„Making the Vision Reality”
Annual Report 2004 2005
## Key figures

ISRA Group, cost of sales method, IFRS

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<tr>
<td><strong>Total operating revenue</strong></td>
<td>49,656</td>
<td>44,254</td>
<td>12</td>
<td>100</td>
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<tr>
<td>Net sales</td>
<td>44,687</td>
<td>40,437</td>
<td>11</td>
<td>90</td>
</tr>
<tr>
<td>Capitalized development expenditure</td>
<td>4,969</td>
<td>3,817</td>
<td>30</td>
<td>10</td>
</tr>
<tr>
<td><strong>Production costs</strong></td>
<td>20,966</td>
<td>20,475</td>
<td>2</td>
<td>42</td>
</tr>
<tr>
<td>Cost of materials</td>
<td>10,144</td>
<td>10,602</td>
<td>−4</td>
<td>20</td>
</tr>
<tr>
<td>Cost of labor</td>
<td>10,822</td>
<td>9,873</td>
<td>10</td>
<td>22</td>
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<tr>
<td><strong>Gross Profit</strong></td>
<td>28,690</td>
<td>23,779</td>
<td>21</td>
<td>58</td>
</tr>
<tr>
<td>Research and development costs</td>
<td>6,553</td>
<td>5,830</td>
<td>12</td>
<td>13</td>
</tr>
<tr>
<td><strong>Sales and administration costs</strong></td>
<td>9,369</td>
<td>8,398</td>
<td>12</td>
<td>19</td>
</tr>
<tr>
<td>Sales and marketing costs</td>
<td>6,385</td>
<td>5,197</td>
<td>23</td>
<td>13</td>
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<tr>
<td>Administration costs</td>
<td>2,984</td>
<td>3,201</td>
<td>−7</td>
<td>6</td>
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<tr>
<td><strong>EBITDA</strong></td>
<td>13,279</td>
<td>10,115</td>
<td>31</td>
<td>27</td>
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<tr>
<td>Depreciation/amortization</td>
<td>4,617</td>
<td>4,458</td>
<td>4</td>
<td>9</td>
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<tr>
<td><strong>Total costs</strong></td>
<td>20,539</td>
<td>18,686</td>
<td>10</td>
<td>41</td>
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<tr>
<td>Other operational revenue</td>
<td>511</td>
<td>564</td>
<td>−9</td>
<td>1</td>
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<tr>
<td><strong>EBIT</strong></td>
<td>8,662</td>
<td>5,657</td>
<td>53</td>
<td>17</td>
</tr>
<tr>
<td><strong>Financial result</strong></td>
<td>36</td>
<td>0</td>
<td>na</td>
<td>0</td>
</tr>
<tr>
<td><strong>EBT</strong></td>
<td>8,698</td>
<td>5,657</td>
<td>54</td>
<td>18</td>
</tr>
<tr>
<td><strong>Taxes</strong></td>
<td>2,718</td>
<td>2,389</td>
<td>14</td>
<td>5</td>
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<tr>
<td><strong>Net profit for the period</strong></td>
<td>5,980</td>
<td>3,268</td>
<td>83</td>
<td>12</td>
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<td>Earnings per share in €</td>
<td>1.51</td>
<td>0.87</td>
<td>74</td>
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<tr>
<td>Shares issued</td>
<td>3,947,940</td>
<td>3,748,109</td>
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**Total operating revenue by segment**

| Surface Vision                             | 35,680                                      | 27,115           | 32                                                          | 72                                                          |
| Industrial Automation                      | 13,976                                      | 17,139           | −18                                                         | 28                                                          |

**EBT by segment**

| Surface Vision                             | 6,583                                       | 3,459            | 90                                                          | 18                                                          |
| Industrial Automation                      | 2,115                                       | 2,198            | −4                                                          | 15                                                          |

**Cash flow from operating activities**

| Surface Vision                             | 8,450                                       | 7,228            | 17                                                          |
| Industrial Automation                      | −7,544                                      | −8,688           | −13                                                         |

**Balance sheet total**

| Balance sheet total                        | 67,034                                      | 61,199           | 10                                                          |
| **Equity ratio**                           | 73 %                                        | 69 %             |
| **ROCE (Return on Capital Employed)**      | 15 %                                        | 11 %             |
| **No of employees (annual average)**       | 246                                         | 244              | 1                                                           |

**Share price (XETRA)**

| (Jan. 27, 2006/Sep. 30, 2004) in €         | 22.50                                       | 11.20            |

**Market capitalization**

| (Jan. 27, 2006/Sep. 30, 2004) in mio. €    | 89                                          | 44               |
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We will achieve even more

Dear shareholders and friends of our company, dear company members,

positive financial figures, increasing stock prices and significant growth potential are the key criteria for investors when buying shares.

In the past fiscal year, we at ISRA have accomplished a great deal. This inspires us to tackle again even more ambitious goals and increase further the value of our company. In the past years we have achieved what we set out to do – more often than not we even surpassed our goal.

We have increased earnings before taxes by 54 percent in the 2004/2005 fiscal year. With this, we were able to boost pre-tax profit for the eighth time in as many years – an annual average growth of 55 percent in this time span. Profit per share has increased by more than 70 percent. Total operating revenue improved by twelve percent in the reporting period.

The ISRA share price has increased by approximately 80 percent during the 2004/2005 fiscal year. And the positive development of the share has continued beyond September 30, 2005.

In eight years revenue increased tenfold, EBT twentyfold
And we are only at the beginning of a period of accelerated growth. Machine vision is a key technology, whose industrial application in factory automation and quality control has only been developed to a small extent. This is the unanimous opinion of industry experts. With an excellent position in the global machine vision growth market, we will profit from this development.

Industrial production has to become faster, more flexible, more streamlined and more efficient. Thus, manufacturers need to improve their technology, screening procedures and control systems continuously. Machine vision creates opportunities for intelligent seeing automation in production and quality control and, thus, will improve the productivity and flexibility of the manufacturers.

One can buy instant profit increases from ISRA – this is a simplified description of our company’s successful business model.

All of us at ISRA are convinced that with our will to succeed, with hard work, creativity and perseverance, we will be able to achieve further strong growth. With significant investments – in particular with regard to the global sales team – we are now laying the foundations for growing our turnover into new orders of magnitude over the course of the next few years. Continued emphasis on increasing our productivity will ensure that our profit will not suffer.

I want to thank you, dear colleagues – also on behalf of the management and the supervisory board – for your great personal commitment. Also, I want to express my thanks to you, our customers, business partners and shareholders, for your confidence and support.

Enis Ersü, Executive Chairman
on behalf of the Management
Keeping the customer’s needs in sight

ISRA’s philosophy is focused on the electronic eye. We are interested in anything having to do with inspection or control by means of optical sensors. With the help of cameras, ISRA, as one of the global leaders in machine vision, lends eyes to production and inspection systems. The “BrainWARE” intelligent software system combines electronic vision with the artificial intelligence of the computer. In this way, material can be recognized, tested, measured, defects can be identified or a robot arm can be guided to the desired position.

ISRA sells systems consisting of standard software and hardware. In this context “BrainWARE” is the core competence of the company. It is the know-how of complex mathematical, optical and physical processes combined with technologically outstanding innovative hardware components of our own manufacture. When combined with additionally purchased standard components such as cameras, PCs and lighting and with an in-depth understanding of our customers’ production processes this results in industry-specific machine vision solutions.

The main focus of ISRA products will always be to increase productivity for the customers. An investment in machine vision has to pay off, and reduce production cost, within the shortest possible time. ISRA products are supposed to increase ROI – Return on Investment – in a sustainable manner. Thus, for most customers, average pay-back time is between three and six months.

In order to systematically speed up our growth we have developed the multi-segment strategy. Following this strategy we concentrate on three technology sectors, the two core competences Robot Vision – seeing robots – and Surface Vision – surface inspection – and also Quality Vision – quality control, which enables our business units to open up selected business sectors. In choosing customer companies, we focus on multinational companies ranging from 3M, Asahi, Audi, via DuPont, DaimlerChrysler, Ford, General Motors, MAN Roland, Pilkington, Saint-Gobin and Schott to VW and Zehejiang Glass Company. They all can use our applications in different production steps and at several locations. The multi-segment strategy guarantees the dynamic global growth of our company independent from structural and economic risks, which usually remain confined to individual industries and local markets.

Currently the biggest business unit in terms of sales, Glass is the global innovation and market leader in the float glass sector and offers the broadest product portfolio worldwide. In addition to systems for yield, quality and production optimization, ISRA offers R&D partnerships to the multinational glass manufacturers. Due to these close relationships, ISRA is involved in the planning and development of new production systems at an early stage.
In the Plastics business unit, we have specialized in the quality inspection of sheet materials and offer surface inspection systems for all steps of production and processing. The scope of application ranges from film, non-woven and plastic sheet to high-tech display film. Customers of ISRA’s Paper business unit achieve productivity increases through the fastest available inspection system for security paper and standard paper. Demanding products such as bank note paper or cardboard boxes for beverages require 100 percent inspection. In Print, ISRA systems inspect various printed surfaces ranging from paper or metal to plastic. The packaging industry in particular is placing increasing demands on optical control. With a new team of industry experts, ISRA is preparing entry of the highly interesting Metal sector. This is an example for the successful strategy of transferring established technologies from one business unit to other industries.

The Automotive business unit is represented with almost 1000 installed systems in approximately 90 plants around the globe. They service more than 30 different standard applications from the press shop, via assembly, to the final paint inspection. However, vision-based automation in the automotive industry still offers great potential for the future. Vision systems are essential for the manufacture of mass products. The Integrated Systems business unit offers their OEM customers – such as equipment manufacturers and system integrators – products for quality control and for the vision-based guidance of handling systems. In these indirect markets – from aircraft construction and adhesive beads on automobiles to the handling of chinaware – the core competences of ISRA are integrated in customer products and thereby improve their ability to compete. The Food Packaging business unit, which is still in the early stages of its development, was able to improve its market position by a follow-up order for optical inspection systems from the worldwide biggest manufacturer of beverage cans.

All business units are supported by ISRA’s high-performance R&D organization, because the speed with which ISRA launches new products and applications onto the market ensures the company’s competitiveness in the long run.
Processing enormous amounts of data for immaculate displays

Ultra-thin glass has to be inspected during the manufacturing stage before it is introduced into the processing of high-quality flat panel displays. Here it is necessary to detect defects which are not even one tenth of the thickness of a human hair.

It is a technological achievement to inspect ultra-thin four meter wide glass sheets for flaws, optical distortions, edge defects or defects in the electronic layers.

In the laboratory, defects such as scratches, inclusions or thickenings are made visible even for the human eye. This is done by introducing intense light into the side of the test sheet which then spreads throughout the entire sheet. Any flaw appears as a brightly shining dot. But it is a particular challenge to guarantee 100 percent inspection during a production process running at high speed in a production environment which is not dust-free.

In close cooperation with the German market leader for glass production for flat panel displays, ISRA has succeeded in integrating defect recognition into the production process for large glass sheets. The system operates with high-resolution cameras and special LED lighting. Imaging is synchronized with the LEDs to form certain patterns. Optical distortions caused by defects are measured by additional signal processing. Defects are identified and their exact size and precise position on the sheet are determined.

In this set-up, more data are processed in one second than 500 modern eight mega pixel digital cameras could collect when triggered at the same time. To guarantee the analysis of signals in such an enormous mass of data within an acceptable period of time, a frame grabber with complex mathematical algorithms developed by ISRA is employed. As in the laboratory test, a high-performance laser takes care of lighting along the edges. To introduce the light to a glass sheet with uneven edges, a special coupler was developed.
With this unique quality inspection procedure, ISRA has further extended its lead in the market for float glass inspection with a considerable technological edge. Thus, the company has succeeded in participating in the growth market for FPD glass (flat panel display). Experts anticipate annual increases of more than 25 percent in this sector.

The manufacture of FPD glass spans a longer production chain, encompassing – in addition to the production of thin glass – subsequent mechanical and electronic processing steps. So far, ISRA systems were only used in some of these steps, which is why ISRA is working intensively to develop systems for additional process steps in order to open the market even more effectively. Moreover, ISRA is already engaged in follow-on developments for the inspection of other materials such as plastics.

ISRA’s economic success did not take long in coming. Already in December 2005, ISRA obtained a major order for inspection systems in Europe and Asia amounting to Euro 1.8 million. The systems will be put into operation during the current fiscal year 2005/2006.
Unremitting in the quest for perfectly painted car bodies

A new car should have an impeccable shine. With ISRA’s fully automatic paint inspection CPV (Car Paint Vision), car manufacturers are a big step closer to this goal.

A perfectly shiny paint coat is the most recognizable feature of a new car. Scratches, drips or inclusions are unthinkable for the proud owner; they detract from the overall impression and thereby decrease the value of the automobile considerably. Manufacturers cannot afford this and therefore deploy specially trained employees to inspect the surface of the paint after its application. However, the human eye has its limits: repetitive activities quickly lead to tiredness and, consequently, mistakes.

ISRA has developed an innovative solution to this problem using machine vision: CPV, a fully automatic inspection system as a combination of ISRA BrainWARE and standard components such as PCs, lighting systems and cameras. The system can be installed either as a stationary unit or mounted onto a flexible robot arm.

When integrated into the automobile manufacturer’s production plant, the car bodies are fed through and inspected at a speed of up to nine meters per minute. All the while, the high-performance cameras record defects with an optimal recognition rate of more than 98 percent, even for defects as small as 0.2 millimeters in size. The positions of the defects on the surface of the car body are then relayed to a computer. The computer directs a robot to the corresponding location, which then labels the defect with a marker. The imperfection can then be quickly and reliably removed at a post-processing station.

The fully automatic paint inspection CPV guarantees that each car is inspected with a reliability that can only be ensured by a “seeing machine”. This guarantees consistent quality for the manufacturer, regardless of the employee, the day of production, the shift or the production plant. The evaluation of the data gained from the inspection increases productivity through early defect recognition. One can react quickly and avoid expensive waste or delayed post-processing. The saved data also offer objective evidence – in the case of complaints or warranty claims – and make quality audits unnecessary. Moreover, using standard components ensures the best possible equipment availability and the automatic monitoring of all essential components makes for maximum process stability and minimal maintenance work. This cuts costs. As a result, when used properly, the system pays for itself in close to one year.

ISRA expects strong growth impulses from the automotive industry due to the CPV innovation. The market potential amounts to almost 300 automotive plants world-wide.
Recognizing and retrieving defects with
top precision at top speed

SMASH, the intelligent and efficient surface inspection system from ISRA, is one of the fastest and most effective systems available worldwide, not only for printed and unprinted standard paper, but also for other printed surfaces, such as metal foil.

ISRA’s web inspection products exceed the performance of most established inspection systems. The systems possess an extremely fine resolution. Taking an example from everyday life, this means that, while driving on the highway at 120 km/h, one would be able to read the writing on the cigarette butts along the side of the road and identify the brands. And at the end of the drive one knows exactly how the brands are distributed along the road – right down to the millimeter. In industrial paper production, the detailed defect images allow for an exact classification and location of defects in the web.

During the inspection, ISRA’s Re-Wind Manager has taken note of the positions of all the defects and stops the re-spooling at the appropriate place. The defect is – if possible – corrected. If the defective spot is too large, it is cut out and the roll is glued back together.

In addition, a wide variety of printed surfaces – not only paper, but also metal or plastics – can be inspected 100 percent by ISRA systems equipped with color cameras. Designers spend much time and effort on creating packaging that is appealing to the customer. Clearly, this impression must not be spoiled by misprints. Not even the smallest imperfections or mistakes in color registration are acceptable.

The demands on optical inspection will continue to increase in the future, because the print is important not only for the visual impression but also for the functionality of a product. Thus, typographical errors on pharmaceutical packaging or misprinted pcb tracks can have potentially severe consequences.

ISRA’s most recent development is a system which inspects 600 meters per minute of a printed web several meters wide for misprints, spillings or color variations. The first machine with this innovative technology is already on its way to the customer.

The users profit from short set-up times – because all actions required for changing the inspection system over to a new print run amount to less than 30 seconds – fast print image optimization and a better utilization of the machine.
The more you see …

We are only in the early stages of the application of machine vision. Until now, the possibilities to optimize industrial production by machine vision and to effectively lower manufacturing costs have been applied only to a limited extent. This is the reason why machine vision represents a growth market par excellence, in whose development ISRA will increasingly participate.

In order to grow strongly all over the world, ISRA is developing industry-specific machine vision products in the technology segments Robot Vision, Surface Vision and Quality Vision. In the selection of its customer industries, ISRA concentrates on markets that show particularly strong growth and that expand on average at double-digit rates per annum. Preferred customers are globally operating companies. After the first ISRA application is successfully implemented, these customers deploy ISRA solutions to their other facilities, not only in one country but internationally. The development of additional products for preceding and subsequent production stages of existing customers and the acquisition of new customers further strengthens market penetration.

This gives ISRA three ways to expand: technology segments, industries and regions. The market share in the existing markets, especially for business units still in the early stages of their development, will be increased by ISRA through innovations – possibly taken from other technology segments – which existing customers can implement globally.

By more efficiently penetrating new markets, proven technologies can be further refined for new industries or installed in regions not yet penetrated. The most recent example is Metal; the new market for the inspection of steel, copper, brass and aluminum offers good opportunities for growth. Market entry is being prepared in the current fiscal year 2005/2006 by a team of industry experts. The technology is a Surface Vision application which has proved its value in other business units. By introducing this technologically leading, cost-efficient niche application, ISRA expects a significant market share. There are also links to the automotive industry, one of the most important metal processors where ISRA has been successfully established with other applications for a long time.

With its dual multi-segment strategy, ISRA hopes to average double-digit turnover rates in the long run. To achieve this, we are strengthening our international sales teams and invest heavily into our worldwide presence. By expanding the site in Shanghai at the beginning of 2006, the progressive manufacturing organization of German locations will be combined with local cost advantages. We expect productivity and competitive benefits from this, as well as further strong growth impulses from the enormous Chinese market. Especially thin glass inspection is in great demand in Southeast Asia.
About 95 percent of all manufacturing capacities for thin glass are located in Korea, Taiwan, Japan and China. This market is particularly interesting at present, because the market for flat panel displays grows by more than 25 percent per annum.

ISRA management expects that turnover in 2005/2006 will grow at least as much as in the previous year. It is foreseeable that growth dynamics will accelerate in the second half of the business year. Continuous optimization measures in production, R&D, purchasing and in the organization in general will help to keep cost under control.

Based on the dynamics of the machine vision market and our good global competitive position, we aim to continue our strong growth. We concentrate our resources on developing our turnover through internal and external growth to a new order of magnitude in the medium-term while not neglecting profitability at the same time.
“Strategic preparation for future growth”
Interview with Enis Ersü

Mr. Ersü, you want to continue to grow strongly. In this regard, you frequently mention Project 100+. What does this mean?

100+ is the project in which we strategically prepare the growth of our company. In addition to deliberations and plans, it includes tangible measures as to how we can realise a consolidated turnover of more than EUR 100 million within four years. Over the past years, ISRA has obtained a good position on the global market. Now we are well equipped to convert the market growth into even more dynamic growth for our company with the help of a two-track innovation campaign and additional acquisitions. Our first priority is to increase market share within the existing industries. Here we have to do our homework in developing new products for preceding and subsequent production steps for our regular customers. Also, through new sales channels we have to convince new customers of our products’ benefits and open up additional geographic regions. Our second priority will be to penetrate new industries with our established products and technologies. Watch out for the momentum of our expansion.

Which markets do you hope to expand to and which are the new products you plan to launch in this year?

We are working hard to enter the new customer industry, Metal. For this purpose, we employ our tried and tested Surface Vision technology in niche applications for steel, aluminum, copper and brass. In addition, we offer new products – more effective ones as well as products suitable for different production steps – in the existing sectors Display Glass (FPD), Print and Food Packaging. Our first priority for regional expansion will be Asia and Eastern Europe.

There is strong competition in the metal sector. How do you plan to assert yourself against, for example, Parsytec and Cognex?

As the market leader in surface inspection, we can plausibly transfer our know-how to the Metal sector. We have a cutting-edge technology mix, and our competitors focus on a different market segment. Our worldwide sales and support infrastructure, in combination with a team that is experienced in the metal sector, offer the customer competent partners, outstanding service and, of course, a very good product. With these qualifications, metal simply belongs in our product portfolio. We shall continue to develop this market and plan also to offer measurement technology.
“We will now make use of our growth opportunities.”
Who are the other established competitors and who do you keep an eye on? How are you different from them?

Most frequently, of course, we encounter Cognex, the worldwide market leader in machine vision. For thin glass we are in competition with Basler, for paper with Parsytec and for print with AVT. However, the overlaps are limited to individual areas and, therefore, affect only part of our revenue.

You mentioned that ISRA is an important participant in the market. Considering the EUR 45 million turnover from two core technologies in six or seven business units, are you left with enough critical mass for the individual areas?

Considering the situation today, you may perhaps be right. But soon each of these – currently six or seven business divisions – will generate more than ten million Euros of turnover. At that point the critical mass will have been attained all-around.

You expect your business to be stimulated by the automotive industry. What makes you so confident – looking at the problems presently encountered by General Motors, for example?

Innovation, innovation and more innovation. We are creating new applications with new and established technologies. As a concrete example, we now present our customers with new products in the fields of three-dimensional positioning and in-line measurement. A general rule is: if new product lines are implemented because the demand for products by our customers is growing, new automation is called for. If, however, not expansion, but streamlining is the order of the day because of an economic slow-down in one particular industry, the pressure on efficiency increases and manufacturing costs must be reduced. In both cases, machine vision provides exactly the right solution. This is why we expect new potential for automation from the automotive industry.

Display glass inspection is a strategically important field for you when considering the rapid market growth. Being a comparatively small European supplier, how will you be able to succeed against the Asian competitors?

We are not afraid of competition from Asia. They are not as powerful as implied by your question. Let's go through the different steps of FPD glass manufacture. At beginning we find the different processes of glass substrate production. Worldwide we are the leader with our technology for the inspection of plain glass – which is a good starting point. After that the glass is cut. Here, you need inspection for scratches, edge defects and point defects. These are areas where ISRA has no need to hide. For this, we have developed a unique inspection method.
Innovation is key for being a proactive and reliable partner to our customers.

The next step is coating, where we are also in a very good position. Electronic steps will follow, such as the application of color filters and TFT structures. We are gradually entering this area of production. Some innovative products are almost ready to be introduced. We have just put together an interesting team for this field to be stationed in Taiwan. Under the leadership of a Manager from Southeast Asia, we combine the tried and tested know-how of the ISRA technologies with experts who have demonstrated their ability in the industry.

You are also in the process of expanding your presence in Shanghai by establishing a production facility. What are your expectations and what importance do you attach to the Asian market?

Asia is important for all of the ISRA business units. The most important reason for a production line in Shanghai is to be close to the customer. In the future, ISRA will supply the entire Asian market from this location, and production and customer support will complement each other. If we manage to combine local presence with lower production costs, we see this as an added benefit, because constant maximization of profitability is a permanent challenge for us.
You are hardly active in Eastern Europe. What is your strategy for this region?

This impression is not correct. For a long time now we have been represented in the automotive industry in the Czech Republic, Slovakia, Poland and Hungary. We have just deployed a sales representative to Bratislava. And with a Manager for Eastern Europe we plan to strategically expand our presence – especially in the Surface Vision segment. New experts will continuously reinforce our team. We focus on the new EU countries, Russia and the former Soviet republics. These countries want to export their goods to the West. Therefore, they have to fulfil international quality standards and, consequently, will need quality inspection.

In the past fiscal year 2004/2005 your margins have strongly increased. How did you achieve this? Is there potential for further increases in productivity?

We have optimized the product mix. This means that we have concentrated on selling systems with higher margins. Of course, we have also increased our market share in the pertinent fields through the acquisition of LASOR. Additionally, we have improved our quotations, and our continuous production improvement program has come to fruition: for instance with reduced production cycle time, more efficient purchasing or through our R&D program “Design for Cost”, which is intended to cut the costs of products.

And all of our potential has not yet been tapped. There are still possibilities for increasing productivity in manufacturing: Bring new products into the market even faster, produce even more efficiently. And there is standardisation, time and again standardisation.

About ten percent of your total operating revenue are capitalized development expenditure. What does this mean?

These are the costs for the development of products that are close to the market. For products that are to be launched shortly, there is a legal obligation to capitalize as per IAS 38. ISRA has spent 6.6 million Euros for research and development in the 2004/2005 fiscal year. Of this amount we have capitalized 5.0 million Euros, which is close to our long-term average of around 10% of total operating revenue. On the other hand, we have written off 3.1 million Euros on capitalized development expenditures form previous years.

ISRA makes for more transparency with this open reporting: 1.6 million Euros have been invested in development which was not close to the market; in the prior year, the corresponding figure stood at 2.0 million Euro. This shows: We have improved our R&D efficiency compared to the prior year. Naturally, each individual development position will be checked by an annual impairment test with regard to its value. So far there has been very little need for adjustment.
Your employees are a valuable asset for you. What is the importance of personnel development have at ISRA?

We have grown strongly and want to continue to grow strongly. This can be achieved only with a highly motivated team. Therefore, our most important investment activity this year has been to invest in our people, in sales teams – for Metal, Display Glas and for the Eastern European region. At the same time, we need to strengthen and systematize our HR management.

Your strategy for growth includes internal and external growth. What is the current status of future acquisitions?

Several projects are in the works. These projects concern smaller firms that would expand our technology portfolio, as well as larger competitors which could help us to enter new markets. But we are very cautious in this matter. It is important that the acquired company can be easily integrated. The success of an acquisition lies in the ability to manage the integration.
Global competitiveness further improved

ISRA has successfully continued its constant course of expansion recorded over the past years into the 2004/2005 fiscal year. As expected, total operating revenue increased by twelve percent to € 49.7 million, while pre-tax earnings (EBT) went up by 54 percent to € 8.7 million. The fiscal year ended – as in the previous year – with a strong fourth quarter which saw pre-tax earnings growth accelerate to 72 percent.

The gross margin (total operating revenue minus production costs) – a key profit figure for the company – showed continuous improvement throughout the fiscal year. In the fourth quarter it reached just below 60 percent. Accumulated over the entire fiscal year the gross margin rose strongly by four percentage points to 58 percent. Thus ISRA has proven that after the completion at the end of March 2005 of the integration of Lasor, which had been acquired in the prior year, the pre-acquisition margin levels have been met again, while at the same time new potential is in evidence. Boosted by further efficiency increases in production, engineering and purchasing, ISRA distinctly exceeded its margin and costs goal of a 55 percent gross margin in the 2004/2005 fiscal year and has reached a level higher than specified in the previously formulated long-term profit vision.

Financing power strengthened

Additionally, ISRA has continued to strengthen its financing power. Cash flow from operating activities rose by 17 percent to € 8.5 million. It was possible to finance all investments directly out of cash flow. Furthermore, fund assets rose by 29 percent to € 5.9 million by the end of the fiscal year. The company has no bank debt and, with financial reserves of over € 10 million, has a solid financial basis. The equity ratio showed a strong improvement by four percentage points up to 73 percent. This puts ISRA clearly above the average of international industrial companies.

Surface Vision grows dynamically – profitability improves

Surface Vision, ISRA’s higher-margin business division improved total revenue by 32 percent, putting it well on its way to world leadership. ISRA achieved over 70 percent of its total revenues in this segment. The profitability continued to improve. EBT skyrocketed by 90 percent, and the EBT margin reached 18 percent. The strongest growth contributions came from the regions Asia and America, while Europe maintained its high level.

Industrial automation expects strengthening of business

Growing indications of a market revitalization were observed in the Industrial Automation segment based on increasing automation investments and supported by a series of innovative products developed by ISRA in the 2004/2005 fiscal year. As expected, the business division consolidated in the reporting year. Timely adjustments of the costs ensured that the EBT margin rose to 15 percent despite lower revenues.
ISRA business units: geared to the market

The greatest growth levels in the 2004/2005 fiscal year could be observed in the Glass and Paper businesses. The Glass business unit has further increased its worldwide market share. ISRA, with its broad product range, is the global innovation and market leader in flat glass inspection. Activities were further increased in the market for thin glass, the key component for flat panel displays. The Asian market remains the motor of growth followed by Europe. The Paper business unit successfully entered the market for standard paper inspection. The strongest growth was achieved through follow-up orders from leading paper manufacturers from the US and Europe. In Print inspection, important contacts to customers in the fields of gravure printed packaging and roll offset printing were established. The plastic film industry was a major driver of the solid growth of the Plastics business unit. Strong growth contributions, primarily from America, were experienced in this field. Automotive is profiting from strong demand by the automobile industry in the US. ISRA presented to the automotive manufacturers innovative solutions indicating how further potential in productivity and efficiency can be developed with the help of new applications. New orders were obtained in this field. The Asian market entry is intensively pursued. The Integrated Systems business unit managed to successfully enter the market of high performance can inspection. The cooperation with Ball, a world market leader in packaging, is the basis for further expansion into the food packaging market. Good turnover was achieved particularly in Europe.

Designed for cost

ISRA spent € 6.6 million for research and development (previous year € 5.8 million). At the forefront were new product developments for existing markets and the enhancement of existing products for new markets where ISRA intends to develop additional sales fields. In addition, progress is being made in the standardization of system components to further reduce production cost.

The research and development strategy is characterized by new collaborations with external partners and by internal strategic teams for specific markets. Apart from standardization and cost reduction, acceleration of worldwide innovation speed is one of the primary goals for ISRA because the flexibility and energy with which ISRA can react to market requirements will be one of the paramount advantages in tomorrow’s global markets.

High innovation speed

The Surface Vision R&D activity concentrates on very high resolutions at high web speeds. New product developments are on the way in automotive glass, display glass and for the film and printing industries. Our customers see their primary benefit in a productivity rise leading to the possibility of profit improvement with the help of ISRA equipment. New product generations will facilitate the transition from pure inspection to economic evaluation. In this field, ISRA plans to employ web-based database technology, which is advantageous in particular for internationally operating companies.

In Industrial Automation, the new generation of FPGA-based processor chips for industrial use was released to production. New projects are intelligently adapting robot vision algorithms as well as the miniaturized integration of cameras and FPGA-based processor chips for the cost optimized application of Robot Vision technology. As a result, intelligent modules will be available for the OEM strategy. Product developments to enter the food packaging market currently concentrate on can inspection and bulk material sorting.
The most valuable asset – the ISRA employees

In the fiscal year 2004/2005 the ISRA group employed an average of 246 people worldwide. The majority works in Germany at the locations Darmstadt, Karlsruhe, Marl und Oerlinghausen. Fourteen percent work at the two US locations, Lansing and Atlanta, three percent in Shanghai. About half of all employees work in production and engineering, approximately 23 percent in research and development. Sales and marketing sum up to 15 percent, 12 percent of all ISRA employees work in the field of administration.

To strengthen further the bigger of its two divisions, ISRA is establishing its worldwide Surface Vision headquarter in Herten. Here, the activities of this division, which are currently scattered around different locations, will be concentrated; however, Oerlinghausen will be maintained as a production site. In addition the Shanghai and Atlanta locations will be further expanded.

Good growth with sustainable improvement in earnings

ISRA’s group sales rose by eleven percent to € 44.7 million, while total operating revenues rose by 12 percent to € 49.7 million. In the Surface Vision segment ISRA achieved a rise of the total operating revenues by 32 percent to € 35.7 million. As a result, the share of this segment with its strong growth and good margins amounted to 72 percent of ISRA’s total business. As expected and taken into account in all planning, the total operating revenue in the Industrial Automation segment diminished to € 14.0 million (previous year: € 17.1 million).

With a rise by two percent to € 21.0 million, production cost has grown clearly under-proportionately to total operating revenues. Thus the gross profit improved by 21 percent to € 28.7 million. Gross margin rose by four percentage points to 58 percent.

Despite an increase in total operating revenue, material cost decreased by four percent to € 10.1 million. Cost of materials therefore declined by four percent to 20 percent. Personnel expenses developed slightly underproportionately to total operating revenue. They rose by ten percent to € 10.8 million. Accordingly the personnel expense ratio stayed at a stable 22 percent.

Research and development cost amounted to € 6.6 million (€ 5.8 million in the previous year) and remain at 13 percent of total operating revenues – as in the last year. Of these expenditures five million Euro were invested into new products with impending product launch (previous year € 3.8 million). These expenditures have been capitalized in accordance with IAS 38. At the same time € 3.1 million (previous year € 2.3 million) were written off for capitalized development expenditures of the previous years and of the reporting year.

Sales and administration expenses total € 9.4 million (previous year € 8.4 million). Therefore their share of 19 percent of total operating performance remains the same as in the preceding year. There was merely a small shift between the types of expenditures: The sales cost ratio rose to 13 percent (12 percent in the previous year) and the administration cost ratio dropped to six percent (7 percent in the previous year).
With € 4.6 million (previous year € 4.5 million), depreciation decreased in comparison to total operating revenues from ten percent in the year before to nine percent in the current fiscal year. Since the beginning of the current fiscal year, goodwill from acquisitions is no longer depreciated on a regular basis. The corresponding cost amounted to € 0.7 million in the previous year.

**EBT rises by 54 percent, net profit by 83 percent**

ISRA substantially improved profitability. EBIT (earnings before interest and taxes) climbed by 53 percent to € 8.7 million. Pre-tax earnings (EBT) soared 54 percent to € 8.7 million. As a result, the EBT-margin gained 5 percentage points to arrive at 18 percent. In the Surface Vision segment, EBT improved by 90 percent to € 6.6 million. The EBT margin progressed by five points to 18 percent. Due to timely cost reduction, Industrial Automation segment EBT stayed almost constant with € 2.1 million in comparison to last year. The corresponding EBT margin improved by two percentage points to 15 percent.

**EPS up by 74 percent**

Net profit jumped to € 6.0 million, an increase of 83 percent. Accordingly, the net profit margin (net profit in relation to total operating revenue) rose by five points to twelve percent. Earnings per share (annual net profit per share) rose by 74 percent to € 1.51. The return on capital employed improved from 11% to 15%.

In addition to its earning power, ISRA was also able to further strengthen its financing power in 2004/2005. Thus cash flow from operating activities improved by 17 percent to € 8.5 million. After investing € 7.5 million (previous year € 8.7 million), ISRA generated a net cash flow of € 1.3 million. Therefore fund assets climbed by 29 percent to € 5.9 million.

**Equity ratio further improved to 73 percent**

In the fiscal year 2004/2005, ISRA increased the group’s total assets by 10 percent to € 67.0 million. In this context, short-term assets rose by 19 percent to € 34.3 million and increased their share of total assets by four percentage points from 47 percent in the previous year to currently 51 percent. The share of long-term assets decreased accordingly to 49 percent (previous year 53 percent).

Liquid assets increased by 21 percent to € 5.9 million. The intangible assets share decreased by two percentage points to 47 percent of total assets. Fixed assets amount to only two percent of total assets.

On the liabilities side of the balance sheet, equity increased by 17 percent to € 49.1 million because of the good annual result. The equity ratio rose by four percentage points to 73 percent. Accordingly the proportion of outside capital dropped to 27 percent of total assets. Short term liabilities decreased by 19 percent to € 10.0 million reducing their share of total assets from 20 to 15 percent. The long-term liabilities’ share rose from eleven to twelve percent of total assets. ISRA has no bank debt.
ISRA stock price climbed by 80 percent

ISRA shares showed a remarkable stock price performance in the 2004/2005 fiscal year. In the 2004/2005 fiscal year – October 1, 2004 to September 30, 2005 – the share price climbed by about 80 percent from € 11.20 to € 20.20. This caused one of the most important benchmarks, the TecDax, to be clearly exceeded. Against the market trend, the good performance of the ISRA share continued after the fiscal year-end. The lowest share price came to € 10.66, the highest to € 21.50. Daily stock trading averaged just about 8,500 shares on the German stock exchanges. Rising prices in the fourth quarter led to increased trading volume. Thus, the average daily trading rate amounted to 10,000 shares in the fourth quarter.

At a share count of 3,947,940 shares as of September 30, 2005, ISRA had a market capitalization of just below € 80 million. With this value, ISRA has reached dimensions which make the ISRA shares interesting for investors not only in Germany but also in foreign countries. This becomes evident by the great interest at road shows and at analyst and investor conferences both at home and abroad. In this context, the cooperation with equinet, LBBW and Sal. Oppenheim is very important.

We seek to establish contact with investors, prospective investors and the public. In doing so, we do not wait for questions to come to us but proactively contact journalists, analysts and investors. In the fiscal year of 2004/2005 in addition to interviews with journalists and the dialogue with investors we have used numerous road shows and capital market conferences to present ISRA's equity story.

ISRA has commissioned two designated sponsors, LBBW and equinet, to continuously set two-way prices and keep sufficient liquidity in ISRA shares in order to provide for fair prices for all investors. To make it easy for investors to get an objective picture of the company and flesh out their investment decision, ISRA is permanently covered by research analysts of equinet, LBBW and Sal. Oppenheim.

Corporate Governance

ISRA VISION SYSTEMS AG has for many years maintained responsible company management and control with the intention of creating long-term added value. This is the basic principle of the company. ISRA therefore welcomes and supports the German Corporate Governance Code. It promotes efficient and faithful cooperation between the Executive Board and the Supervisory Board, respect for the interests of shareholders and candor and transparency in the company's communications. In this respect, the Code is in full agreement with the information policy ISRA has always pursued – versus shareholders, the financial community and the broad public. We are convinced that the Code will strengthen the confidence of international and national investors, customers, employees and the public in the management and supervision of the company.
Declaration of compliance with the Corporate Governance Code as of June 2, 2005

The Executive Board and the Supervisory Board of ISRA VISION SYSTEMS AG hereby declare, in accordance with clause 161 of the AktG that the recommendations of the government commission on the “German Corporate Governance Code” in the version dated June 2, 2005 have been and are fulfilled with the following exceptions:

Until now, it has not been envisioned to ease the personal observance of shareholders rights, nor to appoint a personal representative on behalf of the company. Furthermore, as provided for by clause 134 paragraph 3 sentence 2 of the AktG written notification is still required for the appointment of proxy voting rights in the General Meeting (Code item 2.3.3).

Except for the Chairman of the Executive Board, the D&O insurance policies do not provide for any personal liability on behalf of the members of the executive bodies (Code item 3.8).

The remuneration of the Executive Board members are recorded in the company accounts. They are not recorded in a way which indicates the composition of the individual elements (Code item 4.2.4).

There is no age limit for members of the Supervisory Board (Code item 5.4.1).

The remuneration of the Supervisory Board members takes into account the positions of the Chairman and Vice Chairman of the Supervisory Board. There is no provision for additional remuneration for chairmanship or membership of committees, nor for an additional success-based remuneration of the Supervisory Board members, nor is there any provision to publish individual details concerning the remuneration of the Supervisory Board members (Code item 5.4.7).

The company observes the current statutory requirements and publishes the annual statement of company accounts within 90 days of the end of the fiscal year and interim reports within 60 days of the end of the reporting period (Code item 7.1.2).

The annual statement of company accounts provides individual information on the shareholdings of members of the Executive Board and the Supervisory Board. It is not proposed to provide any additional information (Code item 7.1.5).

Darmstadt, November 28, 2005
**Continuous dynamic growth, increasing profits**

The Machine Vision sector is a worldwide growth market par excellence. The possibilities for applying this key technology are still in an early stage of development. So far only an approximate 15 percent of the market potential have been tapped. Therefore industry associations are expecting a long term double-digit growth of the market as a whole per year. Specific sub-sectors are likely to experience significantly stronger growth.

With its excellent positioning in this global market, ISRA VISION wants to partake in this promising development. In pursuing its growth targets ISRA employs the dual multi-segment strategy in order to make the best of global opportunities and restrict risks to local markets and individual sectors.

ISRA faces these market challenges with a dual innovation push. On the one hand market shares in existing markets are expanded by opening new regions and sales channels for existing products and business units and by developing innovations for existing customer industries. On the other hand existing technology is applied and offered to new customer industries and to unexploited regional markets.

Impulses for growth are expected for 2005/2006 in all regions. Asia will offer opportunities for expansion especially in thin glass inspection. In Paper and Plastics expected growth will be evenly distributed over Asia, America and Europe. The business units Print and Integrated Systems as well as the new area of Food Packaging see their growth potential primarily in America and Europe.

**Innovation push continues**

The innovations initiated in the previous year let us expect growth in the automobile sector even in Europe. In this industry, ISRA expects further growth in the US, while market buildup is further pushed forward in Asia and Eastern Europe. The automobile industry offers a large number of opportunities for Machine Vision applications. In the beginning of October 2005 a leading US American automobile manufacturer has decided to use ISRA’s optical 3D robot guidance for its automatic windshield installation system. This order has an approximate value of one million Euros.

A new market segment where ISRA opens up new industries by applying existing surface inspection technology is the metal market. Market entry in niche applications for steel, aluminum, copper and brass is currently being prepared by a team of experts.

With an order book of just under € 17 million as of December 15, 2005 (previous year € 15 million), ISRA once again expects double-digit profitable growth for the current business year; in all likelihood, growth will be particularly pronounced in the second half year.
Report of the Supervisory Board

The Supervisory Board exercised its legal and statutory responsibilities in fiscal year 2004/2005 by monitoring and advising the Executive Board of ISRA VISION SYSTEMS AG on a continuous basis. The Supervisory Board was supported by the Main Committee and the Audit Committee. The Chairman of the Supervisory Board remained in constant contact with the Chairman of the Executive Board and was immediately informed about all important occurrences.

During the shareholders’ meeting in 2005 there was a slight change to the composition of the Supervisory Board because of the new elections held on a rotational basis for the members acting for a period of five years. Dr. Moog was no longer available and was replaced by Dr.-Ing. h.c. Wiedenhues, so that the Supervisory Board now consists of Messrs. F. Haun, G. Riske, Prof. Dr. H. Tolle, Dr. D. Willasch, Dr. W. Witz and Dr.-Ing. h.c. H. Wiedenhues. During the subsequent board meeting, Prof. Dr. Tolle and Dr. Witz were re-elected, respectively, as Chairman and as Deputy Chairman of the Supervisory Board. The Main Committee includes Prof. Dr. Tolle, Dr. Willasch and Dr. Witz, with Prof. Dr. Tolle as Chairman, where as Dr.-Ing. h.c. Wiedenhues was nominated as Chairman of the Audit Committee comprising himself and Prof. Dr. Tolle. The Supervisory Board was informed regularly and in detail by the Executive Board about the situation and the development of the company and the main business transactions. Four meetings of the Supervisory Board were held, as well as one meeting each of the Main Committee and the Audit Committee.

The Supervisory Board has appointed Messrs E. Ersü (Chairman), H.-J. Christ, Dr. J. Giet and W. Rothermel to the Executive Board of ISRA VISION SYSTEMS AG for the period of March 1, 2005 to February 28, 2010. The Main Committee discussed board compensation, the degree of performance in relation to the performance-based components of compensation for 2003/2004, and the determination of the performance-based components of board compensation for 2004/2005. It has adapted the management contracts to the new elections and informed the Supervisory Board of its work.

The Audit Committee has discussed the AG’s financial results and the consolidated financial statement for 2003/2004 in detail with the Executive Board and the auditors, it has determined that there are no unmentioned risks or problems and has reported accordingly to the Supervisory Board. The Supervisory Board and Executive Board discussed the regulations of the Corporate Governance Code and approved the corresponding declaration.

Important topics in the consultations of the Supervisory Board and Executive Board were the company strategy, extent and type of possible acquisitions, the consolidation of the Marl and Bochum sites in Marl and, at a later date, at another location (Herten), the development in the Automotive and Surface Vision businesses, the establishment of a site in China for the Asian region and the annual audit of risk management. The latter was as evaluated positively, as was the efficiency of the Supervisory Board, which was also discussed.

The annual statement of accounts for 2004/2005 prepared by the Executive Board, with the associated management report of ISRA VISION SYSTEMS AG and the corporate accounts with the report on the corporate position have both been granted the unrestricted approval of the PKF financial auditing firm. The independent audit by the Supervisory Board based on the auditors’ report, their statements at the Supervisory Board meeting held on January 25, 2006 and the report of the Audit Committee gave no reason for objections to the accounts or to conduct additional audits. The Supervisory Board accordingly confirmed and accepted without objection the annual statement of accounts and management report prepared by the Executive Board for ISRA VISION SYSTEMS AG, as well as the corporate accounts with the report on the corporate position.

The business year 2004/2005 was again particularly successful. Determining factors were extremely effective worldwide distribution, successful research and development, which made a number of new products available, efficient production through systematization, resulting in considerably shortened production times, thorough cost control, better cooperation between employees at different locations, a very good result in the United States and an exceptional commitment on the part of management.

Therefore, the Supervisory Board wishes, at this point, to express their gratitude and appreciation to all employees as well as to the management of the ISRA Group of Companies for the meritorious efforts and results in the business year 2004/2005.

Prof. Dr. H. Tolle
Darmstadt, January 25, 2006
Consolidated Financial Statements

of ISRA VISION SYSTEMS AG,
Darmstadt as of September 30, 2005
Consolidated income statement (cost of sales method)

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</thead>
<tbody>
<tr>
<td>Net sales</td>
<td>44,687</td>
<td>40,437</td>
</tr>
<tr>
<td>Capitalized development expenditure</td>
<td>4,969</td>
<td>3,817</td>
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<tr>
<td><strong>Total operating revenue</strong></td>
<td><strong>49,656</strong></td>
<td><strong>44,254</strong></td>
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<tr>
<td>Cost of materials</td>
<td>10,144</td>
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<tr>
<td>Cost of labor</td>
<td>10,822</td>
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<td><strong>Production Costs</strong></td>
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<td><strong>20,475</strong></td>
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<tr>
<td>Gross Profit</td>
<td>28,690</td>
<td>23,779</td>
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<tr>
<td>Research and development costs</td>
<td>6,553</td>
<td>5,830</td>
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<tr>
<td>Sales and marketing costs</td>
<td>6,385</td>
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<tr>
<td>Administration costs</td>
<td>2,984</td>
<td>3,201</td>
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<tr>
<td><strong>Sales and administration costs</strong></td>
<td><strong>9,369</strong></td>
<td><strong>8,398</strong></td>
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<td>Other operational revenue</td>
<td>511</td>
<td>564</td>
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<td><strong>EBITDA</strong></td>
<td><strong>13,279</strong></td>
<td><strong>10,115</strong></td>
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<td>Depreciation/amortization</td>
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<td>4,458</td>
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<td><strong>Total costs</strong></td>
<td><strong>20,539</strong></td>
<td><strong>18,686</strong></td>
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<tr>
<td><strong>EBIT</strong></td>
<td><strong>8,662</strong></td>
<td><strong>5,657</strong></td>
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<tr>
<td>Financial result</td>
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<tr>
<td><strong>EBT</strong></td>
<td><strong>8,698</strong></td>
<td><strong>5,657</strong></td>
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<tr>
<td>Taxes</td>
<td>2,718</td>
<td>2,389</td>
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<tr>
<td><strong>Net profit for the period</strong></td>
<td><strong>5,980</strong></td>
<td><strong>3,268</strong></td>
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<tr>
<td>Earnings per share in €</td>
<td>1.51</td>
<td>0.87</td>
</tr>
<tr>
<td>Shares issued</td>
<td>3,947,940</td>
<td>3,748,109</td>
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</table>

The earnings per share according to IAS 33 (undiluted and diluted) totaled € 1.51 in fiscal year 2004/2005 (previous year € 0.87). This is based on 3,947,940 shares issued (previous year 3,748,109 shares – weighted numbers).

The following “notes” constitute an integral part of the consolidated financial statements.
# Consolidated balance sheet

<table>
<thead>
<tr>
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<tbody>
<tr>
<td><strong>ASSETS</strong></td>
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</tr>
<tr>
<td><strong>Assets</strong></td>
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<tr>
<td><strong>Current Assets</strong></td>
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<tr>
<td>Cash and cash equivalents</td>
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<tr>
<td>Trade receivables</td>
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<td>18,134</td>
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<td>Inventories</td>
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<td>Prepaid expenses</td>
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<td>95</td>
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<tr>
<td>Other assets</td>
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<td>1,175</td>
<td>657</td>
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<td><strong>Total current assets</strong></td>
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<td><strong>34,336</strong></td>
<td><strong>28,964</strong></td>
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<td><strong>Fixed assets</strong></td>
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<tr>
<td>Goodwill</td>
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<td>13,127</td>
<td>13,356</td>
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<tr>
<td>Other intangible assets</td>
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<td>17,966</td>
<td>16,442</td>
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<td>Tangible assets</td>
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<td>1,466</td>
<td>1,505</td>
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<tr>
<td>Deferred tax assets</td>
<td>19</td>
<td>139</td>
<td>931</td>
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<tr>
<td><strong>Total fixed assets</strong></td>
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<td><strong>32,698</strong></td>
<td><strong>32,235</strong></td>
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<tr>
<td><strong>Total Assets</strong></td>
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<td><strong>67,034</strong></td>
<td><strong>61,199</strong></td>
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<tr>
<td><strong>EQUITY AND LIABILITIES</strong></td>
<td></td>
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</tr>
<tr>
<td><strong>Short-term liabilities</strong></td>
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<tr>
<td>Trade payables</td>
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<td>2,885</td>
<td>2,597</td>
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<td>Bank liabilities</td>
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<td>Accruals</td>
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<td>Tax accruals</td>
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<td>777</td>
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<td>Deferred income</td>
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<tr>
<td>Other liabilities</td>
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<td>5,844</td>
<td>8,511</td>
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<td><strong>Total short-term liabilities</strong></td>
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<tr>
<td><strong>Long-term liabilities</strong></td>
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<tr>
<td>Deferred tax liabilities</td>
<td>19</td>
<td>7,264</td>
<td>6,158</td>
</tr>
<tr>
<td>Accruals for obligations to employees</td>
<td>20</td>
<td>729</td>
<td>696</td>
</tr>
<tr>
<td><strong>Total long-term liabilities</strong></td>
<td></td>
<td><strong>7,993</strong></td>
<td><strong>6,854</strong></td>
</tr>
<tr>
<td><strong>Equity</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Issued capital</td>
<td></td>
<td>3,948</td>
<td>3,903</td>
</tr>
<tr>
<td>Capital reserves</td>
<td></td>
<td>28,362</td>
<td>27,763</td>
</tr>
<tr>
<td>Currency exchange variations</td>
<td></td>
<td>-407</td>
<td>-773</td>
</tr>
<tr>
<td>Profit brought forward</td>
<td></td>
<td>11,229</td>
<td>7,961</td>
</tr>
<tr>
<td>Net profit for the period</td>
<td></td>
<td>5,980</td>
<td>3,268</td>
</tr>
<tr>
<td><strong>Total equity</strong></td>
<td></td>
<td><strong>49,112</strong></td>
<td><strong>42,122</strong></td>
</tr>
<tr>
<td><strong>Total equity and liabilities</strong></td>
<td></td>
<td><strong>67,034</strong></td>
<td><strong>61,199</strong></td>
</tr>
</tbody>
</table>
Consolidated cash flow statement

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Consolidated net profit for the period</td>
<td></td>
<td>5,980</td>
<td>3,268</td>
</tr>
<tr>
<td>Taxes paid</td>
<td></td>
<td>–307</td>
<td>–64</td>
</tr>
<tr>
<td>Changes in the deferred tax assets and the</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>accruals for deferred tax liabilities</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Changes in accruals</td>
<td></td>
<td>1,898</td>
<td>2,208</td>
</tr>
<tr>
<td>Depreciation/amortization</td>
<td></td>
<td>4,617</td>
<td>4,458</td>
</tr>
<tr>
<td>Changes in inventories</td>
<td></td>
<td>32</td>
<td>–2,700</td>
</tr>
<tr>
<td>Changes in trade receivables, other assets,</td>
<td></td>
<td>–4,370</td>
<td>204</td>
</tr>
<tr>
<td>prepaid expenses</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Changes in trade receivables, other</td>
<td></td>
<td>169</td>
<td>276</td>
</tr>
<tr>
<td>liabilities, deferred income</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Cash flow from operating activities</strong></td>
<td></td>
<td><strong>8,450</strong></td>
<td><strong>7,228</strong></td>
</tr>
<tr>
<td>Investments in tangible assets</td>
<td></td>
<td>–454</td>
<td>–531</td>
</tr>
<tr>
<td>Investments in intangible assets</td>
<td></td>
<td>–5,694</td>
<td>–4,068</td>
</tr>
<tr>
<td>Investments in shareholdings</td>
<td></td>
<td>0</td>
<td>220</td>
</tr>
<tr>
<td>Investments in acquisitions</td>
<td></td>
<td>22</td>
<td>–1,395</td>
</tr>
<tr>
<td><strong>Cash flow from investment activities</strong></td>
<td></td>
<td>–7,544</td>
<td>–8,688</td>
</tr>
<tr>
<td>Deposit from capital increase</td>
<td></td>
<td>0</td>
<td>3,288</td>
</tr>
<tr>
<td>Interest paid</td>
<td></td>
<td>36</td>
<td>0</td>
</tr>
<tr>
<td><strong>Cash flow from financing activities</strong></td>
<td></td>
<td>36</td>
<td>3,288</td>
</tr>
<tr>
<td>Changes in value resulting from exchange</td>
<td></td>
<td>366</td>
<td>–253</td>
</tr>
<tr>
<td>rate variations</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Changes in fund assets</strong></td>
<td></td>
<td><strong>1,308</strong></td>
<td><strong>1,575</strong></td>
</tr>
<tr>
<td>Fund assets as per October 1, 2004</td>
<td></td>
<td>4,555</td>
<td>2,980</td>
</tr>
<tr>
<td>Fund assets as per September 30, 2005</td>
<td></td>
<td>5,863</td>
<td>4,555</td>
</tr>
</tbody>
</table>
## Consolidated statement of changes in equity

for the period October 1, 2004 to September 30, 2005

<table>
<thead>
<tr>
<th>[in €]</th>
<th>Common stock</th>
<th>Capital reserves</th>
<th>Differences from currency variations</th>
<th>Profit brought forward</th>
<th>Net profit for the period</th>
<th>Equity</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>October 1, 2004</strong></td>
<td>3,903,446</td>
<td>27,762,914</td>
<td>–773,298</td>
<td>11,228,542</td>
<td>42,121,604</td>
<td></td>
</tr>
<tr>
<td>Capital increase by contribution in kind (Explanation 1)</td>
<td>44,494</td>
<td>599,779</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>644,273</td>
</tr>
<tr>
<td>Differences from currency variations</td>
<td>0</td>
<td>0</td>
<td>366,279</td>
<td>0</td>
<td>0</td>
<td>366,279</td>
</tr>
<tr>
<td>Dividends</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Net Profit</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>5,979,757</td>
<td>5,979,757</td>
</tr>
<tr>
<td><strong>September 30, 2005</strong></td>
<td>3,947,940</td>
<td>28,362,693</td>
<td>–407,019</td>
<td>11,228,542</td>
<td>5,979,757</td>
<td>49,111,913</td>
</tr>
</tbody>
</table>

for the period October 1, 2003 to September 30, 2004

<table>
<thead>
<tr>
<th>[in €]</th>
<th>Common stock</th>
<th>Capital reserves</th>
<th>Differences from currency variations</th>
<th>Profit brought forward</th>
<th>Net profit for the period</th>
<th>Equity</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>October 1, 2003</strong></td>
<td>3,440,479</td>
<td>22,668,207</td>
<td>–520,488</td>
<td>7,960,836</td>
<td>0</td>
<td>33,549,034</td>
</tr>
<tr>
<td>Capital increase by cash assets (Explanation 1)</td>
<td>306,200</td>
<td>2,981,488</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>3,287,688</td>
</tr>
<tr>
<td>Capital increase by contribution in kind (Explanation 1)</td>
<td>156,767</td>
<td>2,113,219</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>2,269,986</td>
</tr>
<tr>
<td>Differences from currency variations</td>
<td>0</td>
<td>0</td>
<td>–252,809</td>
<td>0</td>
<td>0</td>
<td>–252,809</td>
</tr>
<tr>
<td>Dividends</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Net Profit</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>3,267,705</td>
<td>3,267,705</td>
</tr>
<tr>
<td><strong>September 30, 2004</strong></td>
<td>3,903,446</td>
<td>27,762,914</td>
<td>–773,297</td>
<td>7,960,836</td>
<td>3,267,705</td>
<td>42,121,604</td>
</tr>
</tbody>
</table>
Segment reporting by division
Primary segments | for selected positions of the consolidated income statement

### Industrial Automation

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Total operating revenue</td>
<td>13,976</td>
<td>17,139</td>
</tr>
<tr>
<td>EBITDA</td>
<td>4,241</td>
<td>4,193</td>
</tr>
<tr>
<td>EBT</td>
<td>2,115</td>
<td>2,198</td>
</tr>
</tbody>
</table>

### Surface Vision

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Total operating revenue</td>
<td>35,680</td>
<td>27,115</td>
</tr>
<tr>
<td>EBITDA</td>
<td>9,038</td>
<td>5,922</td>
</tr>
<tr>
<td>EBT</td>
<td>6,583</td>
<td>3,459</td>
</tr>
</tbody>
</table>

Net sales/POC of € thousand 11,021 in the Industrial Automation segment and € thousand 33,667 in the Surface Vision segment were achieved. There was no interdivisional turnover.

The segment definition is based on the alignment of the corporate structure towards a market-oriented organization. The primary segment reflect the business divisions which sell specific products in particular markets:

- **Industrial Automation**
  
  The target markets of this division are primarily the automobile industry, machine tool manufacturers, the automation industry, general industry, machine and system manufacturers as well as the OEM markets where ISRA products are integrated as OEM systems into customers’ products. In these cases, ISRA applies the entire range of its technologies, i.e. in addition to the primary products Robot Vision and Quality Vision, Surface Inspection products are also applied.

- **Surface Vision**
  
  This segment of the company concentrates on surface inspection technology. This is primarily used for web materials, which are checked for defects during the production process. The main focus is on the float glass, film, non woven, paper and printing industries.
## Segment reporting by division

Primary segments | for the consolidated balance sheet

<table>
<thead>
<tr>
<th></th>
<th>Industrial Automation</th>
<th>Surface Vision</th>
<th>undistributed</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>as at Sept. 30, 2005</td>
<td>as at Sept. 30, 2004</td>
<td>as at Sept. 30, 2005</td>
<td>as at Sept. 30, 2004</td>
</tr>
<tr>
<td><strong>ASSETS</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Assets</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current assets</td>
<td>16,427</td>
<td>14,070</td>
<td>17,909</td>
<td>14,894</td>
</tr>
<tr>
<td>Fixed assets</td>
<td>9,406</td>
<td>8,800</td>
<td>23,292</td>
<td>23,435</td>
</tr>
<tr>
<td>Total assets</td>
<td>25,833</td>
<td>22,870</td>
<td>41,201</td>
<td>38,329</td>
</tr>
<tr>
<td><strong>EQUITY AND LIABILITIES</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Short-term liabilities</td>
<td>5,714</td>
<td>2,784</td>
<td>4,215</td>
<td>9,439</td>
</tr>
<tr>
<td>Long-term liabilities</td>
<td>0</td>
<td>0</td>
<td>729</td>
<td>696</td>
</tr>
<tr>
<td>Equity</td>
<td>49,112</td>
<td>42,122</td>
<td>49,112</td>
<td>42,122</td>
</tr>
<tr>
<td>Total equity and liabilities</td>
<td>5,714</td>
<td>2,784</td>
<td>4,944</td>
<td>10,135</td>
</tr>
</tbody>
</table>

| **Acquisition costs (cumulative)** |                       |                |               |                |                       |                      |
| Goodwill              | 4,693                 | 4,624          | 10,495        | 10,785         | 0                      | 0                    | 15,188            | 15,409 |
| Other intangible assets | 7,925                | 6,030          | 21,024        | 17,697         | 0                      | 0                    | 28,949            | 23,727 |
| Tangible assets       | 2,946                 | 2,141          | 1,909         | 2,342          | 0                      | 0                    | 4,855             | 4,483  |

| **Depreciation/ amortization** |                       |                |               |                |                       |                      |
| Goodwill              | 0                     | 253            | 0             | 493            | 0                      | 0                    | 0                 | 746   |
| Other intangible assets | 1,869                | 1,361          | 2,232         | 1,768          | 0                      | 0                    | 4,101            | 3,129 |
| Tangible assets       | 272                   | 381            | 244           | 202            | 0                      | 0                    | 516              | 583   |
## Segment reporting by region

### Secondary segments

<table>
<thead>
<tr>
<th>[in € thousand]</th>
<th>Germany, Europe</th>
<th>North America</th>
<th>Asia, ROW</th>
</tr>
</thead>
</table>

| Net sales | 21,571 | 19,622 | 10,892 | 9,609 | 12,225 | 11,206 |

### Secondary segments | for the consolidated balance sheet

<table>
<thead>
<tr>
<th>[in € thousand]</th>
<th>Germany, Europe</th>
<th>America/China</th>
<th>undistributed</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>as at Sept. 30, 2005</td>
<td>as at Sept. 30, 2004</td>
<td>as at Sept. 30, 2005</td>
<td>as at Sept. 30, 2005</td>
<td>as at Sept. 30, 2005</td>
</tr>
</tbody>
</table>

| ASSETS |
| Current assets | 28,998 | 25,192 | 5,338 | 3,772 | 0 | 0 | 34,336 | 28,964 |
| Fixed assets | 32,068 | 31,072 | 630 | 1,163 | 0 | 0 | 32,698 | 32,235 |
| Total assets | 61,066 | 56,264 | 5,968 | 4,935 | 0 | 0 | 67,034 | 61,199 |

| EQUITY AND LIABILITIES |
| Short-term liabilities | 8,554 | 11,231 | 1,375 | 992 | 0 | 0 | 9,929 | 12,223 |
| Long-term liabilities | 7,915 | 6,854 | 78 | 0 | 0 | 0 | 7,993 | 6,854 |
| Equity | 49,112 | 42,122 | 49,112 | 42,122 |
| Total equity and liabilities | 16,469 | 18,085 | 1,453 | 992 | 49,112 | 42,122 | 67,034 | 61,199 |
Company organization and financial and legal principles

1 | Basic methods of accounting and valuation

ISRA VISION SYSTEMS AG, Darmstadt (hereinafter “ISRA” or “Company”) was founded on September 23, 1997 and was registered in the commercial register of the Local Court of Darmstadt under the registration number HRB 6820 on September 25, 1997. The Company’s registered office is located in Darmstadt. The fiscal year runs from October 1 to September 30.

The purpose of the Company is to develop, market, employ, distribute and sell products, systems, equipment, and services in the areas of machine vision, automation, software and robot technology.

The Company’s annual consolidated financial statements were prepared in line with the International Financial Reporting Standards (IFRS) of the International Accounting Standards Committee (IASC). In the year under review the IFRS/IAS and interpretations (SIC) valid at the date of finalizing the accounts, and whose application is compulsory, were followed.

The consolidated annual financial statements have been prepared in Euro. As per September 30, 2005, the consolidated companies are as follows:

- The ISRA group of companies has been in existence from the time of its initial consolidation on October 1, 1998. The group of consolidated companies has changed in the previous fiscal year owing to the new foundation of ISRA VISION (Shanghai) Co. Ltd, Shanghai. A company was founded in Canada, however it has not become operational. ISRA GLASS VISION GmbH was merged into ISRA SURFACE VISION GmbH. ISRA VISION SYSTEMS AG holds directly or indirectly 100% of the shares in all group companies. The companies are fully consolidated in accordance with the shareholding relationship.

In relation to the legal basis, the following declaration is made:

The Company’s share capital at the balance sheet date totals € 3,947,940.00, divided into bearer shares of € 1.00 par value.
The capital developed as follows during the current fiscal year:

At the beginning of the fiscal year, the capital amounted to € 3,903,446.00.

- On the basis of a decision by the Executive Board on August 23, 2005 and with a confirmatory decision by the Supervisory Board on August 25, 2005, the base capital of € 3,903,446 was increased by € 44,494 to € 3,947,940 by means of issuing 44,494 new bearer shares with a calculated share in the share capital amounting to € 1.00 per share, in return for contribution in kind. The issue value was fixed at € 14.48 per share. The subscription right of shareholders was excluded in accordance with clause 4 paragraph 5 option 3 of the Articles of Incorporation.

The new shares are fully entitled to receive a share in the distribution of profits for the fiscal year 2003/2004 (from Oct. 1, 2003 onwards). The total issued value in excess of the share capital was allocated to the capital reserve.

In the context of this increase in non-monetary capital, a partial redemption of the purchase price obligation associated with the acquisition of NANOsystems Messtechnik GmbH in the amount of € 644,273.12 was undertaken.

In addition, the General Meeting held on March 30, 2005 resolved an amendment to the Articles of Incorporation. This amendment authorizes the Executive Board to increase the Company’s share capital until March 29, 2010 once only or on multiple occasions by issuing new no-par value shares against cash or non-cash contributions, up to a maximum amount of € 1,951,723.00 (authorized capital). The Executive Board is authorized, with the agreement of the Supervisory Board, to exclude the statutory subscription rights of shareholders.

- for residual amounts

- to secure shares in return for contributions of fixed assets, in particular in the context of mergers with other companies or the purchase of other companies, parts of companies or of an interest in other companies.

If the capital increase takes place by means of a cash contribution and the issued value is not, at the time of the final determination of the issued value by the Executive Board, significantly less than the share price of the shares of a same nature and scope which are already quoted on the stock markets, when judged in terms of the provisions of clauses 203 paragraphs 1 and 2 and 186 paragraph 4 of the German Stock Corporation Law (Aktiengesetz) and the amount of the base capital attributable to the shares issued under exclusion of the statutory subscription rights does not exceed € 390,344.00 and 10 % of the recorded base capital at the time of the issue of the new shares. Realization of stocks have to be charged against this 10 % limitation of base capital if they come to effect due to authorization under shareholder exclusion from subscription according to clause 71 paragraph 1 number 8 (German Stock Corporation Law (Aktiengesetz)) in connection with clause 186 paragraph 3 sentence 4 of the German Stock Corporation Law (Aktiengesetz). In addition, those stocks used to service bonds under option and/or conversion right are also to be charged against the 10 % limitation of base capital if the bond was issued under shareholder exclusion from subscription due to authorization according to clause 186 paragraph 3 sentence 4 of the German Stock Corporation Law.
On the basis of a resolution passed by the General Meeting on March 16, 2000, ISRA VISION SYSTEMS AG may conditionally increase its capital by € 250,000.00 by issuing up to 250,000 no-par value bearer shares to implement an employee equity compensation plan (conditional capital).

On the basis of a resolution passed by the General Meeting on March 30, 2005, the base capital may conditionally be increased by up to € 1,701,723.00 no-par value bearer shares (conditional capital II). The conditional capital increase may only be carried out to the extent that the holder of convertible or negotiable option bonds, issued on the basis of the authorization given to the Executive Board by the general meeting on March 30, 2005, makes use of this conversion or option right, or to the extent that the holders obliged to make the conversion fulfill their obligation to undertake the conversion.

On the basis of the decision of the General Meeting held on March 30, 2005, the Executive Board was authorized to acquire its own shares, up to a total of 390,344 shares in the company, corresponding to approximately 10% of the current base capital. Taking into account the principle of equal treatment (clause 53a of the German Stock Corporation Law), this applies subject to the provision that the shares which are purchased in accordance with this authorization, when added to the other shares in the company which the company has already purchased and still possesses, do not represent more than 10% of the base capital of the company. This authorization may be implemented in full or in parts. Purchases may be undertaken within the period covered by the authorization up to the point where the maximum purchase volume has been reached by partial purchases on various different purchasing dates. Purchases may also be undertaken by subsidiary enterprises of the company in the context of clause 17 of the German Stock Corporation Law or on its or their behalf by third parties.

2 | Accounting and valuation principles

(a) Differences between IFRS/IAS accounting and the German Commercial Code (HGB)

The company prepares its consolidated financial statements in line with the International Financial Reporting Standards/International Accounting Standards (IFRS/IAS) of the International Accounting Standards Committee (IASC). The primary obligatory differences from compulsory accounting disclosures, as required by the German Commercial Code (HGB), are summarized below:

- Percentage of completion method (POC) for evaluation of work in progress according to IAS 11:

According to commercial law (HGB), profits can only be realized for work in progress within very narrow confines – which means that, as a rule, only the completed contract method can be applied. According to IAS 11 and in connection with IAS 18, sales and corresponding profits have to be realized according to the percentage of completion method – insofar as the requisite conditions have been fulfilled. The percentage of completion is defined in line with the status of the work conducted by analyzing in detail the status of order processing in relation to current expenditure, compared with the currently assessed total order expenditure which is to be expected.

Orders are listed under trade receivables. If accumulated order cost and order profit/loss in individual cases exceed advance payments, these orders will be listed on the assets side under trade receivables as “future receivables from product orders”.
Deferred taxes on losses carried forward in line with IAS 12: according to the HGB, deferred tax assets resulting from tax losses carried forward may not appear on the balance sheet as the anticipated future tax savings have not yet been realized. According to IFRS/IAS 12, these future tax reduction claims must be capitalized if it is probable that they will be utilized.

Expenses for in-house product and software development according to IAS 38:

under the terms of the HGB, product development expenses and the costs of software assets developed in-house may be capitalized only in exceptional cases. According to IAS 38, these production costs must be capitalized and depreciated over the standard useful life. The conditions which must be fulfilled and confirmed for this purpose are:

– proof of technical feasibility of production for the planned and intended use or sale,
– proof that it is intended to produce the items in the near future,
– proof that it is possible to use the products in future or to sell them in the near future,
– proof in which way the intangible asset value will increase the net accrual of future economic benefit to the Company,
– proof that adequate resources are available to complete the development and to be able to use or sell the intangible asset,
– proof that it is possible to measure reliably the costs incurred during the development which are attributable to the intangible asset.

All demonstration requirements must be fulfilled; the costs must be purely development costs and are not permitted to contain any research element.

The capitalized development expenditures recorded in the profit and loss accounts contain the audited costs of product development which were assessed based on the costs of production. The amounts recorded in the profit and loss accounts under “development costs” include – in addition to research costs – other development costs which cannot be capitalized. Capitalized development expenditure in the reporting year and in past years is written off on a straight-line basis over six years. Capitalized development expenditure in the relevant reporting year is written off immediately in the reporting year following the start of the capitalization. The corresponding depreciation is recorded as a cost under “depreciation/amortization” in the profit and loss accounts (see also Notes part 11). The validity of the accounting value is ensured by a continuous process of monitoring and support of development projects. The capitalized accounting values are subjected to an audit of their value each year by determining their equivalent cash value. Unscheduled write-offs are undertaken as soon as the value of capitalized development expenditure exceeds the equivalent cash value.

(b) Estimates

The preparation of consolidated financial statements requires that assumptions or estimates be made which have an effect on the methods used in compiling the balance sheet and/or the income statement. The actual figures may deviate from these assumptions and estimates. Essentially, assumptions and estimates concern the valuation of accruals and inventories, as well as the likelihood that the receivables or deferred tax assets will be realized.
(c) Consolidation
In addition to ISRA’s single-entity financial statements, the consolidated financial statements include the single-entity financial statements of its subsidiaries, which were also prepared in line with the provisions of the IFRS/IAS. As a rule, the date of initial consolidation is the date upon which ISRA gained the controlling interest. During initial consolidation, only the hidden reserves and charges attributable to ISRA’s interest as the parent company are disclosed. A difference which cannot be attributed to individual assets is recorded as goodwill and is written off over the expected useful life. In accordance with IFRS 3 (mergers), goodwill is for the first time not written off anymore on a scheduled basis in the reporting year. In accordance with the previous regulation, goodwill depreciations in the reporting year would have amounted to € 792,425.50. Earnings per share in this case would have been € 1.33. The value of the goodwill is confirmed by an impairment test. If the value is found to be impaired, an unscheduled write-off is undertaken. The impairment test was executed by means of an EBIT multiplier which was already utilized to support the purchase decision. Transactions between consolidated companies are eliminated during consolidation.

(d) Currency conversion
The national currencies of the consolidated companies are their functional currencies. The Group currency is the Euro. The functional currency of the Company’s US subsidiaries is the US Dollar. When preparing the consolidated financial statements, the single-entity financial statements are converted into Euro; balance sheet items are converted using the mean exchange rate on the balance sheet date, whereas the items of the profit and loss accounts are converted at the average exchange rate. Currency differences from conversion are recorded as equity so that they will not affect the net profit for the period and are only realized when the relevant financial interest is sold.

Foreign currency entries in the single-entity financial statements are converted during the year in which they occur into the functional currency of the consolidated companies. Gains or losses resulting from the conversion of items are recorded at the time of their conversion so that they are reflected in the net profit for the period.

(e) Realisation of sales and of other revenue
Sales are recorded at the point of time at which the goods are delivered or the services are provided.

(f) Corporate and product-related advertising
The costs of corporate and product-related advertising are recorded as expenses at the time they are incurred.

(g) Research costs
Research is the search for new insights that are intended for use in developing new products and processes as well as in improving existing ones. Costs arising in this context are carried as expenses at the time they are incurred.

(h) Goodwill, impairment test, software and other intangible assets
Derived goodwill of ISRA VISION SYSTEMS Inc. was capitalized. Goodwill derived from the acquisition of part of a company of the Rheinmetall Group was not written off for the current fiscal year. Goodwill derived from the acquisition of ISRA GLASS VISION GmbH was not written off for the current fiscal year. Goodwill derived from the acquisition of ISRA SURFACE VISION GmbH was not written off for the current fiscal year. Goodwill derived from the acquisition of NANOsystems LLC was not written off for the current fiscal year. Goodwill derived from the acquisition of LASOR AG was not written off for the current fiscal year. Additional assets were identified as intangible assets at acquisition of LASOR AG in form of customer base (10 years useful economic life – linear depreciation), patents (15 years useful economic life – linear depreciation), specific measuring systems (15 years useful economic life – linear depreciation) and operational infrastructure in North America and Asia (10 years useful economic life – linear depreciation). For the individual goodwill positions, annual so-called impairment tests are carried out to confirm the value of the relevant items.
Software that has been acquired against payment is capitalized and written off over a normal useful life of four years. Other intangible assets that have been acquired against payment are carried at their acquisition cost and are subject to planned depreciation over their envisaged useful life or at most until the right or license expires.

(i) Cash and cash equivalents
The fund assets in the cash flow statement comprise checks, cash and credit balances as well as liabilities to banks.

(j) Trade receivables and other assets
Trade receivables and other assets are carried at their attainable amount. Possible bad debts are taken into account by way of individual allowances. Other assets include receivables from shareholders resulting from a settlement of accounts, employee travel advances and other assets. Contracted work requiring expenditure on engineering, installation and commissioning activities is evaluated by the percentage of completion method and, in accordance with the rules of the IFRS/IAS, recorded in the balance sheet as trade receivables for the first time in this report.

(k) Inventories
The items are valued at acquisition and production cost or at the lower market price on the balance sheet date. Elements of production expenses are material costs, direct production costs and overheads for materials and production. Financing, sales and administrative costs and depreciation for production equipment are not reflected in the manufacturing costs. An averaging method is applied to calculate expenditure on the consumption of materials.

(l) Fixed assets
Technical equipment and office fittings are carried on the balance sheet at their acquisition or production cost less planned depreciation. The costs of borrowing are carried as an expense at the point in time at which they are incurred. This also applies to repair and maintenance costs. Planned depreciation is calculated using the straight-line method over the expected useful life of the respective assets.

The useful life of the assets to be written down is shown in the following table:

<table>
<thead>
<tr>
<th>Description</th>
<th>Expected Useful Life</th>
</tr>
</thead>
<tbody>
<tr>
<td>Technical equipment</td>
<td>4 years</td>
</tr>
<tr>
<td>Office equipment/furnishings</td>
<td>4–10 years</td>
</tr>
</tbody>
</table>

(m) Unscheduled depreciation/amortization
Unscheduled depreciation/amortization is undertaken if the anticipated income from assets does not cover their residual net asset value. No unscheduled depreciation/amortization was necessary in the year under review.

(n) Trade payables and other payables
Trade accounts payable and other liabilities are carried at their cost of repayment.

These are exclusively current items, so that discounting is not required.

(o) Financial liabilities
Financial liabilities towards banks did not exist in the reporting year.

(p) Accruals
Accruals were made for liabilities recorded on the balance sheet date which are the result of past economic activities, in an amount which, it was felt after careful assessment, would cover the amount most likely to become payable.
(q) Deferred taxes
Taxes are deferred according to the balance sheet-oriented liabilities method. According to this method, differences existing on the balance sheet date between the valuation according to IFRS/IAS and the valuation according to tax law for assets and liabilities are to be taken into account by deferring tax assets or liabilities. This requires that the different valuation either decreases or increases the future taxable income. The period under review is not limited. In the case of deferred tax assets, the possibility of tax losses carried forward is also taken into account. The amount is capitalized to the extent to which realization of this amount is regarded as being realistic on the balance sheet date.

The Company and its subsidiaries are legally independent units and their registered offices are not at the same location. This means that the parent company and its subsidiaries are subject to different fiscal jurisdictions. As a rule, netting out of tax assets and liabilities is only possible within the same fiscal jurisdiction.

(r) Other taxes
Other taxes solely comprise motor vehicle tax – this is shown under “other operating expenses”.

(s) Grants from public authorities
These grants are recorded according to plan as income (under “other operational revenue”) upon receipt to compensate for the corresponding expenses.

(t) Risk concentration
Credit risks
The ISRA Group’s credit risks primarily relate to outstanding trade receivables. These receivables are mainly from companies of international good repute in the automotive and glass sectors and from other customers from large-scale industry. Owing to the nature of these customers, the credit risk must be considered minimal as far as the customers’ credit standing is concerned. Credit risks may additionally occur when the delivery quality is inadequate. In preparing the balance sheet, the Company’s risks were taken into account. Value adjustments have been made in relation to questionable receivables, which does not necessarily imply that the adjusted value of the receivables is not recoverable.

Market risks
The growth rates in the market for industrial image processing have currently decreased to 10% due to the weakness of the trade cycle. However, this is a temporary phenomenon. Nevertheless, there are areas that show growth rates of more than 50%. New requirements constantly give rise to new application opportunities that provide significant potential. ISRA must carefully select those market segments which offer an innovative and global structure – thus allowing customers to realize the relevant competitive advantages offered by ISRA. It is vital that the Company continues to pursue its clear focus consistently in the future. Through globalization and its strategic multi-segment approach, ISRA ensures its independence of individual sectors and customers.

In addition to further focusing on and expanding in these fields, the ISRA Group will make efforts to establish itself in new markets. It continues to pursue the necessary research and development activities. Additional company acquisitions will also be considered. The Company currently has a total of more than 56 R&D employees.

Currency risks
The currency risks have increased during the past fiscal year as compared with the previous year. The management has adjusted the sales calculation methods to the development of the dollar rate and has therewith largely accommodated the currency risk. As a rule, an effort is made to provide quotations in Euro. Only in the US are quotations made in both local and Euro currencies. If the dollar exchange rate remains weak against the Euro in the longer term, it will become necessary for the management to adopt further measures to reduce currency risks.
## Consolidated income statement (total cost method)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Total operating revenue</strong></td>
<td>1</td>
<td>49,843</td>
<td>46,768</td>
</tr>
<tr>
<td>Cost of materials</td>
<td>2</td>
<td>–9,876</td>
<td>–11,408</td>
</tr>
<tr>
<td>Personnel costs</td>
<td>3</td>
<td>–17,652</td>
<td>–16,022</td>
</tr>
<tr>
<td>Depreciation/amortization</td>
<td>4</td>
<td>–4,617</td>
<td>–4,458</td>
</tr>
<tr>
<td>Other operating costs</td>
<td>5</td>
<td>–9,036</td>
<td>–9,223</td>
</tr>
<tr>
<td><strong>Earning from operations</strong></td>
<td></td>
<td>8,662</td>
<td>5,657</td>
</tr>
<tr>
<td>Financial result</td>
<td>6</td>
<td>36</td>
<td>0</td>
</tr>
<tr>
<td><strong>Earning from ordinary business activities</strong></td>
<td></td>
<td>8,698</td>
<td>5,657</td>
</tr>
<tr>
<td>Tax expenses</td>
<td>7</td>
<td>–2,718</td>
<td>–2,389</td>
</tr>
<tr>
<td><strong>Net profit for the period</strong></td>
<td></td>
<td>5,980</td>
<td>3,268</td>
</tr>
</tbody>
</table>
Notes

1 | Operating revenue

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Net sales</td>
<td>40,799,933.56</td>
<td>38,585,437.79</td>
</tr>
<tr>
<td>Revenues according to POC</td>
<td>3,887,505.46</td>
<td>1,851,272.02</td>
</tr>
<tr>
<td>Changes in inventory</td>
<td>-537,194.51</td>
<td>1,613,535.56</td>
</tr>
<tr>
<td>Capitalized development expenditure</td>
<td>4,969,105.25</td>
<td>3,817,425.99</td>
</tr>
<tr>
<td>Other operating income</td>
<td>723,835.29</td>
<td>900,672.15</td>
</tr>
<tr>
<td>Total</td>
<td>49,843,185.05</td>
<td>46,768,343.51</td>
</tr>
</tbody>
</table>

The gross profit in percent of order revenues according to POC approximates the company’s total gross profit in percent.

2 | Cost of materials

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Expenditure on raw materials and supplies</td>
<td>-9,627,062.70</td>
<td>-11,009,992.54</td>
</tr>
<tr>
<td>Expenditure on purchase of services</td>
<td>-248,506.25</td>
<td>-398,283.72</td>
</tr>
<tr>
<td>Total</td>
<td>-9,875,568.95</td>
<td>-11,408,276.26</td>
</tr>
</tbody>
</table>

3 | Personnel costs

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Salaries and wages</td>
<td>-15,201,600.18</td>
<td>-14,083,050.39</td>
</tr>
<tr>
<td>Social security contributions</td>
<td>-2,450,546.30</td>
<td>-1,939,034.98</td>
</tr>
<tr>
<td>Total</td>
<td>-17,652,146.48</td>
<td>-16,022,085.37</td>
</tr>
</tbody>
</table>
### 4 | Depreciation/amortization

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Depreciation on intangible assets</td>
<td>–4,101,535.54</td>
<td>–3,875,191.23</td>
</tr>
<tr>
<td>Tangible assets</td>
<td>–515,110.61</td>
<td>–583,303.11</td>
</tr>
<tr>
<td>Total according to inventory of assets</td>
<td>–4,616,646.15</td>
<td>–4,458,494.34</td>
</tr>
</tbody>
</table>

Of the depreciation/amortization of intangible assets, € 3,095,994.96 (previous year: € 2,333,278.23) relates to capitalized development expenditures, which are written off over a period of six years.

### 5 | Other operating expenses

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Travel costs</td>
<td>–2,053,879.38</td>
<td>–1,801,118.61</td>
</tr>
<tr>
<td>Rent for office space</td>
<td>–948,718.76</td>
<td>–899,308.66</td>
</tr>
<tr>
<td>Costs of external staff</td>
<td>–593,742.37</td>
<td>–751,958.01</td>
</tr>
<tr>
<td>Exhibitions and other promotional costs</td>
<td>–753,673.89</td>
<td>–517,899.87</td>
</tr>
<tr>
<td>Postage, telephone and fax costs</td>
<td>–604,970.20</td>
<td>–488,725.70</td>
</tr>
<tr>
<td>Rent of operational and office equipment</td>
<td>–277,895.51</td>
<td>–306,691.09</td>
</tr>
<tr>
<td>Vehicle costs</td>
<td>–309,704.45</td>
<td>–303,879.91</td>
</tr>
<tr>
<td>Insurances and contributions</td>
<td>–423,756.45</td>
<td>–322,637.79</td>
</tr>
<tr>
<td>Outbound logistics</td>
<td>–516,208.53</td>
<td>–452,624.25</td>
</tr>
<tr>
<td>Legal and consultancy costs</td>
<td>–756,802.35</td>
<td>–534,134.64</td>
</tr>
<tr>
<td>Cost of nonexecuted acquisitions</td>
<td>–212,873.32</td>
<td>0.00</td>
</tr>
<tr>
<td>Debts written off</td>
<td>0.00</td>
<td>–23,174.00</td>
</tr>
<tr>
<td>Commission payments</td>
<td>–570,782.07</td>
<td>–751,622.40</td>
</tr>
<tr>
<td>Other costs</td>
<td>–1,013,070.34</td>
<td>–2,069,284.40</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>–9,066,077.62</td>
<td>–9,223,059.33</td>
</tr>
</tbody>
</table>
### 6 | Financial result

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Net interest income</td>
<td>35,998.17</td>
<td>185.44</td>
</tr>
</tbody>
</table>

### 7 | Tax expenses

The tax expenses shown in the income statement are attributable to Germany and foreign countries as well as to current tax expenses and deferred tax expenses as follows:

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Taxes on current income</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Germany</td>
<td>583,517.45</td>
<td>180,600.00</td>
</tr>
<tr>
<td>Other countries</td>
<td>237,380.44</td>
<td>0.00</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>820,897.89</td>
<td>180,600.00</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Deferred tax expenditure</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Germany</td>
<td>1,819,666.00</td>
<td>1,965,013.92</td>
</tr>
<tr>
<td>Other countries</td>
<td>78,423.43</td>
<td>242,923.59</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>1,898,089.43</td>
<td>2,207,937.51</td>
</tr>
</tbody>
</table>

The tax charges, based on the tax rate applicable to ISRA as a parent company, and the actual tax charges of the Group can be reconciled as follows:

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Earnings before tax</td>
<td>8,698</td>
<td>5,656</td>
</tr>
<tr>
<td>Expected tax expenses on earnings based on the tax rate of the parent company (38.3%)</td>
<td>3,419</td>
<td>2,223</td>
</tr>
<tr>
<td>Effect of tax rates applied to earnings in other countries</td>
<td>–99</td>
<td>–63</td>
</tr>
<tr>
<td>Consolidation effect</td>
<td>–602</td>
<td>228</td>
</tr>
<tr>
<td>Recorded tax on earnings</td>
<td>2,718</td>
<td>2,388</td>
</tr>
</tbody>
</table>
Based on our internal calculations, ISRA VISIONS SYSTEMS AG is subject to a total tax rate of 39.3% – this comprises corporation tax, solidarity surcharge and business income tax. The deferred taxes in the single entity financial statements for ISRA LLC, ISRA VISION SYSTEMS Inc. and INNOMESS Corp., NANOsystems LLC and ISRA SURFACE VISION Inc. were calculated based on a tax rate of 30%. For ISRA VISION (Shanghai) Co. Ltd. a tax rate of 15% was applied.

8 | Trade receivables

<table>
<thead>
<tr>
<th>[in €]</th>
<th>September 30, 2005</th>
<th>September 30, 2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trade receivables of the parent company</td>
<td>4,314,527.45</td>
<td>5,155,191.88</td>
</tr>
<tr>
<td>Trade receivables of German subsidiaries</td>
<td>4,057,888.09</td>
<td>3,893,593.27</td>
</tr>
<tr>
<td>Trade receivables of subsidiaries based outside Germany</td>
<td>2,281,014.91</td>
<td>1,585,127.13</td>
</tr>
<tr>
<td>Receivables from unfinished contracts according to the percentage-of-completion method</td>
<td>7,480,896.09</td>
<td>3,638,266.09</td>
</tr>
<tr>
<td><strong>Balance sheet value</strong></td>
<td><strong>18,134,326.54</strong></td>
<td><strong>14,272,178.37</strong></td>
</tr>
</tbody>
</table>

The devaluations for receivables disclosed as other operating expenses were made exclusively on a case-by-case basis. The audit of the receivables disclosed on the balance sheet date did not result in any other recognizable risks for the Company’s receivables. Advance payments already received in the amount of € 808,741.40 (previous year € 928,265.18) have been deducted from the receivables from unfinished orders evaluated on the percentage-of-completion basis.
9 | Inventories

The inventories include:

<table>
<thead>
<tr>
<th>[in €]</th>
<th>September 30, 2005</th>
<th>September 30, 2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Raw materials, consumables and fuel</td>
<td>3,258,905.13</td>
<td>2,256,876.45</td>
</tr>
<tr>
<td>Unfinished products</td>
<td>4,453,945.82</td>
<td>4,550,702.26</td>
</tr>
<tr>
<td>Finished products</td>
<td>1,470,722.72</td>
<td>2,767,871.66</td>
</tr>
<tr>
<td>Advance payments received</td>
<td>–106,000.00</td>
<td>–464,132.60</td>
</tr>
<tr>
<td>Advance payments made</td>
<td>1,427.82</td>
<td>0.00</td>
</tr>
<tr>
<td><strong>Balance sheet value</strong></td>
<td><strong>9,079,001.49</strong></td>
<td><strong>9,111,317.77</strong></td>
</tr>
</tbody>
</table>

10 | Other assets

Other assets comprise the following items:

<table>
<thead>
<tr>
<th>[in €]</th>
<th>September 30, 2005</th>
<th>September 30, 2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loans to employees and other receivables from employees</td>
<td>147,421.30</td>
<td>195,350.76</td>
</tr>
<tr>
<td>Insurance claims (employer's pension liability insurance)</td>
<td>108,710.03</td>
<td>90,138.40</td>
</tr>
<tr>
<td>Receivables from tax authorities</td>
<td>785,431.55</td>
<td>258,576.96</td>
</tr>
<tr>
<td>Rent deposits</td>
<td>69,287.27</td>
<td>58,287.27</td>
</tr>
<tr>
<td>Other assets</td>
<td>63,616.77</td>
<td>54,153.19</td>
</tr>
<tr>
<td><strong>Balance sheet value</strong></td>
<td><strong>1,174,466.92</strong></td>
<td><strong>656,506.58</strong></td>
</tr>
</tbody>
</table>
### 11 | Intangible assets

The intangible assets include:

<table>
<thead>
<tr>
<th>Acquisition and production costs</th>
<th>Goodwill</th>
<th>Software, licenses</th>
<th>Capitalized developments</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>October 1, 2004</strong></td>
<td>15,409,154.08</td>
<td>10,874,324.14</td>
<td>12,852,893.11</td>
<td>39,136,371.33</td>
</tr>
<tr>
<td>Additions</td>
<td>123,974.07</td>
<td>610,272.92</td>
<td>5,010,964.84</td>
<td>5,745,211.83</td>
</tr>
<tr>
<td>Additions from acquisitions</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Disposals</td>
<td>370,000.00</td>
<td>9,328.34</td>
<td>390,236.06</td>
<td>769,564.40</td>
</tr>
<tr>
<td>Transfers</td>
<td>3,067.75</td>
<td>123,051.89</td>
<td>–126,119.64</td>
<td>0.00</td>
</tr>
<tr>
<td>Currency differences</td>
<td>22,076.18</td>
<td>3,023.17</td>
<td>0.00</td>
<td>25,099.35</td>
</tr>
<tr>
<td><strong>September 30, 2005</strong></td>
<td>15,188,272.08</td>
<td>11,601,343.78</td>
<td>17,347,502.25</td>
<td>44,137,118.11</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Depreciation/Amortization</th>
<th>Goodwill</th>
<th>Software, licenses</th>
<th>Capitalized developments</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>October 1, 2004</strong></td>
<td>2,053,549.18</td>
<td>1,829,376.27</td>
<td>5,455,581.92</td>
<td>9,338,507.37</td>
</tr>
<tr>
<td>Additions</td>
<td>205.09</td>
<td>1,005,335.49</td>
<td>3,095,994.96</td>
<td>4,101,535.54</td>
</tr>
<tr>
<td>Additions from acquisitions</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Disposals</td>
<td>0.00</td>
<td>10,293.91</td>
<td>393,166.32</td>
<td>403,460.23</td>
</tr>
<tr>
<td>Transfers</td>
<td>1,313.66</td>
<td>37,234.10</td>
<td>–38,547.76</td>
<td>0.00</td>
</tr>
<tr>
<td>Unscheduled depreciation</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Appreciation</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Currency differences</td>
<td>6,584.67</td>
<td>945.61</td>
<td>0.00</td>
<td>7,530.28</td>
</tr>
<tr>
<td><strong>September 30, 2005</strong></td>
<td>2,061,652.60</td>
<td>2,862,597.56</td>
<td>8,119,862.80</td>
<td>13,044,112.96</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Balance sheet value intangible assets</th>
<th>Goodwill</th>
<th>Software, licenses</th>
<th>Capitalized developments</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>October 1, 2004</strong></td>
<td>13,355,604.90</td>
<td>9,044,947.87</td>
<td>7,397,311.19</td>
<td>29,797,863.96</td>
</tr>
<tr>
<td><strong>September 30, 2005</strong></td>
<td>13,126,619.48</td>
<td>8,738,746.22</td>
<td>9,227,639.45</td>
<td>31,093,005.15</td>
</tr>
</tbody>
</table>

Under software and licenses, the purchased software, the license costs and the intangible assets purchased in the context of the acquisition, in so far as these were identifiable when the purchase price was allocated, are shown.

Development expenditure is capitalized in accordance with IAS 38. The accumulated depreciation/amortization amounts in total to € thousand 8,120 of which € thousand 3,096 relates to capitalized development expenditure in the reporting year.
### 12 | Tangible assets

Total tangible assets:

<table>
<thead>
<tr>
<th></th>
<th>Real estate, buildings</th>
<th>Technical equipment</th>
<th>Office equipment</th>
<th>Assets under construction</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>October 1, 2004</td>
<td>167,881.97</td>
<td>992,763.57</td>
<td>3,167,142.82</td>
<td>155,615.46</td>
<td>4,483,403.82</td>
</tr>
<tr>
<td>Additions</td>
<td>0.00</td>
<td>106,813.12</td>
<td>365,379.98</td>
<td>0.00</td>
<td>475,772.14</td>
</tr>
<tr>
<td>Additions from acquisitions</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Disposals</td>
<td>0.00</td>
<td>0.00</td>
<td>117,195.26</td>
<td>0.00</td>
<td>117,195.26</td>
</tr>
<tr>
<td>Transfers</td>
<td>0.00</td>
<td>-9,858.78</td>
<td>9,858.78</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Currency differences</td>
<td>0.00</td>
<td>0.00</td>
<td>12,827.51</td>
<td>0.00</td>
<td>12,827.51</td>
</tr>
<tr>
<td>September 30, 2005</td>
<td>167,881.97</td>
<td>1,089,717.91</td>
<td>3,438,013.83</td>
<td>159,194.50</td>
<td>4,854,808.21</td>
</tr>
</tbody>
</table>

#### Depreciation

<table>
<thead>
<tr>
<th></th>
<th>Real estate, buildings</th>
<th>Technical equipment</th>
<th>Office equipment</th>
<th>Assets under construction</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>October 1, 2004</td>
<td>0.00</td>
<td>79,875.21</td>
<td>435,235.40</td>
<td>0.00</td>
<td>515,110.61</td>
</tr>
<tr>
<td>Additions</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Additions from acquisitions</td>
<td>0.00</td>
<td>0.00</td>
<td>115,978.43</td>
<td>0.00</td>
<td>115,978.43</td>
</tr>
<tr>
<td>Disposals</td>
<td>0.00</td>
<td>-5,999.28</td>
<td>5,999.28</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Transfers</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Unscheduled depreciation</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Appreciation in value</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Currency differences</td>
<td>0.00</td>
<td>0.00</td>
<td>11,617.86</td>
<td>0.00</td>
<td>11,617.86</td>
</tr>
<tr>
<td>September 30, 2005</td>
<td>0.00</td>
<td>826,340.56</td>
<td>2,562,402.98</td>
<td>0.00</td>
<td>3,388,743.54</td>
</tr>
</tbody>
</table>

#### Balance sheet value tangible assets

<table>
<thead>
<tr>
<th></th>
<th>Real estate, buildings</th>
<th>Technical equipment</th>
<th>Office equipment</th>
<th>Assets under construction</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>October 1, 2004</td>
<td>167,881.97</td>
<td>240,298.94</td>
<td>941,613.95</td>
<td>155,615.46</td>
<td>1,505,410.32</td>
</tr>
<tr>
<td>September 30, 2005</td>
<td>167,881.97</td>
<td>263,377.35</td>
<td>875,610.85</td>
<td>159,194.50</td>
<td>1,466,064.67</td>
</tr>
</tbody>
</table>
13 | Liabilities to banks

There were no liabilities to banks on the balance sheet date.

14 | Trade payables

Trade payables total € thousand 2,885 (previous year € thousand 2,597). The liabilities are paid off regularly, taking full advantage of discount terms offered. The liabilities are not subject to interest payments.

15 | Other accruals

Other accruals include the following items:

<table>
<thead>
<tr>
<th></th>
<th>Oct. 1, 2004</th>
<th>Additions</th>
<th>Usage</th>
<th>Liquidation</th>
<th>Sept. 30, 2005</th>
<th>Of which due within next fiscal year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Warranties</td>
<td>254,940.00</td>
<td>259,477.55</td>
<td>247,385.00</td>
<td>7,555.00</td>
<td>259,477.55</td>
<td>259,477.55</td>
</tr>
<tr>
<td>Employees’ industrial compensation society</td>
<td>67,425.00</td>
<td>75,200.00</td>
<td>67,425.00</td>
<td>0.00</td>
<td>75,200.00</td>
<td>75,200.00</td>
</tr>
<tr>
<td>Contributions for severely handicapped persons/Mutual Benefit Association for Pension Security</td>
<td>20,155.00</td>
<td>20,520.00</td>
<td>20,155.00</td>
<td>0.00</td>
<td>20,520.00</td>
<td>20,520.00</td>
</tr>
<tr>
<td>Other accruals</td>
<td>116,000.00</td>
<td>0.00</td>
<td>116,000.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td><strong>Balance sheet value</strong></td>
<td><strong>458,520.00</strong></td>
<td><strong>355,197.55</strong></td>
<td><strong>450,965.00</strong></td>
<td><strong>7,555.00</strong></td>
<td><strong>355,197.55</strong></td>
<td><strong>355,197.55</strong></td>
</tr>
</tbody>
</table>

In order to cover its warranty obligations ISRA VISION SYSTEMS AG creates accruals of approx. 0.75% of its sales revenues for sales subject to warranty obligations in any given fiscal year.

The increase in accruals for the employees’ industrial compensation society is linked to the increase in the average number of employees.

These obligations are expected to become due in the following year.

16 | Tax accruals

Accruals for tax charges have been accumulated to cover the taxable earnings recorded in the respective Company financial statements, in the amount of the expected tax charges.
17 | Deferred Income

In relation to advance payments from customers in association with maintenance contracts, a passive accruals and deferrals item has been introduced to cover the remaining duration of the contracts. This amortization item for accruals and deferrals will be amortized over the remaining duration of the contracts.

18 | Other liabilities

(including liabilities to banks)

<table>
<thead>
<tr>
<th>[in €]</th>
<th>September 30, 2005</th>
<th>September 30, 2004</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>short-term</td>
<td>long-term</td>
</tr>
<tr>
<td>Payables to banks</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Wages &amp; salaries, performance bonus payments and remaining holiday entitlements</td>
<td>2,082,722.66</td>
<td>0.00</td>
</tr>
<tr>
<td>Turnover tax</td>
<td>7,180.08</td>
<td>0.00</td>
</tr>
<tr>
<td>Other liabilities</td>
<td>3,753,723.69</td>
<td>0.00</td>
</tr>
<tr>
<td>Balance sheet value</td>
<td>5,843,626.43</td>
<td>0.00</td>
</tr>
</tbody>
</table>

No accrued interest was deducted from these items, which are exclusively current in nature. „Other liabilities“ include liabilities resulting from the acquisition of companies in the amount of € 806,520.56.

19 | Deferred taxes

The calculation of the deferred taxes is based on average profit tax rates of 39.3 % for Germany and 30 % for USA. The deferred tax assets relate to subsidiary companies in Germany and other countries and are derived from existing losses carried forward which can be offset against tax

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Tangible assets</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Intangible assets</td>
<td>5,388,333.90</td>
<td>5,027,834.78</td>
</tr>
<tr>
<td>Inventories</td>
<td>–1,011,535.76</td>
<td>–329,463.65</td>
</tr>
<tr>
<td>Receivables, POC</td>
<td>2,939,992.01</td>
<td>1,429,838.57</td>
</tr>
<tr>
<td>Other items</td>
<td>–52,630.83</td>
<td>30,032.08</td>
</tr>
<tr>
<td>Deferred tax liabilities</td>
<td>7,264,159.32</td>
<td>6,158,241.78</td>
</tr>
<tr>
<td>Deferred tax assets</td>
<td>139,226.03</td>
<td>931,397.92</td>
</tr>
</tbody>
</table>
20 | Accruals for obligations to employees

The accruals for obligations to employees, in association with the company pensions plan, have been evaluated on the basis of the so-called projected unit credit method (current one-time premium payment procedure) in accordance with IAS 19. As part of this process, the values of the defined benefit obligation (DBO) and the current service cost are calculated precisely for each individual case. The amount of the appropriate financial reserve has been extracted from the review carried out on Sept. 30, 2005 in accordance with clause 6a of the income tax law (EStG). The evaluation is based on the following premises: interest on borrowings 4.75 %, trend of salary increases 2.5 % p.a., trend of increase in pensions 1.25 % p.a. An employer’s pension liability insurance has been taken out and is not regarded as part of the plan assets. In the profit and loss accounts, the service costs of € thousand 14 and the interest costs of € thousand 40 have been taken into account, minus the pension payments already provided amounting to € thousand 21.

21 | Other financial liabilities

These liabilities relate to leases of buildings and rentals of motor vehicles, the telephone system as well as of office fittings, which cannot be terminated before expiry. The resulting liabilities are as follows:

<table>
<thead>
<tr>
<th>Expenses during the years</th>
<th>in €</th>
</tr>
</thead>
<tbody>
<tr>
<td>2005 to 2009</td>
<td>1,366,677.11</td>
</tr>
<tr>
<td>after Sept. 30, 2009</td>
<td>0.00</td>
</tr>
<tr>
<td>Expenses in the year under review</td>
<td>1,226,614.27</td>
</tr>
</tbody>
</table>

There were no liabilities from investment projects already started on the balance sheet date.

There are severance payment-related hypothetical liabilities to the Management in the amount of € thousand 755.
22 | Observations on consolidated cash flow statement

The acquisition of companies in the reporting year resulted in a reduction of liquidity amounting to roughly € 1.4 million.

23 | Transactions with associated companies or related parties

In a lease dated August 12, 1998 the Company leased administration, storage, and development premises at the Company’s registered office in Darmstadt from ISRA Bau-Mitarbeiter-Beteiligungsgesellschaft GbR, Darmstadt. The Chairman of ISRA’s Executive Board, Mr. Enis Ersü, is a partner of this civil-law partnership. The lease has a fixed initial term of ten years – it may not be terminated during this period. The rent totals € 9,714 per month plus a lump-sum charge for ancillary services of € 767. The terms and conditions of the lease correspond to those that would have been agreed with a third party.

24 | Personnel

On average during the fiscal year 2004/2005, the number of employees stood at 246 (previous year 244).
25 | Stock option program

As a listed company, ISRA VISION SYSTEMS AG offers its employees the opportunity to participate directly in its success via a stock option program. The conditions for option rights on shares of ISRA VISION SYSTEMS AG on which this program is based were laid down on the basis of the authorization given by the General Meeting on March 16, 2000 and are as follows:

Options may only be issued to members of the Managing Board, managers and employees of ISRA VISION SYSTEMS AG and companies in the ISRA VISION SYSTEMS AG Group. The exact group of authorized participants and the scope of the options to be granted to them in each case will be defined by the Managing Board of ISRA VISION SYSTEMS AG. In the case of members of the Managing Board, these aspects will be determined and options issued exclusively by the Supervisory Board. In total, members of the Managing Board may be issued options for up to 30,000 shares, further employees of ISRA VISION SYSTEMS AG may be issued options for up to 100,000 shares, members of the management of group companies may be issued options for up to 30,000 shares and further employees of group companies may be issued options for up to 90,000 shares. The options may be issued after the quarterly reports for the second and third quarters of each fiscal year have been presented. Each option grants the holder the right to subscribe for one new, no-par value bearer share.

Options may only be exercised after the lock-up period has expired. The lock-up period is two years for 33 % of the options granted to the participant in a single tranche, three years for a further 33 %, and four years after the relevant issue date for the remaining amount. An option holder’s options expire if the option holder is no longer in a non-terminated employment relationship with or a member of a statutory body of ISRA VISION SYSTEMS AG or a group company. Exercise tranches which only become valid for exercise after notice has been given on an employment contract expire. Irrespective of this, options remain in force unchanged if the employment relationship ends due to the employee retiring or owing to professional disability. Options cannot be inherited or transferred.

Options may only be exercised if at least one of the predefined success targets has been reached. These align with the stock performance in relation to purchase price and time of exercise. The subscription price for a share is given by the arithmetic average of the closing prices in XETRA trading for the share in the period between the 15th and 5th stock market day (before the option is issued) multiplied by a factor of 1.1.
The Managing Board is authorized to define the further details of the subscription conditions and of the issue and structure of the options. In addition, the Managing Board is authorized to transfer the shares needed to fulfill the option rights by issuing acquired treasury shares or via new shares by way of a capital increase which is to be implemented. Insofar as members of the Managing Board are affected, the further details will be defined by the Supervisory Board. As of the reporting date, the Managing Board had issued a total of 55,108 options to the group’s employees (previous year 63,448).

26 | Occurrences after the balance sheet date

No significant occurrences have taken place after the balance sheet date.

27 | Notifications in accordance with clause 21 I and Ia of the WpHG

ISRA VISION SYSTEMS AG has received notice of the existence of shareholdings in accordance with clause 21 paragraph 1 or paragraph 1a of the law on dealings in shares (Wertpapierhandelsgesetz). The contents of the notifications are contained in the annex to the individual accounts.

28 | Declaration on Corporate Governance Code

The declaration of compliance required by clause 161 of the AktG has been submitted by the Executive Board and the Supervisory Board and made permanently available to the shareholders on the Company’s website.
Supervisory Board

- Prof. Dr. rer. nat. Dipl.-Ing Henning Tolle, University Professor em., Roßdorf, Chairman of the Supervisory Board

- Dr. Wolfgang Witz, attorney-at-law, Deputy Chairman of the Supervisory Board, with additional Supervisory Board responsibilities within Troester GmbH & Co. KG, Hannover, and TET System Holding GmbH & Co. KG, Heidelberg

- Dr. Rüdiger Moog, lawyer, accountant, Darmstadt (until March 30, 2005)

- Dr.-Ing. h.c. Heribert J. Wiedenhues, Lahnstein – deputy chairman of the supervisory board MASA AG, Andernach; deputy chairman of the supervisory board PM – International AG, Speyer; member of administrative board PM – International AG, Luxemburg; member of supervisory board nova-ratio AG, Ransbach-Baumbach; member of the advisory board BERGROHR GmbH, Siegen; member of the advisory board Capiton Piping GmbH, Essen; member of the advisory board (Vorsitz) VITRULAN GmbH, Marktschorgast (starting March 30, 2005)

- Gordon Riske, Chairman of the Managing Board Deutz AG, Cologne; with additional Supervisory Board responsibility within Drägerwerk AG

- Dr. Dieter Willasch, Physicist, M.Sc., formerly Spokesman of Managing Board of Spectris AG Sensoren und Systeme, Eningen

- Frank Haun, Dipl.-Ing., Managing Director of Krauss-Maffei Wegmann GmbH & Co. KG, Kassel, additional member of the Board of Control of Carl Mahr Holding GmbH, Göttingen and of Nagahama Seisakusho Ltd., Osaka/Japan

The following business relations exist between the members of the Supervisory Board and the Company:

- Dr. Wolfgang Witz is a partner of the law firm Allen & Overy, Frankfurt am Main. Allen & Overy provides advice with respect to stock and stock exchange law and corporate acquisitions.

- Dr. Rüdiger Moog is a partner of the law and audit firm Moog, Moog und Partner, Darmstadt and provides advice with respect to tax, contractual and wage law. His firm also carries out the personnel accounting for the Darmstadt location. The firm has assisted in the acquisition of companies.
Executive Board

- Y. Enis Ersü, Darmstadt (Chairman)
- Hans-Jürgen Christ, Ober-Ramstadt (Deputy Chairman)
- Werner Rothermel, Alsbach-Hähnlein
- Dr. Johannes Giet, Eggenstein
- Mr. Stephan Wienand left the Executive Board on Jan. 13, 2005

Payments to the members of Executive and Supervisory Board

The payments to the members of the Executive Board include a variable compensation amounting to up to 20% of the basic pay, in isolated cases. They are determined by the Supervisory Board on the basis of targets each year. In the fiscal year the remuneration of the Executive Board totaled € thousand 645. The total share option rights granted to the Executive Board as per Sept. 30, 2004 amount to 5,857 (previous year 8,395). In the fiscal year, no new option rights were granted. The cost of the utilized options is included in the remuneration of the Executive Board.

The payments to the members of the Supervisory Board for their activities totaled € thousand 53 in the period under review. No option rights have been granted to members of the Supervisory Board.

Details of shares

Held by members of the Executive Board and of the Supervisory Board.

<table>
<thead>
<tr>
<th>Executive Board</th>
<th>No. of shares as per Sept. 30, 2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>E. Ersü</td>
<td>1,002,794</td>
</tr>
<tr>
<td>H.-J. Christ</td>
<td>60</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Supervisory Board</th>
<th>No. of shares as per Sept. 30, 2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Prof. Dr. H. Tolle</td>
<td>900</td>
</tr>
<tr>
<td>G. Riske</td>
<td>103</td>
</tr>
</tbody>
</table>

Darmstadt, December 30, 2005

ISRA VISION SYSTEMS AG
The Board of Directors
Reproduction of the Auditors’ Report

We have audited the consolidated financial statements, comprising the consolidated balance sheet, the consolidated profit and loss statement, the consolidated cash flow statement and the consolidated statement of changes in equity, as well as the ‘notes’, prepared by ISRA VISION SYSTEMS AG, Darmstadt, for the business year from October 1, 2004 to September 30, 2005. The preparation and the content of the consolidated financial statements are the responsibility of the Company’s Executive Board. Our responsibility is to express an opinion whether the consolidated financial statements are in accordance with International Financial Reporting Standards (IFRS)/International Accounting Standards (IAS) based on our audit.

We conducted our audit of the consolidated financial statement in accordance with German auditing regulations and generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (IDW). These standards and regulations require that we plan and perform the audit in such a manner that inaccuracies and violations which have a material impact on the presentation of the status of the Group with respect to its assets and its financial and profit situation as given by the Group management report and the IFRS/IAS consolidated financial statements prepared under consideration of the principles of proper accounting can be detected with sufficient certainty. Knowledge of the business activities and the economic and legal environment of the Group and expectations concerning possible errors are taken into account in the determination of the audit procedures. The evidence supporting the valuations and disclosures in the consolidated financial statements and the management report is mostly examined on a test basis within the framework of the audit. The audit includes the assessment of the annual financial statements of the companies incorporated in the consolidated statement, of the composition of the companies included in the consolidated statement, of the accounting principles used and of significant estimates made by the Executive Board, as well as an evaluation of the overall presentation of the consolidated financial statements and the management report. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements of ISRA VISION SYSTEMS AG give a true and fair view of the assets, financial position, results of operations and cash flows of the Group for the business year under review in accordance with IFRS/IAS.

Our audit, which also extends to the Group management report prepared by the Executive Board for the business year from October 1, 2004 to September 30, 2005, has not led to any reservations.

In our opinion, on the whole the Group management report together with the consolidated financial statements provides a suitable understanding of the Group’s position and suitably presents the risks of its future development. In addition, we confirm that the consolidated financial statements and the Group management report for the business year from October 1, 2004 to September, 30 2005 satisfy the conditions required for the Company’s exemption from its obligation to prepare consolidated financial statements and a Group management report in accordance with German law.

Frankfurt am Main, January 17, 2006

PKF Pannell Kerr Forster GmbH
Wirtschaftsprüfungsgesellschaft

W. Hofmann R. Brinskelle
Auditor Auditor
Forward-looking statements

This Annual Report contains forward-looking statements which are based on the Executive Board’s assessment of future developments. The statements and projections represent assessments which have been made on the basis of information currently available. In case the underlying assumptions do not materialize, the actual results may differ from the results currently projected.