subscription of each of B.K. Mence, NPM Capital NV and Brandon Limited, of £523,640 5% Convertible Loan Stock at par the conversion terms of which are described in note 14, as well as the award of 300,000 Warrants each. The Warrants did not attract any consideration. Each Warrant entitles the holder to subscribe on or before 31 December 2000, for the one Ordinary Share of £1.46 per share. If not exercised by that date the Warrants shall lapse.

On 20 January 1999 5,000 ordinary shares were issued for cash to an exercising holder of share options at 20p each. On 10 March 1999 340,000 ordinary shares were issued to institutions for cash at a price of £1.47 per share. On 28 April 1999 20,000 ordinary shares were issued for cash to an exercising holder of share options at 20p each.

On 22 November 1999 in an Extraordinary General Meeting of the Shareholders the share capital of Sopheon plc was restructured such that each ordinary share of 20p was converted into one ordinary share of 5p and one deferred share of 15p. The deferred shares carry no rights as to dividend, voting or return of capital on liquidation, and are not listed on any exchange. The number of ordinary shares in issue did not change as a consequence of the restructuring. Similarly, the number, exercise price and other terms of any share options over Ordinary Shares of 20p each remained unchanged as a consequence of the restructuring.

On the same date 6,500,000 ordinary shares of Sopheon plc were placed with institutions at a price of 125p per ordinary share, realizing net proceeds after attributed costs of £7,699,000. Furthermore as referred to in note 11, 6,402,961 ordinary shares of Sopheon plc were issued as consideration for the acquisition of 100% of the ordinary share capital of AppliedNet Limited, at a price of 129p per ordinary share.

Share option scheme

The directors have specified a maximum of 5% of ordinary shares over which options could be granted under any employee share option scheme. Share options are granted by the Board of directors on a discretionary basis under the terms of various schemes as summarized below.

On 28 August 1996 the directors adopted, and the company in general meeting approved, a share option scheme to provide for the grant to certain directors and employees of PolyDoc NV of options over Ordinary Shares in exchange for the surrender by such directors and employees of their existing options over shares in PolyDoc NV. The scheme also provided for the grant by the company of subsequent new options over Ordinary Shares to employees of the Group. On the same date the directors adopted, and the company in general meeting approved, an executive share option scheme in a form approved by the Inland Revenue.

Since the establishment of the schemes several option grants have been made. None of the grants have been made under the Inland Revenue approved scheme however in the majority of cases the rights of the options granted have been consistent with the rights they would have had under that scheme. Certain grants, in particular those relating to employees in the USA, have involved different vesting arrangements whereby employees are entitled to exercise a proportion of their options each year rather than have all of them becoming exercisable at a particular date.

Pursuant to the acquisition of AppliedNet Limited, all options granted under the AppliedNet unapproved share option scheme were released in exchange for the grant of new options over shares in Sopheon plc. The new options are subject to the rules of the original AppliedNet scheme.

A summary of options granted up to and including 1999 is listed below.

Year of grant	*Number*	*Exercise Price*	*Convertible From*	*Convertible To*
1996	660,000	0.2000	28-08-96	21-07-01
1997	10,000	0.8950	04-02-00	04-02-07
1997	1,000	1.9750	01-06-00	01-06-07
1997	20,000	1.7750	01-07-00	01-07-07
1998	36,500	1.7000	29-06-98	29-06-03
1998	30,000	1.7000	29-06-01	29-06-08
1998 (1)	218,008	0.0860	29-12-01	29-12-08
1999	17,500	1.4150	20-01-02	20-01-09
1999	10,000	1.4150	20-01-99	20-01-04
1999 (1)	87,209	0.0860	04-03-02	04-03-09
1999	65,000	1.5000	28-04-99	28-04-04
1999 (2)	42,500	1.5000	28-04-00	28-04-09
1999 (1)	13,080	0.8732	01-06-02	01-06-09
1999 (1)	74,150	0.8732	01-10-02	01-10-09
1999 (2)(3)	75,000	1.5000	03-11-00	03-11-09
1999	50,000	1.5000	03-11-02	03-11-09
1999 (3)	100,000	1.5000	22-11-02	22-11-09

(1) Options arising as a result of options held by employees of AppliedNet and rolled over into Sopheon options.

(2) One fourth of these options become exercisable each year starting on the date indicated. All other options become exercisable in full from the date indicated.

(3) Includes options which are contingent upon certain performance targets.

Options granted to directors are specified in the Directors report.

18 Shareholders' funds

Group

	Share capital £'000	*Shares to be issued £'000*	*Share Premium Account £'000*	*Profit & Loss Account £'000*	*Total £'000*
At 1 January 1998	3,743		2,076	(5,558)	261
Arising on share issues	30	-	137	-	167
Shares to be issued	-	15	-	-	15
Retained loss for the year	-	-	-	(981)	(981)
Exchange differences on retranslation of net assets and results of subsidiary undertaking	-	-	-	47	47
At 31 December 1998	3,773	15	2,213	(6,492)	(491)
Prior year adjustment	-	-	-	(373)	(373)
At 31 December 1998 restated	3,773	15	2,213	(6,865)	(864)
Arising on share issues	718	-	15,747	-	16,465
Adjustment to earn out	-	(5)	-		(5)
Retained loss for the year	-	-	-	(2,072)	(2,072)
Exchange differences on retranslation of net assets and results of subsidiary undertaking	-	-	-	(45)	(45)
At 31 December 1999	4,491	10	17,960	(8,982)	13,479

The prior year adjustment is described in note 19.

The adjustment to earn out represents an adjustment to contingent consideration payable in respect of Lessenger Associates BV as described in note 11.

Company

	Share capital £'000	*Shares to be issued £'000*	*Share Premium Account £'000*	*Profit & Loss Account £'000*	*Total £'000*
At 1 January 1998	3,743	-	2,076	(5)	5,814
Arising on share issues	30	-	137	-	167
Shares to be issued	-	15	-	-	15
At 31 December 1998	3,773	15	2,213	(5)	5,996
Arising on share issues	718	-	15,747	-	16,465
Adjustment to earn out	-	(5)	-	-	(5)
At 31 December 1999	4,491	10	17,960	(5)	22,456

The adjustment to earn out represents an adjustment to contingent consideration payable in respect of Lessenger Associates BV as described in note 11.

19 Prior year adjustment

Historically, development expenditure incurred for specific products was capitalized when its future recoverability could reasonably have been regarded as assured, and amortized in line with the expected future sales from the related product, to a maximum of 5 years. Following the acquisition of AppliedNet Limited and subsequent harmonization of group accounting policies, all such expenditure is now written off as incurred. The effect of changing this policy has been reflected by way of a prior year adjustment to the 1998 financial statements of the group, and has required a one off adjustment of £373,000 being a net debit to reserves. If the original policy had been continued, reported operating loss for 1999 would have been £7,000 higher.

20 Derivatives and other financial instruments

The group's approach to managing financial risk is described in the Directors Report on pages 18 to 21.

Interest rate risk profile of financial liabilities
Excluding the Convertible Loan Stock which bears a fixed rate of 5% on a nominal value of £1,570,920, all the financial liabilities of the group at each year or period end are set out below.

	1999 *£ '000*	*1998* *£ '000*
Fixed rate loans and overdrafts - Sterling	82	-
Fixed rate loans and leases - Dutch Guilder	9	20
	91	20

These financial liabilities bear interest rates that are based on local bank rates.

20 Derivatives and other financial instruments (continued)

Interest rate risk profile of financial assets

The financial assets of the group at each year or period end comprise cash or cash deposits on money market deposit at call and monthly rates. The amounts were as follows:

	1999 *£'000*	*1998* *£'000*
FLOATING RATE		
Sterling	7,004	-
Dutch Guilder	-	379
US Dollar	-	-
	7,004	379
NON-INTEREST BEARING		
Sterling	496	95
US Dollar	97	-
Dutch Guilder	154	200
	747	295
Total financial assets	7,751	674

Currency exposures

The table below shows the group's transactional currency exposures that give rise to the net currency gains and losses recognized in the profit and loss account. Such exposures comprise the monetary assets and monetary liabilities of the group that are not denominated in the operating currency of the operating unit involved, and have arisen only in operating units with a functional currency of sterling.

	Net foreign currency monetary assets			
	US dollar £'000	*Dutch Guilder £ '000*	*Other Currency £ '000*	*Total £ '000*
1998 Sterling	-	379	-	379
1999 Sterling	107	-	-	97

Maturity of financial liabilities

The maturity profile and interest rates of the group's financial liabilities at each relevant period or year end is as set out in Notes 14 and 15.

Borrowing facilities

The group had no undrawn committed facilities available at each relevant period or year end apart from overdraft facilities.

Fair values of financial assets and liabilities

The fair values of financial assets and liabilities are set out below. Finance leases are included in the analysis of long term borrowings. The directors consider that there were no material differences between the book values and fair values of all the group's financial assets and liabilities at each year and period end. As described in note 17, the holders of convertible loan stock are entitled to convert their loan stock and an additional 900,000 warrants at a price of £1.46 per ordinary share.

		Book value
	1999 £ '000	*1998 £ '000*
Cash and short term deposits	7,751	674
Convertible Loan Stock	(1,571)	(1,571)
Current portion of long term borrowings	(36)	(17)
Long term borrowings	(55)	(3)

21 Contingent liabilities

In accordance with Article 403, Paragraph 1, Subsection b, Book 2 of the Dutch Civil Code (B.W.), Sopheon plc guarantees the liabilities of Sopheon NV and agrees with the departure from the regulations in Title 9 Book 2 of the Dutch Civil Code (B.W.), that prescribes the submission of the accounts of Sopheon NV to the Trade Register in Holland. As a consequence Sopheon NV need not file its accounts at the Trade Register.

22 Events since the balance sheet date

Since the year end, and as noted in previous reports, the group has committed funds of £430,000 for a 25% equity stake in ProGram BV, a company established with a number of Dutch healthcare institutions to market knowledge management solutions incorporating Sopheon's software to the Dutch healthcare industry.

Since the year end 455,000 ordinary shares in Sopheon plc have been issued for £91,000 in cash to option holders exercising their options, giving rise to a premium of £68,250. Furthermore, since the year end the directors have approved the grant of options over 82,360 ordinary shares.

A placing of 2,622,500 shares for cash of 800p per share, and a potential acquisition, was announced on 3 March 2000 further details of which are given in the directors report.

As detailed in the directors' report, since the year end Sopheon has entered into an agreement to acquire Teltech Resource Network Corporation, a knowledge management business based in Minneapolis, USA for a minimum net consideration of $34 million comprising a combination of cash, shares and options.

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