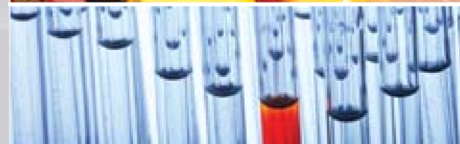
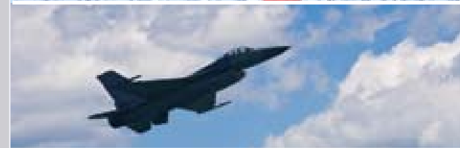
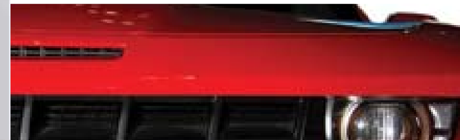
SOPHEON 2008

ANNUAL REPORT







sopheon

Where innovation means business™

Sopheon is an international provider of software and services.
Sopheon's software applications automate product development
and strategic product planning, delivering efficiencies
and decision support that enable companies to generate
more revenue and profit from product innovation.

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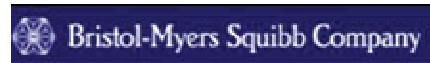
Sopheon's software solves the challenge of synchronizing innovation planning and execution – an industry first – with new capabilities that address the needs of a growing range of companies.

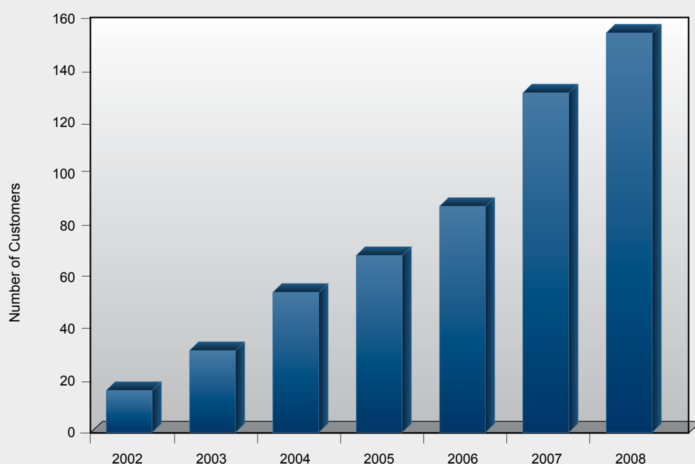


Summary Results and Trends

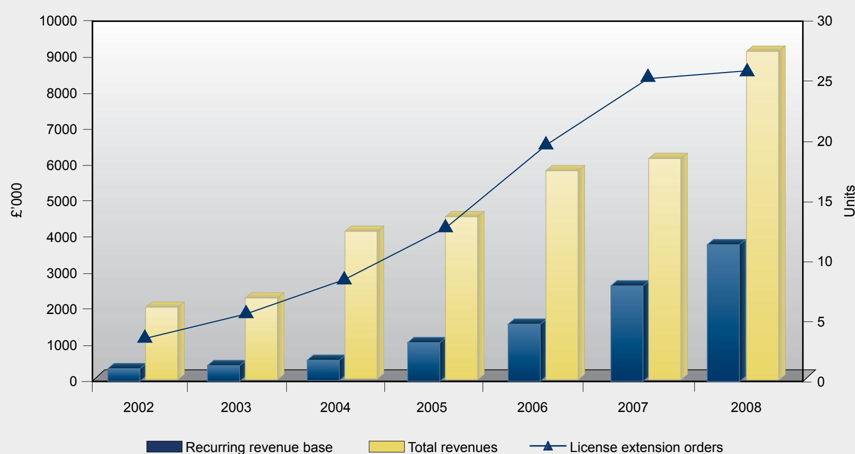
		2008	2007	2006	2005
Revenue	**£'000**	**9,304**	**6,332**	**6,045**	**4,664**
EBITDA	**£'000**	**1,120**	**113**	**33**	**(746)**
Profit before tax	**£'000**	**44**	**(443)**	**(303)**	**(1,236)**
Earnings per share	**pence**	**0.02**	**(0.32)**	**(0.23)**	**(0.94)**
Net assets	**£'000**	**4,268**	**3,310**	**1,620**	**1,951**
Gross cash	**£'000**	**2,586**	**2,053**	**1,034**	**1,970**
Working capital	**£'000**	**3,068**	**2,140**	**1,667**	**1,932**
Long term liabilities	**£'000**	**(1,105)**	**(1,195)**	**-**	**-**

Working capital is calculated as net current assets after adding back deferred income.

2008 was a year of strong growth in revenues and a transformation in EBITDA. In spite of considerable amortization and interest costs, we delivered a positive profit before tax. All key balance sheet metrics improved.



During 2008 we grew our customer base to 157 licensees.



We have grown our business by an annualized average of 36 percent since the launch of Accolade. Our existing customers accounted for over 60 percent of total revenues in 2007 and 2008, providing a solid platform for growth.

STATEMENT FROM THE CHAIRMAN AND CHIEF EXECUTIVE OFFICER

Performance

Sopheon delivered a landmark performance in 2008. We are delighted to report revenues that grew from £6.3m to £9.3m, EBITDA of £1.1m (2007: £0.1m) and a profit after tax of £29,000 (2007: loss of £443,000).

License sales were spread across a total of 53 new and extension orders compared to 47 transactions the year before. We entered 2008 with a licensee base of 135 companies, and grew this to 157 by the end of the year. Performance was geographically balanced, with both the US and Europe showing revenue growth in excess of 40 percent. Our reseller partners accounted for 11 percent of the total, up from 6 percent in the previous year. Vision Strategist™, the solution that we acquired with Alignent in June 2007, contributed 13 percent of revenues in 2008. The remainder was Accolade® related.

Our recurring revenue base coming into 2009 was £3.7m. By comparison, we entered 2008 with recurring revenues totalling £2.6m. Overall, 65 percent of revenues in 2008 came from current customers, highlighting the opportunity that we have to continue to expand the use of our solutions inside existing accounts.

At the date of this report, full-year 2009 revenue visibility incorporating booked revenue, contracted services business and the run rate of recurring contracts already stands at £5.4m. Revenue visibility is more fully defined in Note 3.

These developments underline the growing maturity of our business. However, particularly in these uncertain economic times, our reported performance does remain sensitive to the timing, value and profile of individual sales events.

Strategy and Product

Our acquisition of Alignent in 2007 has been fully integrated and is contributing both strategically and operationally to the progress of our business. Revenues for Alignent's Vision Strategist grew 28 percent compared to the solution's annualized contribution in 2007. Our expectation that the software would improve our ability to break into the aerospace and defense sectors has been validated. Throughout 2008, we invested substantial time and energy in these markets, learning their dynamics and requirements while developing the relationships needed to generate business. As a result of these efforts, we entered 2009 with an active pipeline of significant sales opportunities in these sectors.

Investment in product development has remained a cornerstone of our business philosophy. During 2008 our development team completed four product releases, two each for Accolade and Vision Strategist. This included, in the first quarter, the most significant new release of Accolade since the software was introduced to the market more than seven years ago. These releases have positioned Sopheon for continued leadership in the market.

Accolade® is a registered trademark of Sopheon plc.
Vision Strategist™ is a trademark of Sopheon plc.

Moreover, we believe that our 2008 results reflect the fact that our software can bring immediate value to recession-plagued companies that need to reduce costs, without undercutting their prospects for long-term growth. Our solutions help companies maximize returns from available resources when times are tough, while also supporting the development of programs and strategies to enable them to accelerate out of the downturn and emerge with increased competitive strength. In particular, our software can help them to:

- Improve strategic agility and "uncertainty planning"
- Make faster, better-informed portfolio decisions
- Identify, prioritize and act on the most promising innovation opportunities
- Keep daily operational activities aligned with organizational strategies for growth
- Cut costs by improving innovation process and team efficiencies

These are mission critical improvements in these turbulent times.

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 continuing contribution to our growing success. Over the last two years, we have welcomed many new staff to the Sopheon team; by the end of 2008 we had 105 employees, compared to 65 at the end of 2006 and 92 at the end of 2007.

Sopheon's executive management team has been in place for several years. It has five members. Our Chief Financial Officer Arif Karimjee and the two of us serve on the team, and also act as executive directors. Our Chief Technology Officer Paul Heller and Vice President of Research Huub Rutten complete the group. Executive management is complemented by a strong operational management team that lead the marketing, sales and customer services functions in each of the US and Europe. The Sopheon plc board is made up of the three executive directors, augmented by three non-executive directors, who bring a wealth of knowledge and experience to our business. Details about each of the directors are on the inside back cover of this report.

Outlook

By the end of 2008, Sopheon had 157 licensed customers with strong representation from each of our target markets. During the year, we were recognized by members of the analyst community not just as a best-of-breed offering, but as the most mature within our class of applications.

Companies understand the business importance of continued, prudent investment in product innovation, and Sopheon addresses that need. We are enjoying significant repeat business from our customer base, coupled with a good number of high-quality new clients; since the start of the market downturn, organizations such as Bayer HealthCare, Burger King, Novartis, PepsiCo and the U.S. Army have adopted our software. During the same period, existing customers such as General Motors, Medtronic, Lockheed Martin, SABMiller and Verizon Wireless extended their investment in our solutions.

Anecdotal evidence indicates that many of these investments were made not in spite of the recession, but because of it. However, we are very conscious that the current level of uncertainty in the economic environment is unprecedented, and a number of major corporations find themselves fighting for survival. Although our sales pipelines remain very active, some potential customers are simply deferring all capital investment decisions, irrespective of their potential return. Accordingly, it is tough to predict growth with any accuracy. In response, we have developed tight operational plans that make spending contingent on historic and forecasted revenue performance on a quarter-by-quarter basis. This cautious mindset may well affect our growth trajectory in the short term, but will underpin all hiring and expenditure decisions throughout 2009.

Revenue visibility for 2009 already stands at £5.4m. This gives us a solid base from which to pursue our business goals. We believe that our solutions offer compelling value to companies faced with the need to cut costs without jeopardizing their strategies for growth. However, the market promise is countered by turmoil across the economic landscape. We face this uncertain environment with caution, but with continued optimism.

Barry Mence
Executive Chairman

Andy Michuda
Chief Executive Officer

25 March 2009

FINANCIAL AND OPERATING REVIEW

Trading Performance

Sopheon's consolidated turnover grew to £9.3m (2007: £6.3m). From a geographical standpoint, revenues for the US business increased by approximately 50 percent, with 42 percent growth in Europe. This performance was boosted to a degree by a weakening of the annual average exchange rate between Dollar and Sterling from 1.9969 in 2007 to 1.8521 in 2008. Nevertheless, in dollar terms, total revenues were $17.2m compared to $12.7m in 2007, representing growth of 35 percent, a very creditable performance given the economic conditions. The annualized average growth of the business since the launch of Accolade eight years ago is approximately 36 percent.

Total license transactions including extension orders rose from a total of 47 in 2007 to 53 in 2008. This included 15 transactions relating to the Vision Strategist solution, acquired with the Alignent business in June 2007. Overall, the former Alignent business contributed approximately 13 percent of total revenues during 2008.

Although both our core regions demonstrated strong growth in revenues for 2008, the US business accounted for 63 percent and 64 percent of our total revenues in 2007 and 2008 respectively, and we believe this emphasis will continue.

Business Mix

Overall, in 2008 our business delivered a 44:28:27 ratio of license, maintenance, service respectively compared to 34:29:37 in the prior year. In our last report we had predicted that the proportion of license revenues would rise in 2008, assisted in part by the effect of the transactions that were deferred from the end of 2007, and indeed license revenue almost doubled in Sterling terms.

Consulting revenues grew by almost 40 percent and we expect this to continue to expand steadily, providing a source of stability and maturity to our business even though it may become a smaller overall proportion as license revenues become more prevalent. Services business from existing customers had grown sharply to £1.2m in 2007, and we were pleased to maintain this performance with £1.3m of such business recorded during 2008. While we are very proud of the achievements of our services staff, we believe that in time services will moderate as a proportion of our total revenues by the effect of license business coming through partners, for which associated services work is unlikely to be performed by Sopheon.

Overall revenues from existing customers remained above 60 percent of total revenues for the second year in a row. We believe this underlines both the value of our solutions and the increasing stability of the business.

Recurring income has grown to £3.7m coming into 2009, compared to £2.6m a year before. The majority of this income is represented by maintenance services, but also includes hosting services and license rentals.

Overall gross margins have held fairly steady at 75 percent (2007: 73 percent) but this continues a trend of improvement, with 2006 at 72 percent. One factor that affects margin is the degree to which our services group recruits permanent staff as opposed to using subcontractors. We have gradually built-up our internal resources over the last two years, carefully matching growth in resources to growth in revenue but successfully reducing reliance on subcontractors. This has increased the strength of the services team from 18 to 30 over the two-year period, of which five joined in 2008. In future, margins may also be slightly affected by decisions to embed, rather than build, certain third-party components or methods of working into our software.

Research and Development Expenditure

The R&D effort in 2008 continued the theme of advancing the capabilities in parallel of both of our key product offerings, namely Accolade and Vision Strategist. As a consequence we delivered four releases during the year, two for each product. This effort included the release in the first quarter of the most significant new version of Accolade in Sopheon's history – version 7.0 – which has extended our value not only to the process manufacturing markets that we have historically targeted, but also to the large aerospace, defense and automobile sectors.

Headline R&D expenditure almost doubled, but half of this can be attributed to an increase of £0.5m in amortization and impairment charges. Of this, £0.2m represents higher amortization costs for the group's internally generated R&D assets, largely relating to the Accolade 7.0 release. A further £0.1m is due to the full year effect of amortizing the R&D assets acquired with Alignent in June 2007. The final £0.2m represents impairment charges taken against the Alignent R&D asset. As further detailed in note 14, the decision by certain customers to terminate or convert their legacy installations of Vision Strategist affected the recurring revenue base which formed part of the valuation of the intangible assets acquired with Alignent. The board does not believe that these events have any bearing on the commercial and strategic justification for the Alignent acquisition.

Accordingly, ignoring the effect of the capitalization and amortization of such costs, total R&D expenditure increased by almost £0.5m compared to 2007. Since 2001 Sopheon has maintained R&D spend at above 20 percent of revenues. Sopheon is committed to product leadership and R&D excellence is a core competency of the group. Building on recruitment that took place across 2007, we increased R&D staff from 29 to 33 during 2008. Much of the additional resource was devoted to the research and requirements work associated with the early phases of several planned new releases, in addition to sustaining work to keep existing releases in step with platform changes. As a result of the above, the amount of 2008 R&D expenditure that met the criteria of IAS38 for capitalization remained flat at £0.8m (2007: £0.8m).

Operating Costs

Overall staff costs have increased by approximately £1.6m. Three principal factors have contributed to the increase. Approximately £0.6m can be attributed to the fall in the exchange rate for Sterling against the US dollar and the Euro, the currencies in which the majority of the group's employment costs are denominated. A further £0.2m is due to a higher level of bonus being earned by the group's employees as a result of the improvement in financial results over 2007. The remaining amount can be attributed to the impact of our increased staffing levels. During 2007, headcount rose from 65 to 92, leading to an average of 85 for the year; these staff members joined throughout the year, so the full year cost effect of the expansion did not arrive until 2008. During 2008, we expanded resources to a total of 105 by the end of the year, for an average of 98 during the year. These expansions occurred in the three key operational areas, namely research and development, distribution (sales and marketing), and customer services.

Detailed comments regarding customer services and research and development costs are noted above.

Headline distribution costs were £1m higher than the previous year. This included £0.1m for the full year effect of amortizing the intangible customer assets acquired with Alignent in June 2007, and £0.2m of impairment charges taken in the year against that same asset for the reasons given in the discussion of R&D costs above. Of the remaining £0.7m, over £0.2m of the increase is due to higher bonus and commission payments linked to the higher performance achieved. The remaining increase is due to higher investment in sales and marketing resources in line with revenue growth, in addition to currency exchange factors.

Headline administration costs have fallen by £0.2m. This fall can largely be attributed to exchange gains recorded on the foreign currency cash balances held in Sopheon plc. Underlying administration costs have remained broadly flat year on year; administration staff and related costs have not been expanded during the period, and provisions recorded against investments and loans to the group's reseller partners has remained in line with prior year levels. We continue to operate a conservative policy with regard to the recoverability of such investments.

Results

The combined effect of the revenue and cost performance discussed above had a dramatic effect on Sopheon's EBITDA performance for 2008 which rose to £1.1m (2007: £0.1m).

In common with other businesses in our sector, Sopheon measures its annual performance using EBITDA (Earnings before Interest, Tax, Depreciation and Amortization) which the board believes provides a useful indicator of the operating performance of our business by removing the effect on earnings of tax, capital spend and financing. EBITDA is further defined and reconciled to the profit before tax in Note 12 of the financial statements.

Our calculation of EBITDA is stated after charging (i) share based payments of £0.1m (2007: £0.1m); (ii) impairment charges of acquired intangible assets of £0.3m (2007: £nil); and (iii) exchange gains of £0.2m (2007: £49,000) but excludes depreciation and amortization charges for the year of £0.9m (2007: £0.5m) and net finance costs of £0.2m (2007: £0.1m).

Including the effect of interest, depreciation and amortization, the group reported a profit before tax for the year of £44,000 (2007: loss £0.4m). Although the group has substantial accumulated tax losses in all territories, certain tax jurisdictions do not permit a complete offset of profits against such losses resulting in a small US "Alternative Minimum Tax" charge that reduces the retained profit after tax to £29,000. The profit per ordinary share was 0.02p (2007: loss of 0.32p).

Financing and Balance Sheet

Net assets at the end of the year stood at £4.3m (2007: £3.3m). Gross cash resources at 31 December 2008 amounted to £2.6m (2007: £2.1m). Approximately £1.1m was held in US Dollars, £0.6m in Euros and £0.9m in Sterling.

Intangible assets stood at £4.7m (2007: £3.7m) at the end of the year. This includes (i) £2.4m being the net book value of capitalized research and development arising (2007: £1.4m) and (ii) an additional £2.3m (2007: £2.3m) being the net book value of Alignent intangible assets acquired in 2007. The underlying assets are denominated in US Dollars. Due to amortization and impairment charges, the underlying US Dollar value of these assets lowered during the year, however, the value in Sterling has risen due to the movement in exchange rates. Further details are set forth in Note 14.

As part of the funding raised for the Alignent acquisition, Sopheon secured $3.5m of medium-term debt from BlueCrest Capital Finance LLC ("BlueCrest"). The debt is being repaid in 48 equal monthly installments, and is secured by a debenture and guarantee from Sopheon plc. Since inception, approximately $1.1m of the medium-term debt principal has been repaid. The group also has an additional $750,000 revolving credit facility from BlueCrest, secured on accounts receivable. Further details are set out in Note 20 of the financial statements.

Sopheon's equity line of credit facility with GEM Global Yield Fund Limited ("GEM") remains in place through 23 December 2009. The directors have not yet concluded whether to seek extension of the instrument. In 2007, GEM agreed to implement a two-year extension at no cost to Sopheon. The facility has been used to raise working capital once, in March 2004, leaving approximately 90 percent of the original €10m facility available under the extended agreement. Drawings under the GEM equity line of credit are subject to conditions relating inter alia to trading volumes in Sopheon shares.

Short term borrowings connected with the group's revolving facilities amounted to £0.5m (2007: £0.4m). In both years, this represents $750,000 with the Sterling increase linked to exchange rate movements. Similarly, the overall medium-term loan balance has increased from £1.6m to £1.7m, but this apparent increase disguises payments of $1.1m which actually reduced the dollar carrying value of the debt by $0.8m. These repayments have been funded out of free cash flow.

PRODUCT AND MARKET OVERVIEW

Sopheon's Solutions

In today's difficult economy, nearly every corporate executive is worried about this challenge: how to achieve short-term cost savings *without* sacrificing strategies for long-term growth.

The current business environment is the most uncertain that many organizations have ever faced. Companies are being forced to continually rethink strategies and adjust spending priorities. When it comes to innovation, executives are *literally betting the future* on their decisions about where to invest increasingly limited resources. The choices they make will determine whether their companies emerge successfully from the downturn, falter, or succumb. *Too often, their decisions are wrong.*

Poor decisions on innovation investments can generally be traced to one of three factors:

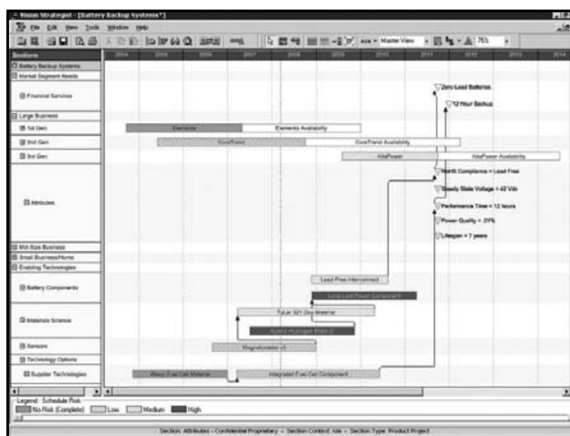
1) **Lack of transparency.** Decision-makers can't get a clear picture of where their innovation resources are being spent.

2) **Inability to judge what is valuable (and what is not).** Organizations often lack market-driven processes for determining the potential business value of investment options. As a result, spending decisions are based on little more than gut feel.

3) **Failure to anticipate consequences.** Decisions are sometimes made without a clear understanding of their probable impact on long-term strategies, or how they might be affected by shifts in market dynamics and other product and technology investments.

These factors typically lead to either of two negative outcomes. One is inaction, whereby low-value projects are allowed to linger and sap valuable resources while high-potential initiatives starve due to lack of support. The second outcome is even worse: truly valuable projects are unwittingly killed, resulting in loss of business opportunity and a glut of low-margin, "me-too" products that accelerate a spiral of declining financial performance.

Sopheon's solutions ensure that company executives make the right decisions about where to spend their innovation resources. Our software synchronizes corporate strategic product planning with new-product development, commercialization and management. Sopheon's offerings are the first in the industry to address and successfully resolve the synchronization challenge.



Sopheon's Accolade system is used by manufacturing companies to automate their processes for developing new products. Our Vision Strategist solution automates processes for strategic product planning. As an integrated offering, they constitute the first software system in the history of product lifecycle management that is able to synchronize product, market and technology planning with day-to-day product development activity.

Sopheon has two principal offerings. Its Accolade solution is a modular software system specifically designed to increase work efficiency and improve decision-making in the development and management of new products. Sopheon's Vision Strategist solution automates and manages the customer's strategic product planning process. Sopheon has integrated these software offerings into a single solution that manages the complete lifecycle of products from their conception as raw ideas until they are retired from the marketplace.

Products fall into three general categories. The first is comprised of new product concepts that are not yet funded as active projects. They represent the product roadmap for the long-term future. The second is made up of products that are actively funded and in development. They represent anticipated sources of financial contribution in the mid-term future. The third category consists of products that have been commercialized and are contributing to the revenue and profit performance of the company today. Sopheon's integrated software system provides a central repository for storing and managing data and information on all types of product innovation projects across the organization. This centralization, augmented by easy access to the stored data, enables executives and product development teams to make quicker, more informed decisions.

The integration of Accolade and Vision Strategist creates the only comprehensive strategic product planning and innovation process support solution in the marketplace. The offering ties product, market and technology roadmapping directly to the operational aspects of product development. Use of Sopheon's software helps to demystify research and development by providing dynamic, real-time visibility to planning and project information and aligning innovation efforts across the organization. It allows executives and cross-functional teams to more effectively assess the business opportunities and risks associated with product innovation initiatives, the short-term cost implications of such initiatives, and their likely impact on long-term strategies and objectives for revenue and profit growth.

Through their use of Sopheon's software, organizations are able to:

1) **Improve strategic agility and "uncertainty planning".**
   Our solutions support agility in strategic planning by rapidly moving decision-relevant information both vertically and horizontally inside the organization. The easy flow of data permits senior executives to know, and react quickly, when project details change or external events suddenly demand adjustments or refinements to active strategies.

2) **Make faster, better-informed portfolio decisions.**
   Strong portfolio management helps organizations optimize limited resources. Sopheon's software makes it possible for users to see in real time where innovation resources are invested. The solutions' dashboards consolidate, aggregate and present metrics so that information can be monitored at a glance. Innovation plans and projects can be stored in one place so that access is quick and easy.

3) **Identify, prioritize and act on the most promising innovation opportunities.**
   Users of Sopheon's software are able to separate winning products from losers early in the development cycle, helping to keep investments concentrated on high-value opportunities. Features such as scorecards, tailored selection criteria, resource reports and information-gathering and presentation templates grounded in best practices strengthen process governance and minimize innovation risk.

4) **Keep daily operational activities aligned with organizational strategies for growth.**
   An estimated 65 percent of companies struggle to keep product portfolios and operational and project activity aligned with corporate strategic plans. Sopheon's solutions create a seamless, automated process and decision framework that continually reconciles strategic product planning and operational execution.

5) **Cut costs by improving innovation process and team efficiencies.**
   According to recent Gartner research, companies whose product lifecycle management priorities include deployment of technology applications such as Sopheon's software can reduce product development costs by 30 percent or more. The savings happen because users are able to identify and abandon low-value or non-strategic projects early, before valuable resources are spent on development.

The Market

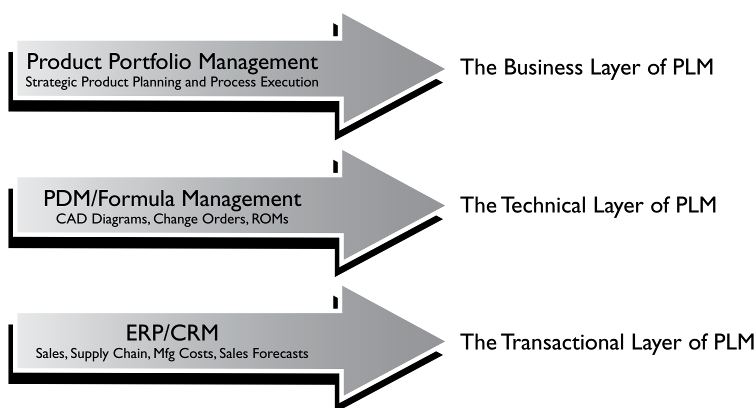
Sopheon's solutions belong to a major class of software applications that concentrate on supporting product lifecycle management (PLM). The purpose of this applications group is to help companies develop and execute their product strategies.

"PRODUCT PORTFOLIO MANAGEMENT IS ONE OF THE **FASTEST GROWING** SEGMENTS OF THE PRODUCT LIFECYCLE MANAGEMENT MARKET. REVENUES FROM PPM APPLICATIONS ARE EXPECTED TO **INCREASE** AT A COMPOUND ANNUAL RATE OF 17% THROUGH 2012"

– AMR Research

"The Product Lifecycle Management Market Sizing Report, 2007-2012"
July 2008

The PLM market is made of multiple submarkets. Some of these submarkets, such as product data management (PDM), are mature. Others are new and emerging. One of the emerging submarkets is called "Product Portfolio Management" (PPM). It is the area where Sopheon is focused. Software solutions in most areas of product lifecycle management concentrate on the engineering or technical challenges involved in managing a product while it is under development. Sopheon's solutions are designed to instead address the *business* challenges associated with product innovation, including the management of innovation risk and reward.



Business analysts have placed Sopheon's Accolade system in a subclass of product lifecycle management applications referred to as product portfolio management solutions.

Analysts have labeled Accolade as best-of-breed among solutions in the product portfolio management sub-class. They view PPM as a strategically critical applications area. Their research findings indicate that adoption of PPM methodologies enables users to more objectively assess product innovation investment options and increase the number of products that achieve commercial success. AMR, an IT research and advisory firm, has determined that product portfolio management is one of the fastest growing segments of the product lifecycle management market. It forecasts that revenues from PPM applications will continue to increase at a compound annual rate of 17 percent through 2012.

A number of vendors of *project* portfolio management solutions that have historically focused their software and go-to-market strategies on the project management needs of corporate information technology organizations continue to step up their attempts to migrate toward the *product* portfolio management space. The increased number of competitors and new entrants into our market will challenge our efforts to sustain a position of market leadership.

*"AMONG **BEST OF BREEDS**, SOPHEON HAS HAD THE MOST TRACTION IN THE PPM MARKET."*

– AMR Research

"The Product Lifecycle Management Market Sizing Report, 2007-2012"
July 2008

Growth Strategy

As we reported last year, Sopheon has been pursuing a five-part strategy for growth, and we made significant progress in 2008. Further details are set out below.

1) Expand Within Client Base

Sopheon entered 2008 with a customer base of 135 companies. We exited the year with 157 customers, a level of growth that attests to both the health of our company and the advancing maturity of our solutions in the marketplace. As the size of our customer population continues to expand, so too do Sopheon's opportunities for growth. In 2008 the number of existing customers that extended their licenses for our software rose to 27. One of the principal contributors to expanded deployment of our solutions is their use to automate business processes other than product development. Examples include management of mergers and acquisitions, capital expenditure projects, supply chain management and technology development. Overall, approximately 60 percent of our revenues in 2008 came from existing accounts, an encouraging indication of the impact that our customer base can have on our efforts to drive consistent growth.

"Prior to our adoption of Sopheon's Accolade system, we had searched unsuccessfully for a PLM solution that could support the layer of business information needed to make sound planning and product range decisions. For manufacturers faced with the challenge of managing product innovation and technology reuse on a global scale, [Accolade's] capabilities are game-changing. For Electrolux, they are indispensable."

— Johan Skåntorp, Vice President, Global Product Planning
Electrolux Floorcare & Small Appliances

2) Expand Product

Sopheon continued to invest substantially during 2008 in expanding the capabilities of its software products. Our product development team completed four product releases during the year, including two new versions of Accolade, and two of Vision Strategist.

Accolade development in 2008 culminated in release of the most significant new version of the software since it was introduced to the market more than seven years ago. It featured a broad mix of new attributes designed to improve the efficiency and effectiveness of cross-functional product innovation planning and execution. Many of the enhancements offered in the software were based on our work with existing customers such as General Motors and Electrolux. These new capabilities underpinned Sopheon's strategies for moving beyond the process manufacturing verticals that we have historically targeted and into the large aerospace, defense and automotive sectors. Development of a subsequent new version of Accolade was completed late in 2008 and introduced to the market early in 2009. This latest version of the software provides advanced decision support that enables senior executives to more effectively prioritize product innovation investments and keep available resources focused on projects promising high business returns. These capabilities are of strategic importance as they open the door for Sopheon to a new area within corporations: the project management office (PMO). The PMO is a centralized coordinating body that integrates and oversees project management across the enterprise. Professionals in this role represent a new functional market for Accolade.

Sopheon also completed two new versions of its Vision Strategist software in 2008. The first, launched early in the year, introduced a variety of enhancements to improve the clarity of roadmaps, reduce the time required to create and manage them, and make it easier to communicate them. A new portfolio management accelerator allows the user to see roadmap data in the context of current product, project and funding commitments, and make informed decisions about whether and how priorities need to be adjusted to take maximum advantage of both near- and long-term opportunities. A second new release, introduced in the autumn, improved the performance of Vision Strategist's roadmapping engine and increased the number of technology platforms the software supports.

3) Expand Within Core Markets

Sopheon's marketing and business development efforts in 2008 continued to focus on manufacturers of chemicals, paper and, within the consumer packaged goods sector, food and beverage producers. Fifty-five percent of the new customers we gained during the period were from these core markets. It is noteworthy that, although our solutions have historically been adopted because of their capacity to help drive additional revenue from new products, their attractiveness is being positively impacted by the fact that the market downturn is forcing companies to come up with creative ways of eliminating unnecessary costs. A major food company recently invested in Accolade not only to improve their innovation results, but to optimize cost-reduction efforts.

"Accolade has provided us with a state-of-the-art innovation management system. For the first time we are able to monitor all aspects of our R&D initiatives and make truly well-informed decisions about which ones to support. As a result, we are in a position to significantly reduce the number of active projects in our development pipeline, and to back the most promising opportunities with more resources. Accolade gives us the foundation we need to achieve profitable growth from product innovation well into the future."

— Martin Riediker, Chief Innovation Officer
Ciba

4) Expand to New Markets

In 2008, Sopheon continued its expansion beyond its core markets into the automotive, aerospace and defense sectors. Nearly 20 percent of new customers during the period came from these industries. At the same time, our pipeline of sales opportunities within these segments grew steadily. Although the sales cycles tend to be longer than in our traditional markets, the average value of transactions is expected to be materially higher. Furthermore, we are seeing significant validation from manufacturers in these discrete verticals of the need for our integrated solution, involving the use of Vision Strategist and Accolade in unison to synchronize innovation planning and execution. We expect that the automotive, aerospace and defense markets will further contribute to Sopheon's growth during 2009.

"We conducted a thorough review process and found that Sopheon's software was the only solution that met our needs. Vision Strategist enables us to objectively review investment options, pool resources across the company and speed the redeployment and development of needed technologies. We expect that with VS we will see a significant increase in our return on technology investments."

— Scott Harris, Technology Innovation Manager
Bell Helicopter

5) Expand Partnerships

Reseller Partners

As we have indicated, a core element of our strategy for growing through partnerships is to distribute our solutions through third-party resellers. We previously reported having established affiliate or reseller relationships with organizations in Germany, Australia, New Zealand, Portugal, France and the United Kingdom. We recently extended our reseller network to the Far East by putting in place a relationship with a leading distributor of product engineering tools in India.

During 2008, resellers generated 11 percent of Sopheon's total revenues, compared to 6 percent in 2007. We are encouraged by this increase in contribution, and will further our investment in the development of these partners with the expectation that their positive impact on Sopheon's sales and financial performance will continue to grow.

"Our relationship with Sopheon allows Maxsoft to provide manufacturers with a solution that will enable them to structure and govern their new product development processes. The Sopheon system has proven consistently that it can connect with a company's innovation strategies and provide automation and decision support that will lead to higher levels of revenue growth and profits from new products. We believe that it is the right solution at the right time for the Indian market. "

— Rajeev Gopalakrishnan, Chief Executive Officer
Maxsoft

Consulting Partners

In 2008, Sopheon's business again benefited from our collaboration with consulting partners. Several of these relationships came about when we were introduced to the consultants by common customers. We work with a core group of organizations that include Hewlett-Packard, Arthur D. Little, Deloitte, Kalypso and PRTM, as well as Robert Cooper and Stage-Gate® Incorporated.

Sopheon continues its relationship with Microsoft® as a Gold-Certified partner, leveraging Microsoft technology wherever it brings value to our business development efforts and to our customers.

Stage-Gate® is a registered trademark of the Product Development Institute.
Microsoft® is a registered trademark of Microsoft Corporation.

DIRECTORS AND ADVISORS

Directors	Barry K. Mence	Executive Chairman
	Andrew L. Michuda	Chief Executive Officer
	Arif Karimjee ACA	Finance Director
	Stuart A. Silcock FCA	Non-executive Director
	Bernard P. F. Al	Non-executive Director
	Daniel Metzger	Non-executive Director

Secretary

Arif Karimjee

Registered Office

Surrey Technology Centre
40 Occam Road, Surrey Research Park
Guildford, Surrey GU2 7YG

Registered Name and Number

Sopheon plc.
Registered in England and Wales No. 3217859

Auditors

BDO Stoy Hayward LLP
55 Baker Street
London W1U 7EU

Principal Bankers and Financiers

Silicon Valley Bank
3003 Tasman Drive
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United States

Lloyds TSB Bank plc.
77 High Street
Southend-on-Sea
Essex SS1 1HT

BlueCrest Capital Finance, LLC
225 West Washington, Suite 200
Chicago, IL 60606
United States

Solicitors and Attorneys

Hammonds
7 Devonshire Square
Cutlers Gardens
London EC2M 4YH

Briggs and Morgan
2200 IDS Center, 80 South Eighth Street
Minneapolis, MN 55402
United States

Loyens & Loeff
Fred Roeskestraat 100
1076 ED Amsterdam
The Netherlands

AIM Nominated Adviser and Broker

Seymour Pierce Limited
20 Old Bailey
London EC4M 7EN

Euronext Paying Agent

Kempen & Co.
Beethovenstraat 300
1077 WZ Amsterdam
The Netherlands

Registrars

Capita Registrars
Northern House
Woodsome Park
Fenay Bridge
Huddersfield HD8 0LA

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 two non-executive directors, B.P.F. Al, as chairman, and S.A. Silcock, together with B.K. Mence, other than in respect of his own remuneration. 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 on a case by case basis. Consideration is given to pay and employment policies elsewhere in the group, especially when considering annual salary increases. From time to time, the remuneration committee may take advice from appropriate remuneration consultants.

Contracts

The service contract between the company and Mr Michuda is terminable on up to 3 months' notice, with 12 months salary in lieu of notice due by the company in the event of termination without cause. Service contracts between the company and the other 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, translated where applicable into Sterling at the average rate for the period. Mr Mence's remuneration is largely fee-based and therefore subject to fluctuations from period to period. Mr Michuda's remuneration is payable in US dollars, the average exchange rate for which has increased significantly compared with the previous year. Details of directors' interests in shares and options are set out in the Directors' Report.

	Pay and fees 2008 £	*Benefits 2008 £*	*Bonus 2008 £*	*Total 2008 £*	*Total 2007 £*
Executive Directors					
B.K. Mence	126,664	2,209	28,500	157,373	141,152
A.L. Michuda	123,575	8,318	30,948	162,841	125,991
A. Karimjee	98,786	1,634	18,342	118,762	101,013
Non-executive Directors					
S.A. Silcock	18,000	-	-	18,000	18,000
B.P.F. Al	18,000	-	-	18,000	18,000
D. Metzger	18,000	-	-	18,000	18,000
	403,025	12,161	77,790	492,976	422,156

The remuneration committee establishes the objectives that must be met for each financial year if a cash bonus is to be paid. With the principal exception of members of Sopheon's sales teams, for whom incentives are tied to individual or territory results, the committee concluded that the cash incentive should be tied to the financial performance of the group as a whole, and in 2008 objectives were set with regard to EBITDA performance. These measures were applied to, and a bonus was earned by, all members of the executive board and management committee of the group, as well as the majority of the group's employees.

In addition to the amounts disclosed above, pension contributions are made to individual directors' personal pension schemes. During 2008 contributions of £4,875, £2,844 and £4,248 (2007 - £4,875, £2,253 and £4,396) were paid respectively to the pension schemes of B.K. Mence, A.L. Michuda and A. Karimjee.

The emoluments of S.A. Silcock are paid to Lawford & Co., a firm of chartered accountants of which S.A. Silcock is a partner.

DIRECTORS' REPORT

The group's principal activities during the year continued to focus on the provision of software and services that improve the return on investment of product development, within the rapidly emerging product lifecycle management (PLM) market. A review of the development of the business during the year, including the requirements of S234 of the Companies Act 1985, is given in the Statement from the Chairman and Chief Executive Officer on page 6 and the subsequent Financial Review. This also includes reference to the group's future prospects. An overview of the group's products and markets incorporating advances in research and development is provided on page 11. The group's result for the year ended 31 December 2008 is a profit after tax of £29,000 (2007: Loss of £443,000). The directors do not intend to declare a dividend.

Corporate Governance

The Sopheon board is committed to high standards of corporate governance and aims to follow appropriate governance practice, although as a company incorporated in the UK and listed on AIM and Euronext, the company is not subject to the requirements of the UK Combined Code or the Netherlands Tabaksblat Committee. The board currently comprises three executive directors and three independent non-executive directors. Their biographies appear on the inside back cover of this annual report, and demonstrate a range of experience and caliber to bring the right level of independent judgment to the board.

The board is responsible for the group's system of internal control and for reviewing its effectiveness. Such a system can only provide reasonable, but not absolute, assurance against material misstatement or loss. The board believes that the group has internal control systems in place appropriate to the size and nature of its business. The board is also responsible for identifying the major business risks faced by the group and for determining the appropriate course of action to manage those risks. Formal meetings are held quarterly to review strategy, management and performance of the group, with additional meetings between those dates convened as necessary. The audit committee, which comprises all of the non-executive directors and is chaired by Stuart Silcock, considers and determines actions in respect of any control or financial reporting issues they have identified or that are raised by the auditors. The board has a formal schedule of matters specifically reserved to it for decision. Details of the constitution of the remuneration committee are provided in the Report on Directors' Remuneration on page 17.

Principal Risk Areas

As with any business at its stage of development Sopheon faces a number of risks and uncertainties. The board monitors these risks on a regular basis.The key areas of risk identified by the board are summarized below.

Sopheon's markets continue to be at a relatively early stage of development and it is possible that Sopheon's products may not sell in the quantities or at the prices required to achieve sustained profitability. The broad market for Sopheon's software products continues to emerge and evolve. Sopheon has sought to focus its resources on the sub-segments that it believes offer the best short-term opportunity for growth, and on developing functionality which its research indicates customers in those segments require. However, determining the potential size, growth rate and needs of a particular market segment remains challenging. This risk has become particularly relevant in view of the economic turmoil that has affected the global economy.

Sopheon has a history of losses and its prospects of achieving profitability are dependent on meeting sales targets. Sopheon has in past years experienced substantial net losses due, in part, to its investment in product development and marketing. Sopheon's ability to continue to finance its activities through to the point that its operations become cash generative on a sustained basis is dependent on the group maintaining sales growth, or in the absence of such growth, its ability to secure funding through the company's facilities or other sources. Details of the resources available to Sopheon and the reasons why management consider that the company is able to continue as a going concern are set out in Note 2 to the financial statements.

Some of Sopheon's competitors and potential competitors have greater financial resources than Sopheon. Sopheon remains a relatively small organization by global standards. Its resources are dwarfed by those of many larger companies that are capable of developing competitive solutions and it is difficult to overcome the marketing engine of a large global firm. Sopheon seeks to compete effectively with such companies by keeping its market communications focused, clear and consistent with its product and market strategy, and working to deliver first class quality of execution so that referenceability of the customer base is maximized.

Sopheon is dependent upon skilled personnel, the loss of whom could have a material impact. While service agreements have been entered into with key executives, retention of key members of staff cannot be guaranteed and departure of such employees could be damaging in the short term. In addition, the competition for qualified employees continues to be difficult and retaining key employees has become accordingly more challenging and expensive.

Sopheon will require relationships with partners who are able to market and implement its products. Historically, Sopheon has devoted substantial resources to the direct marketing of its products, and its strategy to enter into strategic alliances and other collaborative relationships to widen the customer base and create a broad sales and implementation channel for its products is not yet mature. The successful implementation of this strategy is crucial to Sopheon's prospects and its ability to scale effectively. However, Sopheon cannot be sure that it will select the right partners, or that the partners it does select will devote adequate resources to promoting, selling and becoming familiar with Sopheon's products.

Sopheon could be subject to claims for damages for errors in its products and services. Sopheon may be exposed to claims for damages from customers in the event that there are errors in its software products or should support and maintenance service level agreements fail to meet agreed criteria. Sopheon has sought to protect itself from such risks through its development methodologies, its contract terms and insurance, and is not aware of any such claims at this time.

Share Option Schemes
Details of options granted are shown in Note 29 to the financial statements.

Supplier 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 2008 the company had approximately 49 days' purchases outstanding (2007: 39 days).

Charitable and Political Donations
The group has made no charitable or political donations during the year.

Auditors
All of the current directors have taken all the steps that they ought to have taken to make themselves aware of any information needed by the company's auditors for the purposes of their audit and to ensure that the auditors are aware of that information. The directors are not aware of any relevant audit information of which the auditors are unaware. A resolution to reappoint BDO Stoy Hayward LLP as auditors will be put to the members at the Annual General Meeting.

Financial Instruments
Details of the group's financial instruments and its policies with regard to financial risk management are given in Note 23 to the financial statements.

Directors and Their Interests
The interests of the directors, who held office at the end of the year, 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*	
At 31 December	*2008*	*2007*	*2008*	*2007*
B.K. Mence	485,000	385,000	14,423,847	14,423,847
A.L. Michuda	3,789,251	3,309,251	155,188	155,188
A. Karimjee	1,000,000	825,000	87,667	87,667
S.A. Silcock	-	-	950,000	918,716
S.A. Silcock*	-	-	76,639	98,077
B.P.F. Al	25,000	25,000	650,000	650,000
D. Metzger	-	-	100,000	100,000

Of the 14,423,847 ordinary shares mentioned above B.K. Mence beneficially owns and is the registered holder of 8,275,227 ordinary shares. A further 2,300,000 ordinary shares are held by Inkberrow Limited, a company in which B.K. Mence and his family trust are the majority shareholders and in which S.A. Silcock is a minority shareholder. In addition B.K. Mence is, or his wife or children are, potential beneficiaries under trusts holding an aggregate of 3,847,800 ordinary shares.

The table overleaf provides summary information for each of the directors who held office during the year and who held options to subscribe for Sopheon ordinary shares. All options were granted without monetary consideration.

	Date of grant	*Exercise price*	*At 31 December 2007*	*Granted during year*	*Lapsed during year*	*At 31 December 2008*
B.K. Mence (1)	2 May 2001	77.5p	22,500	-	-	22,500
B.K. Mence (1)	30 April 2002	14.75p	100,000	-	-	100,000
B.K. Mence (7)	15 April 2005	25.25p	62,500	-	-	62,500
B.K. Mence (8)	3 May 2006	22p	100,000	-	-	100,000
B.K. Mence (9)	29 June 2007	19p	100,000	-	-	100,000
B.K. Mence (10)	1 April 2008	13.25p	-	100,000	-	100,000
A.L. Michuda (2)	15 September 2000	230p	7,846	-	-	7,846
A.L. Michuda (2)	15 September 2000	322p	12,501	-	-	12,501
A.L. Michuda (3)	2 October 2000	427.5p	16,280	-	-	16,280
A.L. Michuda (3)	1 January 2001	160p	5,030	-	-	5,030
A.L. Michuda (3)	2 May 2001	77.5p	54,662	-	-	54,662
A.L. Michuda (4)	30 April 2002	14.75p	487,932	-	-	487,932
A.L. Michuda (4)(5)	5 November 2003	16.25p	2,225,000	-	-	2,225,000
A.L. Michuda (6)	15 April 2005	25.25p	150,000	-	-	150,000
A.L. Michuda (8)	3 May 2006	22p	100,000	-	-	100,000
A.L. Michuda (9)	29 June 2007	19p	250,000	-	-	250,000
A.L. Michuda(10)	1 April 2008	13.25p	-	250,000	-	250,000
A.L. Michuda	27 June 2008	14p	-	230,000	-	230,000
A. Karimjee (1)	22 November 1999	150p	100,000	-	-	100,000
A. Karimjee (1)	2 May 2001	77.5p	12,500	-	-	12,500
A. Karimjee (1)	30 April 2002	14.75p	150,000	-	-	150,000
A. Karimjee (5)(7)	5 November 2003	16.25p	300,000	-	-	300,000
A. Karimjee (6)	15 April 2005	25.25p	62,500	-	-	62,500
A. Karimjee (8)	3 May 2006	22p	100,000	-	-	100,000
A. Karimjee (9)	29 June 2007	19p	100,000	-	-	100,000
A. Karimjee (10)	1 April 2008	13.25p	-	175,000	-	175,000
A. Karimjee	27 June 2008	14p	-	100,000	-	100,000
B.P. F. Al (1)	2 May 2001	77.5p	25,000	-	-	25,000

None of the directors exercised any share options during the year.

(1) Exercisable between the third and tenth anniversary of the date of grant.
(2) Fully vested options, which were granted as part of the acquisition of Teltech Resource Network Corporation.
(3) One fourth of these options becomes exercisable on each of the first four anniversaries of the date of grant and they expire on the tenth anniversary of the date of grant.
(4) One third of these options are exercisable from the date of grant, one third from the first anniversary of the date of grant and one third from the second anniversary.
(5) Vesting of a proportion of these options was subject to performance conditions relating to the achievement of positive EBITDA in two successive quarters. The conditions were met.
(6) One third of these options are exercisable from the first anniversary of the date of grant, one third from the second anniversary, and the remainder from the third anniversary.
(7) 93,846 of these options are exercisable between the third and tenth anniversary of the date of grant and 206,154 options are exercisable as to one third immediately and one third on each of the first and second anniversaries of the date of grant.
(8) Vesting of one half of these options was subject to performance conditions based on the achievement of certain financial objectives in 2006. The conditions were met.
(9) Vesting of one half of these options is subject to performance conditions based on the achievement of certain financial objectives in 2007. The conditions were met.
(10) Vesting of one half of these options is subject to performance conditions based on the achievement of certain financial objectives in 2008.

The mid-market price of Sopheon ordinary shares at 31 December 2008 was 7.5p. During the financial year the mid-market price of Sopheon ordinary shares ranged from 7.00p to 15.25p.

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 25 March 2009 were 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*
B.K. Mence (director)	14,423,847	9.9
Norman Nominees Limited	9,691,260	6.7

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

Approved by the board on 25 March 2009 and signed on its behalf by:

A. Karimjee
Director

STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE FINANCIAL STATEMENTS

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company, for safeguarding the assets of the company, for taking reasonable steps for the prevention and detection of fraud and other irregularities and for the preparation of a Directors' Report and Directors' Remuneration report which comply with the requirements of the Companies Act 1985.

The directors are responsible for preparing the annual report and the financial statements in accordance with the Companies Act 1985. The directors are also required to prepare financial statements for the group in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs) and the rules of the London Stock Exchange for companies trading securities on the Alternative Investment Market. The directors have chosen to prepare financial statements for the company in accordance with IFRSs.

International Accounting Standard 1 requires that financial statements present fairly for each financial year the company's financial position, financial performance and cash flows. This requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the International Accounting Standards Board's 'Framework for the preparation and presentation of financial statements'. In virtually all circumstances, a fair presentation will be achieved by compliance with all applicable IFRSs. A fair presentation also requires the Directors to:

- consistently select and apply appropriate accounting policies;

- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information; and

- provide additional disclosures when compliance with the specific requirements in IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance.

Financial statements are published on the group's website in accordance with legislation in the United Kingdom governing the preparation and dissemination of financial statements, which may vary from legislation in other jurisdictions. The maintenance and integrity of the group's website is the responsibility of the directors. The directors' responsibility also extends to the ongoing integrity of the financial statements contained therein.

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF SOPHEON PLC

We have audited the group and parent company financial statements (the "financial statements") of Sopheon plc for the year ended 31 December 2008 which comprise the Consolidated Income Statement, the Consolidated and Company Balance Sheets, the Consolidated and Company Cash Flow Statements, the Consolidated and Company Statement of Recognized Income and Expense and the related notes. These financial statements have been prepared under the accounting policies set out therein.

Respective Responsibilities of Directors and Auditors

The directors' responsibilities for preparing the Annual Report, the Directors' Remuneration Report and the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and have been properly prepared in accordance with the Companies Act 1985 and whether the information given in the Directors' Report is consistent with those financial statements. We also report to you if, in our opinion, 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 information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. The other information comprises only the Directors' Report, the Report on Directors' Remuneration, the Statement from the Chairman and Chief Executive Officer, the Financial and Operating Review and the Product and Market Overview. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Our report has been prepared pursuant to the requirements of the Companies Act 1985 and for no other purpose. No person is entitled to rely on this report unless such a person is a person entitled to rely upon this report by virtue of and for the purpose of the Companies Act 1985 or has been expressly authorized to do so by our prior written consent. Save as above, we do not accept responsibility for this report to any other person or for any other purpose and we hereby expressly disclaim any and all such liability.

Basis of Audit Opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the group's and company'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 financial statements 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 financial statements.

Opinion

In our opinion:

- the group financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the group's affairs as at 31 December 2008 and of its profit for the year then ended;

- the parent company financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union as applied in accordance with the provisions of the Companies Act 1985, of the state of the parent company's affairs as at 31 December 2008;

- the financial statements have been properly prepared in accordance with the Companies Act 1985; and

- the information given in the directors' report is consistent with the financial statements.

Emphasis of Matter – Going Concern

In forming our opinion on the financial statements, which is not qualified, we have considered the adequacy of the disclosures made in Note 2 to the financial statements concerning the group's ability to continue as a going concern. As in prior years, these disclosures identify certain factors that indicate the existence of material uncertainties which may cast significant doubt about the group's ability to continue as a going concern. As discussed in Note 2, the appropriateness of the going concern basis remains reliant on the group achieving an adequate level of sales in order to maintain sufficient working capital to support its activities, or if this objective is not met, being able to raise sufficient additional finance.

BDO Stoy Hayward LLP
Chartered Accountants and Registered Auditors
London

25 March 2009

CONSOLIDATED INCOME STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2008

	Notes	*2008* *£'000*	*2007* *£'000*
Revenue	3	9,304	6,332
Cost of sales		(2,304)	(1,703)
Gross profit		7,000	4,629
Distribution expense		(3,516)	(2,523)
Research and development expense		(1,995)	(1,027)
Other administrative expense		(1,289)	(1,462)
Total administrative expense		(3,284)	(2,489)
Operating profit/(loss)		200	(383)
Finance income	8	55	70
Finance expense	9	(211)	(130)
Profit/(loss) before tax		44	(443)
Income tax expense	10	(15)	-
Profit/(loss) for the year (all attributable to equity holders of the parent company)		29	(443)
Earnings/(loss) per share			
Basic and diluted (pence)	12	0.02p	(0.32p)

CONSOLIDATED AND COMPANY BALANCE SHEET AT 31 DECEMBER 2008

	Notes	Group 2008 £'000	Group 2007 £'000	Company 2008 £'000	Company 2007 £'000
Assets					
Non-current Assets					
Property, plant and equipment	13	235	182	-	-
Intangible assets	14	4,706	3,725	-	-
Investments in subsidiaries	15	-	-	6,119	6,119
Other receivable	16	12	10	-	-
Total non-current assets		4,953	3,917	6,119	6,119
Current Assets					
Trade and other receivables	17	3,568	2,221	28	40
Cash and cash equivalents	18	2,586	2,053	1,421	1,391
Total current assets		6,154	4,274	1,449	1,431
Total assets		11,107	8,191	7,568	7,550
Liabilities					
Current Liabilities					
Trade and other payables	19	2,003	1,376	473	443
Borrowings	20	1,080	755	-	-
Obligations under finance leases	21	3	3	-	-
Deferred revenue		2,648	1,552	-	-
Total current liabilities		5,734	3,686	473	443
Non-current Liabilities					
Borrowings	20	1,103	1,192	-	-
Obligations under finance leases	21	2	3	-	-
Total non-current liabilities		1,105	1,195	-	-
Total liabilities		6,839	4,881	473	443
Net assets		4,268	3,310	7,095	7,107
Equity					
Share capital	24	7,279	7,279	7,279	7,279
Other reserves	25	73,627	73,499	65,862	65,734
Translation reserve	26	587	(191)	-	-
Retained losses	26	(77,225)	(77,277)	(66,046)	(65,906)
Total equity (all attributable to equity holders of the parent company)		4,268	3,310	7,095	7,107

Approved by the board and authorized for issue on 25 March 2009.

Barry K. Mence
Director

Arif Karimjee
Director

CONSOLIDATED AND COMPANY STATEMENT OF RECOGNIZED INCOME AND EXPENSE FOR THE YEAR ENDED 31 DECEMBER 2008

	Group		*Company*	
	2008 *£'000*	*2007* *£'000*	*2008* *£'000*	*2007* *£'000*
Exchange differences on translation of foreign operations	778	(27)	-	-
Net income/(expense) recognized directly in equity	778	(27)	-	-
Profit/(loss) for the year	29	(443)	(153)	(1,616)
Total recognized income and expense for the year (all attributable to equity holders of the parent company)	807	(470)	(153)	(1,616)

CONSOLIDATED AND COMPANY CASH FLOW STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2008

	Notes	Group		Company	
		2008	*2007*	*2008*	*2007*
		£'000	*£'000*	*£'000*	*£'000*
Operating Activities					
Profit/(loss) for the year		29	(443)	(163)	(1,616)
Adjustments for:					
Finance income		(55)	(70)	(49)	(62)
Finance costs		211	130	2	14
Depreciation of property, plant and equipment		96	94	-	-
Amortization and impairment of intangible assets		1,148	402	-	-
Share-based payment expense		151	105	151	105
Intra-group credits and charges		-	-	(235)	(147)
Provisions against intra-group loans		-	-	14	1,171
Operating cash flows before movements in working capital		1,580	218	(280)	(535)
(Increase)/decrease in receivables		(506)	399	11	(4)
Increase/(decrease) in payables		649	(375)	47	14
Net cash generated from/(used in) operating activities		1,723	242	(222)	(525)
Investing Activities					
Finance income		55	70	49	62
Purchases of property, plant and equipment		(85)	(78)	-	-
Acquisition of business		-	(1,894)	-	-
Recognition of development costs		(797)	(785)	-	-
Intra-group loans		-	-	190	(911)
Net cash used in investing activities		(827)	(2,687)	239	(849)
Financing Activities					
Proceeds of issues of shares		-	2,011	-	2,011
Proceeds from borrowings		-	1,758	-	-
Repayment of borrowings		(469)	(150)	-	-
(Decrease) in bank overdrafts and lines of credit		-	(37)	-	-
Interest paid		(211)	(130)	(2)	(13)
Net cash from financing activities		(680)	3,452	(2)	1,998
Net increase in cash and cash equivalents		216	1,007	15	624
Cash and cash equivalents at the beginning of the year		2,053	1,034	1,391	741
Effect of foreign exchange rate changes		317	12	15	26
Cash and cash equivalents at the end of the year					
Bank balances and cash	18	2,586	2,053	1,421	1,391

1. GENERAL INFORMATION

Sopheon plc. ("the Company") is a public limited company incorporated in England and Wales. The address of its registered office and principal place of business is set out on page 16. The principal activities of the Company and its subsidiaries are described in Note 3. The financial statements have been prepared in Pounds Sterling and rounded to the nearest thousand.

2. SIGNIFICANT ACCOUNTING POLICIES

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. The principal accounting policies are set out below. The policies have been applied consistently to all the years presented.

The group has adopted the following new standards:

- *IFRIC 11, IFRS 2 Group and Treasury Share Transactions* (effective for accounting periods beginning on or after 1 March 2007). IFRIC 11 requires share-based payment transactions in which an entity receives services as consideration for its own equity instruments to be accounted for as equity-settled. There was no impact on the group's financial statements from its adoption.

- *IFRIC 12 Service Concession Agreements* (effective for accounting periods beginning on or after 1 January 2008). There was no impact on the group's financial statements from its adoption.

- *IFRIC 14, IAS 19 The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction* (effective for accounting periods beginning on or after 1 January 2008). There was no impact on the group's financial statements from its adoption.

- *Amendments to IAS 39 and IFRS 7 Reclassification of Financial Instruments* (effective from 1 July 2008). This Amendment permits an entity to reclassify non-derivative financial assets (other than those designated at fair value through profit or loss by the entity upon initial recognition) out of the fair value through profit or loss category in particular circumstances. The Amendment also permits an entity to transfer from the available-for-sale category to the loans and receivables category a financial asset that would have met the definition of loans and receivables (if the financial asset had not been designated as available for sale), if the entity has the intention and ability to hold that financial asset for the foreseeable future. There was no impact on the group's financial statements from its adoption.

The following new standards, amendments and interpretations to existing standards have been published that are mandatory for the group's accounting periods beginning on or after 1 January 2009 or later periods and which the group has decided not to adopt early. These fall into three categories:

i) New standards, amendments or interpretations, the adoption of which may have a material impact on the results or net assets of the group:

   There are none in this category.

ii) New standards, amendments or interpretations, the adoption of which would affect the presentation of the group's financial statements:

- *Amendment to IAS 1 Presentation of Financial Statements Agreements* (effective for accounting periods beginning on or after 1 January 2009). Amendments to the presentation of owner changes in equity and comprehensive income.

- *Revised IFRS 3 Business Combinations Agreements* (effective for accounting periods beginning on or after 1 July 2009). This revised statement makes certain changes to the accounting for acquisitions, including a requirement to write off acquisition costs to profit and loss account instead of including them in the costs of acquisition, but does not require past acquisitions to be restated.

- *IFRS 8 Operating Segments* (effective for accounting periods beginning on or after 1 January 2009).

iii) New standards, amendments or interpretations, the adoption of which would have no material impact on the results or net assets of the group or the presentation of the group's financial statements:

- *Revised IFRS 1 First-time adoption of International Financial Reporting Standards* (effective for accounting periods beginning on or after 1 January 2009).

- *IFRIC 13 Customer Loyalty Programmes* (effective for accounting periods beginning on or after 1 July 2008).

- *IFRIC 15 Agreements for the Construction of Real Estate* (effective for accounting periods beginning on or after 1 January 2009).

- *IFRIC 16 Hedges of a Net Financial Investment in a Foreign Operation* (effective for accounting periods beginning on or after 1 October 2008).

- *IFRIC 17 Distribution of Non-cash Assets to Owners* (effective for accounting periods beginning on or after 1 July 2009).

- *Amendment to IAS 23 Borrowing costs* (effective for accounting periods beginning on or after 1 January 2009).

- *Amendment to IFRS 2 Share-based payments: Vesting Conditions and Cancellations* (effective for accounting periods beginning on or after 1 January 2009).

- *Amendments to IAS 27 Consolidated and Separate Financial Statements Cancellations* (effective for accounting periods beginning on or after 1 July 2009).

- *Amendments to IAS 32 and IAS 1 Puttable Financial Instruments and Obligations Arising on Liquidation* (effective for accounting periods beginning on or after 1 January 2009).

- *Amendment to IAS 39 Financial Instruments Recognition and Measurement: Eligible Hedged Items* (effective for accounting periods beginning on or after 1 July 2009).

- *Embedded Derivatives (Amendments to IFRIC 9 and IAS 39)* (effective for accounting periods ending on or after 30 June 2009).

- *Improving Disclosures about Financial Instruments (Amendments to IFRS 7)* (effective for accounting periods beginning on or after 1 January 2009).

- *IFRIC 18 Transfer of Assets from Customers* (effective to transfers received from customers from 1 July 2009).

- *Improvements to IFRSs* (effective for accounting periods beginning on or after 1 January 2009).

Going Concern

The financial statements have been prepared on a going concern basis. In reaching their assessment, the directors have considered a period extending at least 12 months from the date of approval of these financial statements and have considered both the forecast performance for the next 12 months and the cash and financing facilities available to the group.

In 2008, the group achieved revenues of £9.3m and generated a profit of £29,000. The directors are positive about the direction, focus and momentum of the business and believe that the group's existing resources and facilities described below provide it with adequate funding to support its activities through to the point at which they anticipate that operations will become cash generative on a sustained basis. This is however dependent on the group continuing to deliver an adequate level of sales. Furthermore, the time-to-close and the order value of individual sales can vary considerably, factors which constrain the ability to accurately predict revenue performance, and which are heightened by the tough economic conditions. These conditions are also likely to result in customers taking longer to pay amounts owed to the group.

At 31 December 2008, the group reported net assets of £4.3m and gross cash resources of £2.6m. The group has a loan note from BlueCrest Capital Finance ("BlueCrest") which is repayable in equal monthly installments of £63,000 through July 2011 and stood at £1.6m at year end. The group also has access to a bank line of credit with BlueCrest which is secured against the trade receivables of Sopheon's North American business, and was fully drawn down at 31 December 2008 for a value of £521,000.

If sales fall short of expectations or if the group's bank facilities prove insufficient, the group may need to raise additional finance. Sopheon continues to have access to the equity markets. In addition, the group has access to an equity line of credit facility from GEM Global Yield Fund Limited ("GEM") for an aggregate of €10m, the current term of which expires in December 2009. The facility originally expired in December 2005 and has been extended twice, each time for an additional two year period. 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 one call on the equity line of credit facility, raising just under €1m in March 2004, leaving a maximum €9m potentially available.

The directors have concluded that these circumstances represent material uncertainties, however believe that taken as a whole, the factors described above enable the group to continue as a going concern for the foreseeable future. The financial information does not include the adjustments that would be required if the company or group were unable to continue as a going concern.

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.

Business Combinations

The acquisition of subsidiaries is accounted for using the purchase method. The cost of the acquisition is measured at the aggregate of the fair values at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the group in exchange for control of the entity being acquired, together with any costs directly attributable to the business combination. The results of the acquired entities are included in the consolidated income statement from the date on which effective control is obtained. The identifiable assets, liabilities and contingent liabilities of the entity being acquired that meet the conditions for recognition under IFRS 3 Business Combinations are recognized at their fair values of the date of acquisition.

Identifiable intangible assets are capitalized at fair value as at the date of acquisition. The useful lives of these intangible assets are assessed and amortization is charged on a straight-line basis, with the expense taken to the income statement. Intangible assets are tested for impairment when a trigger event occurs. Useful lives are also examined on an annual basis and adjustments, where applicable, are made on a prospective basis.

Significant Accounting Estimates and Judgments

Management is required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates, and accordingly they are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods. Assumptions regarding the depreciation of property, plant and equipment, and the amortization and impairment of intangible assets, are set out in Notes 13 and 14 respectively. The group's policy with regard to impairment of such assets is set out below.

Goodwill

Goodwill arising on the acquisition of a subsidiary represents the excess of the cost of acquisition over the group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of the subsidiary at the date of acquisition. If, after reassessment, the group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of the entity being acquired exceeds the cost of the business combination, the excess is recognized immediately in profit or loss. Goodwill is initially recognized at cost and is subsequently measured at cost less any accumulated impairment losses.

For the purposes of impairment testing, goodwill is allocated to those cash-generating units of the group expected to benefit from the synergies of the business combination. Cash-generating units to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than the carrying value of the unit, the impairment loss is allocated firstly to reduce the carrying cost of any goodwill allocated to the unit and then to any other assets of the unit pro rata to the carrying value of each asset of the unit. An impairment loss recognized for goodwill is not reversed in a subsequent period.

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 recognized on delivery, and when no significant vendor obligations remain. Revenues relating to maintenance and post contract support agreements are deferred and recognized over the period of the agreements.

Revenues from implementation and consultancy services are recognized as the services are performed, or in the case of milestone based or long term contracts, recognized 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 recognized 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.

Interest on Borrowings

All interest on borrowings is recognized in profit or loss in the period in which it is incurred.

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.

Foreign Currencies

The individual financial statements of each group entity are presented in the currency of the primary economic environment in which the entity operates (its functional currency). 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.

In preparing the financial statements of the individual entities, transactions in currencies other than the entity's functional currency (foreign currencies) are recorded at rates approximating to the transaction rates. At each balance sheet date, monetary items denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences arising on the settlement of monetary items and on the retranslation of monetary items are included in profit or loss for the period. Exchange differences arising on the retranslation of non-monetary items carried at fair value are included in profit or loss for the period except for differences on the retranslation of non-monetary items in respect of which gains or losses are recognized directly in equity. For such non-monetary items any exchange component of that gain or loss is also recognized directly in equity.

For the purpose of presenting 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 recognized in profit or loss in the period in which the foreign operation is disposed of.

On disposal of a foreign operation the cumulative exchange differences recognized in the foreign exchange reserve relating to that operation up to the date of disposal are transferred to the income statement as part of the profit or loss on disposal.

Deferred Tax

Deferred tax is recognized 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 recognized for all taxable temporary differences, but deferred tax assets are recognized only to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilized.

Deferred tax is calculated at tax rates that have been enacted or substantively enacted at the balance sheet date, and that are expected to apply in the period when the liability is settled or the asset realized. 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.

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 recognized in profit or loss.

Investments

Investments in subsidiaries are stated at cost less impairment. Impairment tests are undertaken whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. Where the carrying value of an investment exceeds its recoverable amount, the investment is written down accordingly.

Externally Acquired Intangible Assets

Externally acquired intangible assets are initially recognized at cost and subsequently amortized on a straight-line basis over their useful economic lives. The amortization expense in respect of externally acquired technology and intellectual property ("IPR") is included in research and development costs in the income statement, and the amortization expense in respect of externally acquired customer relationships is included in distribution costs.

Internally Generated Intangible Assets (Research and Development Expenditure)

Development expenditure on internally developed software products is capitalized 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.

Capitalized development costs are amortized over the period over which the group expects to benefit from selling the product developed, typically over four years. The amortization expense in respect of internally generated intangible assets is included in research and development costs.

Development costs not satisfying the above criteria and expenditure on the research phase of internal projects are recognized in profit or loss as incurred.

Impairment of Tangible and Intangible Assets (Excluding Goodwill)

At each balance sheet date, the group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amount is the higher of the fair value less costs to sell and value in use. In assessing the value in use, the estimated future cash flows are discounted to their net present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

If the recoverable amount of an asset or cash-generating unit is estimated to be less than its carrying amount, the carrying amount of the asset or cash-generating unit is reduced to its recoverable amount. An impairment loss is recognized immediately in the administrative expenses line item in the income statement, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying value of the asset or cash-generating unit is increased to the revised recoverable amount, but so that the increased carrying amount does not exceed the carrying amount which would have been determined had no impairment loss been recognized in prior years. A reversal of an impairment loss is recognized immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

Financial Instruments

1. Financial Assets

The group's financial assets fall into the category of loans and receivables. The group does not have any financial assets in the categories of fair value through profit and loss or available for sale. The group has not classified any of its financial assets as held to maturity.

Unless otherwise indicated, the carrying values of the group's financial assets are a reasonable approximation of their fair values.

Loans and Receivables

These assets are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise principally through the provision of goods and services (e.g. trade receivables) but also include cash and cash equivalents and other types of contractual monetary asset. They are initially recognized at fair value plus transaction costs that are directly attributable to the acquisition or issue and subsequently carried at amortized cost using the effective interest rate method, less provision for impairment. The effect of discounting on these financial instruments is not considered material.

Impairment provisions are recognized when there is objective evidence (such as significant financial difficulties, default or significant delay in payment on the part of the counter-party) that the group will be unable to collect all the amounts due under the terms of the receivable, the amount of such provision being the difference between the net carrying amount and the present value of the future expected cash flows associated with the receivable. For trade receivables, such provisions are recorded in a separate allowance account with the loss being recognized within administrative expenses in the income statement. On confirmation that the trade receivable will not be collectable, the gross carrying value of the asset is written off against the associated provision.

2. Financial Liabilities

The group classifies its financial liabilities in the category of financial liabilities measured at amortized cost. The group does not have any financial liabilities at fair value through profit or loss.

Unless otherwise indicated, the carrying values of the group's financial liabilities are a reasonable approximation of their fair values.

Financial Liabilities Measured at Amortized Cost

Financial liabilities measured at amortized cost include:

- Trade payables and other short-dated monetary liabilities, which are initially recognized at fair value and subsequently carried at amortized cost using the effective interest rate method.

- Bank and other borrowings, which are initially recognized at fair value net of any transaction costs directly attributable to the acquisition of the instrument. Such interest-bearing liabilities are subsequently measured at amortized cost using the effective interest rate method, which ensures that the interest expense over the period to repayment is at a constant rate on the balance of the liability carried in the balance sheet. Interest expense in this context includes initial transaction costs and premiums payable on redemption, as well as any interest payable while the liability is outstanding.

3. Share Capital

Financial instruments issued by the group are treated as equity only to the extent that they do not meet the definition of a financial liability. The group's ordinary shares are classified as equity. For the purpose of the disclosures given in Note 23(6) the group considers its capital to comprise its ordinary share capital, share premium and other capital reserves less its accumulated retained loss.

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.

As set out in Note 24, the group has also issued warrants to certain financing institutions which are also treated as equity-settled share-based payments and expensed over the life of the warrant instrument as set out above.

3. REVENUE

All of the group's revenue in respect of the years ended 31 December 2008 and 2007 derived from the group's single business segment, the design, development and marketing of software products with associated implementation and consultancy services, as more particularly described in the Director's Report.

	2008	*2007*
	£'000	*£'000*
Continuing Operations		
Software and associated consultancy services	9,304	6,332

Revenue visibility at any point in time comprises revenue expected from (i) closed license orders, including those which are contracted but conditional on acceptance decisions scheduled later in the year; (ii) contracted services business delivered or expected to be delivered in the year; and (iii) recurring maintenance, hosting and rental streams. The visibility calculation does not include revenues from new sales opportunities expected to close during the remainder of the year.

4. GEOGRAPHICAL SEGMENTS

The group's primary reporting format for segment information is geographical segments. Information relating to the group's geographical segments, which are North America, United Kingdom and Rest of Europe, is given below. The group's principal operations are based in the United States, the United Kingdom and the Netherlands.

For management purposes, the group is organized as a single business segment, namely the design, development and marketing of software products with associated implementation and consultancy services. Therefore, no analysis of the group's trading result and balance sheet in terms of a secondary reporting format for business segments is presented in this note.

The information in the following table relating to external revenues includes analysis both by location of customer and by location of operations. The information relating to other items provides analysis by location of operations only. Inter-segment revenues are priced on an arms length basis.

Year ended 31 December 2008	*North America £'000*	*United Kingdom £'000*	*Rest of Europe £'000*	*Total £'000*
Income Statement				
External revenues - by location of customer	5,993	1,357	1,954	9,304
External revenues - by location of operations	6,777	1,781	746	9,304
Inter-segment revenues	667	-	680	1,347
Net profit/(loss) before interest and tax	472	156	(428)	200
Income tax expense	15	-	-	15
Depreciation and amortization	(915)	-	(5)	(920)
Balance Sheet				
Capital expenditure	77	1	7	85
Total assets	8,976	1,823	308	11,107
Total liabilities	(5,504)	(780)	(555)	(6,839)

Year ended 31 December 2007	*North America £'000*	*United Kingdom £'000*	*Rest of Europe £'000*	*Total £'000*
Income Statement				
External revenues - by location of customer	4,002	1,087	1,243	6,332
External revenues - by location of operations	4,177	1,212	943	6,332
Inter-segment revenues	564	-	555	1,119
Net loss before interest and tax	(44)	(137)	(202)	(383)
Income tax expense	-	-	-	-
Depreciation and amortization	(491)	(1)	(4)	(496)
Balance Sheet				
Capital expenditure	74	1	3	78
Total assets	6,192	1,869	130	8,191
Total liabilities	(3,792)	(732)	(357)	(4,881)

5. PROFIT/(LOSS) FOR THE YEAR

The profit/(loss) for the year has been arrived at after charging/(crediting):

	2008 £'000	*2007 £'000*
Continuing Operations		
Net foreign exchange gains	(216)	(49)
Research and development costs (excluding amortization)	1,171	707
Amortization of intangible assets	824	402
Impairment of intangible assets	324	-
Depreciation of property, plant and equipment	96	94
Operating lease rentals – land and buildings	330	265
Operating lease rentals – other	90	87

Net foreign exchange gains arise on the translation of certain cash and trade balances held in Euros and US Dollars and are accordingly included in administration expense.

6. AUDITORS' REMUNERATION

	2008 £'000	*2007 £'000*
Audit of the financial statements of the group	56	64

Fees for the audit of the company are not segregated from those for the group and are included in the above amounts.

7. STAFF COSTS

	Group		Company	
	2008	*2007*	*2008*	*2007*
	£'000	*£'000*	*£'000*	*£'000*
Wages and salaries	5,313	3,929	135	130
Social security costs	390	294	20	19
Pension contributions	98	76	10	10
Employee benefits expense	318	223	2	1
Share-based payments expense (all equity-settled)	151	105	21	17
	6,270	4,627	188	177

Included within the above are staff costs capitalized as development expenditure amounting to £797,000 (2007: £785,000).

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

	Group		Company	
	2008	*2007*	*2008*	*2007*
	Number	*Number*	*Number*	*Number*
Development and operations	65	55	-	-
Sales and management	33	30	2	2
	98	85	2	2

The above staff costs and the numbers of employees during the year include the executive directors.

The fees and emoluments of all directors were as follows:	*2008*	*2007*
	£'000	*£'000*
Fees and emoluments	493	423
Pension contributions	12	12
Share-based payments expense (all equity-settled)	44	29
	549	464

No director exercised share options during the year (2007: None). Pension contributions are to personal defined contribution schemes and have been made for three directors (2007: three) who served during the year.

The emoluments of the highest paid director were as follows:

	2008	*2007*
	£'000	*£'000*
Emoluments	155	139
Benefits	8	2
Pension contributions to defined contribution scheme	3	5
Share-based payments expense (all equity-settled)	21	8
	187	154

Full details of directors' remuneration are disclosed in the Report on Directors' Remuneration on page 17.

8. FINANCE INCOME

	2008	*2007*
	£'000	*£'000*
Income on financial assets measured at amortized cost		
Interest income on bank deposits	55	70

9. FINANCE EXPENSE

	2008 £'000	2007 £'000
Interest expense on financial liabilities measured at amortized cost		
Interest on borrowings	(211)	(130)

10. INCOME TAX EXPENSE

	2008 £'000	2007 £'000
Income tax expense for the year – current tax	15	-

The charge for the year can be reconciled to the accounting profit/(loss) as follows:

	2008 £'000	2008 %	2007 £'000	2007 %
Profit/(loss) before tax	44		(443)	
Tax (charge)/credit at the UK corporation tax rate of 28% (2007: 30%)	(12)	28%	133	30%
Adjustment for differing rates of corporate taxation in overseas jurisdictions	(30)	67%	(1)	-
Tax effect of expenses that are not deductible in determining taxable losses	(286)	(650%)	(122)	(27%)
Timing differences arising from the capitalization and amortization of internally generated development costs	102	232%	166	37%
Losses for the year not relievable against current tax	-	-	(176)	(40%)
Utilization of prior year losses	211	(480%)	-	-
Income tax expense for the year	(15)	-	-	-

The tax charge represents US Alternative Minimum Tax ("AMT"), which is payable notwithstanding the availability of tax losses from prior years. For AMT purposes, the use of prior year tax losses to offset current taxable profits is restricted to 90% of current year taxable profits, with AMT chargeable at a rate of 20% on the remaining 10%.

The group has an unrecognized deferred tax asset arising from its unrelieved trading losses, which has not been recognized owing to uncertainty as to the level and timing of taxable profits in the future.

The unrecognized deferred tax asset is made up as follows:

	2008 £'000	2007 £'000
Shortfall of tax depreciation compared to book depreciation	165	165
Effect of timing differences arising from capitalization of internally generated development costs	(1,023)	(623)
Unrelieved trading losses	27,554	21,904
Unrecognized deferred tax asset	26,696	21,446

At 31 December 2008, tax losses estimated at £70 million were available to carry forward by the Sopheon group, arising from historic losses incurred. These losses represent a potential deferred tax asset of £27.6 million, based on the tax rates currently obtaining in the relevant tax jurisdictions.

Of these tax losses, an aggregate amount of £22 million (representing £9.7 million of the potential deferred tax asset) represents pre-acquisition tax losses of Sopheon Corporation (Minnesota), Orbital Software Inc. and Alignent Software, Inc. The future utilization of these losses may be restricted under section 382 of the US Internal Revenue Code, whereby the ability to utilize net operating losses arising prior to a change of ownership is limited to a percentage of the entity value of the corporation at the date of change of ownership.

11. LOSS DEALT WITH IN THE FINANCIAL STATEMENTS OF THE PARENT COMPANY

The loss dealt with in the financial statements of the parent company for the year ended 31 December 2008 was £163,000 (2007: £1,616,000). Advantage has been taken of Section 230 of the Companies Act 1985 not to present an income statement for the parent company.

12. EARNINGS/(LOSS) PER SHARE AND EBITDA

Earnings/(loss) per share

	2008	*2007*
	£'000	*£'000*
Profit/(loss) after tax	29	(443)
	'000s	*'000s*
Weighted average number of ordinary shares for the purpose of basic earnings per share	145,579	140,286

The profit attributable to ordinary shareholders and the weighted average number of ordinary shares for the purpose of calculating the diluted earnings/(loss) per ordinary share are the same as those used for calculating the basic earnings/(loss) per ordinary share in both 2008 and 2007. This is because the exercise of warrants to subscribe for 502,790 ordinary shares and of share options to subscribe for 13,104,438 ordinary shares, all of which are "out of the money" (details of which are set out in Notes 24 and 29), would have the effect in 2008 of increasing earnings per ordinary share (by virtue of interest receivable on subscription proceeds) and in 2007 of reducing the loss per ordinary share, and are therefore not dilutive.

EBITDA

The directors consider that EBITDA, which is defined as earnings before interest, tax, depreciation and amortization, is an important measure, since it is widely used by the investment community. It is calculated as follows:

	2008	*2007*
	£'000	*£'000*
Profit/(loss) for the year after tax	29	(443)
Income tax expense	15	-
Interest expense	211	130
Interest income	(55)	(70)
Amortization of intangible assets	824	402
Depreciation of tangible fixed assets	96	94
EBITDA	1,120	113

13. PROPERTY, PLANT AND EQUIPMENT

Group	*Computer equipment £'000*	*Furniture & fittings £'000*	*Total £'000*
Cost			
At 1 January 2007	1,585	335	1,920
Additions	73	5	78
Acquisitions	73	13	86
Exchange differences	22	7	29
At 1 January 2008	1,753	360	2,113
Additions	81	4	85
Exchange differences	429	98	527
At 31 December 2008	2,263	462	2,725
Accumulated Depreciation			
At 1 January 2007	1,492	318	1,810
Depreciation charge for the year	83	11	94
Exchange differences	20	7	27
At 1 January 2008	1,595	336	1,931
Depreciation charge for the year	84	12	96
Exchange differences	372	91	463
At 31 December 2008	2,051	439	2,490
Carrying Amount			
At 31 December 2008	212	23	235
At 31 December 2007	158	24	182

The following rates are used for the depreciation of property, plant and equipment:

Computer equipment	20% to 33% on a straight-line basis
Furniture and fittings	20% to 25% on a straight-line basis

The net carrying amount of property, plant and equipment includes £1,000 (2007: £4,000) in respect of assets held under finance leases.

Company

The company has no property, plant and equipment.

14. INTANGIBLE ASSETS

	Development costs (internally generated)	*Technology and IPR*	*Customer relationships*	*Goodwill*	*Total*
	£'000	*£'000*	*£'000*	*£'000*	*£'000*
Cost					
At 1 January 2007	2,218	-	-	-	2,218
Additions (internally generated)	785	-	-	-	785
Acquisitions	-	700	1,312	493	2,505
Exchange differences	(36)	-	1	-	(35)
At 1 January 2008	2,967	700	1,313	493	5,473
Additions (internally generated)	797	-	-	-	797
Exchange differences	1,371	224	458	191	2,244
At 31 December 2008	5,135	924	1,771	684	8,514
Amortization					
At 1 January 2007	1,370	-	-	-	1,370
Charge for the year	233	87	82	-	402
Exchange differences	(24)	-	-	-	(24)
At 1 January 2008	1,579	87	82	-	1,748
Charge for the year	459	188	177	-	824
Exchange differences	741	89	82	-	912
At 31 December 2008	2,779	364	341	-	3,484
Accumulated Impairment Losses					
At 1 January 2008	-	-	-	-	-
Impairment losses in year	-	161	163	-	324
At 31 December 2008	-	161	163	-	324
Carrying Amount					
At 31 December 2008	2,356	399	1,267	684	4,706
At 31 December 2007	1,388	613	1,231	493	3,725

The amortization period for the internally generated development costs relating to the group's software products is 4 years. The amortization periods for (a) technology & IPR and (b) customer relationships, arising from the acquisition of Alignent Software, Inc., are 4 years and 8 years respectively. Goodwill is not amortized. The residual goodwill arising on the acquisition of Alignent is attributable to the enhanced market position of the group as a whole, due to the completeness of the solution that Sopheon can offer the market, in addition to the ability to penetrate wholly new markets such as aerospace and defense for the overall product set. The recoverable amount of the goodwill can be underpinned on a value in use basis by the expected performance of the group as a whole.

The initial valuation of the intangible assets acquired with Alignent relating to technology and IPR, and to customer relationships, used an income-based approach. During 2008 the recurring income from the acquired Alignent customer base reduced, due to a mix of factors including the conversion of certain rental licenses to perpetual, changes in rental levels, and cancellations. The overall reduction exceeded the rate of attrition of such recurring income estimated in the original valuation exercise, leading to impairments in the carrying value of the acquired Alignent technology and IPR, and the acquired Alignent customer relationships, of $298,000 (2007: $nil) and $302,000 (2007: $nil) respectively. All other assumptions of the original valuation have been retained in the impairment review. The valuation exercise, and the recoverable amount of the intangible assets and goodwill, are based on value in use with a discount rate of 14.6%.

Company
The company has no intangible assets.

15. SUBSIDIARIES

At 31 December 2007 and at 31 December 2008

	Company *£'000*
Cost	41,560
Less: Amounts provided	35,441
Carrying amount	6,119

Details of the company's subsidiaries at 31 December 2008 are set out below. Companies marked with an asterisk* are held via Sopheon UK Ltd and those with an obelus† are held via Orbital Software Holdings plc. The common stock of Alignent Software, Inc. is held by Sopheon Corporation, Delaware, USA.

Name of Company *Place of Incorporation*	*Nature of Ownership Interest*	*Proportion of Voting Rights Held*	*Nature of Business*
Sopheon Corporation Minnesota, USA	Common Stock	100%	Software sales and services
Sopheon Corporation Delaware, USA	Common Stock	100%	Software development and sales
Alignent Software, Inc. California, USA	Common Stock	100%	Software sales and services
Sopheon NV The Netherlands	Ordinary Shares	100%	Software sales and services
Sopheon UK Ltd. United Kingdom	Ordinary Shares	100%	Software sales and services
Orbital Software Holdings plc. United Kingdom	Ordinary Shares	100%	Holding company
Orbital Software Inc.† Delaware, USA	Common Stock	100%	Dormant
Sopheon Edinburgh Ltd.† United Kingdom	Ordinary Shares	100%	Dormant
Orbital Software Europe Ltd.† United Kingdom	Ordinary Shares	100%	Dormant
Network Managers (UK) Ltd.* United Kingdom	Ordinary Shares	100%	Dormant
AppliedNet Ltd.* United Kingdom	Ordinary Shares	100%	Dormant
Future Tense Ltd.* United Kingdom	Ordinary Shares	100%	Dormant
Polydoc Ltd. United Kingdom	Ordinary Shares	100%	Dormant
Applied Network Technology Ltd.* United Kingdom	Ordinary Shares	100%	Employee Share Ownership Trust

16. OTHER RECEIVABLE

	Group		*Company*	
	2008	*2007*	*2008*	*2007*
	£'000	*£'000*	*£'000*	*£'000*
Non-current receivable	12	10	-	-

The other receivable represents a deposit paid in respect of a property leased by the group.

17. TRADE AND OTHER RECEIVABLES

	Group		*Company*	
	2008	*2007*	*2008*	*2007*
	£'000	*£'000*	*£'000*	*£'000*
Trade receivables	3,293	1,980	-	-
Other receivables	25	82	-	14
Total receivables	3,318	2,062	-	14
Prepayments	242	132	28	26
Accrued income	8	27	-	-
	3,568	2,221	28	40

Trade and other receivables are stated net of allowances totalling £4,000 (2007: £47,000) for estimated irrecoverable amounts. The directors consider that the carrying amount of trade and other receivables approximates to their fair value.

A full provision has been made against amounts totalling £39,412,000 (2007: £39,398,000) owed to the company by subsidiary undertakings, which are due after more than one year and are subordinated to the claims of all other creditors.

18. CASH AND SHORT-TERM BANK DEPOSITS

	Group		*Company*	
	2008	*2007*	*2008*	*2007*
	£'000	*£'000*	*£'000*	*£'000*
Cash at bank	1,165	1,043	-	381
Short term bank deposits	1,421	1,010	1,421	1,010
	2,586	2,053	1,421	1,391

Cash and short term bank deposits comprise cash held by the group, bank current accounts and short-term bank deposit accounts with maturities of three months or less and bearing interest at variable rates. The carrying amount of these assets represents a reasonable approximation to their fair value.

Included in cash at bank of the group is an amount of £23,000 held by the group's employee share ownership trust.

19. TRADE AND OTHER PAYABLES

	Group		Company	
	2008	*2007*	*2008*	*2007*
	£'000	*£'000*	*£'000*	*£'000*
Trade payables	367	211	45	22
Other payables	158	137	170	184
Tax and social security costs	157	141	-	-
Accruals	1,321	887	258	237
	2,003	1,376	473	443

Trade payables principally comprise amounts outstanding for trade purchases and ongoing costs.

The directors consider that the carrying amounts of trade and other payables represent a reasonable approximation to their fair values.

20. BORROWINGS

	Group		Company	
	2008	*2007*	*2008*	*2007*
	£'000	*£'000*	*£'000*	*£'000*
Current Loans and Borrowings				
Line of credit	522	377	-	-
Loan notes (current portion)	558	378	-	-
	1,080	755	-	-
Non-current Loans and Borrowings				
Loan notes	1,103	1,192	-	-
Total loans and borrowings	2,183	1,947	-	-

The line of credit and the loan notes are denominated in US Dollars.

The loan notes are for an initial principal amount of $3,500,000 repayable in equal installments over the four-year period to July 2011 and bear interest at a fixed rate of 11.03%.

The line of credit bears interest at a variable rate based on a margin of 1.25% over the bank's US Prime Rate. The line of credit is a revolving facility limited to the lesser of $750,000 and 75% of the eligible trade receivables of the group's US subsidiaries, which at 31 December 2008 amounted to $4,174,000 (£2,903,000) (2007: $2,341,000 (£1,176,000)).

The loan notes and the line of credit, both of which are provided by BlueCrest Capital Finance LLC, are secured by a debenture and guarantee provided by Sopheon plc. The company has estimated the risk of this guarantee being called at 5% of the carrying value of the loan, and in its financial statements has included a provision for this amount within other payables.

The fixed interest rate on the loan note of 11.05% was based on the yield on the 3 year US Treasury Note at the time of issue, plus a spread of 6.05%. Although Treasury Note yields have now fallen, spreads on similar mezzanine financing instruments have also widened. Accordingly, the directors consider that the carrying amounts for loan notes and the line of credit represent a reasonable approximation of the financial instruments' fair values.

21. OBLIGATIONS UNDER FINANCE LEASES

The present value of future lease payments is analyzed as:

	Group		*Company*	
	2008	*2007*	*2008*	*2007*
	£'000	*£'000*	*£'000*	*£'000*
Current liabilities	3	3	-	-
Non-current liabilities	2	3	-	-
	5	6	-	-

The group leases a telephone system with a net carrying value at 31 December 2008 of £2,000 (2007: £4,000). The lease is for a five year period to May 2010 and carries an implied rate of interest of 4%.

Future lease payments are due as follows:

At 31 December 2008	*Minimum lease payments*	*Interest*	*Present value*
	£'000	*£'000*	*£'000*
Within one year	3	-	3
Due in one-to-five years	2	-	2
	5	-	5

At 31 December 2007	*Minimum lease payments*	*Interest*	*Present value*
	£'000	*£'000*	*£'000*
Within one year	3	-	3
Due in one-to-five years	4	1	3
	7	1	6

22. OPERATING LEASE ARRANGEMENTS

At the balance sheet date, the group had outstanding commitments under operating leases in respect of which the total future minimum lease payments were due as follows:

	Land & buildings 2008	*Other 2008*	*Land & buildings 2007*	*Other 2007*
	£'000	*£'000*	*£'000*	*£'000*
Due within one year	375	75	331	71
Due after one year and within five years	153	92	207	15
	528	167	538	86

The group leases its office accommodation in the US, UK and the Netherlands and has operating leases for office equipment and vehicles.

Company
The company has no operating leases.

23. FINANCIAL INSTRUMENTS

Categories of Financial Assets and Liabilities

The following table sets out the categories of financial instruments held by the group. All of the group's financial assets are in the category of loans and receivables, and all of its financial liabilities are in the category of financial liabilities measured at amortized cost.

Financial Assets

		Loans and receivables			
		Group		*Company*	
	Notes	*2008 £'000*	*2007 £'000*	*2008 £'000*	*2007 £'000*
Current Financial Assets					
Trade receivables	17	3,293	1,980	-	-
Other receivables	17	25	82	-	14
Accrued income	17	8	27	-	-
Cash and cash equivalents	18	2,586	2,053	1,421	1,391
		5,912	4,142	1,421	1,405
Non-current Financial Assets					
Other receivable	16	12	10	-	-

The group does not have any financial assets in any other categories.

Financial Liabilities

		Financial liabilities measured at amortized cost			
		Group		*Company*	
	Notes	*2008 £'000*	*2007 £'000*	*2008 £'000*	*2007 £'000*
Current Financial Liabilities					
Trade payables	19	367	211	45	22
Other payables	19	158	137	170	184
Accruals	19	1,321	887	258	237
Loans and borrowings	20	1,080	755	-	-
Obligations under finance lease	21	3	3	-	-
		2,929	1,993	473	443
Non-current Financial Liabilities					
Loans and borrowings		1,103	1,192	-	-
Obligations under finance lease		2	3	-	-
		1,105	1,195	-	-
		4,034	3,188	473	443

The group does not have any financial liabilities in any other categories.

Financial Instrument Risk Exposure and Management

The group is exposed to risks that arise from its use of financial instruments. This note describes the group's objectives, policies and processes for managing those risks and the methods used to measure them.

There have been no changes in the group's exposure to financial instrument risks, its objectives, policies and processes for managing those risks or the methods used to measure them from previous periods, unless otherwise disclosed in this note.

Principal Financial Instruments

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

- Trade receivables
- Cash and cash equivalents
- Trade and other payables
- Loan notes
- Bank line of credit

General Objectives, Policies and Processes

The board has overall responsibility for the determination of the group's risk management objectives and policies and, whilst retaining ultimate responsibility for them, it has delegated the authority for designing and operating processes that ensure the effective implementation of the objectives and policies to the group's finance function. The board receives quarterly reports from the group finance director through which it reviews the effectiveness of the processes put in place and the appropriateness of the objectives and policies it sets. The group's risk management procedures are also reviewed periodically by the Audit Committee.

The overall objective of the board is to set policies that seek to reduce risk as far as possible without unduly affecting the group's competitiveness and flexibility. Further details regarding these policies are set out below:

1. Credit Risk

Credit risk arises principally from the group's trade receivables, other receivables and accrued income. It is the risk that the counterparty fails to discharge its obligations in respect of the instrument.

The group's software is principally marketed at major international corporations of good credit standing, and the group's historical bad debt experience is very low. Due to the potentially large size of certain individual sales, in a particular year one customer can account for a substantial proportion of revenues recorded. However, such concentrations rarely persist for multiple years and therefore the directors do not believe that the group is systematically exposed to credit risk concentration in respect of particular customers. In 2008, the largest single customer accounted for 9% of group revenues (2007: 9%).

Credit risk also arises from cash and cash equivalents and deposits with banks and financial institutions. At the year end the group was holding a proportion of its deposits and bank balances with each of Lloyds Banking Group plc, Royal Bank of Scotland plc, and Silicon Valley Bank.

The group does not enter into derivatives to manage credit risk.

The following table illustrates the group's maximum exposure to credit risk, by class of financial instruments, at the balance sheet date, including a geographical analysis of exposure in respect of trade receivables:

	2008 Carrying value £'000	*2008 Maximum exposure £'000*	*2007 Carrying value £'000*	*2007 Maximum exposure £'000*
Trade receivables				
North America	2,784	2,784	1,568	1,568
United Kingdom	321	321	377	377
Rest of Europe	188	188	35	35
Total trade receivables	3,293	3,293	1,980	1,980
Other receivables	37	37	92	92
Accrued income	8	8	27	27
Cash and cash equivalents	2,586	2,586	2,053	2,053
Maximum credit risk exposure	5,924	5,924	4,152	4,152

The group's customers are major international corporations of high credit standing and therefore the group does not typically obtain credit ratings for individual customers. Nevertheless, current economic conditions have resulted in such major corporations slowing down payments and this is reflected in the ageing profile of the group's receivables. However, impairment of trade receivables is very rare, and in the three years ending 31 December 2008 provisions or write-offs against customer receivables amounted in total to less than 0.5% of revenues. Such impairments do not arise from credit defaults, but principally from disagreements with a very small number of former customers over their responsibility for renewal fees for maintenance or hosting contracts. Sopheon's policy is to pursue collection of such fees but to make provision against the applicable receivable if collection is uncertain.

The following is an analysis of the group's trade receivables identifying the totals of trade receivables which are current and those which are past due but not impaired:

	Total	*Current*	*Past due +30 days*	*Past due +60 days*
	£'000	*£'000*	*£'000*	*£'000*
At 31 December 2008	3,293	2,824	243	226
At 31 December 2007	1,980	1,864	36	80

The following is an analysis of the group's provisions against trade receivables, analyzed between the geographical segments in which the group's operations are located:

		2008			*2007*	
	£'000 Gross value	*£'000 Provision*	*£'000 Carrying value*	*£'000 Gross value*	*£'000 Provision*	*£'000 Carrying value*
Trade receivables						
North America	2,784	-	2,784	1,611	43	1,568
United Kingdom	325	4	321	381	4	377
Rest of Europe	188	-	188	35	-	35
	3,297	4	3,293	2,027	47	1,980

The group records impairment losses on its trade receivables separately from the gross amounts receivable.
The movements on this allowance during the year are summarized below:

	2008	*2007*
	£'000	*£'000*
Opening balance	47	41
Increases in provisions	-	39
Written off against provisions	(43)	(14)
Recovered amounts reversed	-	(19)
Closing balance	4	47

The main factors used in assessing the impairment of the group's trade receivables are the age of the balances and the circumstances of the individual customer.

2. Liquidity Risk

Liquidity risk arises from the group's management of working capital, and more particularly its ability to reach a point where its trading is cash generative, together with the finance charges and principal repayments on its debt instruments. It is the risk that the group will encounter difficulties in meeting its financial obligations as they fall due.

The group's policy is to maintain significant cash balances, short term bank deposits and facilities with a view to having sufficient cash to meet its liabilities when they become due. The board annually approves budgets including cashflow projections for each of the operating companies within the group and receives regular information as to cash balances held and progress against budget. Attention is particularly drawn to the detailed discussion of the factors which enable the group to continue as a going concern for the foreseeable future in the section headed "Going Concern" in Note 2 to the financial statements.

The following table sets out an analysis of the contractual maturity of the group's and the company's financial liabilities that must be settled gross, based on exchange rates prevailing at the relevant balance sheet date.

Group

At 31 December 2008	*Within one year £'000*	*Within five years £'000*	*Total £'000*
Trade and other payables	2,003	-	2,003
Line of credit	522	-	522
Loan notes	558	1,103	1,661
Future interest - Loan notes	157	103	260
Finance lease	3	2	5
Total financial liabilities	3,243	1,208	4,451

At 31 December 2007	*Within one year £'000*	*Within five years £'000*	*Total £'000*
Trade and other payables	1,376	-	1,376
Line of credit	377	-	377
Loan notes	378	1,192	1,570
Future interest - Loan notes	158	188	346
Finance lease	3	4	7
Total financial liabilities	2,292	1,384	3,676

Company

At 31 December 2008	*Within one year £'000*	*One to five years £'000*	*Total £'000*
Trade and other payables	473	-	473
Total financial liabilities	473	-	473

At 31 December 2007	*Within one year £'000*	*One to five years £'000*	*Total £'000*
Trade and other payables	443	-	443
Total financial liabilities	443	-	443

3. Market Risk

Market risk arises from the group's use of interest-bearing and foreign currency financial instruments. It is the risk that the future cash-flows of a financial instrument will fluctuate because of changes in interest rates (interest rate risk) or foreign exchange rates (currency risk).

The group does not have any financial instruments that are publicly traded securities and is not exposed to other price risk associated with changes in the market prices of such securities.

4. Interest Rate Risk

The group's interest bearing liabilities comprise loan notes with a carrying value of £1,662,000 which bear a fixed interest rate of 11.03% and accordingly do not give rise to interest rate risk, together with a line of credit for £522,000 which bears a variable interest rate based on a margin of 1.25% above the lender's Prime Rate. Should this rate vary by 2% the annualized effect would be to increase or reduce finance costs by £10,000.

The group invests its surplus cash in bank deposits denominated in Dollars, Euros or Sterling, which bear interest based on short-term money market rates, and in doing so exposes itself to fluctuations in money market interest rates. The group's and the company's surplus cash held in the form of bank deposits at the balance sheet date was £1,421,000. The annualized effect of a movement of 2% in the average interest rate received on the group's and the company's bank deposits at the balance sheet date would result in an increase or decrease in the group's and the company's interest income of £28,000.

5. Currency Risk

The following is an analysis of the group's financial assets and liabilities, analyzed by the currency in which they are denominated:

At 31 December 2008

	US Dollars £'000	*Sterling £'000*	*Euro £'000*	*Total £'000*
Financial assets:				
Receivables and accrued income	2,817	331	190	3,338
Cash and cash equivalents	1,075	877	634	2,586
Total financial assets	3,892	1,208	824	5,924
Financial liabilities:				
Trade and other payables	1,141	430	432	2,003
Borrowings	2,188	-	-	2,188
Total financial liabilities	3,329	430	432	4,191

At 31 December 2007

	US Dollars £'000	*Sterling £'000*	*Euro £'000*	*Total £'000*
Financial assets:				
Receivables and accrued income	1,642	420	37	2,099
Cash and cash equivalents	584	1,046	423	2,053
Total financial assets	2,226	1,466	460	4,152
Financial liabilities:				
Trade and other payables	619	469	288	1,376
Borrowings	1,953	-	-	1,953
Total financial liabilities	2,572	469	288	3,329

The group's policy is, where possible, to allow group entities to settle liabilities denominated in the functional currency with cash generated from their own operations in that currency. The group also maintains cash and bank deposits in the currencies which are the functional currencies of its operating entities, which are the US Dollar, the Euro and Sterling.

The group is exposed to currency risk in respect of such foreign currency denominated bank deposits and bank loans. Taking into account the fact that a large proportion of the group's income and expenditure arise in US Dollars and, to a lesser extent, in Euros, the group's policy is not to seek to hedge such currency risk.

Foreign currency risk also arises where individual group entities enter into transactions denominated in currencies other than their functional currency, with fluctuations in exchange rates giving rise to gains or losses in the income statement. Where the foreign currency risk to the group is significant, consideration is given to hedging the risk through the forward currency market and, whilst this would be an economic hedge of the cash-flow risk, the group does not employ hedge accounting.

Assets and liabilities of group entities located in the United States and the Netherlands are denominated respectively in US Dollars and Euros and are therefore exposed to currency risk giving rise to gains or losses on translation into Sterling, which are recognized directly in equity through the translation reserve. Such assets include the group's intangible assets, which are denominated in US Dollars, and the group's line of credit and loan notes, which are also denominated in US Dollars. It is not the group's policy to hedge its net investments in foreign operations, because it judges that the necessary hedging techniques would involve risks to cash flow.

The following table shows the effects, all other things being equal, of changes to exchange rates on the group's loss after tax and on the exchange differences on retranslation of the assets and liabilities of foreign operations which is recognized directly in equity. It illustrates the effects if the exchange rates for the US Dollar and the Euro had been higher or lower than those which actually applied during the year and at the year end.

	2008	*2007*	*2008*	*2007*
	Increase/ (decrease) in profit after tax	*Decrease/ (increase) in loss after tax*	*Effect on exchange differences on translation of assets and liabilities of foreign operations*	
	£'000	*£'000*	*£'000*	*£'000*
Weakening of US Dollar by 10c	(25)	11	(31)	(138)
Strengthening of US Dollar by 10c	31	(12)	45	148
Weakening of Euro by 10c	(9)	34	(57)	(19)
Strengthening of Euro by 10c	47	(31)	61	16

The company holds certain assets, mainly bank deposits, and liabilities denominated in the functional currencies of its principal operating subsidiaries, which are the US Dollar, the Euro and Sterling. The following table shows the effects, all other things being equal, of changes to exchange rates at the year end on the loss after tax of the company. It is based on the company's assets and liabilities at the relevant balance sheet date.

	2008	*2007*
	(Increase)/decrease in loss after tax	
	£'000	*£'000*
Weakening of US Dollar by 10c	4	3
Strengthening of US Dollar by 10c	(3)	(3)
Weakening of Euro by 10c	(48)	(93)
Strengthening of Euro by 10c	61	108

6. Capital

The group considers its capital to comprise its share capital and share premium and other capital reserves less the accumulated retained losses. The group is not subject to any externally imposed capital requirements. In managing its capital, the group's primary objective is to support the development of the group's activities through to the point where they are cash generative on a sustained basis.

The group's capital is all equity capital and is summarized in Note 24.

24. SHARE CAPITAL

Authorized	*2008 Number*	*2008 £'000*	*2007 Number*	*2007 £'000*
Ordinary shares of 5p each	200,000,000	10,000	175,000,000	8,750

Issued and Fully Paid	*2008 Number*	*2008 £'000*	*2007 Number*	*2007 £'000*
Ordinary shares of 5p each	145,579,027	7,279	145,579,027	7,279

The company has one class of ordinary shares, which carry no right to fixed income.

At 31 December 2008, the company had outstanding 502,790 warrants to subscribe for ordinary shares at a price of 20p per share, which were issued in June 2007 to BlueCrest Capital Finance, LLC in connection with the financing of the acquisition of Alignent Software, Inc.

25. CAPITAL RESERVES

Group

	Share premium £'000	*Merger reserve £'000*	*Capital redemption reserve £'000*	*Share options reserve £'000*	*Total £'000*
At 1 January 2007	50,685	17,944	2,884	1,314	72,827
Shares issued at a premium	1,411	-	-	-	1,411
Recognition of share-based payments	-	-	-	149	149
Lapsing of share options	-	-	-	(888)	(888)
At 1 January 2008	52,096	17,944	2,884	575	73,499
Recognition of share-based payments	-	-	-	151	151
Lapsing of share options	-	-	-	(23)	(23)
At 31 December 2008	52,096	17,944	2,884	703	73,627

Company

	Share premium £'000	*Merger reserve £'000*	*Capital redemption reserve £'000*	*Share options reserve £'000*	*Total £'000*
At 1 January 2007	50,685	10,179	2,884	1,314	65,062
Shares issued at a premium	1,411	-	-	-	1,411
Recognition of share-based payments	-	-	-	149	149
Lapsing of share options	-	-	-	(888)	(888)
At 1 January 2008	52,096	10,179	2,884	575	65,734
Recognition of share-based payments	-	-	-	151	151
Lapsing of share options	-	-	-	(23)	(23)
At 31 December 2008	52,096	10,179	2,884	703	65,862

Share premium represents the premium arising on the issue of shares and its use is governed by the provisions of the Companies Act 1985.

Merger reserve is a non-statutory reserve representing the premium on the issue of shares pursuant to certain past business combinations which meet specified criteria.

The capital redemption reserve is a non-distributable reserve arising from the cancellation in 2001 of deferred shares.

The share options reserve comprises the deemed value of outstanding share options granted in connection with the acquisitions of Teltech Resource Network Corporation in 2000 and of Orbital Software Holdings plc in 2001, together with the fair value of share-based payments to employees pursuant to the group's share option schemes and the fair value of warrants to subscribe for Sopheon shares issued to BlueCrest Capital Finance LLC.

26. CHANGES IN EQUITY

Group

	Share capital £'000	*Capital reserves £'000*	*Translation reserve £'000*	*Retained earnings £'000*	*Total £'000*
At 1 January 2007	6,679	72,827	(164)	(77,722)	1,620
Shares issued at a premium	600	1,411	-	-	2,011
Recognition of share-based payments	-	149	-	-	149
Lapsing of share options	-	(888)	-	888	-
Exchange differences on translation of foreign operations	-	-	(27)	-	(27)
Loss for the year	-	-	-	(443)	(443)
At 1 January 2008	7,279	73,499	(191)	(77,277)	3,310
Recognition of share-based payments	-	151	-	-	151
Lapsing of share options	-	(23)	-	23	-
Exchange differences on translation of foreign operations	-	-	778	-	778
Profit for the year	-	-	-	29	29
At 31 December 2008	7,279	73,627	587	(77,225)	4,268

The translation reserve represents accumulated differences on the translation of assets and liabilities of foreign operations. Retained losses represent accumulated trading losses, including amortization and impairment charges in respect of goodwill and intangible assets arising from past acquisitions.

Company

	Share capital £'000	*Capital reserves £'000*	*Retained earnings £'000*	*Total £'000*
At 1 January 2007	6,679	65,062	(65,178)	6,563
Shares issued at a premium	600	1,411	-	2,011
Recognition of share-based payments	-	149	-	149
Lapsing of share options	-	(888)	888	-
Loss for the year	-	-	(1,616)	(1,616)
At 1 January 2008	7,279	65,734	(65,906)	7,107
Recognition of share-based payments	-	151	-	151
Lapsing of share options	-	(23)	23	-
Loss for the year	-	-	(163)	(163)
At 31 December 2008	7,279	65,862	(66,046)	7,095

27. RETIREMENT BENEFIT PLANS

The group operates defined contribution retirement benefit plans which employees are entitled to join. The total expense recognized in the income statement of £98,000 (2007: £76,000) represents contributions paid to such plans at rates specified in the rules of the plans.

28. RELATED PARTY TRANSACTIONS

Details of transactions between the group and related parties are disclosed below.

Compensation of Key Management Personnel

Details of directors' remuneration are given in Note 7. The total remuneration of directors and members of the group's executive management committee during the year was as follows:

	2008	*2007*
	£'000	*£'000*
Emoluments and benefits	743	617
Pension contributions	18	17
Share-based payments	70	46
	831	680

Transactions with Related Parties who are Subsidiaries of the Company

The following is a summary of the transactions of the company with its subsidiaries during the year:

	2008	*2007*
	£'000	*£'000*
Net amounts repaid by/(advanced to) subsidiaries by way of interest-free loans	190	(911)
Net management charges to subsidiaries	210	209

The amounts owed by subsidiary companies to the parent company at 31 December 2008 totalled £39,412,000 (2007: £39,398,000). A full provision has been made against these amounts, which are unsecured and are subordinated to the claims of all other creditors.

During 2008 and 2007 the company granted share options to employees of subsidiary companies, details of which are disclosed in Note 29.

Other Related Party Transactions

There were no other related party transactions during the year under review or the previous year.

29. SHARE-BASED PAYMENTS

Equity-Settled Share Option Schemes

The group has a number of share option schemes for all employees. Options are exercisable at a price equal to the market price on the date of grant. The normal vesting periods are as set out below.

	Vesting
Sopheon plc (USA) stock option plan	In three equal tranches between the first and third anniversary of grant
Sopheon UK approved share option scheme	On third anniversary of grant
Sopheon UK unapproved share option scheme	Immediate or as per USA plan
Sopheon NV share option scheme	Immediate or as per USA plan

Details of the share options outstanding during the year are as follows:

	Number of share options 2008	*Weighted average exercise price 2008 £*	*Number of share options 2007*	*Weighted average exercise price 2007 £*
Outstanding at the beginning of the year	10,925,314	0.27	9,439,665	0.33
Granted during the year	2,731,224	0.14	1,857,500	0.19
Exercised during the year	-	-	-	-
Lapsed during the year	(552,100)	0.14	(371,851)	1.47
Outstanding at the end of the year	13,104,438	0.24	10,925,314	0.27
Exercisable at the end of the year	8,786,131	0.27	7,752,875	0.30

No share options were exercised during the year (2007: Nil). The options outstanding at the end of the year have a weighted average contractual life of 6.3 years (2007: 6.4 years).

In 2008, share options were granted on 1 April 2008 and on 27 June 2008. The exercise prices of the options granted on 1 April 2008 was 13.25p, and the estimated fair value was 7.8p. The exercise prices of the options granted on 27 June 2008 were 14p (for options granted mainly under the US and UK schemes) and 14.75p (for certain options granted under the Dutch scheme), and the estimated fair values were 8.3p and 4.9p respectively. In 2007, share options were granted on 28 June 2007. The exercise price of the options granted on that date was 19p, and the estimated fair value was 11.25p.

The fair values were calculated using the binomial option-pricing model. The principal assumptions used were:

	27 June 2008	*27 June 2008*	*1 April 2008*	*11 October 2007*
Share price at time of grant	14.75p	14p	13.25p	19p
Exercise price	14.75p	14p	13.25p	19p
Expected volatility	40%	40%	40%	40%
Risk-free rate	5%	5%	5%	5%
Expected dividend yield	Nil	Nil	Nil	Nil

The expected contractual life of the options used was either 5 or 10 years depending on the particular scheme rules. Expected volatility was determined by reference to the historic volatility of the company's share price in the period before the date of grant.

The group and company recognized total expenses of £151,000 (2007: £149,000) relating to equity-settled share based payments during the year.

31. APPROVAL OF FINANCIAL STATEMENTS

The financial statements were approved by the board of directors and authorized for issue on 25 March 2009.

DIRECTORS

Barry Mence, Executive Chairman. Barry Mence has served as executive chairman and as a director and substantial shareholder of Sopheon since its inception in 1993 when he was one of the founding members. From 1976 to 1990, Mr. Mence was a major shareholder and group managing director of the Rendeck Group of Companies, a software and services group based in the Netherlands.

Andrew Michuda, Executive Director. Andrew Michuda was appointed chief executive officer of Sopheon in September 2000. From 1997 to 2000 he served as chief executive officer and an executive director of Teltech Resource Network Corporation, which was acquired by Sopheon. He earlier held senior leadership positions at Control Data, including general manager of the business that evolved into Decision Data, the world's largest independent computer services provider.

Arif Karimjee, ACA, Executive Director. Arif Karimjee has served as chief financial officer of Sopheon since February 2000. Mr. Karimjee was previously an auditor and consultant with Ernst & Young in London, Brussels and Reading, from August 1988 until joining Sopheon.

Stuart Silcock, FCA, Non-executive Director. Stuart Silcock has served as a director of Sopheon from its inception in 1993. Since 1982, Mr. Silcock has been a principal partner of Lawfords & Co. and a director of Lawfords Ltd., chartered accountants. Mr. Silcock was a non-executive director of Brown & Jackson plc. for four years from June 2001 to July 2005 and currently holds a number of other directorships in the United Kingdom.

Bernard Al, Non-executive Director. Bernard Al was appointed as director of Sopheon in January 2001. He is a former chief executive officer of Wolters Kluwer in the Netherlands and has a background in science and linguistics.

Daniel Metzger, Non-executive Director. Daniel Metzger was until 1998 an executive vice president of Lawson Software, a leading ERP provider, where he was responsible for corporate strategy and marketing. Since then he has held similar roles at Parametric Technologies, where he led the business strategy and marketing around collaborative product development technologies, and at nQuire Software, which was subsequently sold to Siebel.

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