# Annual Report
# 2006

TEMENOS

# Corporate Profile

TEMENOS™ (TEMENOS) provides 24/7 functionality to the retail, wholesale, universal and private banking sectors, and partners with central banks on core system replacements. TEMENOS also has a seven-year history in working with world banks to create and deploy solutions for economic development in third world economies.

Key to TEMENOS' success is its pragmatic and innovative approach to delivering TEMENOS T24™ (T24), its modular core banking system. Most recently, the company has developed the TEMENOS T24™ Model Bank approach, which ensures a safe, quick and economical implementation. TEMENOS brings its considerable experience, and expertise to bear on every project with commitment and professionalism. In recognition of its superior technology, TEMENOS won the Financial-i 'Leaders in Innovation Awards' for T24 in December 2006.

TEMENOS' second flagship product, TEMENOS™COREBANKING (TCB) meets the requirements of large-scale, high volume, domestic retail banks (tier one and tier two banks usually) and multi-bank outsourcing centres. This system is being used by some of the most innovative banking organisations in the world.

Headquartered in Geneva, Switzerland, the company has 39 offices in 31 countries and generated revenues of US$ 216.3 million for the year ended 31 December 2006. In June 2001, TEMENOS became a public company listed on the SWX Swiss Exchange (TEMN).

**Trading details**

Listing : SWX Swiss Exchange
Symbol : TEMN
Swiss security number : 124 5391
ISIN : CH 00124 53913
Common Code : 13169144

**Key Figures (December 31)**

*All financial units in thousands of US dollars except employee numbers, earnings per share, operating margin and EBITDA margin.*

| | 2006 | 2005 |
|---|---|---|
| Employees (including consultants) | 1,726 | 1,373 |
| Revenues | 216,267 | 168,652 |
| Operating profit | 33,315 | 22,747 |
| Operating margin | 15.4% | 13.5% |
| EBITDA | 43,082 | 33,927 |
| EBITDA margin | 19.9% | 20.1% |
| Net profit attributable to the Group | 34,445 | 18,257 |
| Cash generated from operating activities | 26,244 | 3,665 |
| Total assets | 352,166 | 181,370 |
| Shareholders' equity | 135,812 | 100,630 |
| | | |
| Basic earnings per share | US$ 0.60 | US$ 0.33 |
| Diluted earnings per share | US$ 0.57 | US$ 0.32 |

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# Financial Highlights

*(in millions of US dollars except earnings per share)*

| | 2006 | 2005 | 2004 | 2003 | 2002 |
|---|---|---|---|---|---|
| Revenues | 216.3 | 168.7 | 153.6 | 146.2 | 113.3 |
| Operating costs | 183.0 | 145.9 | 141.8 | 135.5 | 157.7 |
| Other operating income | - | - | 1.0 | - | - |
| Operating profit (loss) | 33.3 | 22.8 | 12.8 | 10.7 | (44.4) |
| Profit (loss) before taxation | 38.6 | 20.2 | 15.1 | 12.7 | (47.1) |
| Net profit (loss) after tax | 34.4 | 17.9 | 12.1 | 10.9 | (49.5) |
| EBITDA | 43.1 | 33.9 | 28.8 | 25.2 | (31.6) |
| Diluted earnings (losses) per share (in US$) | 0.57 | 0.32 | 0.22 | 0.19 | (0.95) |
| Cash generated from operating activities | 26.2 | 3.7 | 15.9 | 16.4 | (4.8) |
| Current assets | 262.7 | 127.8 | 114.5 | 108.2 | 69.4 |
| Non-current assets | 89.4 | 53.6 | 49.6 | 43.6 | 53.0 |
| Total assets | 352.1 | 181.4 | 164.1 | 151.8 | 122.4 |
| Current liabilities (excluding deferred revenues) | 62.4 | 40.9 | 36.8 | 49.5 | 32.3 |
| Deferred revenues | 45.0 | 33.6 | 34.6 | 35.9 | 22.2 |
| Total current liabilities | 107.4 | 74.5 | 71.4 | 85.4 | 54.5 |
| Non-current liabilities | 108.6 | 5.8 | 8.5 | 0.2 | 15.2 |
| Total liabilities | 216.0 | 80.3 | 79.9 | 85.6 | 69.7 |
| Total equity | 136.1 | 101.1 | 84.2 | 66.2 | 52.7 |
| Total equity and liabilities | 352.1 | 181.4 | 164.1 | 151.8 | 122.4 |

# Chairman's Statement



This time last year I commented that in 2005 we had delivered what was probably then the best performance in TEMENOS' history. It is always a greater challenge to follow a good year than a poor one, so it gives me great pleasure to confirm that in 2006 we not only improved on our 2005 results, but did so by a substantial margin.

This is important on several counts.

Firstly, while one positive year can be dismissed as a 'blip', our latest results demonstrate that we are continuing along a sustainable growth path. Indeed, over the past four years our revenues have almost doubled, from US$113.3 million in 2002 to US$216.3 million today. In 2006 our growth actually accelerated. This upwards trend is the result of strong organic growth, alongside a small number of strategic acquisitions.

Secondly, following several sluggish years in the banking systems replacement market, we have seen increased spending on core systems across most market sectors, regions and tiers. Core system replacement is one of the top priorities for CIOs of large financial institutions. This renewed activity is being driven by the inadequacy of incumbent systems to support new banking business models and growth strategies.

Thirdly, our investment in products, people and infrastructure is coming to fruition and now sees us in a prime position to deliver the new core systems being sought in the market. This is evidenced by the record number of new clients whom we welcomed in 2006: 41 in total, including a further two tier 1 banks. The latter included Sumitomo Mitsui Banking Corporation (SMBC), one of the largest banks in Japan. T24 is being installed in all 13 of SMBC's Asia Pacific branches, across seven countries.

With T24, COREBANKING (TCB) and T-Risk, we continue our commitment in striving to create upgradeable products which are obsolescence-proofed. We continue to invest in product development - more than 20% of our income each year – the highest investment as a proportion of revenues amongst banking system suppliers today. And our commitment to innovation was formally recognised in 2006, when, in November, we were awarded the Financial-i 'Leaders in Innovation Award' for T24. These awards recognise the banks and technology vendors which are shaping the delivery of business solutions in wholesale transaction banking.

In 2006 we began the development of ARC (Acquire, Retain and Cross-sell) which, as its name implies, will provide our clients with a market-leading customer service capability across multiple delivery channels. We also announced the TEMENOS Data Warehouse which will sit alongside T24 and help our customers with risk management and CRM. This project is progressing well.

But software is only part of the solution. In 2006, based on feedback from our customers, we also introduced three new services initiatives with the aim of further increasing the business value which customers gain from using our products. In our first initiative, we focused on the point of implementation, where the introduction of the TEMENOS Model Bank methodology has helped new clients to cut implementation times by at least half, and to significantly reduce implementation costs. One of our first Model Bank customers was Bank of East Asia which implemented T24 to replace Misys Equation in its London and Birmingham branches. The project was accomplished within ten months.

Our second services initiative was  the introduction of the TEMENOS Application Management Service (TAMS), whereby we centralise the development and ongoing maintenance of non-core, client developments to our products, leaving our clients to focus on what they are good at - the business of banking.

Our third services initiative was to build on the huge amount of expertise and experience within TEMENOS and to supplement it with additional people recruited from the banking industry. The ultimate aim is to be able to offer focused management consultancy services from the outset of the implementation.

I cannot reiterate too often the fact that our people are one of our strongest assets - like me, they believe passionately in what we are trying to achieve.

Our other major asset is our client base - now totalling some 550 clients across all continents. Our clients are under pressure to meet the increasing expectations of their customers. We must ensure that our solutions continue to add value to their businesses. We must be just as customer-centric as our clients. We must also recognise that variations exist across banking sectors and regions. So, 2006 also saw us reorganise our operations around vertical sectors to allow us to focus in greater detail on the requirements of each. And, while we are a global operation, we don't believe in losing contact with our clients; we now have a total of 39 local offices, including four opened in 2006 (Riyadh in Saudi Arabia, Hanoi in Vietnam, Almaty in Kazakhstan and Cape Town in South Africa).

Our industry is consolidating and we expect this trend to continue. Only those companies with critical mass will survive - and TEMENOS is leading the way. We have enjoyed exceptional growth over the last few years - largely strong, organic growth. But where we can add further value for shareholders and clients, we continue to pursue targeted acquisitions with the proviso that they strengthen our core business, rather than take us into new areas.

Despite the momentous changes taking place in the market and within our company, we will of course take care to maintain a balance between investment for growth and profitability, so continuing to deliver value to shareholders. Acquisitions require capital and in March 2006 we launched a convertible bond offering with a value of CHF 132m.

As for the future, we are feeling very bullish. Our value proposition centres on being able to give banks the ability to manage their client relationships effectively, launch new products rapidly and do this from a modern technology platform. This is 100% aligned with market needs. A recent Forrester report, The Forrester Wave™: Core Banking Suites, Q1 2007 placed TEMENOS in the 'Leaders' category. The report also found that T24 received the highest score in terms of core banking functionality and installed base. My conviction that we can continue to be a leader in this market in the years to come is stronger than ever.

But TEMENOS' success derives from the creativity, hard work and dedication of many people. As ever, I would like to thank TEMENOS' management team and staff for their dedication in 2006; our partners, whose many products and services complement our solutions; and our clients for their faith in selecting us and their commitment to our ongoing partnership.

I look forward to reporting continued positive progress for 2007.

**George Koukis** Chairman

TEMENOS Children’s Foundation

«To create a TEMENOS community which spans continents and cultures and share a common vision»

Andreas Andreades, CEO



TEMENOS Children’s Foundation – Calendar 2006-2007


Boat TEMENOS II with Dominique Wavre, Swiss skipper, sponsored by TEMENOS.

# Business Report

**Our financial results**

2006 was another outstanding year for TEMENOS. Our revenues reached USD 216.3 million, up 28% compared to 2005. Over the past four years revenues have grown from USD 113.3 million in 2002 to USD 216.3 million in 2006, a compound annual growth rate which exceeds 18%. This represents acceleration from our strong performance in 2005.

The primary driver for improving revenues is the very strong growth in our licence revenues. In 2006, these represented USD 97.9 million, up 52% compared to 2005. The increase in licence revenues in 2006 was achieved by signing deals with a record number of new customers - 41 in total, confirming our leadership position in the industry.

Maintenance revenues, a measure of our long term success and profitability, have continued to increase significantly at a double digit rate: an increase of 18% over 2005. Our Professional Services revenue also continues to grow at 10% compared to 2005.

Cost leverage continues to be very good, with costs growing at 25% compared to 2005, allowing us to deliver improvements in margin whilst also continuing to invest for the strong growth we see continuing into 2007.

Management is committed to the organic growth of the business and remains focused on improving profitability and creating shareholder value. As we further develop our target markets, our maintenance revenues will continue to grow, improving both net margins and net profitability, whilst driving enhanced shareholder value. In addition, we will continue to consider selected acquisitions that will leverage our core assets and will be accretive to shareholders.

**Client update**

In the course of 2006 we welcomed 41 new customers to TEMENOS, expanding our global customer base to 550 banks and entering a number of new geographical markets. Major contracts were signed with Fortis and Sumitomo Mitsui Banking Corporation who selected TEMENOS T24™ (T24) to support their expansion plans across a number of countries. We also established relationships with six banks in entirely new countries for TEMENOS, so proving our ability to provide a truly global solution to our customers, from an appropriate local platform. So, we are providing T24 on a Canadian platform for North Shore Credit Union in Vancouver, T24 with Islamic Banking for Al Salam Bank in Bahrain, and Bank Muscat in Oman; and we are extending our Asia Pacific presence with the provision of a system for Phongsavanh Bank in Laos.

As well as expanding the global client base in 2006, TEMENOS continued to focus on the needs of existing and prospective customers. A number of initiatives were launched, designed to deliver an increase in the business value gained from the use of our software and services.

The first of these initiatives, the TEMENOS Model Bank Implementation Methodology, has been remarkably successful with 20 banks adopting this approach since its launch in February 2006. Customers adopting the Model Bank approach have been able to achieve implementations in less than half the usual time. Model Bank brings far greater control over deliverables and significantly lower implementation costs. This new methodology also incorporates the industry knowledge which we have gained from over 500 implementations around the world, as we have configured market best practice processes into our base line deliverable.

During 2006 we also launched the TEMENOS Application Management Service which has allowed a number of our customers to take advantage of our Chennai based offshore development facility for the development and maintenance of non-core software and the daily management of their applications. This has removed an unnecessary and expensive overhead and allowed our customers to concentrate their scarce resources on adding value to their core business.

**The Banking Software market**

During 2006 banks continued to invest significantly in core banking software replacement. This trend is being driven by a number of factors including:

- The increased risk of remaining on legacy in-house applications as the technology in these systems becomes more and more difficult to support
- A move towards growth rather than cost containment, driving a need for increasingly flexible and scaleable systems
- Increased competition in the financial services markets, exacerbated by new entrants from outside of the industry or from other regions

- The high cost of implementing fast changing compliance and regulatory rules using inflexible, legacy applications.

We also saw a significant movement from tier 1 banks embarking on major re-architecting projects, designed to resolve the complex IT environments that have resulted from growth and acquisition over recent years.

This is combined with an increasing acceptance that modern, commercial software packages such as those offered by TEMENOS, are much better placed to support banks' requirements for robustness, scalability and flexibility. We expect that these trends will keep the issue of core system replacement at the top of banks' priorities.

**Our products**

We have invested in excess of USD 33.8 million in research and development in the course of 2006, following our commitment to significant product investment and innovation. We firmly believe that our record of high investment is key to our ability to deliver product superiority, at a functional level as well as at a technology and architecture level. 2006 saw investment in three areas of particular importance:

ARC (Acquire, Retain, Cross-Sell) sees a major investment in the front office capabilities of our T24 platform. This area is increasingly important as our clients concentrate on customer service and growth through effective marketing and selling. Our unique vision of a fully integrated front to back office solution is seeing wide-spread acceptance in a market that has experienced high costs and inflexibility resulting from disparate, separate systems.

Data Warehouse is a new development that has resulted directly from consultations with our clients. They told us that they needed us to deliver higher level tools to access the rich wealth of information stored in the T24 database.

The release of T24 on Microsoft's SQL Server database completes our support for Microsoft's platform. This ensures that clients who wish to take advantage of the cost, performance and usability benefits of the Microsoft platform and products when running T24, are now able to do so.

**Organisation**

Following strong growth over the past few years, TEMENOS continues to strengthen its management team to ensure it has the appropriate people in place to service the needs of an increasing customer base and to oversee the implementation of business growth initiatives.

In early 2006 we created a number of new senior corporate roles. Mark Cullinane was appointed chief operating officer; Mark Gunning became group strategy director; and Greg Green was appointed managing director of TCB. Peter McKenna joined TEMENOS in September 2006 as marketing director. In October 2006 Philip Barnett was appointed regional director for Asia Pacific, having already made an extremely valuable contribution as sales director for that region.

The creation of a third region in EMEA late in 2006 reflected TEMENOS' commitment to investing in its operations across this important and diverse market. The new region was created by splitting the current EMEA region into two independent regions: Southern Europe Middle East and Africa (SEMEA) and Central and Eastern Europe (CEE), each with responsibility for their own sales, services and support organisations. Jean Michel Hilsenkopf retained responsibility for the Middle East, Africa, France, Spain and Portugal (SEMEA). Armin Holst joined TEMENOS in November 2006 to take up the new role of regional director for Central and Eastern Europe (CEE).

**Our partners**

We continue to develop our critical and strategic relationships with the leading industry technology providers including HP, IBM, Microsoft, Oracle and Sun Microsystems.

We also work with a number of partners who provide complementary products, as well as with service providers who assist in the delivery of first rate professional services to our clients. These partners include EFS Autoform, offering a full document management solution; IMTF, with an AML and fraud prevention solution; and FE Mobile, a partner working in mobile banking. Services providers include Inlaks in Nigeria and NDC in Pakistan.

A. Andreades

Below from left to right:
David Arnott, Chief Financial Officer – Max Chuard, Corporate Finance & Investor Relations Director – Mark Cullinane, Chief Operating Officer – Andreas Andreades, Chief Executive Officer

# Product Summary



2006 saw excellent new business growth for TEMENOS and it marked another year of important progress for TEMENOS T24™ (T24) and TEMENOS™ COREBANKING (TCB).

T24 was selected by 41 new customers. It also received strong market endorsement, being selected by market-leading institutions in each of its main market segments. For example, in retail banking, T24 was selected as the core processing platform for Fortis' groundbreaking single European retail platform strategy; while in wholesale banking it was chosen by Sumitomo Mitsui Banking Corporation (SMBC) to support 13 of the bank's Asia Pacific branches, across seven countries.

In February 2006, we announced a significant investment in the development of front office capabilities, based on T24 technology. The resulting product, ARC (Acquire, Retain and Cross-Sell) will enable banks to provide superior customer service, delivered through multiple channels and will provide excellent customer relationship management capabilities. ARC is initially being offered to new and existing T24 customers, although in the future it will be available for deployment independently of T24.

We also announced a new Data Warehouse capability at our Client Forum. This has generated considerable interest in our client base in anticipation of its availability for early adopters during 2007.

2006 also saw us introduce a new implementation approach for T24 which would be tailored for each of the vertical markets addressed: retail, universal, wholesale, private banking and wealth management. The first to be launched was T24 Model Bank for Universal and Retail Banks, a pre-configured T24 system that incorporates extensive best market practice from those sectors and significantly reduces the time-to-value for client implementations. This initiative has proved to be very successful. The first three projects using the Model Bank approach achieved live operation with average implementation times which ranged from seven to eleven months. The Bank of East Asia in London was the first to implement a special version of T24 Model Bank, which had been customised to facilitate migration from the Misys Equation package. The Model Bank approach has proved highly attractive to our clients.

In 2006, 20 clients opted for the Model Bank in order to reduce their implementation time-to-market and significantly improve the ROI of their projects.

In the last quarter of 2006 our second model was launched – this time for private banks and wealth management operations. A first implementation, for a leading organisation in this area, began towards the end of the year.

In total, 33 clients achieved live operations in 2006, demonstrating our ability to fulfil our commitment to our customers. Satisfied live clients will always be the major driver of new business growth in our industry.

We continue to add value for existing clients too, as evidenced by our ongoing new release strategy, whereby every enhancement carried out is incorporated in the core system and made available to all clients under the terms of our maintenance agreement. So, Release 07 of T24 (developed during 2006 and available for general release in early 2007) contains over 100 new enhancements including a new retail Mutual Funds module and a new Off-Line Branch Processing capability. These are significant enhancements to our core product.

Our new risk management offering, T-Risk, launched at the beginning of 2006 offers dynamic management of credit risk based firmly on Basel II foundations. This has proved attractive to our market with five new clients. Since then, we have begun extending the scope of T-Risk into market risk and enterprise risk management. This latest version of the system has been taken by two further clients with implementations underway at both as the year ended.

TEMENOS eMERGE™ (eMERGE), is our T24 offering for smaller tier 4 and 5 retail banks and other financial institutions in emerging markets. eMERGE addresses mass market retail, microfinance and community banking functionality. eMERGE had another strong year, being selected by eleven new installations on Release 5 of this system, which was made available in July 2006. The latest eMERGE release includes a major upgrade of the configuration layer and takes full advantage of significant upgrades based upon later T24 functionality.

Our TCB business continues to grow and we were pleased to sign a large corebanking customer, KASIKORNBANK Plc in Thailand, in 2006 after an extensive evaluation by the bank. The TCB business unit has expanded its operations in Asia to reflect the growing number of implementations with regional services expanding in Thailand to meet this need. The TCB business unit has also expanded its business operations in North America in the course of 2006 to meet expected demand for TCB in 2007 and beyond in this market. TCB continues to be functionally enriched, both through internal investments and customer-sponsored developments. Major new developments are being prepared that will see the platform move towards a componentised solution over the next two to three years.

In terms of TCB's existing technology initiatives, its JAVA version has been prepared for first general availability release in 2007, providing technology alternatives to the large, domestic retail space. Together with our technology partners we also proved that TCB can be delivered as a COBOL UNIX version of the software in 2006, opening up an alternative delivery option for the solution on UNIX.

# Corporate Governance

## Introduction

This report has been prepared in compliance with the Directive on Information Relating to Corporate Governance (hereafter"DCG") and its Commentary issued by the SWX Swiss Exchange, applicable for fiscal year 2006.

In the present Annual Report, the corporate governance information has been summarised in a separate section, whereas references to other parts of the Annual Report have been included in certain instances in an effort to avoid duplication.

In order to enhance readability, the present corporate governance section follows the suggested structure as described in the DCG's annex.

If there is a specific disclosure listed in the DCG that is not addressed in the following statements, the given item does not apply to TEMENOS Group AG (hereafter "TEMENOS", "the Group" or "the Company") or is considered immaterial.

Unless otherwise indicated, the information provided in this report reflects the situation as at 31 December 2006.

## Group structure and shareholders

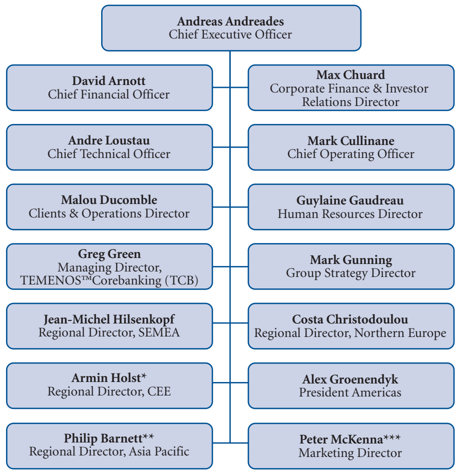
### 1.1 Group structure

The ultimate holding company, TEMENOS Group AG, is registered in Geneva and its shares have been listed on the SWX Swiss Exchange since 26 June 2001. TEMENOS is headquartered in Geneva.

| | |
|---|---|
| Swiss Security Number: | 1245391 |
| ISIN number: | CH0012453913 |
| Common Code: | 013169144 |
| Symbol: | TEMN |
| Reuters: | TEMN.S |
| Bloomberg: | TEMN SW |

### 1.1.1 Operational Group structure

The TEMENOS Group is organised and managed by the CEO who is the head of the Executive Board as shown on the organisation chart below:




* since November 2006
** since October 2006
*** since September 2006

**1.1.2** TEMENOS Group AG is the sole listed company and owns all companies belonging to the TEMENOS Group.

**1.1.3** Under the direction of the CEO, the Executive Board is responsible for managing, coordinating and executing the Company's business operations.

The Executive Board includes directors of the Group's software products, its main regional sales and services organisations and the principal corporate functions.

In particular and without limitation, the Executive Board has the following responsibilities:
- Implementation of the strategy and policies agreed upon by the Board of Directors;
- Management of the Company on a day to day basis;
- Managing and improving the performance of the Company;
- Ensuring efficient operational performance and attainment of the business targets.

The Group is managed using a matrix of global business functions supported by regional sales and service operations, incorporating activities of product development, product management, services management, marketing, key customer relationship management and product support functions.

From an operation perspective, the Group's product sales and services operations are divided into five main geographic regions:

- Southern Europe, Middle East and Africa (SEMEA) – including Middle East, Africa, Switzerland (French part), France, Spain and Portugal.
- Central and Eastern Europe (CEE) – including Belgium, Netherlands, Switzerland (German part), Luxembourg, Poland, Germany, Austria.
- Northern Europe (NEU) – including UK and Ireland, the Nordic countries, Russia, CIS and the Baltic States.
- Asia Pacific (APAC) region.
- Americas – including North and South Americas region.

The Group Development and Product Support centres are based in India (Chennai), Spain (Madrid) and United Kingdom (Hemel Hempstead). TEMENOS Development Centres and Help Desk departments operate from these locations.

With the exception of FOMENTO EMPRESARIAL DE SERVICIOS INFORMATICOS SA de CV (a 51% owned Mexican joint-venture) all the subsidiaries are, either directly or indirectly, wholly owned by TEMENOS Group AG, as the ultimate parent company of the Group.

Please refer to note 4 of the consolidated financial statements for the list of the principal group companies belonging to the Group.

Please refer to the Information for Investors section for statistics on TEMENOS shares.

As of 31 December 2006, the market capitalisation amounts to CHF 1,194,425,344.00.

### 1.2 Significant shareholders

To the best of our knowledge, please find below the list of shareholders who hold more than 5 percent of the voting rights of all issued shares, as at 31 December 2006.

| | |
|---|---|
| George Koukis: | 16,86% |
| Schroders plc* | 8,08% |
| Fidelity International Limited | 5,21% |

*deposited shares (art. 689d CO)

Please also refer to note 3 of the unconsolidated financial statements of TEMENOS Group AG.

In 2006, the following publications were made in the Swiss Commercial Gazette (SHAB):

**Publication of 13 March 2006**

- Mr. George Koukis (1256 Troinex-Switzerland) holds 17,48% (9,752,064 registered shares) of the voting rights in TEMENOS Group AG.
- Mr. Angelos Plakopitas (Athens-Greece) through GLOBAL FINANCE SA (10673 Athens-Greece), the fund manager of GLOBAL CAPITAL INVESTORS LP (St Peter Port GY1 4NN- Guernsey) and GLOBAL CAPITAL INVESTORS (II) LP (St Peter Port GY1 4NN- Guernsey) holds less than 5% of the voting rights in TEMENOS Group AG.

**Publication of 18 August 2006**

- Fidelity International Limited, principal address located at Pembroke Hall, 42 Crow Lane, Hamilton, Bermuda, and its direct and indirect subsidiaries hold 5,4% of the voting rights in TEMENOS Group AG, by holding 3,013,889 registered shares.

**1.3** There are no cross-shareholdings to report.

## Capital structure

### 2.1 Capital

On 31 December 2006 the ordinary capital amounted to CHF 289,207,105, consisting of 57,841,421 registered shares, each with a par value of CHF 5. All the shares are fully paid-up. Each recorded share entitles its holder to one vote.

TEMENOS has an authorised capital totalling CHF 132,551,215 and a conditional capital totalling CHF 51,296,460 for shares that may be issued on the exercising of share options granted to employees of the Group. Additional conditional capital totalling CHF 69,653,400 exists for shares that may be issued in conjunction with financial instruments.

### 2.2 Authorised and conditional capital

**Authorised capital**

Pursuant to the Articles of Association (article 3ter), the Board of Directors is authorised to increase the share capital to a maximum aggregate amount of CHF 132,551,215 through the issuance of a maximum of 26,510,243 fully paid-in registered shares with a par value of CHF 5 per share. An increase in partial amounts is permitted. This power expires on 23 May 2008.

The Board of Directors shall determine the date of issue of such new shares, the issue price, type of payment, conditions of exercising pre-emptive rights, and the beginning of the dividend entitlement. The Board of Directors may issue new shares by the means of a firm underwriting by a banking institution or syndicate with subsequent offer of those shares.
The Board of Directors may allow the expiry of pre-emptive rights which have not been exercised or it may place these rights as well as shares, the pre-emptive rights for which have not been exercised, at market conditions.
The Board of Directors is authorised to restrict or withdraw the pre-emptive and subscription rights of existing shareholders and allocate them to third parties if (i) the shares are to be used for the take-over of another company or enterprise, of parts of an enterprise or of participations or for the financing of such transactions; or if (ii) the shares are to be used for the purpose of expanding the scope of shareholders in connection with the quotation of shares on national and foreign stock exchanges.

**Conditional capital for employee participation**

Pursuant to the Articles of Association (article 3quater (1)), the company's share capital shall be increased by a maximum aggregate amount of CHF 51,296,460, through the issuance of a maximum of 10,259,292 registered shares, which shall be fully paid-in, with a par value of CHF 5 each through exercise of the rights that TEMENOS Holdings N.V., a subsidiary of the Company (the" Subsidiary") or the Company may grant to officers, directors and employees at all levels of the Company and group companies. The pre-emptive rights as well as the right for advance subscription of existing shareholders are precluded.
The issue of shares or respective option rights through the Subsidiary or through the Company, to officers, directors and employees of the Company and group companies, is subject to one or more regulations to be issued by the Board of Directors on the basis of the following general rules: (i) new shares may only be issued to the Subsidiary or to the Company for purposes of distribution to directors, officers or employees of the Company and group companies; (ii) new shares to be issued through the Subsidiary or through the Company, to employees of the Company or group companies shall be issued against payment of the par value of CHF 5 per each share in cash.

**Conditional capital for financial instruments**

Pursuant to the Articles of Association (article 3 quarter (2)), the share capital may be increased by an amount not exceeding CHF 69,653,400 by issuing up to 13,930,680 registered shares -to be fully paid-in with a par value of CHF 5 each - through the exercise of conversion and/or option rights which are granted in connection with bonds or similar debt instruments of the Company or one of its group companies. Out of these 13,930,680 shares, 9,000,000 are reserved for the Convertible Bond.
The conditions of the option rights, including the exercise period and the exercise price, are to be determined by the Board of Directors whereby the exercise price may be fixed at a price lower than the market or intrinsic value. The pre-emptive rights, as well as the right for advance subscription of existing shareholders, are precluded.

## 2.3 Changes in capital

TEMENOS Group AG was incorporated on 7 June 2001 and is the ultimate holding company of the Group.

**Statutory accounts**

| in thousands of CHF | **31.12.2006** | **31.12.2005** | **31.12.2004** |
|---|---|---|---|
| Share capital | 289,207 | 276,751 | 274,762 |
| Share premium and reserve for treasury shares | 181,240 | 175,534 | 175,034 |
| Profit (loss) carried forward | (988) | (168) | (19) |
| Total equity | 469,459 | 452,117 | 449,777 |

## 2.4 Shares

All equity securities of TEMENOS are in the form of registered shares, each with a par value of CHF 5. Each share confers the right to one vote at the Annual General Meeting of Shareholders and all shares are fully entitled to receive dividends. The Company did not pay any dividend in 2006. TEMENOS does not currently anticipate paying any dividends, as it intends to retain future earnings to finance the development and growth of its business.

## 2.5 Profit sharing certificates

As above-mentioned, the Company does not currently issue such equity securities.

## 2.6 Limitations on transferability and nominee registrations

There are no restrictions on the transfer of shares.
Only shareholders entered in the share register as shareholders or as usufructuaries may exercise the voting rights linked to the shares or the other rights connected with these voting rights. The Company shall recognise only one representative for each share. Nominee registrations are permitted.

### 2.7 Convertible bonds and warrants/options

Regarding stock options granted to employees, please refer to note 18 of the consolidated financial statements and to section 5.6 below.
Regarding the Convertible Bond issued on March 2006, please refer to note 13 of the consolidated financial statements.

## Board of Directors

The Board of Directors is elected by the shareholders and holds the ultimate decision-making authority of the Company for all matters except those reserved by law to the shareholders. The Board of Directors shall manage the business of the Company insofar as it has not been delegated to the CEO, who chairs the Executive Board of the Company.
The Board of Directors exercises inalienable and non-transferable functions as provided by law, by the Company's Articles of Association and by its Charter.

### 3.1 Members of the Board of Directors

As at 31 December 2006 the Board of Directors comprises six members, four of whom are non-executive. The non-executive members of the Board have no material business dealings with TEMENOS.

**a) Status as at 31 December 2006**

**George Koukis** (60) - *Chairman, executive director*
Mr. George Koukis has been active in the software industry for more than 20 years, having begun at Qantas where he was heavily involved with the computerisation of the company's management accounting department. He then spent six years with Management Science America (MSA) in Australia where he held various management positions, including that of the managing director. Mr. Koukis holds a degree in commerce from the University of Technology in Sydney, Australia and is a registered CPA.
As Chairman and founder of TEMENOS, Mr. Koukis participates actively in the strategy of the Group. Mr. Koukis is a Greek and Australian national and continues to hold positions on the Board of Directors of a small number of operating companies within the Group.
Mr. Koukis remains the largest shareholder in TEMENOS Group AG as mentioned in section 1.2. Mr. Koukis was elected in 2001, re-elected in 2002 and in 2005 for a three-year term of office.

**Paul Selway-Swift** (62) - *Vice-Chairman, non-executive and independent director*
Mr. Paul Selway-Swift has many years of experience in the financial services industry with The HSBC Group where he held senior management positions in both Hong Kong and London. He is currently Chairman of Novae Group plc (formerly SVB Holdings plc) and a non-executive director of Alba PLC; both of which are quoted on The London Stock Exchange. He is Chairman of The Atlantis China Fund and a director of Li and Fung Ltd, which is quoted on The Hong Kong Stock Exchange and of China Export Finance Ltd, incorporated in the United Kingdom.
Mr. Selway-Swift was educated in England and subsequently attended Massachusetts Institute of Technology Program for Senior Executives.
Mr. Selway-Swift is a British national. He is interested in a small number of shares in TEMENOS but does not hold TEMENOS share options; he has never held a management position in the TEMENOS Group nor does he have any other business connections with the Group.
Mr. Selway-Swift chairs the Compensation Committee and is a member of the Audit and Nomination Committees. He was elected in 2001, re-elected in 2003 and in 2006 for a three-year term of office.
Mr. Selway-Swift was appointed Vice-Chairman of the Board of Directors in October 2006 for a period of one year.

**Andreas Andreades** (41) - *Chief Executive Officer, executive director*
Mr. Andreas Andreades joined TEMENOS in 1999, initially in the position of Chief Financial Officer, before assuming the responsibilities of the Deputy Chief Executive Officer in 2001 and then the Chief Executive's role in July 2003. Mr. Andreades started his career with KPMG in London in 1988. After spending five years in the accounting profession, he joined PepsiCo, where he held a number of strategic, sales and general management positions. Mr. Andreades holds an engineering degree from the University of Cambridge and is a U.K. chartered accountant.
Mr. Andreades is a Cypriot national and holds positions on the Board of Directors of a number of operating companies within the Group.
Mr. Andreades was elected in 2001, re-elected in 2004 and is due for re-election at the forthcoming Annual General meeting of Shareholders.
Mr. Andreades is a member of the Nomination Committee.

**Mark Austen** (57) - *non-executive and independent director*
Mr. Mark Austen, a qualified accountant has had considerable experience at an executive level in international financial markets and financial services consulting.

Members of the Board of Directors
Standing from left to right: Lewis Polk Rutherfurd, Mark Austen, Chris Pavlou, Paul Selway-Swift
Seated from left to right: Andreas Andreades, George Koukis

Up to early 2005, he served as an executive in IBM's Business Consulting Services, following a 20-year career with PricewaterhouseCoopers (PwC). There, he was Managing Partner of the Global Financial Services consulting practice, and from 2000 to 2002 was an elected member of PwC's Global Board. He was also a member of the transaction group that oversaw the sale of the consulting business to IBM. Mr. Mark Austen is also a non-executive director of Standard Bank PLC, Liverpool Victoria Friendly Society Ltd, IFB International AG and The Philharmonia Trust Ltd.
Mr. Austen is a British national. Mr. Austen was elected in 2006 for a three-year term of office and chairs the Audit Committee.

**Chris Pavlou** (61) - *non-executive and independent director*
Mr. Chris Pavlou has formerly served as the Treasurer of Barclays Bank in London and New York, of the Hong Kong & Shanghai Banking Corporation in Hong Kong and of HSBC Midland in Tokyo. He was the Asia Pacific Regional Delegate of the International Forex Association. He retired from HSBC in 1998. In 1999, Mr. Pavlou joined Laiki Bank Cyprus as a consultant and served on the Board from 2001 to 2004.
Mr. Pavlou is currently CEO of TF1, a Cyprus based financial company.
Mr. Pavlou is a British national and does not hold TEMENOS share options.
Mr. Pavlou has never held a management position in the Group and has no business connections with the Group.
Mr. Pavlou was elected in 2001, re-elected in 2002 and 2005 for a three-year term of office.
Mr. Pavlou chairs the Nomination Committee and is a member of the Audit and Compensation Committees.

**Lewis Polk Rutherfurd** (62) - *non-executive and independent director*
Mr. Lewis Polk Rutherfurd holds a bachelor's degree in East Asia Studies from Princeton University and an MBA with distinction from Harvard Business School. Mr. Rutherfurd is co-founder and managing director of Inter-Asia Management, Inter-Asia Venture Management II Partnership, Inter-Asia Capital III (the Founder investor in TEMENOS) and of Inter-Asia Capital IV. He is a former Governor and Vice President of the American Chamber of Commerce in Hong Kong. He is a co-founder and past chairman of the HK Venture Capital Association.
Mr. Rutherfurd is an American national and does not hold TEMENOS share options.
Mr. Rutherfurd has never had a managing position in the TEMENOS Group and has no business connections with the Group.
Mr. Rutherfurd was elected in 2001, re-elected in 2003 and in 2006 for a three-year term of office.
Mr. Rutherfurd is a member of the Audit Committee (past Chairman of the Committee 2001-2007) and of the Nomination Committee.

### 3.2 Other activities and vested interests

Please refer to the information provided in section 3.1.

### 3.3 Cross-involvement

There are no other cross involvements among the members of the Board of Directors and boards of other listed companies.

### 3.4 Elections and term of office

#### 3.4.1 Principles of the election procedure and term limits

The members of the Board of Directors are elected by the General Meeting of Shareholders for a term of office of three years, whereby one year shall be understood to be the period from one ordinary General Meeting of Shareholders to the next one. Upon the expiration of their terms of office the members may be re-elected immediately and without limitations. Moreover, the Board of Directors shall organise the election of its members in such a way as to ensure that at each ordinary General Meeting of Shareholders approximately one-third of the members shall complete their term of office. Members newly appointed during a term of office shall complete the term of office of their predecessor. At the Annual General Meeting of Shareholders, the Board members are individually (re)-elected.

#### 3.4.2 First election and remaining term of office of each director

Please refer to the information provided in section 3.1.

### 3.5 Internal organisational structure

#### 3.5.1 Allocation of tasks within the Board of Directors

The Board of Directors, together with its Audit, Compensation and Nomination Committees, exercises inalienable and non-transferable functions as provided by law, by the Company's Articles of Association and by its Charter. The Board of Directors of TEMENOS decides in particular on significant acquisition, disposal, strategic alliances, share repurchase program and change in the Group's structure and organisation, though is not limited to this.
Once a year, the Board of Directors reviews its conformity to corporate governance rules and evaluates its own performance. Moreover, the non-executive members of the

Board of Directors assess the performance of each of the executive director and vice versa.

The Board meets as often as business matters require, but at least four times a year.

Based on Article 17 of the Articles of Association of TEMENOS Group AG, and on Article 3.5 of the Organisation By-Laws of the Company, the Board of Directors has delegated the day-to-day operational management of the Company to the Chief Executive Officer, except where the law, the Articles of Association or the Organisation By-laws provide differently.

Please refer to section 3.1 for complementary information.

### 3.5.2 Composition, tasks and areas of responsibility for each Committee

The Audit, Compensation and Nomination Committees are governed by terms of reference defining their duties and compositions. As mentioned in section 3.1, these Committees comprise mainly non-executive and independent directors. These committees report regularly to the Board of Directors.

**Audit Committee**

The Audit Committee is required to meet at least twice a year to consider the Group's public reports, to liaise with the external and internal auditors, and to review the Group's internal controls, compliance with corporate governance rules and any other matter that may be brought to its attention by the internal and/or external auditors.

The external and internal auditors are systematically invited to the Audit Committee meetings

**Compensation Committee**

The Group reviews on an ongoing basis, the compensation of its employees worldwide, by reference to the prevailing market norms, at each of the locations in which it operates.

At least twice a year, the Compensation Committee reviews, approves and makes recommendations on compensation practices and policies designed to develop a competitive, equitable and performance based package allowing TEMENOS to attract and retain top talent within the Group. The Compensation Committee also reviews, approves and makes recommendations on compensation packages concerning the executive members of the Board of Directors and members of the Executive Board and seeks to confirm that such compensation is in line with market norms.

**Nomination Committee**

A Nomination Committee of three members has been set up by the Board of Directors. The main duties of this Committee are (i) to annually review the structure, size and composition required of the Board of Directors and make recommendations to the Board of Directors with regard to any changes, (ii) to establish qualification criteria for Board of Directors' membership and (iii) to give full consideration to succession planning for both members of the Board of Directors and members of the Executive Board.

### 3.5.3 Work methods of the Board of Directors and its Committees

During 2006 the following numbers of meetings were held:

| | |
|---|---|
| Board of Directors | 6 |
| Audit Committee | 6 |
| Compensation Committee | 3 |
| Nomination Committee | 3 |

The attendance at the meetings of the Board of Directors was 100%.
All directors may take independent professional advice, at the Company's expense, if they deem such a course of action necessary or appropriate for discharging their duties adequately. An external legal counsel was present at each of the Board of Directors meetings.
At the meetings of the Board of Directors and of its Committees, those members of the Executive Board who have the relevant information and expertise required for the respective body to perform its duties are normally present. Such persons do not take part in any resolutions.
Furthermore, and during each Board of Directors meeting, a business report is systematically presented by the Chief Executive Officer. Together with the Financial Report presented by the Chief Financial Officer, this information enables the Board members to assess the course of the Company's business activities on a current basis.

### 3.6 Definition of areas of responsibility

The Board of Directors has delegated the entire operational management and conduct of business operations to the Chief Executive Officer, who chairs the Executive Board. With the active participation and guidance of the Company's Chairman, the Executive Board is responsible for managing, coordinating and executing the Company's business operations. The members of the Executive Board are appointed by the CEO.
Moreover, the Executive Board delegates some of its responsibilities to the Operating, T24 and TCB Product, Development and Technology & Research Boards.

### 3.7 Information and control instruments

The Board of Directors is responsible for the Group's system of internal control, which covers, among others, objectives to ensure effective and efficient operation, accurate financial reporting, compliance with laws and regulations and safeguarding of assets.

The Head of Internal Audit reports directly to the Audit Committee and administratively to the Chief Executive Officer. Internal Audit operates according to The International Standards for the Professional Practice of Internal Auditing issued by The Institute of Internal Auditors.

Financial results are monitored by the Board of Directors on a quarterly basis. The executive directors monitor financial results on the basis of a formal monthly financial reporting system and on an ad hoc basis, whenever circumstances demand.

Towards the end of each financial year, detailed budgets for each area of business are prepared for the following year and then reviewed and approved by the Board of Directors. Responsibilities for financial performance against plans and for capital expenditure are delegated, with limits, to line management. A significant part of the Group's financial and management information is processed by, and stored on, computer systems. Accordingly, the Group has established controls and procedures over the security of data held on computer systems. The Board ensures that measures continue to be taken to reinforce internal controls and to deal with necessary improvements that come to the management's and Board's attention. This is a goal which is pursued on an on-going basis while ensuring that equilibrium is maintained between the minimisation of risk and of the costs associated with controls.

## Executive Board

### 4.1 Members of the Executive Board

**Andreas Andreades** - *Chief Executive Officer*
Please refer to the information provided in section 3.1.

**David Arnott** (37) - *Chief Financial Officer*
Mr. Arnott has served as the Chief Financial Officer of TEMENOS since April 2001. Prior to joining the Group, he had worked as Chief Financial Officer of Société Européenne de Communication in Luxembourg. From 1996 to 1999 Mr. Arnott held a number of senior finance positions at Anglo-American plc, a mining and precious metals trading company. Mr Arnott holds a BS from the University of Southampton and a Masters Degree from the University of Freiburg. Mr. Arnott then spent three years with Touche Ross where he qualified as a chartered accountant.
Mr. Arnott is a British national and holds positions on the Board of Directors of a number of operating companies within the Group.

**Max Chuard** (33) - *Corporate Finance & Investor Relations Director*
Mr. Chuard joined TEMENOS in 2002, initially responsible for acquisitions and special projects; he then assumed responsibilities for the Corporate Finance and Investor Relations division of the Group. Prior to joining TEMENOS, Mr. Chuard spent five years in investment banking, at JP Morgan first and then at SWICORP a Swiss merchant bank. Mr. Chuard holds a BA from the University of Lausanne. Mr. Chuard is a Swiss national and holds positions on the Board of Directors of a number of operating companies within the Group.

**Andre Loustau** (48) - *Chief Technical Officer*
Mr. Loustau has been with TEMENOS and its predecessor companies since 1984, serving in a variety of positions, including Development Manager and Project Manager prior to assuming the responsibilities of the Chief Technical Officer. Mr. Loustau is a British national.

**Mark Cullinane** (42) - *Chief Operating Officer*
Mr. Cullinane has over 18 years of experience in the provision of banking solutions internationally. For the past 12 years he has lived and worked in Asia where he has been responsible for the sales, implementation and support of numerous banking solutions. He joined TEMENOS as Regional Manager for Asia Pacific in February 2004 before assuming the role of Chief Operating Officer for the Group in January 2006. Mr. Cullinane is a British national and holds a degree in Business Studies (BA Hons.).

**Malou Ducomble** (51) *Clients and Operations*
Mrs. Ducomble, prior to joining TEMENOS in 1995, held a number of operating and managerial positions in MPCT Solutions Limited (now Aleri Inc.), Winter Partners, First Chicago International Corp. (now BankOne) and Commerzbank. Mrs. Ducomble has wide ranging experience in large projects management and multinational account relationships. Mrs. Ducomble is an American national and holds a Business degree and a Financial Management diploma from New York University.

**Guylaine Gaudreau** (37) - *Human Resources Director*
Mrs. Gaudreau has joined TEMENOS as the Worldwide Compensation & Benefits Director in 2002. Prior to joining the Group, she has held various positions as consultant and manager for Towers Perrin in Canada, France and Geneva. Mrs. Gaudreau is an actuary, qualified both in Canada (FCIA) and USA (FSA). Mrs. Gaudreau is a Canadian national and holds a MBA.

**Greg Green** (46) - *Managing Director, Temenos™Corebanking (TCB)*
Mr. Green joined TEMENOS in May 2005 as SVP of Operations in the Americas before assuming the responsibilities of Managing Director TCB in January 2006. Mr. Green has 20 years experience in the Information Systems industry. Prior to joining TEMENOS, he was Chief Operating Officer for Fiserv CBS Worldwide, directly responsible for all aspects of domestic operations, as well as operations around the globe. Mr. Green is an American national.

**Mark Gunning** (44) - *Group Strategy Director*
Mr. Gunning was educated at the London School of Economics before beginning his employment with Kapiti, a predecessor of the Misys group and the developer of the Equation banking system. He then worked for nine years for HSBC Bank in various capacities involving international IT. These included long term assignments in New York, Paris and Jersey. He joined TEMENOS in 1993 and has worked in Development, Client Services and Sales before assuming the responsibilities of General Manager for North America and of Group Strategy Director in 2005. Mr. Gunning is a British national.

**Jean-Michel Hilsenkopf** (43) - *Regional Director, SEMEA*
Mr. Hilsenkopf started his career as a banking consultant for a large international French bank. Mr. Hilsenkopf joined TEMENOS when it was incorporated in 1993. His expertise and experience of the sales organisation and as regional general manager during the past 10 years at TEMENOS has given him the vision and understanding of the business and market to drive the marketing efforts forward.
Mr. Hilsenkopf holds an engineering degree from a French Grande Ecole and has an MBA (International Marketing) from Geneva University. Mr. Hilsenkopf is a French national.

**Costa Christodoulou** (48) - *Regional Director, Northern Europe & CIS*
Mr. Christodoulou joined TEMENOS in January 2006 as Regional Director for Northern Europe region including UK, Ireland, the Nordic countries, Russia, CIS and the Baltic States. Mr. Christodoulou brings with him 22 years of sales and general management experience in the banking software and financial services IT industry. Prior to joining TEMENOS, Mr. Christodoulou was CEO of City Networks Ltd and prior to this, he carried P&L responsibility for major business units in Misys, Unisys and Alltel Information Services Ltd. Mr. Christodoulou is a British national and holds a degree in Chemical Engineering (BSc Honours) from the University of Salford.

**Armin Holst** (48) - *Regional Director, CEE*
Mr. Holst joined TEMENOS in November 2006 as Regional Director, Central and Eastern Europe. Mr. Holst brings with him more than 20 years of sales and general management experience in the banking software and IT industry. Prior to joining TEMENOS, Mr. Holst was worldwide Sales Director and member of the Board of the banking division of Misys plc and prior to this, he carried P&L responsibility for Europe within Misys and held senior Sales and Marketing positions with Nixdorf Computer AG.
Mr. Holst is a German national and holds a degree in Electronics (Dipl.-Ing.) and a degree in business economics (Dipl. Wirtschafts-Ing.) from the University of Cologne.

**Alex Groenendyk** (50) - *President Americas*
Mr. Groenendyk joined TEMENOS in May 2005 as President for Americas. Prior to joining TEMENOS, Mr Groenendyk served as President of Fiserv CBS Worldwide, a supplier of financial solutions to mid and large tier banking organisations. Mr. Groenendyk was also responsible for both the delivery of these solutions on a license and outsourcing basis. Mr. Groenendyk is a Dutch national.

**Philip Barnett** (43) - *Regional Director, Asia Pacific*
Mr. Barnett joined TEMENOS in 2003 as Sales Director for the Asia Pacific region and since October 2006 has held the position of Regional Director Asia Pacific.
Mr. Barnett is an Irish national and Educated in Ireland at St Andrews College. Mr. Barnett previously held positions in Irish Life and Permanent (Retail Bank in Dublin) and

various Sales, Sales Management and Regional Management positions in Kindle and subsequently Misys (since 1990) in the Americas, Europe and Middle East.

**Peter McKenna** (48) - *Marketing Director*
Mr. McKenna joined TEMENOS in September 2006 as Marketing Director.
Mr. McKenna has 20 years' experience working in the financial technology sector. His career includes senior management roles at Reuters in sales, business administration and product management, e-business director at QSP Financial Information Systems and head of investor services and transactions at Interactive Investor International. He also held the position of marketing director at Misys Asset Management Systems from 2002 and was most recently marketing and then sales director at Gissing Software. In this time he has accumulated knowledge and proven senior management expertise across all areas in product, marketing and sales management. Prior to working in the financial technology sector Mr. McKenna worked in management consultancy. Mr. McKenna is a British national and studied Engineering Technology at Kingston University.

### 4.2 Other activities and vested interests

Not applicable to the members of the Executive Board.

### 4.3 Management contracts

Other than as disclosed, no member of the Board of Directors or of the Executive Board holds management or advisory positions in any business group, Swiss or foreign, which could in any way give rise to conflicts of interest.
Furthermore, no member of the Board of Directors or of the Executive Board has contractual arrangements with the Group, that could be deemed as onerous or, in the case of the members of the Executive Board, that are substantially different from the terms and conditions under which other senior employees of the Group are engaged.

## Compensations, shareholdings and loans

### 5.1 Content and method of determining the compensations

Please refer also to section 3.5.2.
TEMENOS' compensation programs are designed to attract, motivate and retain top talent who can lead the business towards achievement of TEMENOS strategic plan and create shareholder value. The on-target short-term variable compensation applicable to the members of the Executive Board represents approximately 65% of their base salary.
For the other employees this variable target varies depending on the job position and achievement of specific key performance objectives. Annual short-term variable compensation and long-term incentive programmes (e.g. stock option plan and stock appreciation rights) are conditional upon either achievement of key financial performance targets (EPS, Profits, cash collection, revenue) strategic individual business objectives and/or continuous employment, depending on their functions within the Group. In case an employee is below those predefined thresholds, there is no bonuses and/or Stock Appreciation Rights grant; in case of overachievement, there is an accelerator up to a maximum of 200%.

No severance payments were made to the members of the Board of Directors or to the members of the Executive Board during 2006.

### 5.2 Compensation for acting members of governing bodies

*(exchange rates: USD/GBP: 0.5107; USD/CHF: 1.2197)*

The total 2006 compensation granted to members of the Board of Directors and members of the Executive Board amounted to USD 10,286,958. Out of this total USD 10,046,958 was paid to executive members of the Board of Directors and members of the Executive Board, and USD 240,000 to the non-executive members of the Board. The increase of the total compensation of executive members of the Board of Directors and members of the Executive Board is due to new additions to the Executive Board and overachievement of financial targets. The emoluments of the non-executive members of the Board are quantified by reference to the time spent on Board and on its Committees meetings and related matters. No severance payments were made to persons whose duties on the governing bodies had come to an end during the financial year 2006.

### 5.3 Compensation for former members of governing bodies

No compensation was paid to any former member of a governing body of TEMENOS.

### 5.4 Share allocation

There was no allotment of shares to members of the Board of Directors in 2006 or to members of the Executive Board, or parties closely linked to such persons.

### 5.5 Share ownership

- Number of shares held on 31 December 2006 by executive members of the Board: 9,752,064.
- Number of shares held on 31 December 2006 by non-executive members of the Board: 22,900.
- No shares held on 31 December 2006 by members of the Executive Board.

### 5.6 Options

- Options held on 31 December 2006 by executive members of the Board of Directors and by members of the Executive Board:

| | |
|---|---|
| Number of options | 4,962,382 |
| Lowest exercise price | CHF 1.30 |
| Highest exercise price | USD 15 |
| Earliest exercise date | 15 February 2004 |
| Latest exercise date | 01 January 2018 |

The executive members of the Board of Directors and the members of the Executive Board in the aggregate hold 4,962,382 Options under the ESOPs, with the following key terms:

| Grant Year | | Exercise Price | Options Outstanding | Unvested 31.12.06 |
|---|---|---|---|---|
| 2001 | USD | 15.00 | 12,200 | – |
| 2002 | CHF | 1.30 | 2,000 | 1,000 |
| 2002 | CHF | 16.00 | 10,000 | 2,000 |
| 2002 | CHF | 3.00 | 1,300 | 1,300 |
| 2003 | CHF | 1.30 | 75,000 | – |
| 2003 | CHF | 5.60 | 30,000 | – |
| 2003 | USD | 4.10 | 220,000 | – |
| 2004 | CHF | 8.60 | 105,000 | – |
| 2004 | USD | 6.80 | 200,000 | – |
| 2005 | CHF | 1.30 | 34,600 | – |
| 2005 | CHF | 1.80 | 8,200 | – |
| 2005 | USD | 6.90 | 255,000 | 180,000 |
| 2005 | USD | 6.95 | 590,500 | 411,000 |
| 2005 | USD | 8.52 | 2,685,000 | 2,685,000 |
| 2006 | CHF | 12.00 | 300,000 | 300,000 |
| 2006 | CHF | 12.55 | 50,000 | 50,000 |
| 2006 | USD | 10.03 | 30,000 | 30,000 |
| 2006 | USD | 11.32 | 30,000 | 30,000 |
| 2006 | USD | 6.90 | 223,582 | 223,582 |
| 2006 | USD | 9.78 | 100,000 | 100,000 |
| | | Total | **4,962,382** | **4,013,882** |

The Company did not allocate stock options or other kinds of options to non- executive members of the Board of Directors. Each option entitles the holder to purchase one registered share of the Company (subscription ratio 1:1). Options granted prior to 2004 have vesting periods of 3 to 5 years and exercise periods from 5 to 7 years. Options granted in 2004 and 2005 have vesting periods of 0 to 4 years and exercise periods from 6 to 10 years. Options granted in 2006 have vesting periods of 1 to 3 years and exercise periods from 8 to 10 years.

The executive members of the Board and the members of the Executive Board in the aggregate hold 814,853 Stock Appreciation Rights (SAR) under the SAR Plan with the following key terms:

| Grant Year | Options Outstanding | Exercise Price | Unvested as at the date hereof |
|---|---|---|---|
| 2006 | 814,853 | USD 9.78 | 814,853 |

Those SARs are conditional to achievement of 2006-2008 EPS targets and continuous employment. In case EPS is below predefined thresholds, all or a portion of SARs will be forfeited; in case of overachievement, there is an accelerator up to a maximum of 200%.

According to the insider trading section of the TEMENOS Business Code of Conduct, the black out periods are defined as follows:

No director or employee should make any purchase or sale of TEMENOS securities (shares, options, SARs, etc.):

- during the period beginning 10 trading days prior to publication of quarterly financial results and ending on the day of such public announcement;
- during the period beginning at the time of any public earnings-related announcement or public announcement of a significant corporate transaction or event and ending upon the completion of the second full trading day after such announcement;
- during such other periods as may be established from time to time by management in light of particular events or developments affecting TEMENOS; and
- during any other period when he or she has knowledge of any material non-public information concerning TEMENOS.

Please also refer to note 18 of the consolidated financial statements.

### 5.7 Additional fees and remunerations

Nothing to report.

### 5.8 Loans granted to members of governing bodies

As of 31 December 2006 the Company has outstanding loans of a total amount of USD 259,370 (CHF 316,354) to two members of the Executive Board. These loans bear no interests and will be fully repaid in 2007. No additional loans have been provided in 2006 to members of the Board of Directors or members of the Executive Board or members of their families.

### 5.9 Highest total compensation

Total 2006 base and short-term variable compensation and benefit of the highest paid member of the Board of Directors, Andreas Andreades, CEO, amounted to USD 1,406,973.

## Shareholders' participation

### 6.1 Voting-rights and representation restrictions

There are no voting-right restrictions and no statutory group clauses. Each registered share entitles the holder to one vote at the shareholders' meetings of the Company. At such meeting, shareholders may attend in person or by written proxy. Shareholders who do not attend in person may either appoint a representative by a written proxy, their custodian bank, the Company or the independent proxy holder.

### 6.2 Statutory quorums

There are no statutory quorums. The General Meeting of Shareholders shall pass its resolutions and carry out its elections by a simple majority of the votes validly cast, subject to the compulsory exceptions provided by law.

### 6.3 Convocation of the general meeting of shareholders

In compliance with the Swiss Code of Obligations, the General Meeting of Shareholders is convened by publication of the invitation and the agenda, at least twenty days before the date of the meeting in the Swiss Official Gazette of Commerce (Schweizerische Handelsamtsblatt, Feuille Officielle Suisse du Commerce). Shareholders representing at least 10% of the share capital may convene an Extraordinary General Meeting.

### 6.4 Agenda

One or more shareholders representing shares of an aggregate nominal value of at least CHF 1 million may, up to 45 days before the date of the General Meeting, request an item to be included on the agenda. Such request must be in writing and shall specify the items and the proposals of these shareholders.

### 6.5 Inscriptions into the share register

Pursuant to Article 13 §1 of the Company's Articles of Association, shareholders entered in the share register as shareholders on a specific qualifying date designated by the Board of Directors shall be entitled to attend and vote at the General Meeting.

In order to attend and vote at the Annual General Meeting of Shareholders, proxy holders of deposited shares (according to article 689d CO) are requested to inform the Company of the number of shares represented by them as early as possible, but not later than 4 business days before the Annual General Meeting of Shareholders.

Only persons registered in the share register are considered as shareholders by TEMENOS.

The Sixth Annual General Meeting of Shareholders of the Company will be held in Geneva on 1 June 2007. The agenda of the Annual General Meeting of Shareholders is published and sent to each shareholder in German, French and English. Shareholders recorded in the share register on 30 April 2007 are entitled to vote.

## Changes of control and defence measures

### 7.1 Duty to make an offer

None, other than applicable provisions of the Federal Act on Stock Markets and Securities Trading.

### 7.2 Clauses on change of control

There are no clauses on changes of control.

## Auditors

### 8.1 Duration of the mandate and term of office of the lead auditor

PricewaterhouseCoopers SA were re-elected as statutory and group auditors at the Annual General Meeting of Shareholders held on 23 May 2006, for a period of one year.

### 8.2 Auditing fees

Included in general and administrative expenses is an amount of USD 681,000 representing audit fees charged to the TEMENOS Group by PricewaterhouseCoopers (these fees are inclusive of the statutory audit fees).

### 8.3 Additional fees

In addition, other fees of approximately USD 616,000 have been incurred through the provision of tax advisory and other professional services by PricewaterhouseCoopers, as follows: USD 250,000 for tax advisory and USD 366,000 related to the Convertible Bond issued in March 2006.

### 8.4 Supervisory and control instruments vis-à-vis the auditors

The Audit Committee is responsible for monitoring the performance of external auditors, checking their independence, approving their annual work plan and fees, and reviewing their findings on quality control procedures as well as steps taken by the auditors to respond to changes in regulatory and other requirements. At the end of almost all Audit Committee meetings, the Audit Committee members spent time with the external auditors without the presence of management.

## Information policy

In December 2004, TEMENOS Children Foundation was set up to create a TEMENOS community which spans continents and cultures and shares a common vision. Children of TEMENOS employees are involved in an annual charity event and contest. In 2006, the focus was Africa, specifically Burkina Faso, by contributing to the building of a new school, and through plans to send computers to help local young pupils. Further information is available at www.temenos-children-foundation.com.

It is crucial for TEMENOS to conduct business in an ethical way everywhere and in all circumstances. The TEMENOS Business Code of Conduct (available on www.temenos.com) has been drawn up in this respect. This Code of Conduct describes the policies and procedures governing the relationship between the employee and TEMENOS, and is considered as part of the employment relationship.

TEMENOS encourages a two-way communication with both institutional and private investors and endeavours to respond promptly to queries.

TEMENOS publishes its annual report as at 31 December and interim consolidated financial statements as at 30 June. All this information and additional company-specific information are available at www.temenos.com.

For more information, please contact either Max Chuard, Corporate Finance & Investor Relations Director at mchuard@temenos.com or Ariel Boussiba, Company Secretary at aboussiba@temenos.com.

# TEMENOS Group AG

Consolidated Financial Statements

31 December 2006

and Report of the Group Auditors thereon

PricewaterhouseCoopers SA
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## REPORT OF THE GROUP AUDITORS TO THE GENERAL MEETING OF TEMENOS GROUP AG

As auditors of the group, we have audited the consolidated financial statements (balance sheet, income statement, statement of cash flows, statement of changes in equity and notes) on pages 27 to 60 of TEMENOS Group AG for the year ended 31 December 2006

These consolidated financial statements are the responsibility of the board of directors. Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We confirm that we meet the legal requirements concerning professional qualification and independence.

Our audit was conducted in accordance with Swiss Auditing Standards and with the International Standards on Auditing, which require that an audit be planned and performed to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement. We have examined, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. We have also assessed the accounting principles used, significant estimates made and the overall consolidated financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements give a true and fair view of the financial position, the results of operations and the cash flows in accordance with the International Financial Reporting Standards (IFRS) and comply with Swiss law.

We recommend that the consolidated financial statements submitted to you be approved.

PricewaterhouseCoopers SA

M. Foley S. Harvey

Auditor in charge

Geneva, 27 February 2007

# TEMENOS Group AG

*The amounts are expressed in thousands of US dollars*

consolidated income statement

*for the year ended 31 December*

| | 2006 | 2005 |
|---|---|---|
| **Revenues** | | |
| Software licensing | **97,897** | 64,374 |
| Maintenance | **54,961** | 46,776 |
| Services | **63,409** | 57,502 |
| *Total revenues* (note 19) | **216,267** | 168,652 |
| **Operating costs and expenses** | | |
| Cost of sales | **10,050** | 3,978 |
| Services | **64,931** | 61,557 |
| Software development and maintenance | **33,767** | 23,923 |
| Sales and marketing | **38,237** | 29,381 |
| General and administrative | **35,967** | 27,066 |
| *Total operating costs and expenses* | **182,952** | 145,905 |
| **Operating profit** | **33,315** | 22,747 |
| **Other income (expenses)** | | |
| Fair value gain (loss) from financial instruments, net (note 23) | **5,354** | (736) |
| Financial instrument related expenses (note 23) | **(305)** | (260) |
| Foreign exchange gains (losses), net | **254** | (948) |
| *Total other income (expenses)* | **5,303** | (1,944) |
| **Finance income (expenses)** | | |
| Interest expense | **(4,142)** | (805) |
| Interest income | **4,141** | 238 |
| *Net finance expenses* | **(1)** | (567) |
| **Profit before taxation** | **38,617** | 20,236 |
| Taxation (note 11) | **(4,236)** | (2,328) |
| **Profit for the year** | **34,381** | 17,908 |
| **Attributable to:** | | |
| Equity holders of the Company | **34,445** | 18,257 |
| Minority interest | **(64)** | (349) |
| | **34,381** | 17,908 |
| ***Earnings per share* (in US$)** (note 24): | | |
| ***basic*** | **0.60** | 0.33 |
| ***diluted*** | **0.57** | 0.32 |

The attached notes form part of these consolidated financial statements.

# TEMENOS Group AG

*The amounts are expressed in thousands of US dollars*

consolidated balance sheet

*as at 31 December*

## Assets

| | 2006 | 2005 |
|---|---|---|
| ***Current assets*** | | |
| Cash and cash equivalents (note 6) | **111,368** | 15,584 |
| Trade and other receivables (note 7) | **138,740** | 107,730 |
| Prepayments and other assets | **12,606** | 4,492 |
| *Total current assets* | **262,714** | 127,806 |
| ***Non–current assets*** | | |
| Property, plant and equipment (note 9) | **10,873** | 9,402 |
| Intangible assets (note 10) | **53,722** | 36,937 |
| Trade and other receivables (note 7) | **19,323** | 4,725 |
| Deferred tax assets (note 11) | **5,534** | 2,500 |
| *Total non-current assets* | **89,452** | 53,564 |
| *Total assets* | **352,166** | 181,370 |

## Liabilities and equity

| | 2006 | 2005 |
|---|---|---|
| ***Current liabilities*** | | |
| Trade and other payables (note 12) | **55,183** | 37,226 |
| Deferred revenues | **44,973** | 33,596 |
| Income taxes payable | **5,727** | 3,357 |
| Borrowings (note 13) | **1,220** | - |
| Provisions for other liabilities and charges (note 26) | **320** | 316 |
| *Total current liabilities* | **107,423** | 74,495 |
| ***Non–current liabilities*** | | |
| Borrowings (note 13) | **103,674** | - |
| Deferred tax liabilities | **1,258** | - |
| Other long-term payables | **3,668** | 5,848 |
| *Total liabilities* | **216,023** | 80,343 |
| ***Capital and reserves attributable to the Company's equity holders*** | | |
| Share capital (note 15) | **168,828** | 159,009 |
| Treasury shares (note 15) | **(2,974)** | (196) |
| Share premium and capital reserves (note 16) | **(66,521)** | (63,973) |
| Fair value and other reserves (note 17) | **(4,719)** | (963) |
| Retained earnings | **41,198** | 6,753 |
| | **135,812** | 100,630 |
| ***Minority interest*** | **331** | 397 |
| *Total equity* | **136,143** | 101,027 |
| *Total liabilities and equity* | **352,166** | 181,370 |

# TEMENOS Group AG

*The amounts are expressed in thousands of US dollars*

consolidated cash flow statement

*for the year ended 31 December*

| | 2006 | 2005 |
|---|---|---|
| **Cash flows from operating activities** | | |
| **Profit before taxation** | **38,617** | 20,236 |
| Adjustments: | | |
| Depreciation and amortisation (note 22) | **9,767** | 11,180 |
| Loss on disposal of assets (note 9) | **261** | 39 |
| Cost of employee share option scheme (note 18) | **5,132** | 3,843 |
| Interest expense - net | **1** | 567 |
| Fair value (gain) loss from financial instruments (note 23) | **(5,354)** | 736 |
| Financial instrument related expenses (note 23) | **305** | 260 |
| *Changes in net working capital* | | |
| Trade and other receivables and prepayments | **(51,616)** | (32,728) |
| Trade and other payables | **19,134** | 2,034 |
| Deferred revenues | **11,268** | (1,032) |
| *Cash generated from operations* | **27,515** | 5,135 |
| Income taxes paid | **(1,271)** | (1,470) |
| *Net cash generated from operating activities* | **26,244** | 3,665 |
| **Cash flows from investing activities** | | |
| Purchase of property, plant and equipment | **(3,855)** | (3,361) |
| Disposal of property, plant and equipment | **262** | 159 |
| Purchase of intangible assets | **(2,128)** | (1,534) |
| Capitalised development costs (note 10) | **(15,594)** | (10,841) |
| Disposal of available-for-sale investment (note 8) | **300** | 1,800 |
| Acquisitions, net of cash acquired (note 5) | **(3,813)** | (4,270) |
| Settlement of financial instruments (note 23) | **745** | - |
| Interest received | **4,125** | 247 |
| *Net cash used in investing activities* | **(19,958)** | (17,800) |
| **Cash flows from financing activities** | | |
| Proceeds from issuance of shares, net of related expenses | **4,172** | 1,169 |
| Proceeds from issuance of convertible bond, net of related expenses | **99,089** | - |
| Acquisition of treasury shares | **(13,592)** | (88) |
| Interest payments | **(311)** | (500) |
| Payment of financial instrument related expenses | **(146)** | (666) |
| Payment of finance lease liabilities | **(375)** | (169) |
| *Net cash generated from (used in) financing activities* | **88,837** | (254) |
| **Effect of exchange rate changes** | **661** | (815) |
| **Increase (decrease) in cash and cash equivalents in the year** | **95,784** | (15,204) |
| **Cash and cash equivalents at the beginning of the year** | **15,584** | 30,788 |
| **Cash and cash equivalents at the end of the year** | **111,368** | 15,584 |

## TEMENOS Group AG

*The amounts are expressed in thousands of US dollars*

consolidated statement of changes in equity

*for the year ended 31 December*

| | Share capital (note 15) | Treasury shares (note 15) | Share premium and capital reserves (note 16) | Fair value and other reserves (note 17) | Retained earnings | Minority interest | Total |
|---|---|---|---|---|---|---|---|
| **Balance at 1 January 2005** | **157,454** | **(124)** | **(67,357)** | **4,991** | **(11,504)** | **723** | **84,183** |
| Cumulative translation adjustment | - | - | - | (2,402) | - | 23 | (2,379) |
| Cash flow hedges, net of tax (note 17) | - | - | - | (3,552) | - | - | (3,552) |
| Net income (expense) recognised directly in equity | - | - | - | (5,954) | - | 23 | (5,931) |
| Profit for the year | - | - | - | - | 18,257 | (349) | 17,908 |
| Total recognised income | - | - | - | (5,954) | 18,257 | (326) | 11,977 |
| Cost of employee share option scheme | - | - | 3,843 | - | - | - | 3,843 |
| Exercise of share options (note 18) | 1,555 | - | (421) | - | - | - | 1,134 |
| Shares issued in relation to acquisitions | - | 16 | (14) | - | - | - | 2 |
| Share issuance costs | - | - | (24) | - | - | - | (24) |
| Acquisition of treasury shares | - | (88) | - | - | - | - | (88) |
| | 1,555 | (72) | 3,384 | (5,954) | 18,257 | (326) | 16,844 |
| **Balance at 31 December 2005** | **159,009** | **(196)** | **(63,973)** | **(963)** | **6,753** | **397** | **101,027** |
| Cumulative translation adjustment | - | - | - | (6,115) | - | (2) | (6,117) |
| Cash flow hedges, net of tax (note 17) | - | - | - | 2,359 | - | - | 2,359 |
| Net expense recognised directly in equity | - | - | - | (3,756) | - | (2) | (3,758) |
| Profit for the year | - | - | - | - | 34,445 | (64) | 34,381 |
| Total recognised income | - | - | - | (3,756) | 34,445 | (66) | 30,623 |
| Cost of employee share option scheme | - | - | 5,132 | - | - | - | 5,132 |
| Exercise of share options (note 18) | 8,090 | 10,856 | (14,755) | - | - | - | 4,191 |
| Shares issued in relation to acquisitions | 1,729 | 16 | 3,044 | - | - | - | 4,789 |
| Share issuance costs | - | - | (158) | - | - | - | (158) |
| Convertible bond - equity component (note 13) | - | - | 4,189 | - | - | - | 4,189 |
| Acquisition of treasury shares | - | (13,650) | - | - | - | - | (13,650) |
| | 9,819 | (2,778) | (2,548) | (3,756) | 34,445 | (66) | 35,116 |
| **Balance at 31 December 2006** | **168,828** | **(2,974)** | **(66,521)** | **(4,719)** | **41,198** | **331** | **136,143** |

**1. General information**

TEMENOS Group AG (“the Company”) was incorporated in Glarus, Switzerland on 7 June 2001 as a stock corporation (Aktiengesellschaft). Since 26 June 2001 the shares of TEMENOS Group AG have been publicly traded on the SWX Swiss Exchange. On incorporation, TEMENOS Group AG succeeded TEMENOS Holdings NV in the role of the ultimate holding company of the Group. From 23 May 2006 the Company moved its seat of incorporation to Geneva, Switzerland. The registered office is 18 Place des Philosophes, Geneva.

The Company and its subsidiaries (the “TEMENOS GROUP” or “the Group”) are engaged in the development and marketing of integrated banking software systems. The Group is also involved in supporting the implementation of the systems at various client locations around the world as well as in offering help desk support services to existing users of TEMENOS software systems. The client base consists of mostly banking and other financial services institutions.

These consolidated financial statements have been approved for issue by the Board of Directors on 20 February 2007.

**2. Accounting policies**

The principal accounting policies adopted in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

(a) Basis of preparation

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS). The consolidated financial statements have been prepared under the historical cost convention as modified by the revaluation of available-for-sale financial assets and financial instruments at fair value.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group’s accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in note 3.

**Amendments to published standards effective in 2006**

- IAS 19 (Amendment), Employee Benefits, is mandatory for the Group’s accounting periods beginning on or after 1 January 2006. It introduces the option of an alternative recognition approach for actuarial gains and losses. It may impose additional recognition requirements for multi-employer plans where insufficient information is available to apply defined benefit accounting. It also adds new disclosure requirements. As the Group does not intend to change the accounting policy adopted for recognition of actuarial gains and losses and does not participate in any multi-employer plans, adoption of this amendment only impacts the format and extent of disclosures presented in the financial statements.
- IAS 39 (Amendment), Cash Flow Hedge Accounting of Forecast Intragroup Transactions, allows the foreign currency risk of a highly probable forecast intragroup transaction to qualify as a hedged item in the consolidated financial statements, provided that: (a) the transaction is denominated in a currency other than the functional currency of the entity entering into that transaction; and (b) the foreign currency risk will affect consolidated profit or loss. The Group does not hedge intragroup transactions and therefore adoption of this amendment does not impact the Group’s operations or financial results.

**Amendments to published standards effective after 1 January 2007**

- IFRS 7, Financial Instruments: Disclosures, and a complementary amendment to IAS 1, Presentation of Financial Statements – Capital Disclosures, are mandatory for the Group’s accounting periods beginning on or after 1 January 2007. IFRS 7 introduces new disclosures relating to financial instruments. It requires the disclosure of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk and market risk, including sensitivity analysis to market risk. It replaces IAS 30, Disclosures in the Financial Statements of Banks and Similar Financial institutions, and disclosure requirements in IAS 32, Financial Instruments: Disclosure and Presentation. The amendment to IAS 1 introduces disclosures about the level of an entity’s capital and how it manages capital. The main additional disclosures will be the sensitivity analysis to market risk and the capital disclosures required by the amendment of IAS 1. The Group will apply IFRS 7 and the amendment to IAS 1 from annual periods beginning 1 January 2007.

**Standards, amendments and interpretations effective in 2006 but not relevant to the Group’s operations**

The following standards, amendments and interpretations are mandatory for accounting periods beginning on or after 1 January 2006 but are not relevant to the Group’s operations:

- IAS 39 (Amendment), The Fair Value Option;
- IAS 39 and IFRS 4 (Amendment), Financial Guarantee Contracts;
- IFRS 1 (Amendment), First-time Adoption of International Financial Reporting Standards;
- IFRS 6, Exploration for and Evaluation of Mineral Resources;
- IFRIC 4, Determining whether and Arrangement contains a Lease;
- IFRIC 5, Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds;
- IFRIC 6, Liabilities arising from Participating in a Specific Market - Waste Electrical and Electronic Equipment.

**Interpretations to existing standards that are not yet effective and have not been early adopted by the Group**
The following interpretations to existing standards have been published that are mandatory for the Group's accounting periods beginning on or after 1 May 2006 or later periods but that the Group has not early adopted:

- IFRIC 8, Scope of IFRS 2 (effective for annual periods beginning on or after 1 May 2006). IFRIC 8 requires consideration of transactions involving the issuance of equity instruments - where the identifiable consideration received is less than the fair value of the equity instruments issued - to establish whether or not they fall within the scope of IFRS 2. The Group will apply IFRIC 8 from 1 January 2007 but it is not expected to have any impact on the Group's accounts; and
- IFRIC 10, Interim Financial Reporting and Impairment (effective for annual periods beginning on or after 1 November 2006). IFRIC 10 prohibits the impairment losses recognised in an interim period on goodwill, investments in equity instruments and investments in financial assets carried at cost to be reversed at a subsequent balance sheet date. The Group will apply IFRIC 10 from 1 January 2007, but it is not expected to have any impact on the Group's accounts.

**Interpretations to existing standards that are not yet effective and are not relevant for the Group's operations**
The following interpretations to existing standards have been published that are mandatory for the Group's accounting periods beginning on or after 1 May 2006 or later periods but are not relevant for the Group's operations:
- IFRIC 7, Applying the Restatement Approach under IAS 29, Financial Reporting in Hyperinflationary Economies (effective from 1 March 2006). IFRIC 7 provides guidance on how to apply the requirements of IAS 29 in a reporting period in which an entity identifies the existence of hyperinflation in the economy of its functional currency, when the economy was not hyperinflationary in the prior period. As none of the group entities have a currency of a hyperinflationary economy as its functional currency, IFRIC 7 is not relavant to the Group's operations; and
- IFRIC 9, Reassessment of Embedded Derivatives (effective for annual periods beginning on or after 1 June 2006). IFRIC 9 requires an entity to assess whether an embedded derivative is required to be separated from the host contract and accounted for as a derivative when the entity first becomes a party to the contract. Subsequent reassessment is prohibited unless there is a change in the terms of the contract that significantly modifies the cash flows that otherwise would be required under the contract, in which case reassessment is required. As none of the group entities have changed the terms of their contracts which may include embedded derivatives, IFRIC 9 is not relevant to the Group's operations.

## (b) Basis of consolidation

The consolidated financial statements include the financial statements of TEMENOS Group AG as well as its subsidiaries.

Subsidiaries are all entities in which the Group has an interest of more than 50% of the voting rights or otherwise has power to govern the financial and operating policies. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group.They are de-consolidated from the date that control ceases. All assets and liabilities as well as expenses and earnings of the Group companies are included effective from the date of acquisition. Intercompany transactions, balances and unrealised gains on transactions between Group companies are eliminated; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement as other operating income.

Associates are entities over which the Group generally has between 20% and 50% of the voting rights or over which the Group has significant influence, but which it does not control. Investments in associates are accounted for by the equity method of accounting and are initially recognised at cost. Under this method the Group's share of the post-acquisition profits or losses of associates is recognised in the income statement and its share of post-acquisition movements in reserves is recognised in reserves. The cumulative post-acquisition movements are adjusted against the cost of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, the Group does not recognise further losses, unless the Group has incurred obligations or made payments on behalf of the associate.

## (c) Foreign currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The consolidated financial statements are presented in

US dollars, which is the Group's presentation currency and the currency in which the majority of the Group's transactions are denominated. The Company's functional currency is Swiss Francs.

Foreign currency transactions are translated into the functional currency using the exchange rates prevaling at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at the balance sheet date of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement, except when deferred in equity as qualifying cash flow hedges and qualifying net investment hedges.

The results and financial position of all the Group entities (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented (excluding intragroup balances which are denominated in US dollars and are eliminated on consolidation) are translated at the closing rate at the date of that balance sheet;
- income and expenses for each income statement (excluding intragroup transactions which are denominated in US dollars and are eliminated on consolidation) are translated, on a monthly basis, at the average exchange rates of each monthly period where this represents a reasonable approximation of the exchange rate applicable on the date of the transaction;
- the resulting exchange differences are recognised in shareholders' equity within "fair value and other reserves".

On consolidation, exchange differences arising from the translation of the net investment in foreign operations, and of borrowings and other currency instruments designated as hedges of such investments, are taken to shareholders' equity and are included within "fair value and other reserves". When a foreign operation is partially disposed of or sold, exchange differences that were recorded in equity are recognised in the income statement as part of the gain or loss on sale. Gains or losses resulting from long term intragroup balances for which settlement is neither planned nor likely to occur in the foreseeable future are treated as a net investment in foreign operations.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

### (d) Cash and cash equivalents

Cash and cash equivalents includes cash in hand, deposits held with banks with original maturities of three months or less, and other short-term highly liquid investments with original maturities of three months or less.

### (e) Trade receivables

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision made for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. Impairments are recorded against revenue when a credit note will be granted for a disputed receivable and in "sales and marketing" expense when it relates to a collection risk. The amount of the provision is the difference between the carrying amount and the recoverable amount calculated as the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate.

### (f) Property, plant and equipment

Property, plant and equipment is stated at historical cost less accumulated depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Depreciation on assets is calculated using the straight-line method to allocate their cost over their estimated useful lives, as follows (in years):

| | |
|---|---|
| Furniture and fixtures | 10 |
| Office equipment | 5 |
| Computer equipment | 4-5 |
| Vehicles | 4 |

Leasehold improvements are depreciated over the shorter of the lease term and useful life (ten years).

The assets' residual values and useful lives are reviewed and adjusted if appropriate at each balance sheet date. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

## (g) Intangible assets

**Goodwill**
Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary at the date of acquisition. Goodwill on acquisitions of subsidiaries is included in intangible assets.

For goodwill arising on acquisitions prior to the adoption of IFRS 3, Business Combinations, amortisation was calculated and recorded using the straight-line method, over a period of five years in the case of business-related purchased goodwill and over a period of three years in the case of personnel-related purchased goodwill. Following the introduction of IFRS 3, goodwill amortisation ceased at 31 December 2004 and separately recognised goodwill is tested annually for impairment and is carried at cost less accumulated impairment losses. Impairment losses are not reversed.

Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose.

**Computer software**
Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised using the straight-line method over a period of three, four or five years to allocate the cost over their estimated useful lives.

## (h) Capitalisation of development costs

The Group follows a strategy of investing a substantial part of its revenues in research and development work which is directed towards the enhancement of its two primary product platforms, TEMENOS T24 and TEMENOS CoreBanking.

The costs associated with the development of new or substantially improved products or modules are capitalised when a project has achieved the stage of technical feasibility, the likelihood of success is probable, costs can be reliably measured and a future revenue stream can be justified. In contrast, the cost of the enhancements effected to TEMENOS T24 or TEMENOS CoreBanking on an on-going basis, as well as the cost of developing products specifically commissioned by clients, is charged to operations in the year in which such costs are incurred. Costs include the employee costs incurred as a result of developing software and an appropriate portion of relevant overheads.

The capitalised development costs are amortised, using the straight-line method, commencing one quarter after the product is available for distribution. Development costs related to architecture developments are amortised over a five-year period and development costs related to functional developments are amortised over a three-year period.

## (i) Impairment of non-financial assets

Assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount, which is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest level for which there are separately identifiable cash flows. Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

## (j) Taxation

Current taxation is provided based on the taxable income reported for fiscal purposes in the various tax jurisdictions in which the Group operates. The nominal and effective tax rates applicable vary substantially between jurisdictions.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax base of assets and liabilities and their carrying amounts in the financial statements. Currently enacted or substantially enacted tax rates are used in the determination of deferred income tax.

Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

The Group incurs withholding tax in various jurisdictions. An assessment is made of the ability to recover these withholding taxes against the normal tax liabilities occuring within the Group, and a provision is made to the extent that withholding tax is considered irrecoverable.

### (k) Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Where the Group expects a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain. Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation.

### (l) Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

The fair value of the liability portion of a convertible bond is determined using a market interest rate for an equivalent non-convertible bond. This amount is recorded as a liability on an amortised cost basis until extinguished on conversion or maturity of the bonds. The remainder of the proceeds is allocated to the conversion option. This is recognised in shareholders' equity.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

### (m) Leases

Leases of property, plant and equipment where the Group has substantially all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalised at the inception of the lease at the lower of the fair value of the leased property or the present value of the minimum lease payments. The corresponding rental obligations, net of finance charges, are included as liabilities in the balance sheet. The interest elements of the lease obligations are charged to the profit and loss account over the period of the lease so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. Fixed assets held under finance leases are depreciated over the shorter of the useful life of the asset or the lease term. Payments made under operating leases are charged to the income statement on a straight line basis over the lease term.

### (n) Share capital

Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

Where any Group company purchases the Company's equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs is deducted from equity attributable to the Company's equity holders until the shares are cancelled or reissued. Where such shares are subsequently reissued, any consideration received (net of any directly attributable incremental transaction costs and the related income tax effects) is included in equity attributable to the Company's equity holders.

### (o) Employee share options

The Group operates equity-settled, share-based compensation plans. The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted, excluding the impact of any non-market vesting conditions. Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. At each balance sheet date, the Group revises its estimates of the number of options that are expected to vest. The impact of the revision of original estimates is recognised in the income statement over the remaining vesting period.

The proceeds received are credited to share capital (nominal value) and share premium when the options are exercised.

### (p) Revenue recognition

The Group derives revenues from the following sources: (1) software licences and the provision of software development services specifically commissioned by clients; (2) software maintenance (help desk services and rights to future product enhancements); and (3) software implementation and support services.

While the Group’s basis for revenue recognition is substantially defined by IAS 18 "Revenue", it applies the detailed principles of SOP 97-2 "Software Revenue Recognition" when consistent with the general principles of IAS 18. This requires the exercise of judgement and the use of estimates in connection with the determination of the amount of revenue to be recognised in each accounting period. SOP 97-2 is a US accounting standard issued by the American Institute of Certified Public Accountants that offers more detailed guidance for companies in the software industry.

The Group begins to recognise revenue from arrangements when all of the following conditions are met: (1) the Group has entered into a legally binding agreement with a customer; (2) the software or services have been delivered; (3) the licence fee is fixed and the agreement is free of uncertainties that may alter the agreement such that it may not be complete and final; and (4) collection is probable.

**Software licensing**
Software licence revenues represent all fees earned from granting customers licences to use our banking applications software, either through an initial licence or through the purchase of additional modules or user rights, but excludes any amounts that are related to maintenance. For software licence arrangements that do not require significant modification or customisation of the underlying software, revenue is recognised when the base criteria have been met.

If the software licence arrangement requires significant modification or customisation of the underlying software, the initial software licence revenue is generally recognised together with the services based on percentage-of-completion as defined in IAS 18 and IAS 11, “Construction Contracts”, and as explained in the description of services below.

Software development services revenue represents fees charged to clients for developing requested additional functionality and is recognised on a percentage-of-completion basis.

**Maintenance**
Software maintenance is included in most software licence arrangements and is generally priced as a percentage of the initial software licence fees. Maintenance provides customers with rights to unspecified software product upgrades, maintenance enhancements and access to the help desk during the term of the support period and is recognised ratably on a straight-line basis over the term of the arrangement.

**Services**
Software implementation and support services represents income from consulting and implementation services sold separately under services contracts. Service contracts are accounted for on a percentage-of-completion basis in accordance with the rules applicable to long-term contract revenue recognition as defined in IAS 11, “Construction Contracts”, whereby revenue and profit recognised during the year is based on project hours incurred as a proportion of total projected hours to complete. These estimates are continually re-evaluated and revised, when necessary, throughout the life of the contract. Any adjustments to revenue and profit due to changes in estimates are accounted for in the period in which the change in estimates occurs. When estimates indicate that a loss will be incurred on a contract upon completion, a provision for the expected loss is recorded in the period in which the loss becomes evident.

**Multiple element arrangements**
In many cases, the Group enters into transactions with customers that include software licence, maintenance and services revenues. The revenues from these arrangements are generally accounted for separately. The factors considered in determining whether the revenue should be accounted for separately include the nature of the services (i.e. whether they are essential to the functionality of the software licence), availability of services from other vendors, timing of payments and acceptance criteria on the realisability of the software licence fee.

For arrangements with multiple elements, revenue is allocated to each element of a transaction based upon its fair value determined by the normal pricing and discounting practices for those products and services. Revenue is deferred for any undelivered elements, and recognised when the product is delivered or over the period in which the service is performed. To the extent that the initial licensing fee incorporates the provision of unspecified upgrades and help desk support services for an agreed period, the value of these services is recognised ratably over the period.

If fair value cannot be objectively determined for any undelivered element included in bundled software and service arrangements, revenue is deferred until all elements are delivered and services have been performed.

**Payment terms**
Payment terms vary according to the individual contracts. Management reviews the nature of all non-standard payment terms to assess whether collection of the payments are considered probable.

Licensing and service fees that have been invoiced but have not been recognised as revenue are reported on the balance sheet under “deferred revenues” while fees which have been earned but have not been invoiced are reported under “trade and other receivables”.

### (q) Cost of sales

The direct costs associated with sales contracts, such as sales commissions and third-party licensing costs, are expensed as a "cost of sales" on an accrual basis. Service costs are recognised as incurred and primarily represent payroll costs for implementation support consultants and fees paid to third party consultants. Payments received in respect of out of pocket expenses are netted against the associated cost.

### (r) Pensions

Group companies operate various pension schemes including both defined benefit and defined contribution plans. A defined contribution plan is a pension plan under which the Group pays fixed contributions into a separate entity. The Group has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior period. A defined benefit plan is a pension plan that is not a defined contribution plan. Typically defined benefit plans define an amount of pension benefit that an employee will receive on retirement.

The liability in respect of defined benefit pension plans is the present value of the defined benefit obligation at the balance sheet date less the fair value of plan assets, together with adjustments for unrecognised actuarial gains or losses and past service cost. The defined benefit obligation is calculated annually by actuaries using the projected unit credit method, however salary increase rates are not applicable to these defined benefit plans. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in the currency in which the benefits will be paid and that have terms to maturity approximating to the terms of the related pension liability.

Actuarial gains and losses arising from experience adjustments, changes in actuarial assumptions in excess of the greater of 10% of the value of plan assets or 10% of the defined benefit obligation, and amendments to pension plans are charged or credited to income over the expected average remaining service lives of the related employees.

Under defined contribution plans the relevant contributions are expensed as they accrue. Once the contributions have been paid, the Group has no further payment obligations.

### (s) Earnings per share

Basic earnings per share are computed by dividing net income by the weighted average number of common shares outstanding during the period. Diluted earnings per share are computed by dividing net income by the weighted average number of common shares and common share equivalents outstanding during the period. The weighted average shares used to compute diluted earnings per share include the incremental shares of common stock relating to outstanding options to the extent such incremental shares are dilutive.

### (t) Segment reporting

A business segment is a group of assets and operations engaged in providing licences or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing licences or services within a particular economic environment that is subject to risks and returns that are different from those of components operating in other economic environments.

### (u) Financial risk management

The Group's activities expose it to a variety of financial risks: credit risk, foreign exchange risk, interest rate risk, and liquidity risk. The Group's risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance. The Group uses financial instruments to hedge certain risk exposures.

The Group's main financial instruments are cash, short-term receivables and payables, currency hedging instruments, available-for-sale investments, debt and certain other forms of financing, such as finance leases. Currency hedging instruments are carried at fair value. Management believes that the carrying amounts of other financial instruments approximate their fair value because of their short-term nature. Management further believes that the interest rates applicable to its debt and other forms of financing represent fair market rates and, therefore, their carrying value approximates fair value.

**Credit risk**
Concentration of credit risk is principally associated with accounts receivable and accrued (unbilled) revenue generated by licensees. This credit risk is, however, mitigated by the fact that the Group's licensees are highly rated financial institutions and the amounts due are spread over a large number of institutions. The Group does not generally require security guarantees to support these financial instruments. The Group does not anticipate non-performance by the counterparties in excess of the recorded impairment provision for receivables which are deemed doubtful of collection.

**Foreign exchange risk**
As a result of the diverse nature of the business, foreign currency exchange rate fluctuations affect the Group significantly. A significant portion of the Group's revenue and cash in-flows are in US dollars, whereas a large part of the cost base is denominated in Sterling and other currencies. To mitigate this mismatch the Group is making efforts to migrate the revenue streams to currencies that match the cost base and also enters into contracts for derivative financial instruments such as foreign exchange contracts. Group Treasury identifies, evaluates and hedges financial risks in close cooperation with the operating units and operates under written guidelines approved by the Board.

**Interest rate risk**
The Group's interest rate risk arises from the cash balance and from long-term borrowings. The Group's objective is to maximize interest return with minimal risk on the capital value.

**Liquidity risk**
Prudent liquidity risk management implies maintaining sufficient cash and marketable securitites, the availability of funding through an adequate amount of committed credit facilities and the ability to close out market positions. Due to the dynamic nature of the underlying business, Group Treasury aims at maintaining flexibility in funding by keeping committed credit lines available.

### (v) Accounting for derivative financial instruments and hedging contracts

Derivative financial instruments are initially recognised in the balance sheet at fair value and are subsequently remeasured to fair value at each balance sheet date. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Group designates certain derivates as hedges of highly probable forecast transactions (cash flow hedges).

The Group documents at the inception of the transaction the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives designated as hedges to specific assets and liabilities or to specific firm commitments or forecast transactions. The Group also documents its assessment, both at the hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

Changes in the fair value of financial instruments that qualify as cash flow hedges and that are highly effective are recognised in equity in the line "net fair value gain on cash flow hedge". Amounts accumulated in equity are recycled in the income statement in the periods when the hedged item will affect profit or loss.

Certain derivative transactions, while providing effective economic hedges under the Group's risk management policies, do not qualify as hedges under IAS 39 "Financial Instruments: Recognition and Measurement". Changes in the fair value of these derivatives are recognised immediately in the income statement in the line "income from financial instruments" and are disclosed separately.

The fair value of financial instruments is determined by reference to quoted market prices.

### (w) Financial assets

The Group classifies its financial assets in the following categories: loans and receivables, and available for sale. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition and re-evaluates this designation at every reporting date.

**Loans and receivables**
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the balance sheet date. Loans and receivables are classified as 'trade and other receivables' in the balance sheet (Note 2e).

**Available-for-sale financial assets**
Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. Regular purchases and sales of investments are recognised on trade-date – the date on which the Group commits to purchase or sell the asset. Investments are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss.

The Group assess at each balance sheet date whether there is objective evidence that a financial asset or a Group of financial assets is impaired.

## 3. Critical accounting estimates and judgements

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The resulting accounting estimates may differ from the actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

**Critical accounting estimates and assumptions**
Estimated impairment of goodwill
The Group tests annually whether goodwill and other intangible assets have suffered any impairment in accordance with the accounting policy stated in Note 2i. The recoverable amounts of cash-generating units have been determined based on value-in-use calculations. These calculations require the use of estimates (Note 10).

If the future sales of the Group's products and the size of the market opportunities are significantly lower than management's estimates the carrying value of goodwill and other intangible assets may need to be reduced accordingly. However, unless any downturn is particularly severe it is unlikely to have a material impact on the carrying value of goodwill and other intangible assets.

**Income taxes**
The Group is subject to income taxes in numerous jurisdictions. Judgement is required in determining the worldwide provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Group recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made. Were the actual final outcome (on the judgement areas) to differ by 10% from management's estimates, the Group would need to:

- decrease the income tax liability by US$ 171 thousand and increase the deferred tax asset by US$ 398 thousand, if favourable; or
- increase the income tax liability by US$ 171 thousand and decrease the deferred tax asset by US$ 398 thousand, if unfavourable.

**Employee share option scheme**
The fair value of the employee services received in exchange for the grant of share options is recognised as an expense, whereby the total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted. At each balance sheet date, the Group revises its estimates of the number of options that are expected to vest. Were the actual number of options exercised to differ by 10% from management's estimates, the Group would need to:

- increase retained earnings and decrease share premium by US$ 76 thousand, if favourable; or
- decrease retained earnings and increase share premium by US$ 76 thousand, if unfavourable.

**Critical judgements in applying the Group's accounting policies**
**Revenue recognition**

As detailed in Note 2p the Group is required to make an assessment for each new software licence contract as to whether the underlying software requires significant modification or customisation by the Group in order to meet the customer's requirements. If significant modification or customisation is required the software licence revenue is recognised based on percentage-of-completion. This assessment is made at the outset of the contract.

*The amounts are expressed in thousands of US dollars*

### 4. Principal group companies

The consolidated financial statements include the accounts of TEMENOS Group AG and the following entities as of 31 December 2006:

| Company name | Country of incorporation | Ownership interest |
|---|---|---|
| TEMENOS Headquarters SA | Switzerland | 100% |
| TEMENOS Suisse SA | Switzerland | 100% |
| T-TCB SA | Switzerland | 100% |
| T-TFR SA | Switzerland | 100% |
| T-jBASE SA | Switzerland | 100% |
| TEMENOS Luxembourg SA | Luxembourg | 100% |
| TEMENOS (NL) BV | Netherlands | 100% |
| TEMENOS Holland BV | Netherlands | 100% |
| TEMENOS France SAS | France | 100% |
| Quetzal Informatique SA | France | 100% |
| TEMENOS Deutschland GmbH | Germany | 100% |
| TEMENOS Hispania SA | Spain | 100% |
| TEMENOS UK Limited | United Kingdom | 100% |
| TEMENOS Systems Ireland Limited | Ireland | 100% |
| TEMENOS Hellas SA | Greece | 100% |
| TEMENOS Eastern Europe Limited | Cyprus | 100% |
| TEMENOS Polska Sp. Zoo | Poland | 100% |
| TEMENOS (Russia) Limited | Cyprus | 100% |
| TEMENOS Middle East Limited | Cyprus | 100% |
| TEMENOS Africa Pty Limited | South Africa | 100% |
| DBS Global Solutions (Pty) Limited | South Africa | 100% |
| TEMENOS USA, Inc. | USA | 100% |
| TEMENOS Mexico SA de CV | Mexico | 100% |
| Fomento Empresarial de Servicios Informaticos S.A. de C.V. | Mexico | 51% |
| TEMENOS Ecuador SA | Ecuador | 100% |
| TEMENOS Software Canada Limited | Canada | 100% |
| TEMENOS Holdings NV | Netherlands Antilles | 100% |
| TEMENOS Singapore Pte Limited | Singapore | 100% |
| TEMENOS Hong Kong Limited | Hong Kong | 100% |
| TEMENOS Software Shanghai Co. Limited | China | 100% |
| TEMENOS India Pte Limited | India | 100% |
| TEMENOS Application Services Pte Limited | India | 100% |
| TEMENOS (Thailand) Co. Limited | Thailand | 100% |
| TEMENOS (Malaysia) Sdn Bhd | Malaysia | 100% |
| TEMENOS Philippines, Inc. | Philippines | 100% |
| TEMENOS Japan KK | Japan | 100% |
| TEMENOS Korea Limited | Korea | 100% |
| TEMENOS Australia Pty Limited | Australia | 100% |
| TEMENOS Vietnam Co. Limited | Vietnam | 100% |

In addition to the Group companies listed above, some Group subsidiaries maintain branches or representative offices at the following locations: Beirut (Lebanon); Dubai (United Arab Emirates); Riyadh (Saudi Arabia); Moscow (Russia); Almaty (Kazakhstan); Kiev (Ukraine); Copenhagen (Denmark); Taipei (Taiwan); and Jakarta (Indonesia).

### 5. Business combinations

**TLC Consulting Limited**
On 11 January 2006 the Group acquired the business and assets of TLC Consulting Limited, a company specialising in risk management solutions. The initial consideration of £2.724 million is satisfied by the issue of shares in Temenos Group AG and payment of £0.1 million in cash. Any further payments will be dependent and based on the future performance of the business during the course of the next two years. The acquired business did not have a significant impact on the revenues or profits of the Group for the period.

As part of the assets of TLC Consulting Limited, TEMENOS acquired the rights to the Barracuda intellectual property.

*The amounts are expressed in thousands of US dollars*

Details of net assets acquired and goodwill are as follows:

| | |
|---|---|
| Purchase consideration | |
| - Cash paid | 175 |
| - Fair value of shares issued (note 15) | 4,788 |
| - Direct costs relating to the acquisition | 65 |
| Total purchase consideration | 5,028 |
| Fair value of net assets acquired | (1,200) |
| Goodwill | 3,828 |

The goodwill is attributable to the significant opportunities that exist within the risk management segment.

The fair value of the shares issued was based on the published share price. Deferred consideration, dependent upon future sales of the risk management software acquired, has not been accounted for. To the extent that additional payments are made in the future these will be treated as an increase in goodwill.

The identifiable assets and liabilities arising from the transaction are as follows:

| | Fair value | Acquiree's carrying amount |
|---|---|---|
| Intangible assets acquired | 1,200 | - |

**DBS Global Solutions (Pty) Limited**
On 22 November 2006 the Group acquired the business and assets of DBS Global Solutions (Pty) Limited, a company specialising in Microfinance solutions and operating as a reseller of TEMENOS eMerge. The acquired business did not have a significant impact on the revenues or profits of the Group for the period.

Details of net assets acquired and goodwill are as follows:

| | |
|---|---|
| Purchase consideration | |
| - Cash paid | 500 |
| - Deferred consideration due | 1,192 |
| Total purchase consideration | 1,692 |
| Fair value of net assets acquired | (199) |
| Goodwill | 1,493 |

The goodwill is attributable to the profitability of the acquired business and the opportunities that exist within the microfinance area.

The identifiable assets and liabilities arising from the transaction are as follows:

| | Acquiree's carrying amount |
|---|---|
| Cash and cash equivalents | 118 |
| Trade and other receivables | 517 |
| Prepayments and other assets | 176 |
| Property, plant and equipment | 13 |
| Trade and other payables | (625) |
| Net assets acquired | 199 |

The fair value of the assets and liabilities acquired is considered equivalent to the carrying value in all cases.

In addition to the above acquisitions, cash paid during 2006 in respect of acquisitions includes US$ 3,191 thousand in respect of the acquisition of the minority shareholding of TEMENOS Eastern Europe Limited in 2004 for total consideration of US$ 15,500 thousand.

The amounts are expressed in thousands of US dollars

### 6. Cash and cash equivalents

| The balance in respect of cash and cash equivalents consists of: | 2006 | 2005 |
|---|---|---|
| Cash at bank | 16,838 | 12,975 |
| Short term deposits with banks | 94,530 | 2,609 |
| | 111,368 | 15,584 |

The effective interest rate on short-term bank deposits was 4.94% (2005: 1.87%); these deposits have a weighted average maturity of 5 days (2005: 8 days).

### 7. Trade and other receivables

| | 2006 | 2005 |
|---|---|---|
| Trade receivables | 84,757 | 73,126 |
| Accrued revenues | 77,397 | 34,605 |
| VAT and other taxation recoverable | 3,021 | 2,424 |
| Other receivables | 2,608 | 3,854 |
| Provision for doubtful debts | (9,720) | (1,554) |
| | 158,063 | 112,455 |
| Less non-current portion: trade receivables | (19,323) | (4,725) |
| | 138,740 | 107,730 |

The fair value of trade and other receivables, based on discounted cash flows, equates to the values given above.

The expense for doubtful debts recorded in operating expenses is included in “sales and marketing” and amounts to US$ 39 thousand (2005: US$ 905 thousand).

There is no concentration of credit risk with respect to trade receivables, as the Group has a large number of customers which are internationally dispersed.

A number of minor reclassifications have been made during the year and the 2005 comparative figures have been amended accordingly.

### 8. Available-for-sale financial assets

In December 2004 TEMENOS Holdings NV entered into an agreement to sell its 20% equity interest in a private Italian company to the original shareholders for US$ 2.1 million resulting in the recording of a gain in the 2004 consolidated statement of income. Proceeds of US$ 0.3 million were received during 2006 (2005: US$ 1.8 million).

*The amounts are expressed in thousands of US dollars*

## 9. Property, plant and equipment

Tangible fixed assets consist of:

| | Leasehold improvements | Vehicles | Fixtures fittings & equipment | Total |
|---|---|---|---|---|
| **Cost** | | | | |
| At 1 January 2006 | 8,689 | 1,820 | 12,285 | 22,794 |
| Foreign currency exchange differences (1) | 799 | 39 | 1,023 | 1,861 |
| Additions (2) | 367 | 1,585 | 2,500 | 4,452 |
| Disposals (2) (3) | (221) | (247) | (1,551) | (2,019) |
| 31 December 2006 | 9,634 | 3,197 | 14,257 | 27,088 |
| **Depreciation** | | | | |
| At 1 January 2006 | 5,132 | 536 | 7,724 | 13,392 |
| Foreign currency exchange differences (1) | 543 | 29 | 706 | 1,278 |
| Charge for the year (2) (4) | 1,130 | 312 | 1,689 | 3,131 |
| Disposals (2) (3) | (166) | (200) | (1,220) | (1,586) |
| 31 December 2006 | 6,639 | 677 | 8,899 | 16,215 |
| **Net book value** | | | | |
| 31 December 2006 | 2,995 | 2,520 | 5,358 | 10,873 |

**Year ended 31 December 2005**

| | Leasehold improvements | Vehicles | Fixtures fittings & equipment | Total |
|---|---|---|---|---|
| **Cost** | | | | |
| At 1 January 2005 | 9,401 | 882 | 14,209 | 24,492 |
| Foreign currency exchange differences (1) | (1,102) | (90) | (1,345) | (2,537) |
| Additions (2) | 807 | 1,053 | 1,345 | 3,205 |
| Disposals (2) (3) | (417) | (25) | (1,924) | (2,366) |
| 31 December 2005 | 8,689 | 1,820 | 12,285 | 22,794 |
| **Depreciation** | | | | |
| At 1 January 2005 | 4,885 | 397 | 8,816 | 14,098 |
| Foreign currency exchange differences (1) | (583) | (34) | (857) | (1,474) |
| Charge for the year (2) (4) | 1,236 | 197 | 1,437 | 2,870 |
| Disposals (2) (3) | (406) | (24) | (1,672) | (2,102) |
| 31 December 2005 | 5,132 | 536 | 7,724 | 13,392 |
| **Net book value** | | | | |
| 31 December 2005 | 3,557 | 1,284 | 4,561 | 9,402 |

(1) The amounts have been restated to reflect the changes in the parity of the functional currencies of the operating entities owning the assets with the US dollar.

*The amounts are expressed in thousands of US dollars*

(2) Leased assets included in the table above, where the Group is a lessee, comprise mainly of motor vehicles and some office equipment.

| | Cost | Depreciation | Net book value |
|---|---|---|---|
| At 1 January 2006 | 872 | (572) | 300 |
| Additions | 562 | (268) | 294 |
| Disposals | (505) | 461 | (44) |
| Foreign currency exchange differences (1) | 59 | (31) | 28 |
| 31 December 2006 | 988 | (410) | 578 |

In most cases the assets leased are pledged as collateral against the lease liability.

(3) The loss on the disposals charged to the income statement in 2006 amounted to US$ 261 thousand (2005: US$ 39 thousand).

(4) The depreciation charge reported above has been quantified as follows:

| | Charge for the year | Currency translation adjustments | Total |
|---|---|---|---|
| *Year ended:* | | | |
| 31 December 2006 | 3,091 | 40 | 3,131 |
| 31 December 2005 | 2,998 | (128) | 2,870 |

During the year the Group completed construction of a boat to be used for marketing purposes (included within vehicles) for a total cost of US$ 2,371 thousand.

## 10. Intangible assets

| | Capitalised development costs | Purchased business related goodwill | Purchased personnel related goodwill | Purchased copyrights | Computer software | Purchased maintenance agreements | Total |
|---|---|---|---|---|---|---|---|
| **Cost** | | | | | | | |
| At 1 January 2006 | 37,657 | 16,747 | 1,108 | 21,567 | 3,814 | 2,498 | 83,391 |
| Foreign currency exchange differences (1) | - | - | - | - | 67 | - | 67 |
| Additions | 15,594 | 5,321 | - | 1,200 | 1,328 | - | 23,443 |
| Disposals (2) | - | - | - | - | (121) | - | (121) |
| 31 December 2006 | 53,251 | 22,068 | 1,108 | 22,767 | 5,088 | 2,498 | 106,780 |
| **Amortisation** | | | | | | | |
| At 1 January 2006 | 18,173 | 4,443 | 863 | 19,879 | 2,207 | 889 | 46,454 |
| Foreign currency exchange differences (1) | - | - | - | - | 95 | - | 95 |
| Charge for year (3) | 4,311 | - | - | 1,021 | 751 | 544 | 6,627 |
| Disposals (2) | - | - | - | - | (118) | - | (118) |
| 31 December 2006 | 22,484 | 4,443 | 863 | 20,900 | 2,935 | 1,433 | 53,058 |
| **Net book value** | | | | | | | |
| 31 December 2006 | 30,767 | 17,625 | 245 | 1,867 | 2,153 | 1,065 | 53,722 |

*The amounts are expressed in thousands of US dollars*

| | Capitalised development costs | Purchased business related goodwill | Purchased personnel related goodwill | Purchased copyrights | Computer software | Purchased maintenance agreements | Total |
|---|---|---|---|---|---|---|---|
| **Year ended 31 December 2005** | | | | | | | |
| **Cost** | | | | | | | |
| At 1 January 2005 | 26,784 | 16,747 | 1,108 | 20,783 | 4,261 | 2,498 | 72,181 |
| Foreign currency exchange differences (1) | - | - | - | - | (445) | - | (445) |
| Additions | 10,873 | - | - | 784 | 531 | - | 12,188 |
| Disposals (2) | - | - | - | - | (533) | - | (533) |
| 31 December 2005 | 37,657 | 16,747 | 1,108 | 21,567 | 3,814 | 2,498 | 83,391 |
| **Amortisation** | | | | | | | |
| At 1 January 2005 | 14,302 | 4,443 | 863 | 16,806 | 2,390 | 244 | 39,048 |
| Foreign currency exchange differences (1) | - | - | - | - | (209) | - | (209) |
| Charge for year (3) | 3,871 | - | - | 3,073 | 559 | 645 | 8,148 |
| Disposals (2) | - | - | - | - | (533) | - | (533) |
| 31 December 2005 | 18,173 | 4,443 | 863 | 19,879 | 2,207 | 889 | 46,454 |
| **Net book value** | | | | | | | |
| 31 December 2005 | 19,484 | 12,304 | 245 | 1,688 | 1,607 | 1,609 | 36,937 |

(1) The amounts have been restated to reflect the changes in the parity of the functional currencies of the operating entities owning the assets with the US dollar.

(2) The loss on disposals charged to the income statement in 2006 was US$ nil (2005: US$ nil).

(3) The amortisation charge reported above has been quantified as follows:

| | Charge for the year | Currency translation adjustments | Total |
|---|---|---|---|
| Year ended: | | | |
| 31 December 2006 | 6,676 | (49) | 6,627 |
| 31 December 2005 | 8,182 | (34) | 8,148 |

**Impairment tests for goodwill**

Goodwill is allocated to the Group’s cash-generating units identified according to country of operation or business segment. A segment-level summary of the goodwill allocation is presented below:

| | 2006 | | | 2005 | | |
|---|---|---|---|---|---|---|
| | **Software licensing** | **Services** | **Total** | **Software licensing** | **Services** | **Total** |
| Europe, Middle East and Africa | 12,504 | 84 | 12,588 | 11,011 | 84 | 11,095 |
| Asia | 1,293 | 122 | 1,415 | 1,293 | 122 | 1,415 |
| Americas | - | 39 | 39 | - | 39 | 39 |
| Corporate | 3,828 | - | 3,828 | - | - | - |
| | 17,625 | 245 | 17,870 | 12,304 | 245 | 12,549 |

The recoverable amount of a cash-generating unit is determined based on value-in-use calculations. These calculations use forecasts of contract signings and/or estimates of growth rates related to specific business segments. Forecasts of contract signings are based on an evaluation of the Group's current pipeline. The growth rates used in the calculations for specific business segments are 5%. If a nil growth rate had been used in the calculations this would not have a material impact on the carrying value of goodwill. The discount rate used in the calculations is 15%.

*The amounts are expressed in thousands of US dollars* — *31 December 2006*

## 11. Taxation

| Tax expense: | 2006 | 2005 |
|---|---|---|
| Domestic current income taxes | 507 | 273 |
| Overseas current income taxes, including non-recoverable withholding tax | 5,361 | 2,775 |
| Total current taxes | 5,868 | 3,048 |
| Deferred income taxes | (1,632) | (720) |
| Total tax expense | 4,236 | 2,328 |

TEMENOS Group AG is incorporated in Switzerland but the Group operates in various countries with various tax laws and rates. Consequently, the effective tax rate may vary from period to period to reflect the generation of taxable income in tax jurisdictions. A reconciliation between the reported income tax expense and the amount computed using a basic Swiss statutory corporate tax rate of 25%, is as follows:

| | 2006 | 2005 |
|---|---|---|
| Profit before tax | 38,617 | 20,236 |
| Tax at the domestic rate of 25% | 9,654 | 5,059 |
| Effects of different tax rates | (8,207) | (4,826) |
| Tax holiday | (1,120) | (1,402) |
| Utilisation of previously unrecognised losses | (1,884) | (3,079) |
| Current year's losses not utilised | 5,964 | 7,152 |
| Other movement on deferred tax assets and liabilities | (1,965) | (1,300) |
| Effect of current period adjustment for tax of prior period | (18) | (781) |
| Non deductible expenses | 944 | 865 |
| Other tax and credits | 868 | 640 |
| Total tax expense | 4,236 | 2,328 |

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority. Deferred tax assets and liabilities shown in the consolidated balance sheet are as follows:

| | 2006 | 2005 |
|---|---|---|
| Deferred tax assets | 5,534 | 2,500 |
| Deferred tax liabilities | (1,258) | - |
| Net deferred tax assets | 4,276 | 2,500 |

An assessment of the realisability of deferred tax assets is made on a country by country basis, based on the weight of available evidence including factors such as recent earnings history and expected future taxable income. Deferred tax assets are recognised to the extent that realisation of the related tax benefit through the future taxable profits is probable. The majority of the deferred tax assets are expected to be utilised after more than twelve months.

In addition to the deferred tax assets recognised above, the Group has unrecognised deferred tax assets relating to losses carried forward of US$ 34,490 thousand (2005: US$ 32,582 thousand) of which US$ 1,875 thousand (2005: US$ 1,893 thousand) will expire within five years and the remaining amount thereafter. There are no unrecognised deferred tax liabilities.

The gross movement on the deferred income tax account is as follows:

| | 2006 | 2005 |
|---|---|---|
| At 1 January | 2,500 | 2,174 |
| Income statement credit | 1,632 | 720 |
| Foreign exchange movement on deferred tax assets held in local currencies | 144 | (432) |
| Other | - | 38 |
| At 31 December | 4,276 | 2,500 |

*The amounts are expressed in thousands of US dollars* *31 December 2006*

The movement in deferred tax assets is as follows:

| | Tax losses | Other | Total |
|---|---|---|---|
| At 1 January 2005 | 2,045 | 129 | 2,174 |
| Charged to the income statement | 716 | 4 | 720 |
| Exchange differences | (427) | (5) | (432) |
| Other | 38 | - | 38 |
| At 31 December 2005 | 2,372 | 128 | 2,500 |
| Charged (credited) to the income statement | (978) | 3,868 | 2,890 |
| Exchange differences | 142 | 2 | 144 |
| At 31 December 2006 | 1,536 | 3,998 | 5,534 |

The movement in deferred tax liabilities is as follows:

| | Investments in subsidiaries | Total |
|---|---|---|
| At 31 December 2005 | - | - |
| Charged to the income statement | (1,258) | (1,258) |
| At 31 December 2006 | (1,258) | (1,258) |

## 12. Trade and other payables

| | 2006 | 2005 |
|---|---|---|
| Trade payables | 16,740 | 16,098 |
| Accrued expenses | 29,023 | 16,665 |
| Other payables | 9,420 | 4,463 |
| | 55,183 | 37,226 |

## 13. Borrowings

**Bank loans**
On 21 March 2005 the Group negotiated financing facilities with two large financial institutions which replace existing financing facilities. The pertinent details of the facilities available to the Group are as follows:

**Facilities available for general working capital needs:**
US$ 20 million bearing interest at LIBOR/EURIBOR (depending on drawing currency) + 1.5%. This is repayable as follows:
US$ 10 million repayable in full on 20 March 2008
US$ 10 million repayable in full on 20 March 2007
Commitment fees are due at 0.75% of the margin on the above facilities.

**Facility available for issuing guarantees (e.g. performance bonds, rent deposits):**
US$ 10 million repayable in full on 20 March 2008. No commitment fees are due on this facility. Instead, industry standard guarantee setup fees are applied to any usage of this facility.

Under the arrangements entered into, the Group is restricted from becoming further indebted to financial institutions. The facilities granted are subject to various financial covenants, which are based on conservative projections of the Group's results.

As at 31 December 2006 and 31 December 2005 the general working capital facilities were not drawn upon. As at 31 December 2006 guarantees totalling US$ 7,669 thousand (2005: US$ 3,984 thousand) were in issue.

**Convertible bond**
On 21 March 2006 the Group issued a convertible bond with a nominal value of CHF 132.25 million and a coupon rate of 1.50%. The bonds mature seven years from the issue date at a redemption value of CHF 152.83 million or can be converted into shares at the holder's option at a conversion price of CHF 18.06 per share.

The amounts are expressed in thousands of US dollars

The fair values of the liability component and the equity conversion component were determined at the issuance of the bond.

The fair value of the liability component, included in long-term borrowings, was calculated using a market interest rate for an equivalent loan. The residual amount, representing the value of the equity conversion component, is included in shareholders' equity in other reserves.

The convertible bond recognised in the balance sheet is calculated as follows:

| | **2006** |
|---|---|
| Nominal value of convertible bond issued on 21 March 2006, net of transaction costs | 98,948 |
| Equity component | (4,189) |
| Liability component on initial recognition at 21 March 2006 | 94,759 |
| Interest expense | 3,569 |
| Foreign exchange movement | 6,566 |
| Liability component at 31 December 2006 | 104,894 |

Interest expense on the bond is calculated using the effective interest method by applying the effective interest rate of 4.56% to the liability component.

The fair value of the liability component of the convertible bond at 31 December 2006, based on cash flows discounted using a market interest rate for an equivalent loan, was US$ 106,700 thousand.

## 14. Liabilities under finance leases

| | **2006** | **2005** |
|---|---|---|
| Obligations under finance leases: | | |
| repayable within one year | 278 | 172 |
| repayable between two and five years | 292 | 120 |
| | 570 | 292 |
| Finance charges allocated to future accounting periods | (39) | (12) |
| | 531 | 280 |

## 15. Share capital

As at 31 December 2006, the issued and outstanding shares of TEMENOS Group AG, the ultimate holding company of the Group, comprised 57,655,448 common shares of a nominal value of CHF 5 each. All issued shares are fully paid.

The changes in the number of issued and outstanding shares in the year ended 31 December 2006 are summarised below:

| | **number** | **Nominal value in CHF** | **in US$** |
|---|---|---|---|
| Issued, as at 1 January 2005 | 54,952,435 | 274,762 | 157,454 |
| Shares issued on exercise of employee share options | 397,757 | 1,989 | 1,555 |
| Total number of shares issued, as at 31 December 2005 | 55,350,192 | 276,751 | 159,009 |
| Shares issued on acquisition of TLC (note 5) | 441,084 | 2,205 | 1,729 |
| Shares issued on exercise of employee share options | 2,050,145 | 10,251 | 8,090 |
| Total number of shares issued, as at 31 December 2006 | 57,841,421 | 289,207 | 168,828 |
| Treasury shares | (185,973) | (3,627) | (2,974) |
| Total number of shares outstanding, as at 31 December 2006 | 57,655,448 | 285,580 | 165,854 |

The amounts are expressed in thousands of US dollars 31 December 2006

As at 31 December 2006 the number of treasury shares held by the Group amounted to 185,973 (2005: 44,342). Treasury shares include shares held for resale and other shares alloted to members of the TEMENOS Employee Share Option Scheme or other option holders at the time that they exercise their options.

The Group issued 441,084 shares to the shareholders of TLC Consulting Limited as part of the purchase consideration for the business and assets of the company on 11 January 2006. The ordinary shares issued have the same rights as the other shares in issue. The fair value of the shares issued amounted to US$ 4,788 thousand (US$ 10.86 per share).

TEMENOS Group AG also has authorised and conditional capital, comprising:

| | |
|---|---|
| authorised shares that may be issued in the context of acquisitions (available to the Board until 23 May 2008) | 26,510,243 |
| conditional shares that may be issued on the exercise of employee share options | 10,259,292 |
| conditional shares that may be issued in conjunction with financial instruments (of which 9,000,000 are reserved for the Convertible bond) | 13,930,680 |

The share capital of all subsidiaries has been eliminated on consolidation.

In the year ended 31 December 2001, 344,826 share options were allotted to the ex-shareholders of Integrated Core Technologies Participations SA when the company was acquired by the Group. As at 31 December 2006 none of these share options were outstanding (2005: 4,258). A warranted share subscription reserve was established at the time of the transaction, and the exercise of these share options reduced this reserve accordingly (note 16).

Based on the average market value of the shares of TEMENOS Group AG for each quarter, and the vested portion of the potentially dilutive options as at 31 December 2006, the dilution effect of the latter has been quantified as follows:

| | **Common shares outstanding** | **Weighted average number of outstanding common shares** | **Employee share options outstanding** | **Share warrants outstanding** | **Equivalent potentially dilutive common shares** |
|---|---|---|---|---|---|
| 31 December 2006 | 57,655,448 | 56,980,170 | 9,608,156 | - | 3,315,760 |
| 31 December 2005 | 55,305,850 | 55,024,848 | 11,628,353 | 4,258 | 2,774,271 |

*The amounts are expressed in thousands of US dollars*

### 16. Share premium and capital reserves

| | Convertible bond | Share premium | Warranted share subscription reserve | Employee share options reserve | Discount on shares issued to employees | Negative premium arising on creation of Temenos Group AG | Total |
|---|---|---|---|---|---|---|---|
| Balance at 1 January 2005 | - | 3,863 | 28 | 5,051 | (7,843) | (68,456) | (67,357) |
| Cost of employee share option scheme | - | - | - | 3,843 | - | - | 3,843 |
| Exercise of share options (note 18) | - | 404 | - | - | (825) | - | (421) |
| Shares issued in relation to acquisitions | - | - | (14) | - | - | - | (14) |
| Share issuance costs | - | (24) | - | - | - | - | (24) |
| Balance at 31 December 2005 | - | 4,243 | 14 | 8,894 | (8,668) | (68,456) | (63,973) |
| | - | | | | | | |
| Cost of employee share option scheme | - | - | - | 5,132 | - | - | 5,132 |
| Exercise of share options (note 18) | - | 1,626 | - | - | (16,381) | - | (14,755) |
| Shares issued in relation to acquisitions | - | 3,058 | (14) | - | - | - | 3,044 |
| Share issuance costs | - | (158) | - | - | - | - | (158) |
| Convertible bond - equity component (note 13) | 4,189 | - | - | - | - | - | 4,189 |
| | - | | | | | | |
| Balance at 31 December 2006 | 4,189 | 8,769 | - | 14,026 | (25,049) | (68,456) | (66,521) |

**Convertible bond**
On 21 March 2006 the Group issued a convertible bond. The fair value of the liability component, included in long-term borrowings, was calculated using a market interest rate for an equivalent loan. The residual amount, representing the value of the equity conversion component, is included in shareholders' equity.

**Share premium**
The share premium account reflects the premium on issuance of new shares at a price above their par value or negative premium when issued at a discount.

**Reserve for treasury shares**
Under Swiss law a legal reserve must be established for an amount equal to the cost of treasury shares held by the Group. This reserve is included within share premium. As at 31 December 2006 the cost of treasury shares held by the Group was US$ 2,974 thousand (2005: US$ 196 thousand).

**Warranted share subscription reserve**
The balance under this reserve represents the estimated fair market value, at the time of the transaction, of the share options granted in the context of an acquisition of a subsidiary which had not been exercised by the aforesaid dates. The warranted share subscription reserve was credited with the approximate fair value of the options on issuance.

**Employee share options reserve**
As detailed in note 18, the Group operates an employee share options scheme. The excess of the market price over the grant price is charged to personnel costs over the period during which the options vest, with a corresponding credit made to the employee share options reserve.

**Discount on shares issued to employees**
Under the terms of the employee share options scheme the Group issues shares to employees at option prices ranging from US$ 0.005 to US$ 15 per share. To the extent that shares are issued at a value that is lower than the nominal value of CHF 5 per share, this amount is allocated to discount on shares issued to employees.

**Negative premium arising on creation of TEMENOS Group AG**
TEMENOS Group AG was incorporated on 7 June 2001. The issued and outstanding shares of TEMENOS Holdings NV were exchanged shortly before the initial public offering for TEMENOS Group AG shares, thus rendering TEMENOS Holdings NV a wholly owned subsidiary of TEMENOS Group AG. The number of shares acquired was 40,104,336 which prior to the exchange had a nominal value of US$ 0.001 per share, totalling US$ 39 thousand. The new shares in TEMENOS Group AG were issued at nominal value of CHF 5 which resulted in a negative premium of US$ 113,538 thousand. Expenses related to the initial public offering of TEMENOS

*The amounts are expressed in thousands of US dollars*

Group AG, and share premium items arising prior to the creation of TEMENOS Group AG, were recorded against this account.

A deficit of US$ 62,277 thousand was recorded to share premium on the cancellation of shares repurchased in 2000. This was transferred into "negative premium arising on creation of TEMENOS Group AG" during the period ended 31 December 2001.

## 17. Fair value and other reserves

Included within fair value and other reserves are the following:

**Cumulative translation adjustment**
The cumulative translation adjustment represents the foreign exchange gains and losses resulting from the translation of the subsidiaries' assets, liabilities and results of operations from their functional currency into the Group's reporting currency (US$).

**Fair value gains on cash flow hedges**
The fair value reserve on cash flow hedges represents the fair value gain on forward foreign currency exchange contracts that were outstanding at the end of the reporting period that qualify as cash flow hedges.

| | Cumulative translation adjustment | Fair value gains (losses) on qualifying cash flow hedges | Total |
|---|---|---|---|
| Balance at 1 January 2005 | 2,785 | 2,206 | 4,991 |
| Currency translation differences | (2,402) | - | (2,402) |
| Transfers to net profit | - | (205) | (205) |
| Net fair value loss on cash flow hedge, net of tax (note 23) | - | (3,347) | (3,347) |
| Balance at 31 December 2005 | 383 | (1,346) | (963) |
| Currency translation differences | (6,115) | - | (6,115) |
| Transfers to net profit | - | 905 | 905 |
| Net fair value gain on cash flow hedge, net of tax (note 23) | - | 1,454 | 1,454 |
| Balance at 31 December 2006 | (5,732) | 1,013 | (4,719) |

## 18. Employee share options

Share options and share appreciation rights are granted to executive board members and selected employees. Options are conditional on the employee completing a specified period of service (the vesting period) and share appreciation rights are only exercisable if the Group achieves its targets of profitability. The options and share appreciation rights have a contractual term of ten years. The Group has no legal or constructive obligation to repurchase or settle the options or share appreciation rights in cash.

The cumulative options and share appreciation rights granted as at 31 December 2006, net of cancellations, were 16,722,604 (as at 31 December 2005: 14,918,915) with exercise prices ranging from US$ 0.005 to US$ 15.00. The vesting period ranges from one to five years and the options and share appreciation rights expire ten years after the grant date. The cumulative options exercised as at 31 December 2006 amounted to 7,114,449 (period ended 31 December 2005: 3,290,563).

The amounts are expressed in thousands of US dollars

A summary of the movements in the number of share options outstanding and their related weighted average exercise prices are as follows:

| | 2006 | | 2005 | |
|---|---|---|---|---|
| | **Number of shares** | **Weighted average exercise price** | **Number of shares** | **Weighted average exercise price** |
| Outstanding at the beginning of the year | 11,628,353 | $ 6.21 | 6,757,736 | $ 4.63 |
| Granted during the year | 1,969,813 | $ 9.30 | 5,724,550 | $ 7.87 |
| Cancelled during the year | (166,124) | $ 7.44 | (456,176) | $ 4.60 |
| Exercised during the year | (3,823,886) | $ 3.95 | (397,757) | $ 2.97 |
| Outstanding at the end of the year | 9,608,156 | $ 7.82 | 11,628,353 | $ 6.21 |

Of the 9,608,156 outstanding options and share appreciation rights (2005: 11,628,353), 3,037,859 (2005: 2,851,543) were exercisable at the balance sheet date with a weighted average exercise price of US$ 6.17 (2005: US$ 5.94). The options exercised during the year had a weighted average share price at the time of exercise of US$ 9.50 (2005: US$ 8.23).

Share options and share appreciation rights outstanding at the end of the year have exercise prices and weighted average remaining contractual lives as follows:

| **2006**<br>Exercise price | **Number** | **Remaining contractual life (years)** |
|---|---|---|
| $0.01-$0.35 | 107,205 | 0.82 |
| $1.00-$1.48 | 560,200 | 6.03 |
| $2.46-$2.50 | 17,700 | 2.81 |
| $4.10-$6.09 | 868,370 | 4.90 |
| $6.80-$7.96 | 2,171,832 | 7.97 |
| $8.11-$9.84 | 5,264,109 | 8.90 |
| $10.00-$15.00 | 618,740 | 5.81 |
| | 9,608,156 | |

| **2005**<br>Exercise price | **Number** | **Remaining contractual life (years)** |
|---|---|---|
| $0.01-$0.35 | 623,300 | 2.47 |
| $0.99-$1.37 | 1,815,400 | 7.05 |
| $2.28-$2.50 | 29,500 | 4.31 |
| $4.10-$6.09 | 1,498,476 | 6.03 |
| $6.47-$7.96 | 3,250,550 | 8.66 |
| $8.25-$9.33 | 3,861,051 | 9.50 |
| $10.00-$15.00 | 550,076 | 5.93 |
| | 11,628,353 | |

**Fair value of stock options**

The weighted average fair value of options and share appreciation rights granted during the period determined using the Black-Scholes valuation model was US$ 2.79 (2005: US$ 2.24). The significant inputs into the model were weighted average share price at grant date of US$ 9.55 (2005: US$ 7.80), weighted average exercise price of US$ 9.30 (2005: US$ 7.87), standard deviation of expected share price returns of 36%-37% (2005: 37%-38%), weighted average option lives of 3.22 years (2005: 3.52 years) and weighted average annual risk-free interest rate of 1.50% (2005: 0.87%). The volatility measured at the standard deviation of expected share price returns is based on statistical analysis of daily share prices over the relevant historical period. Where there is no relevant historical period the standard deviation of expected share price returns is based on calculations derived from a relevant peer group.

*The amounts are expressed in thousands of US dollars*

The cost of employee share options, including the amount in respect of key management, is disclosed in note 20.

## 19. Segmental reporting

Segment information of the TEMENOS GROUP is based on two segment formats. The primary reporting segment format consists of the two distinct business activities: software licensing; and services. The secondary reporting segment format consists of the major geographical regions in which the Group operates. The company's internal organisational structure and internal financial reporting address both segments.

**(a) Primary reporting format - business segments**

The Group is organised into two main business segments:
Software licensing - comprising of licensing, development and maintenance of the Group's software
Services - comprising of consultancy services related to implementation of the Group's software

| | | 2006 | | | 2005 | |
|---|---|---|---|---|---|---|
| | **Software licensing** | **Services** | **Total** | **Software licensing** | **Services** | **Total** |
| Segment revenues | 152,858 | 63,409 | 216,267 | 111,150 | 57,502 | 168,652 |
| Segment operating result | 119,091 | (1,522) | 117,569 | 83,249 | (4,055) | 79,194 |
| Unallocated operating costs | | | (84,254) | | | (56,447) |
| **Operating profit** | | | 33,315 | | | 22,747 |
| **Other income (expenses)** | | | | | | |
| Fair value gain (loss) from financial instruments, net (note 23) | | | 5,354 | | | (736) |
| Financial instrument related expenses (note 23) | | | (305) | | | (260) |
| Foreign exchange gains (losses), net | | | 254 | | | (948) |
| *Total other income (expenses)* | | | 5,303 | | | (1,944) |
| **Finance income (expenses)** | | | | | | |
| Interest expense | | | (4,142) | | | (805) |
| Interest income | | | 4,141 | | | 238 |
| *Net finance expense* | | | (1) | | | (567) |
| **Profit before taxation** | | | 38,617 | | | 20,236 |
| Taxation | | | (4,236) | | | (2,328) |
| **Profit for the year** | | | 34,381 | | | 17,908 |
| **Attributable to:** | | | | | | |
| Equity holders of the Company | | | 34,445 | | | 18,257 |
| Minority interest | | | (64) | | | (349) |
| | | | 34,381 | | | 17,908 |

*The amounts are expressed in thousands of US dollars*

**Other segment items (not including unallocated items)**

| | 2006 Software licensing | 2006 Services | 2006 Total | 2005 Software licensing | 2005 Services | 2005 Total |
|---|---|---|---|---|---|---|
| **Assets** | | | | | | |
| Segment assets | 170,962 | 33,161 | 204,123 | 114,427 | 24,449 | 138,876 |
| Unallocated assets | | | 148,043 | | | 42,494 |
| Total assets | | | 352,166 | | | 181,370 |
| **Liabilities** | | | | | | |
| Segment liabilities | (39,822) | (4,782) | (44,604) | (31,340) | (2,101) | (33,441) |
| Unallocated liabilities | | | (171,419) | | | (46,902) |
| Total liabilities | | | (216,023) | | | (80,343) |
| Capital expenditure | 16,789 | - | 16,789 | 10,841 | - | 10,841 |
| Depreciation and amortisation | 5,876 | - | 5,876 | 8,182 | - | 8,182 |

There are no transactions between the segments. However, revenues for software licensing and services from multi-element contracts are reallocated between the segments based on the fair value of the contract elements as a result of the application of the Group's revenue recognition policy.

Unallocated operating costs represent sales and marketing expenses and administrative expenses as these are not separately identifiable to either business segment. For 2006, unallocated operating costs also include cost of sales.

Segment assets consist primarily of receivables, accrued revenue and intangible assets. Management do not consider it appropriate to allocate cash, prepayments and tangible fixed assets to business segments.

Segment liabilities comprise of deferred revenues. Management do not consider it appropriate to allocate accounts payable, accrued expenses and loans to business segments.

**(b) Secondary reporting format - geographical segments**

**Revenue by region of destination of product or service**

| | Asia | Americas | Europe, Middle East and Africa | Total |
|---|---|---|---|---|
| Year ended 31 December 2006 | 51,156 | 34,604 | 130,507 | 216,267 |
| Year ended 31 December 2005 | 27,930 | 27,805 | 112,917 | 168,652 |

Certain prior year revenues have been reclassified within geographic segments to conform with current year presentation.

*The amounts are expressed in thousands of US dollars*

**Assets by region**

| | | | | |
|---|---|---|---|---|
| **Year ended 31 December 2006** | | | | |
| Segment assets | 41,559 | 19,669 | 106,027 | 167,255 |
| Unallocated assets | | | | 184,911 |
| Total assets | | | | 352,166 |
| **Year ended 31 December 2005** | | | | |
| Segment assets | 24,289 | 9,121 | 83,958 | 117,368 |
| Unallocated assets | | | | 64,002 |
| Total assets | | | | 181,370 |

Segment assets consist primarily of receivables and accrued revenue. The majority of intellectual property is considered a corporate asset. Management do not consider it appropriate to allocate cash, deferred expenses and tangible fixed assets by geographical segment.

Capital expenditure, depreciation and amortisation are not allocated to geographical segments.

## 20. Personnel costs

| | **2006** | **2005** |
|---|---|---|
| Salary, bonuses and commissions | 87,619 | 64,878 |
| Termination payments | 505 | 681 |
| Social charges | 9,339 | 7,091 |
| Defined contribution and defined benefit pension costs (note 21) | 3,047 | 3,166 |
| Cost of employee share option scheme | 5,132 | 3,843 |
| Other personnel costs | 5,317 | 4,320 |
| | 110,959 | 83,979 |

Included in the personnel costs shown above, are the following amounts in respect of remuneration for key management personnel:

| | **2006** | **2005** |
|---|---|---|
| Key management personnel of Temenos Group AG | | |
| - short-term employee benefits | 9,747 | 5,107 |
| - post-employment benefits | 301 | 219 |
| - share-based payment | 4,016 | 2,148 |
| | 14,064 | 7,474 |
| Non-executive directors | | |
| - short-term employee benefits | 240 | 180 |

## 21. Pensions

Throughout the world the Group maintains defined contribution plans for its employees under which the relevant contributions are expensed as they accrue. The aggregate cost of these plans, many of which are state-sponsored, in the year 31 December 2006, amounted to US$ 2.3 million (2005: US$ 2.6 million). Generally, the Group does not maintain, nor is it committed to support, any defined benefit plans for its current or former employees.

*The amounts are expressed in thousands of US dollars*

TEMENOS Headquarters SA and TEMENOS Suisse SA each have a funded contributory defined benefit pension plan covering their employees. The pertinent details relating to these pension plans are set out below:

**The amounts recognised in the balance sheet at 31 December are as follows:**

| | **2006** | **2005** |
|---|---|---|
| Present value of funded obligations | 7,271 | 6,822 |
| Fair value of plan assets | (8,678) | (7,737) |
| | (1,407) | (915) |
| Unrecognised actuarial gains | 1,049 | 671 |
| Assets not recognised | - | 29 |
| Net asset in the balance sheet | (358) | (215) |
| Amounts in the balance sheet: | | |
| liabilities | - | - |
| prepaid asset | 358 | 215 |
| Net asset in the balance sheet | 358 | 215 |

**The movement in the defined benefit obligation over the year is as follows:**

| | **2006** | **2005** |
|---|---|---|
| As at 1 January | 6,822 | 6,710 |
| Current service cost | 709 | 632 |
| Interest cost | 209 | 197 |
| Contributions by plan participants | 563 | 564 |
| Actuarial gains | (116) | (265) |
| Exchange differences | 537 | (993) |
| Benefits paid | (1,453) | (23) |
| As at 31 December | 7,271 | 6,822 |

**The movement in the fair value of plan assets over the year is as follows:**

| | **2006** | **2006** |
|---|---|---|
| As at 1 January | 7,737 | 6,820 |
| Actual return on plan assets | 468 | 662 |
| Exchange differences | 619 | (1,050) |
| Employer contributions | 744 | 764 |
| Employee contributions | 563 | 564 |
| Benefits paid | (1,453) | (23) |
| As at 31 December | 8,678 | 7,737 |

**The amounts recognised in the income statement are as follows:**

| | **2006** | **2005** |
|---|---|---|
| Current service cost | 709 | 632 |
| Interest cost | 209 | 197 |
| Expected return on plan assets | (262) | (222) |
| Amortisation of net gain | (4) | - |
| Assets not recognised | (32) | 29 |
| Total costs included in personnel costs and external consultants | 620 | 636 |

*The amounts are expressed in thousands of US dollars*

**Principal weighted average actuarial assumptions at the balance sheet date:**

| | 2006 | 2005 |
|---|---|---|
| Discount rate at 31 December | 3.25% | 3.25% |
| Expected return on plan assets at 31 December | 3.25% | 3.25% |

**Plan assets are comprised as follows:**

| | | |
|---|---|---|
| **2006** | | |
| Equity | 2,346 | 27% |
| Debt | 4,163 | 48% |
| Other | 2,169 | 25% |
| | 8,678 | 100% |
| **2005** | | |
| Equity | 2,644 | 34% |
| Debt | 3,503 | 45% |
| Other | 1,590 | 21% |
| | 7,737 | 100% |

The expected return on plan assets was determined by considering the expected returns available on the assets underlying the current investment policy. Expected yields on fixed interest investments are based on gross redemption yields as at the balance sheet date. Expected returns on equity and property investments reflect long-term real rates of return experienced in the respective markets.

Expected contributions to post-employment benefit plans for the year ending 31 December 2007 are US$ 778 thousand.

## 22. Expenses by nature

| | 2006 | 2005 |
|---|---|---|
| Third party licences and commissions | 10,050 | 3,978 |
| Personnel costs and external consultants | 132,517 | 99,818 |
| Depreciation and amortisation | 9,767 | 11,180 |
| Travel expenses | 18,747 | 17,669 |
| Rent and other occupancy costs | 10,481 | 9,175 |
| Marketing and other professional costs | 7,374 | 5,591 |
| Other costs | 9,610 | 9,335 |
| Capitalised expenditure | (15,594) | (10,841) |
| | 182,952 | 145,905 |

The depreciation and amortisation charge is analysed as follows:

| | Depreciation of tangible fixed assets (note 9) | Amortisation of other intangible assets (note 10) | Amortisation of capitalised development costs (note 10) | Aggregate amount charged to operations |
|---|---|---|---|---|
| Year ended: | | | | |
| 31 December 2006 | 3,091 | 2,360 | 4,316 | 9,767 |
| 31 December 2005 | 2,998 | 4,311 | 3,871 | 11,180 |

The amortisation charge for purchased goodwill is included on a separate line on the face of the income statement. The amortisation charge for purchased copyrights and capitalised development costs is included in the profit and loss statement in the line "software development". The depreciation charge for tangible fixed assets and the amortisation charge for computer software is allocated to the respective operating costs in the profit and loss statement based on headcount.

## 23. Financial instruments

**Derivative financial instruments**

The Group enters into forward foreign currency exchange contracts to hedge a portion of the Group's operating costs. The loss on contracts that qualified as cash flow hedges under IAS 39 generated losses for the year of US$ 905 thousand (2005: profits of US$ 156 thousand). This loss has been offset against operating expenses. The gain on contracts that did not qualify as hedges under IAS 39 is recorded as "fair value gain (loss) from financial instruments" and amounts to US$ 5,354 thousand (2005: loss of US$ 736 thousand).

The fair value contracts outstanding at 31 December 2006 are as follows :

Forward foreign currency exchange contracts for 2007 and 2008

| | Assets |
|---|---|
| Qualifying as cash flow hedges | 134 |
| Held at fair value through profit and loss | 4,753 |

The net fair value gain on open forward foreign exchange contracts which mostly hedge anticipated future foreign currency operating costs will be transferred from reserves to the income statement in the period these costs are incurred.

**Financial instrument related expenses**

In March 2005 an arrangement was signed with a major international bank for a loan facility (as described in note 13). Legal and set up fees relating to the arrangement of US$ 305 thousand have been expensed in 2006.

## 24. Earnings per share calculations

**Basic**

Basic earnings per share is calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year, excluding ordinary shares purchased by the Company and held as treasury shares (note 15).

| | **2006** | **2005** |
|---|---|---|
| Profit attributable to equity holders of the Company | 34,445 | 18,257 |
| Weighted average of common shares outstanding during the year (in thousands) (note 15) | 56,980 | 55,025 |
| Basic earnings per share (US$ per share) | 0.60 | 0.33 |

**Diluted**

Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. The Group has two categories of dilutive potential ordinary shares: convertible debt and share options. The convertible debt is assumed to have been converted into ordinary shares and the net profit is adjusted to eliminate the interest expense to the extent that this would be dilutive. For 2006 the assumed conversion of the convertible debt would increase the profit by US$ 3,462 thousand and increase the equivalent common shares by 5,718 thousand. This would be anti-dilutive and therefore the conversion of the convertible debt has been excluded from the calculation. For the share options a calculation is performed to determine the number of shares that could have been acquired at fair value (determined as the average annual market share price of the Company's shares) based on the monetary value of the rights attached to outstanding share options.

| | 2006 | 2005 |
|---|---|---|
| Profit attributable to equity holders of the Company | 34,445 | 18,257 |
| Weighted average of common shares outstanding during the year (in thousands) (note 15) | 56,980 | 55,025 |
| Equivalent common shares relating to outstanding share options and share warrants (in thousands) (note 15) | 3,316 | 2,774 |
| Aggregate number of equivalent common shares for purposes of calculating the diluted earnings per share (in thousands) | 60,296 | 57,799 |
| Diluted earnings per share (US$ per share) | 0.57 | 0.32 |

## 25. Commitments and contingencies

The Group has obligations under operating leases relating to office premises and leased equipment. The leases have varying terms, escalation clauses and renewal rights. Operating lease expenses relating to office premises for the year ended 31 December 2006 amounted to US$ 8.1 million (2005: US$ 7.6 million) and operating lease expenses relating to leased equipment were US$ 1.5 million (2005: US$ 1.6 million).

As at 31 December 2006 the future minimum lease payments to which the Group was committed under non-cancellable operating leases were as follows:

| | 2006 | 2005 |
|---|---|---|
| No later than 1 year | 8,716 | 8,254 |
| Later than 1 year and no later than 5 years | 18,626 | 18,686 |
| Later than 5 years | 9,307 | 8,349 |
| Total | 36,649 | 35,289 |

The Group has contingent liabilities in respect of bank and other guarantees and is also involved in various lawsuits, claims, investigations and proceedings incidental to the normal conduct of its operations. These matters mainly include the risks associated with personnel litigation, tax claims and contractual disputes. Management believes that these contingencies will not have a material adverse effect on the business, financial condition or results of the Group. Information relating to provisions recorded in the financial statements is included in note 26.

## 26. Provisions for liabilities and charges

| | Legal claims | Onerous lease | Total |
|---|---|---|---|
| At 1 January 2006 | 194 | 122 | 316 |
| Charged to income statement | 33 | 21 | 54 |
| Foreign currency exchange differences | 11 | 18 | 29 |
| Used during the year | (79) | - | (79) |
| 31 December 2006 | 159 | 161 | 320 |

**Legal claims**
The amounts represent provisions for certain legal claims brought against the Group. The outcome of the legal disputes, and the timing of any payments, is uncertain. In the directors' opinion the outcome of these legal claims will not give rise to any significant loss beyond the amounts provided at 31 December 2006.

**Onerous lease**
During 2004 one of the Group's subsidiaries sublet a property to a third party. The difference between the amount that will be received from the tenant, and the amount that will be paid to the landlord, has been fully provided.

### 27. Related party transactions and balances

Remuneration of executive and non-executive directors is described in note 20. Equity compensation for executive and non-executive directors granted in the form of stock options is described in note 18.

In December 2003 an office building that is leased by TEMENOS Headquarters SA was acquired by one of the directors and major shareholders of TEMENOS Group AG. The annual rent payable in respect of this lease is CHF 475 thousand, and the terms and conditions of the lease agreement conform to standard market practices.

Since December 1999 TEMENOS Suisse SA has leased an office building that is owned by a company which is managed and controlled by one of the major shareholders and directors of TEMENOS Group AG. The annual rent payable in respect of this lease is CHF 360 thousand, and the terms and conditions of the lease agreement conform to standard market practices.

As at 31 December 2006 loans to key management personnel of US$ 259 thousand (2005: US$ 72 thousand) were outstanding. The loans are expected to be repaid in cash during 2007.

During the year one of the major shareholders and directors of TEMENOS Group AG agreed to contribute US$ 400 thousand to the 2006 running costs of the TEMENOS boat.

There were no other large or significant transactions with related parties during the year ended 31 December 2006.

### 28. Post balance sheet events

There are no reportable post balance sheet events.

# TEMENOS Group AG

Unconsolidated Financial Statements

31 December 2006

and Report of the Statutory Auditors thereon

PRICEWATERHOUSECOOPERS

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## REPORT OF THE STATUTORY AUDITORS TO THE GENERAL MEETING OF TEMENOS GROUP AG

As statutory auditors, we have audited the accounting records and the financial statements (balance sheet, income statement and notes) on pages 63 to 65 of TEMENOS Group AG for the year ended 31 December 2006.

These financial statements are the responsibility of the board of directors. Our responsibility is to express an opinion on these financial statements based on our audit. We confirm that we meet the legal requirements concerning professional qualification and independence.

Our audit was conducted in accordance with Swiss Auditing Standards, which require that an audit be planned and performed to obtain reasonable assurance about whether the financial statements are free from material misstatement. We have examined, on a test basis, evidence supporting the amounts and disclosures in the financial statements. We have also assessed the accounting principles used, significant estimates made and the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the accounting records and financial statements comply with Swiss law and the company's articles of incorporation.

We recommend that the financial statements submitted to you be approved.

PricewaterhouseCoopers SA

M. Foley S. Harvey

Auditor in charge

Geneva, 27 February 2007

# TEMENOS Group AG

balance sheet

*The amounts are expressed in thousands of Swiss Francs*

*as at 31 December*

| | 2006 | 2005 |
|---|---|---|
| **Assets** | | |
| ***Current assets*** | | |
| Other receivables | **23** | 14 |
| Treasury shares | **3,627** | 186 |
| Liquid funds | **1,603** | 62 |
| *Total current assets* | **5,253** | 262 |
| ***Non-current assets*** | | |
| Investments in, and advances to, subsidiaries (note 2) | **458,548** | 458,248 |
| Receivable from other Group entities | **10,149** | 2,248 |
| *Total non-current assets* | **468,697** | 460,496 |
| *Total assets* | **473,950** | 460,758 |
| **Liabilities and shareholders' equity** | | |
| ***Current liabilities*** | | |
| Trade payables | **105** | 36 |
| Accrued expenses | **26** | 26 |
| Tax payable | **293** | 6 |
| *Total current liabilities* | **424** | 68 |
| ***Non-current liabilities*** | | |
| Payable to other Group entities | **4,067** | 8,573 |
| *Total non-current liabilities* | **4,067** | 8,573 |
| ***Shareholders' equity*** | | |
| Share capital (note 3) | **289,207** | 276,751 |
| Share premium (note 4) | **177,613** | 175,326 |
| Reserve for treasury shares (note 4) | **3,627** | 208 |
| Retained deficit | **(988)** | (168) |
| *Total shareholders' equity* | **469,459** | 452,117 |
| *Total shareholders' equity and liabilities* | **473,950** | 460,758 |

## income statement

*for the year ended 31 December*

| | 2006 | 2005 |
|---|---|---|
| Expenses associated with the maintenance of the Register of Shareholders and other related costs | **(520)** | **(149)** |
| ***Net loss before taxation*** | **(520)** | **(149)** |
| Taxation | **(300)** | - |
| ***Net loss after taxation*** | **(820)** | (149) |
| Retained deficit at beginning of year | **(168)** | (19) |
| ***Retained deficit at end of the year*** | **(988)** | (168) |

*The amounts are expressed in thousands of Swiss Francs*

## 1. Legal status and principal activities

TEMENOS Group AG ("the Company") was incorporated in Glarus, Switzerland on 7 June 2001 as a stock corporation (Aktiengesellschaft). Since 26 June 2001 the shares of TEMENOS Group AG have been publicly traded on the SWX Swiss Exchange.

TEMENOS Group AG succeeded TEMENOS Holdings NV in the role of the ultimate holding company of the Group but is not otherwise engaged in trading, financing, investing activities, except as the holder of all the issued and outstanding shares of TEMENOS Holdings NV, TEMENOS Headquarters SA, TEMENOS Suisse SA, T-TCB SA, T-TFR SA, T-jBASE SA and IT Services Limited.

## 2. Investments in, and advances to, subsidiaries

The investments of TEMENOS Group AG represent the shares of its four wholly owned subsidiary companies, as follows:

| | 2006 | 2005 |
|---|---|---|
| TEMENOS Holdings NV, Netherlands Antilles (holding and licensing company) | | |
| 40,105 shares of a nominal value of US$ 1 each, at cost | 200,522 | 200,522 |
| Advances for the acquisition of new shares | 249,052 | 249,052 |
| TEMENOS Headquarters SA, Switzerland (management company) | | |
| 1,000 shares of a nominal value of CHF 100 each, at cost | 5,625 | 5,625 |
| TEMENOS Suisse SA, Switzerland (services company) | | |
| 15,000 shares of a nominal value of CHF 500 each, at cost | 2,948 | 2,948 |
| T-TCB SA, Switzerland (licensing company) | | |
| 1,000 shares of a nominal value of CHF 100 each, at cost | 100 | - |
| T-TFR SA, Switzerland (licensing company) | | |
| 1,000 shares of a nominal value of CHF 100 each, at cost | 100 | - |
| T-jBASE SA, Switzerland (licensing company) | | |
| 1,000 shares of a nominal value of CHF 100 each, at cost | 100 | - |
| I.T. Services Limited, Cyprus (dormant) | | |
| 100 shares of a nominal value of CY£1 each, at cost | 101 | 101 |
| | 458,548 | 458,248 |

## 3. Share capital

As at 31 December 2006 the issued and outstanding shares of TEMENOS Group AG, the ultimate holding company of the TEMENOS GROUP, comprised 57,841,421 common shares of a nominal value of CHF 5 each.

The changes in the number of issued and outstanding shares, in the year ended 31 December 2006, are summarised below:

| | 2006 | | 2005 | |
|---|---|---|---|---|
| | number | Nominal value in CHF | number | Nominal value in CHF |
| Authorised share capital issued | 51,473,309 | 257,366 | 51,473,309 | 257,366 |
| Conditional or contingent capital issued | 6,368,112 | 31,841 | 3,876,883 | 19,385 |
| Total number of TEMENOS Group AG shares issued, as at 31 December | 57,841,421 | 289,207 | 55,350,192 | 276,751 |

The amounts are expressed in thousands of Swiss Francs

| The shares issued by the Company during the year are set out below: | **2006 number** | **2005 number** |
|---|---|---|
| Total number of TEMENOS Group AG shares issued, as at 1 January | 55,350,192 | 54,952,435 |
| Shares issued and alloted in relation to acquisitions | 441,084 | - |
| Shares issued and alloted on exercising of employee share options | 2,050,145 | 397,757 |
| Total number of TEMENOS Group AG shares issued, as at 31 December | 57,841,421 | 55,350,192 |

It should be noted that the above tables includes treasury shares which had not been allotted to third parties. As at 31 December 2006 the number of treasury shares held by the Group amounted to 185,973 (2005: 44,342). A reserve has been created for these Treasury shares. These treasury shares are held for resale or for alloting to members of the TEMENOS Employee Share Option Scheme at the time that they exercise their options. During the year the company acquired 1,103,000 shares at market value and disposed of 957,111 shares to option holders at market value.

TEMENOS Group AG also has authorised and conditional capital, comprising:

| | |
|---|---|
| authorised shares that may be issued in the context of acquisitions (available to the Board until 23 May 2008) | 26,510,243 |
| conditional shares that may be issued on the exercise of employee share options | 10,259,292 |
| conditional shares that may be issued in conjunction with financial instruments (of which 9,000,000 are reserved for the Convertible bond) | 13,930,680 |

The only holdings of 5% or more in the issued share capital of the Company are as follows:

| | |
|---|---|
| George Koukis | 16.9% |
| Schroders plc | 8.1% |
| Fidelity International Limited | 5.2% |

## 4. Share premium

The share premium is reported after:

- deduction of expenses, amounting to CHF 201 thousand (2005: CHF 28 thousand), which were incurred in conjunction with the issuance of new shares

- deduction for reserve for treasury shares of CHF 3,627 thousand (2005: CHF 208 thousand)

## 5. Treasury shares

TEMENOS Group AG holds 185,973 shares at 31 December 2006 intended for resale or for alloting to members of the TEMENOS Employee Share Option Scheme at the time that they exercise their options (2005: 40,084).

## 6. Contingent liabilities

TEMENOS Group AG has provided certain guarantees to third parties, primarily in favour of TEMENOS Holdings NV, in the context of credit facilities placed at the disposal of the latter for a total of US$ 30 million. Management believes that these guarantees are unlikely to be activated.

# Information for Investors

### CAPITAL STRUCTURE

The share capital is divided into 57.9 million registered shares of a par value of CHF 5.

### APPROPRIATION OF PROFITS

TEMENOS does not expect to pay dividends in the foreseeable future.

### REGISTRARS

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### ANNUAL GENERAL MEETING

01 June 2007

Development of the TEMENOS share price

### STATISTICS ON TEMENOS SHARES

| Registered shares of CHF 5 nominal | 2006 |
|---|---|
| Sector: | Technology/Software |
| Market Segment: | SWX Main Market |
| Index Member: | SPI |
| Swiss Security No: | 124 5391 |
| ISIN No: | CH0012453913 |
| Symbol: | TEMN |
| Number of shares | 57,841,421 |
| Market price high/low (CHF) | 21.10/10.70 |
| Market price 31.12.2005 (CHF) | 12.80 |
| Market price 31.12.2006 (CHF) | 20.65 |
| Market capitalisation high/low (CHF m) | 1,220/619 |
| Share capital nominal value at 31.12.2006 (CHF m) | 289 |

| Key Figures per Share | |
|---|---|
| Basic earnings per share (in US$) | 0.60 |
| Diluted earnings per share (in US$) | 0.57 |
| Consolidated shareholders' equity (US$ m) | 135.8 |
| Consolidated shareholders' equity per share (US$) | 2.38 |

| Major shareholders (>5%) of TEMENOS Group AG* | |
|---|---|
| George Koukis* | 16.86% |
| Schroders plc** | 8.08% |
| Fidelity International Limited | 5.21% |

** as of 1 March 2007*

*** deposited shares (art. 689d CO) - as of 31 December 2006*

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