

ANNUAL REPORT 2005

Key Figures Overview of the *aap* Group of Companies

	1.1.-12.31.2005	1.1.-12.31.2004
● Sales	€13,367K	€11,530K
● Total Output	€15,634K	€12,571K
● Special Factors*	€0	€2,544K
● Net Profit/Loss	€655K	€-140K
● Operating Income	€860K	€-315K
● EBITDA	€2,326K	€1,203K
● EBIT	€855K	€-316K
● EBT	€1,076K	€-1,260K
● DVFA/SG Earnings	€655K	€-561K
● DVFA/SG Earnings per Share	€0.04	€-0.07
● DVFA/SG Cash Earnings	€2,153K	€833K
● DVFA/SG Cash Earnings per Share	€0.14	€0.10

* Extraordinary 2004 result, that is not included in the figures stated

Selected Balance sheet data

	Dec. 31,2005	Dec. 31,2004
● Non-current Assets	€14,134K	€10,761K
● Current Assets	€10,947K	€9,686K
● Total Assets	€25,081K	€20,447K
● Shareholder's Equity	€19,366K	€15,533K
● Non-current Liabilities	€1,308K	€322K
● Current Liabilities	€4,407K	€4,592K
● Equity Ratio	77%	76%
● Employees	139	109

T€ corresponds to €K.

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ANNUAL REPORT 2005

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Bruke Seyoum Alemu

Oliver Bielenstein

Foreword by the Board of Management

Ladies and Gentlemen,
Dear Shareholders,
Dear Employees and Business Partners,

aap has delivered on the Management Board's March 2005 "double-digit growth and return to profitability" forecast. The year behind us was a successful year of realignment, initiating changes and reorganizing the company. We are proud of it.

In 2005 *aap* was able to set many crucial courses that in the future will enable the company to achieve sales and earnings growth well above the market level, as was demonstrated impressively by the sales figures for the first quarter of 2006.

After the Group's financial reorganization in 2004, our aim in 2005 was to initiate a focus on *aap*'s strengths in developing and making biomaterials, bone cements and osteosynthesis products and to improve marketing competence. As underscored by the financial statements for 2005 and the *aap* share price trend, we are well on our way to doing so.

Along with the successful establishment of new development, production and distribution partnerships with Biomet and Heraeus in bone cements and cementing techniques, a sector in which *aap* is one of the world's leading providers, *aap* was able to expand into the innovative biomaterials sector (bone cements, infection care and bone & tissue regeneration) by means of two acqui-

sitions (*Osartis*, *ADC*). Both companies are now successfully integrated and will contribute in 2006 toward the growth and success of the *aap* Group.

In the course of the September 2005 capital increase, which was placed successfully and oversubscribed, to finance the acquisitions and the expansion of existing business, *aap* was able to welcome well-known institutional investors as new shareholders.

It goes without saying that all of this would have been inconceivable without the commitment, motivation and performance disposition of *aap*'s employees. We owe them all our special thanks.

Uwe Ahrens, *aap*'s founder and long-time CEO, stepped down from the Management Board in September 2005. He retains his ties with the company as a major shareholder, however, and in May 2006 his name will be put forward to the annual meeting of shareholders for election to the Supervisory Board. Here too we should once more like to express our grateful thanks to him for his long years of service to the company.

We must also thank our shareholders and business partners for the confidence they have shown in us, and we look forward to further good cooperation.

Oliver Bielenstein
Vorstand

Bruke Seyoum Alemu
Vorstand

Lines of Business

6

aap Implantate AG

aap has set itself the task of harnessing the constantly expanding knowledge potential in medicine and technology to ensure, in close partnership with physicians, the best possible patient care. Our central objective is to restore the patient's mobility, to maintain it on a long-term basis and thereby to ensure a crucial part of the patient's quality of life. The rising life expectancy and ageing of the population confront us with serious challenges, with the focus on pain-free mobility in sporting and leisure activities up to old age and on swift healing times by means of as little additional intervention as possible that harms the body.

In addition, aap fulfills the requirements of hospitals and clinics for all-inclusive single-source solutions that strictly observe case-based lump sum payments and contribute toward the efficacy and cost-efficiency of the healing process by means of consistently good quality and a balanced price-performance ratio.

Since 1990 aap's business activity has been aimed at developing, manufacturing and marketing innovative implants and biomaterials for trauma and joint reconstruction. Use is made of synergy effects between individual areas and products are bundled to constitute total solutions. The company's two divisions **Trauma & Joint Reconstruction** and **Biomaterials** each have research and development departments of their own and offer the physician both standard products at an optimal price and innovative products of high quality.

Within these divisions seven product areas are being developed successively and in a targeted manner. They are **trauma, shoulder, hip, knee and bone cements, infection care and bone & tissue regeneration**.

Biomaterials

Bone Cements

Bone & Tissue Regeneration

Infection Care



Trauma

Trauma



Joint Reconstruction

Shoulder

Hip

Knee



Trauma

8 **oap Implantate AG** In trauma segment, also known as osteosynthesis, broken bones are stabilized during healing by the insertion of usually temporary implants made of steel or titanium. Metal implants thereby become a supporting structure in treating fractures of bones that are subject to high stress. With a wide and balanced range of products that are tried and tested in the market we focus first and

foremost on treating fractures of the upper and lower extremities. The cannulated screw system, dynamic hip screw system and steel and titanium used in standard osteosynthesis are supplemented by special angle-stable plates for the upper and lower arm and by AcroPlate® for fractures of the shoulder joint.

Cannulated Screws

Cannulated screws support minimally invasive surgery. They can be pulled through the cavity by a guide wire and placed exactly on the bone fracture. Our cannulated screws are self-tapping and self-cutting, thereby ensuring a swift and safe course of the operation.

Angle-stable Plates

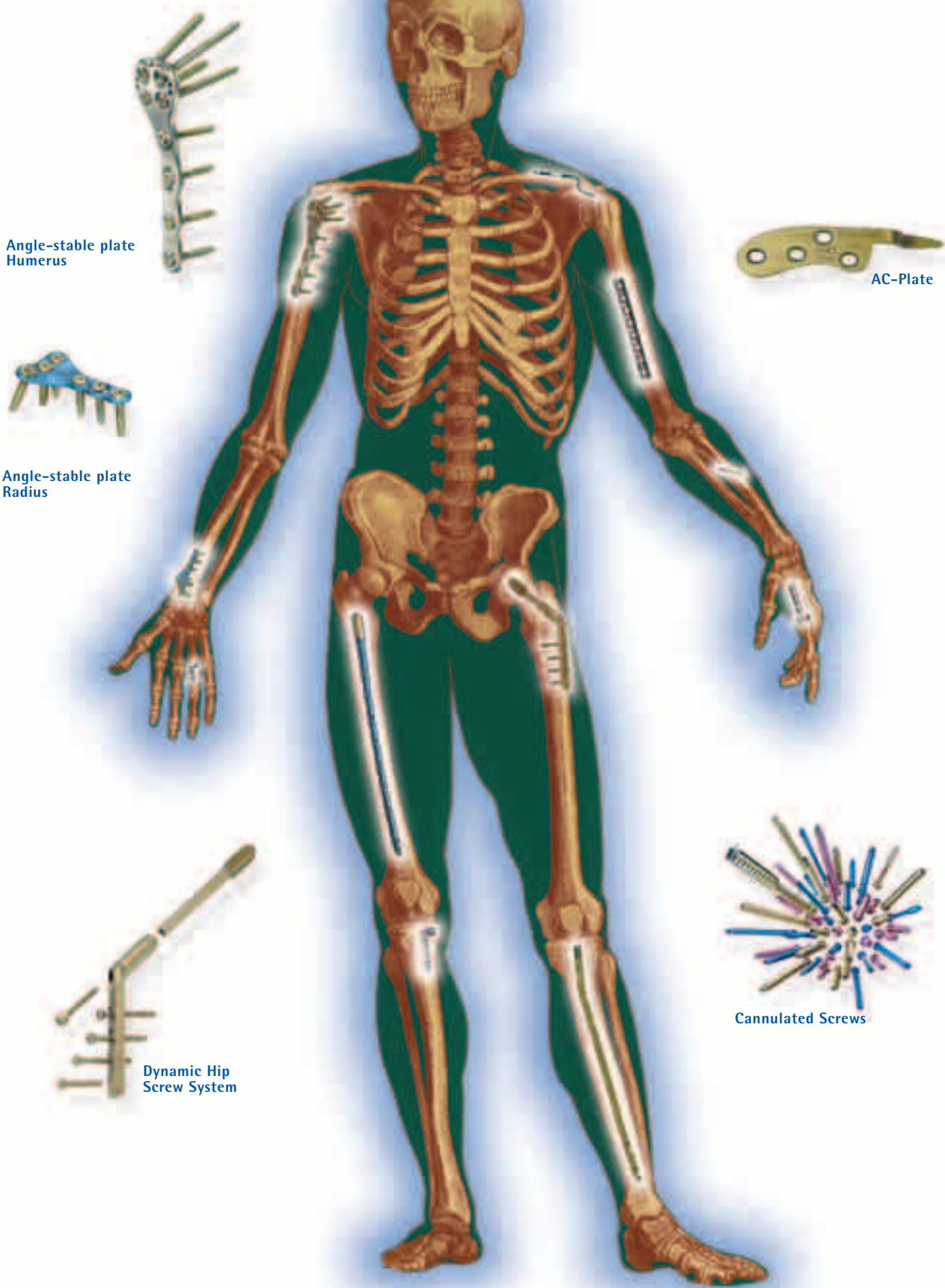
The angle-stable plates are anatomically pre-shaped and the angle-stable anchor in the bone incorporates a spherical thread. Plates are held in place by either angle-stable or ordinary screws as preferred. They can therefore be fixed permanently and firmly even in osteoporotic bone.

AC-Plate

This anatomically adjusted hook plate makes a safe and uncomplicated treatment of lateral clavicular fractures possible. Minimally invasive surgery and early patient mobility as a result of secure fixation of the injury are this implants decisive advantages.

Dynamic Hip Screw System

The dynamic hip screw system makes secure fracture stabilization and thereby facilitates swift patient mobilization possible. The safe and simple handling of the instrument kit helps to ensure an efficient course of the operation. Self-cutting screws reduce the number of essential work steps. Pressing the fractured parts together speeds up the healing process.



Angle-stable plate
Humerus

Angle-stable plate
Radius

AC-Plate

Dynamic Hip
Screw System

Cannulated Screws

Joint Reconstruction

10 **Our Joint Reconstruction division is specialized in endoprosthesis, i.e. joint replacement. Innovative prostheses that largely support natural motion sequences and**

oap Implantate AG

Shoulder

One of our most successful implants is the innovative trauma shoulder system. It offers a unique opportunity of fixation to the musculature and, as a consequence, good prospects of regaining the shoulder joint's form and function. On the basis of user experience over the past five years a successor model is being developed with modifications that will make the implant even safer.

Hip

The VarioFit® family takes up a central position in the hip product area. The modular VarioFit® endoprosthesis makes minimally invasive implantation possible and a combination of implants adjusted to the patient's individual anatomical situation. That sets new standards for the restoration of a hip geometry that is right for the patient. The patented raster cone gives the surgeon an unpre-

ensure full functionality over a long period are our objective here. In this area we concentrate on three joints – shoulder, hip and knee.

cedented intraoperative flexibility. The VarioFit® Classic completes the hip product area with a fixed cone for cost-effective patient care and a choice of hip sockets and femoral heads made of metal or ceramics and a standard instrument platform.

Knee

The Mebio knee is an endoprosthesis that has been tried and tested for years and provides a total joint replacement. Identical in construction to the Scan knee, the outstanding quality of which is documented by Swedish knee endoprosthesis register data, is a universal implant for the right and left knee that serves certain age and indication groups. Our claim is that we can, by means of an artificial joint, restore as far as possible in view of wear and tear the natural movement and functions of the knee and offer the physician optimal support with the aid of a tried and tested concept and a state-of-the-art instrument kit.



Trauma-Shoulder-System

Mebio Knee

VarioFit®

Biomaterials

12 The Biomaterials division comprises three product focal points: bone cements along with cementing techniques, bone and tissue regeneration, and drug carriers for infection care. Bone substitute materials in combination with stabilizing nails, plates and screws support the

aap Implantate AG

Bone Cements

Anchoring the implant in the bone is of decisive importance for growing service life expectations of endoprosthesis in the view of rising life expectancy. A very well prepared bone bed and high-quality cement are fundamental prerequisites for the success of a joint implantation. An optimal bone cement mixing system ensures safe and simple cement application during surgery and improves its mechanical properties.

In all three steps aap can assist the physician with cementing technique products. Marrow areas and bone surfaces can be cleansed easily and prepare the bone effectively for the insertion of a cemented prosthesis by means of the MicroAire® pulse lavage system. Bone cements such as Refobacin® Bone Cement R or Versabond™ (in both cases aap is the OEM manufacturer) can be mixed and applied easily and safely, saving time and material, with the aid of EASYMIX®. The EASYMIX® vacuum mixing technique leads to an improvement in bone integration and long-term stability of cements used with a view to long-life joint replacement.



healing of bone defects by providing a guide rail for bone-generating cells and by stimulating bone growth. In infected bone tissues as local drug carriers support the therapy by means of a targeted drug delivery.

Bone & Tissue Regeneration



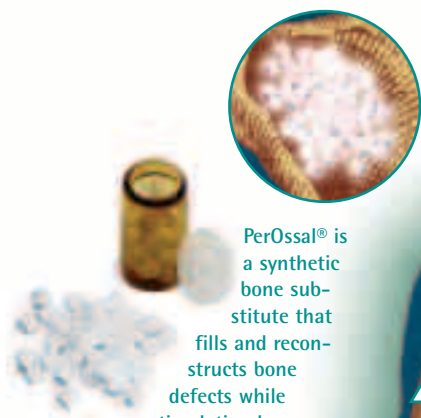
Innovative bone substitute materials for use in treating a wide range of bone defects make up the bone & tissue regeneration area.

The philosophy of our products is geared to the model that nature provides in respect of structural composition and ability to offer the body guiding structures for self-regeneration. Ostim® is a pasty bone substitute material based on nanotechnology that combines the speed and quality of healing of endogenous bone with the safety and availability of a synthetic material. Ease of use and perfect-fit filling of defects of various kinds make Ostim® a hitherto one-of-a-kind product. Should increased initial stability be required for bone defects in the load-bearing area, Cerabone® is a stable and at the same time porous ceramic matrix. Surrounding bone grows into this material, creating a firm bond and thereby restoring the patient's lost or damaged function.

Infection Care

Using bone substitute as both a bone substitute and a carrier substance for pharmaceutical drugs opens up even wider scope for use. PerOssal® for example, when used as a carrier for patient-matched antibiotics opens up new and individual treatment options in bone infection therapy.

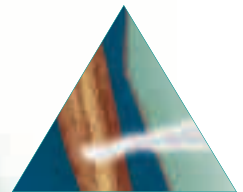




PerOssal® is a synthetic bone substitute that fills and reconstructs bone defects while stimulating bone healing and growth and can be charged individually as a carrier material for local antibiotic treatment.



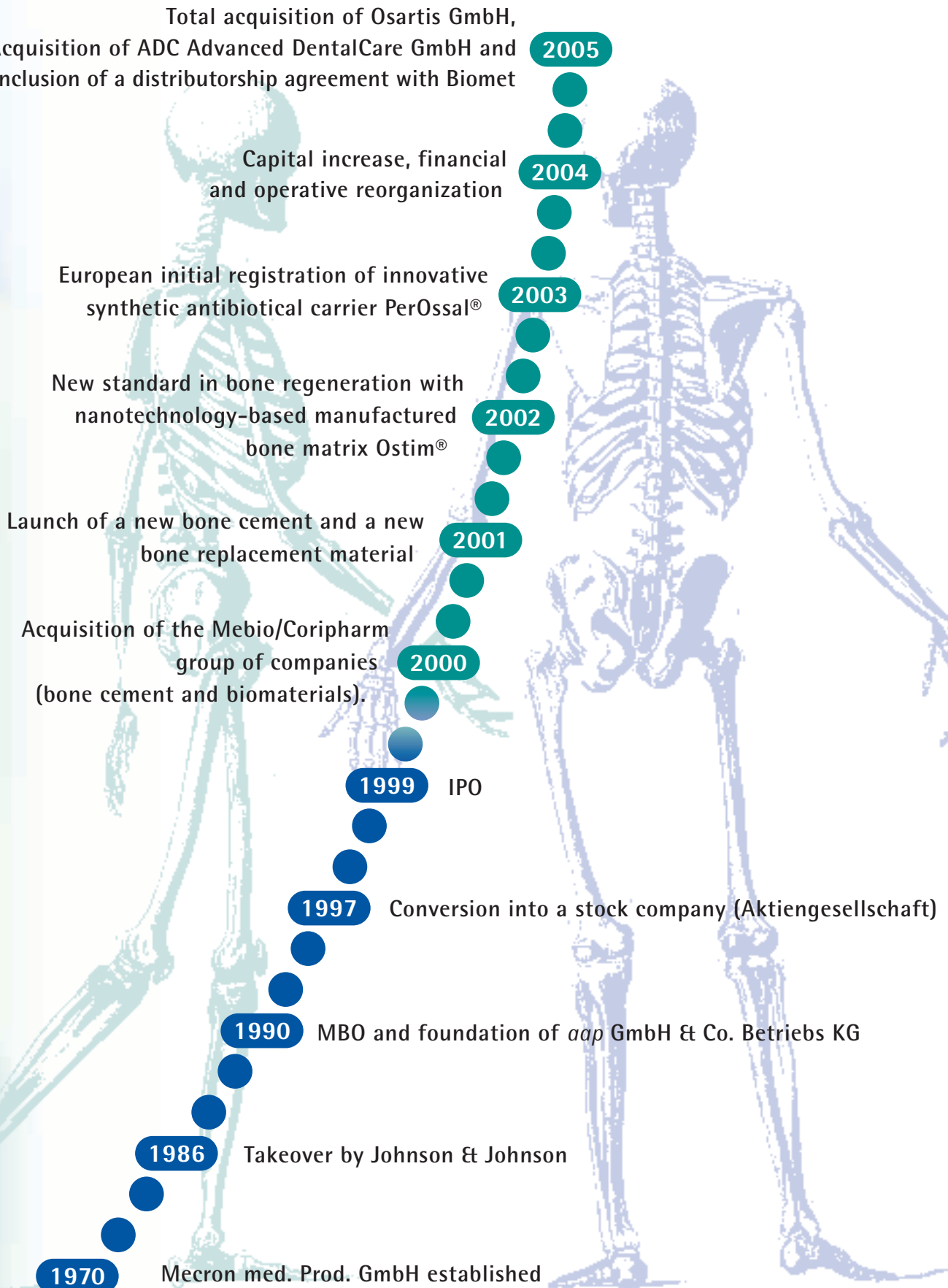
Cerabone® is a stable, non-resorbable bone matrix with a pore structure that is very similar to that of human bone. Available in different forms and sizes, this ceramic material serves as a splint or guide rail for natural bone growth to bridge defects. The result is a composite of ceramic and newly formed bone, filling bone defects and reconstruct them permanently.



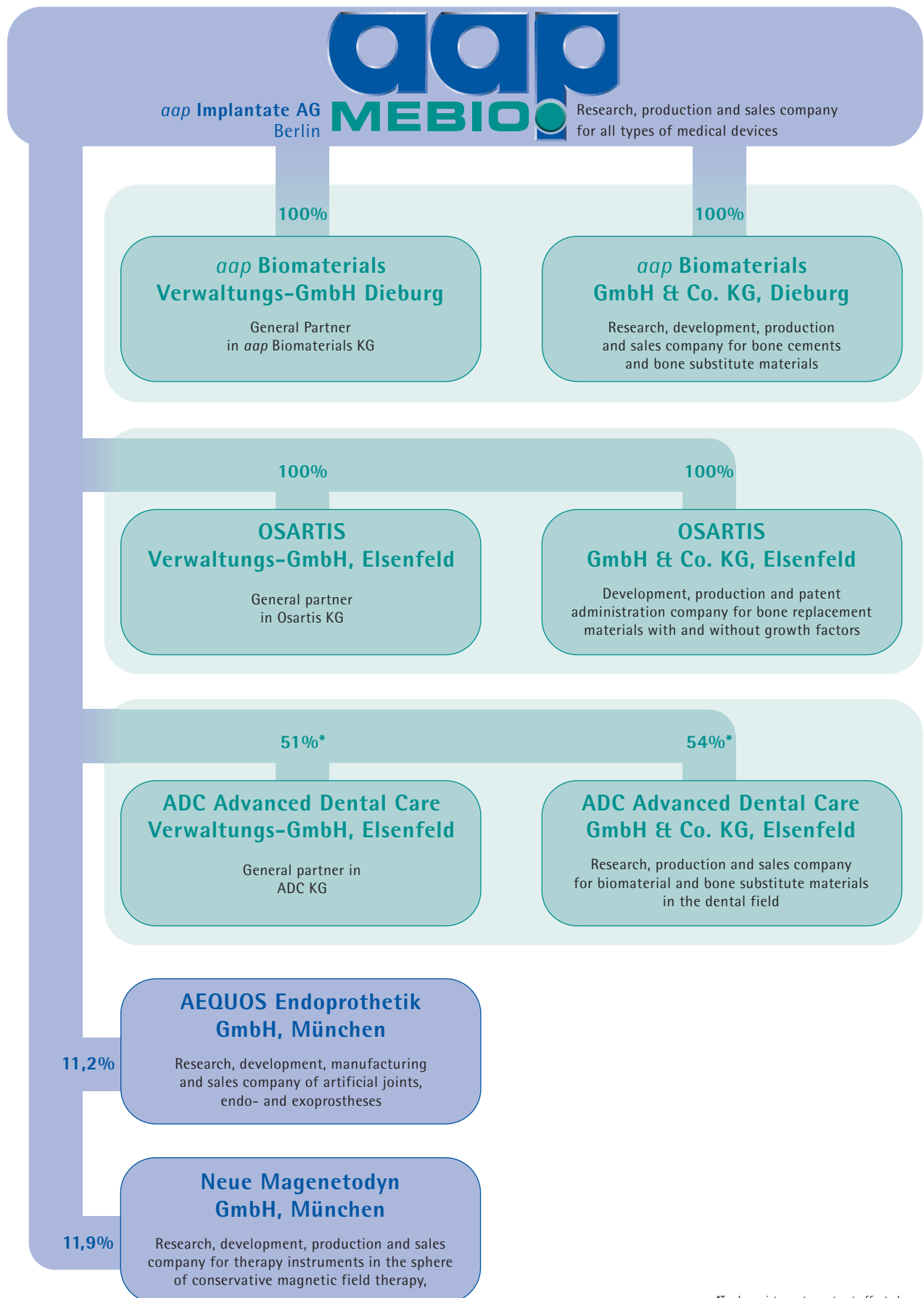
Ostim® is fully resorbable, in other words incorporated by the body and degraded. It supports and accelerates the process of natural bone regeneration and growth. The nanoparticulate particles of this fully synthetic material resemble nearly the bone mineral in size and chemical composition, thereby making possible a swift influx of bone-generating cells. Because of its paste-like quality, Ostim® can be injected directly as a perfect fit into the bone defect.



History



Group Structure Chart



*Trade register entry not yet effected

- aap Implantate AG on December 19, 2005 issued the following declaration of compliance: •

Declaration by the Management Board and Supervisory Board of aap Implantate AG on the recommendations of the Government Commission German Corporate Governance Code as per § 161 of the German Stock Corporation Act (AktG)

aap Implantate AG complies with the recommendations of the June 2, 2005 version of the German Corporate Governance Code (GCGC) as published by the Federal Ministry of Justice in the electronic edition of the Federal Gazette (Bundesanzeiger) on July 20, 2005 with the following exceptions:

The D&O policy taken out for the Management Board and Supervisory Board does not include a deductible (GCGC No. 3.8 Par. 2).

The Management Board does not currently have a chairman or a spokesman (GCGC 4.2.1 Sentence 1).

Retroactive changes to performance targets or comparison parameters are not ruled out in the overall compensation of the members of the Management Board. The Supervisory Board has not agreed to a possibility of limitation (cap) for extraordinary, unforeseen developments (GCGC 4.2.3 Sentence 2).

No age limit is specified for Management Board and Supervisory Board members (GCGC 5.1.2 Par. 2; GCGC 5.4.1 Sentence 2).

The Supervisory Board has not set up any committees (GCGC 5.3.1 and 5.3.2).

The compensation paid to members of the Supervisory Board does not include a performance-related component (GCGC 5.4.7 Par. 2).

Since its last declaration of conformity on December 13, 2004, aap Implantate AG has complied with the recommendations of the June 2, 2005 version of the German Corporate Governance Code (GCGC) as published by the Federal Ministry of Justice in the electronic edition of the Federal Gazette (Bundesanzeiger) on July 20, 2005 or, until July 20, 2005, the previous version, with the following exceptions:

The D&O policy taken out for the Management Board and Supervisory Board did not include a deductible (GCGC No. 3.8 Par. 2).

Since October 1, 2005 the Management Board has no longer had a chairman or spokesman (GCGC 4.2.1 Sentence 1).

Retroactive changes to performance targets or comparison parameters were not ruled out in the overall compensation of the members of the Management Board. The Supervisory Board did not agree to a possibility of limitation (cap) for extraordinary, unforeseen developments (GCGC 4.2.3 Sentence 2).

Compensation paid to members of the Management Board was not listed individually in the Notes to the Consolidated Financial Statements and not subdivided into a fixed payment, a performance-related component and components with a long-term incentive (GCGC 4.2.4).

No age limit was specified for Management Board and Supervisory Board members (GCGC 5.1.2 Par. 2 and 5.4.1 Sentence 2).

The Supervisory Board did not set up any committees (GCGC 5.3.1 and 5.3.2).

Compensation paid to members of the Supervisory Board did not include a performance-related component, and payments to members of the Supervisory Board were not listed individually and by component in the Notes to the Consolidated Financial Statements (GCGC 5.4.7 Par. 3).

The first interim report was not published within 45 days of the end of the reporting period (GCGC 7.1.2).

Not all relationships with shareholders considered to be "related parties" pursuant to the applicable accounting regulations were noted in the Consolidated Financial Statements (GCGC 7.1.5).

Berlin, December 19, 2005

The Supervisory Board



Jürgen Krebs
Chairman

The Management Board



Oliver Bielenstein
Member of the Board



Bruke Seyoum Alemu
Member of the Board

The Management Board, after consulting with the Supervisory Board, has issued the following notes on its exceptions to the recommendations of the German Corporate Governance Code (GCGC) as listed in the December 19, 2005 Declaration of Compliance:

● GCGC 3.8 ●

aap's D&O insurance is a group policy for management employees in Germany and abroad that does not include a deductible and covers third-party claims for negligence or deliberate dereliction of duty. Given that a deductible for negligence is not usual in other countries, *aap* chose to dispense with a deductible because it might otherwise make it more difficult to recruit top industry figures from other countries for the company's executive bodies.

● GCGC 4.2.1 ●

The Management Board does not currently have a chairman or a spokesman. The two directors manage the company jointly with equal areas of responsibility.

● GCGC 4.2.3 ●

Retroactive changes to performance targets or comparison parameters have not been ruled out so as to enable the Management Board to respond to economic changes. Given the company's economic development, a cap has so far been unnecessary.

● GCGC 5.1.2 and 5.4.1 ●

Specifying an age limit for members of executive bodies for one restricts the shareholders' right to elect representatives of their choice to the Supervisory Board. For another, it may prevent the Supervisory Board from appointing the best-qualified candidate to the Management Board. Furthermore, specifying an arbitrary age limit in compliance with the Code's recommendations is not considered to be appropriate.

● GCGC 5.3.1 and 5.3.2 ●

The three-member Supervisory Board did not set up committees. For a body with so few members to set up committees is not considered likely to boost efficiency.

● GCGC 5.4.7 ●

The compensation paid to members of the Supervisory Board consists only of fixed components and thereby ensures the supervisory body's independence in every respect.

Management Remuneration

Members of the Management Board receive a fixed annual remuneration and a share in *aap* Implantate AG's profits as stated in the annual financial statements subject to § 86 of the German Stock Corporation Act (AktG). Profit-sharing does not apply if profits are less than 4% of the year's sales revenues. For profits over and above 4% a share in profits is paid on the basis of a percentage scale. Each Management Board member also has a company car.

Management Board remuneration in fiscal 2005 totaled €388K and breaks down as follows:

Mr. Uwe Ahrens (until Sept. 30, 2005)

126.861 €

Mr. Bruke Seyoum Alemu

138.182 €

Mr. Oliver Bielenstein

123.059 €

Supervisory Board Remuneration

Members of the Supervisory Board are each paid, in addition to their expenses per meeting, €1,250 in remuneration. The chairman receives twice and the vice-chairman one and half times this amount.

Supervisory Board remuneration in fiscal 2005 totaled €28K and breaks down as follows:

Mr. Jürgen W. Krebs

€12,500

Mr. Rubino Di Girolamo

€9,375

Mr. Prof. Dr. Dr. med. Reinhard Schnettler

€6,250

Directors' Dealings

The following is a list of all trading in *aap* shares or financial instruments relating thereto, especially derivatives, in fiscal 2005 by persons holding management positions at *aap* and by persons closely related to them as specified in § 15a of the German Securities Trading Act (WpHG):

Date of transaction	Name of person subject to the disclosure requirement	Position	Type of transaction	Unit price paid in €	No. of units	Transaction volume in €
Sept. 19, 2005	Jürgen W. Krebs	Supervisory Board	Shares loan	free of charge	1,460,857	free of charge
Sept. 24, 2005	Uwe Ahrens	Management Board (until Sept. 30, 2005)	Capital increase by contribution in kind	1.6366	449,713	736,000
Sept. 27, 2005	Deepblue Holding AG	Closely associated to the Supervisory Board	Purchase	1.60	117,142	187,427.20
Sept. 27, 2005	Oliver Bielenstein	Management Board	Purchase	1.60	14,659	23,454.40
Sept. 27, 2005	Bruke Seyoum Alemu	Management Board	Purchase	1.60	8,480	13,568
Sept. 30, 2005	Uwe Ahrens	Management Board (until Sept. 30, 2005)	Sale	1.65	141,200	232,980
Sept. 30, 2005	Jürgen W. Krebs	Supervisory Board	Purchase	1.65	141,200	232,980

Shareholdings of the Boards

	2005	2004
Supervisory Board		
Jürgen W. Krebs	2,941,200	2,800,000
Rubino Di Girolamo	1,347,142	1,230,000
Prof. Dr. Dr. med.		
Reinhard Schnettler*	68,094	68,094
Management Board		
Uwe Ahrens		
(in his capacity as CEO		
until Sept. 30, 2005)		
	1,666,949	1,358,436
Bruke Seyoum Alemu	35,000	26,520
Oliver Bielenstein	484,548	469,889

* Prof. Dr. Dr. med. Reinhard Schnettler is entitled to a further 98,000 shares from the capital increase in kind in connection with the acquisition of shares in ADC.

MANAGEMENT REPORT 2005

by *aap* Implantate AG

Company and Group

Share and Stock Market

20 In this report on the state of the Group, use will be made of the terms *aap*, *aap* Group, Group or group of companies. Remarks on *aap* Implantate AG results will be described as such.

aap Implantate AG Company and Group Management Report 2005



aap Implantate AG Share Price Development

The *aap* Implantate AG share price improvement in 2005 reflected the company's economic recovery. The share price's high water mark for the year was €2.06 on March 31, 2005. Its low for the year was €1.24 on January 19, 2005. Once the financial year was over and the sales figures for 2005 were published this trend continued, and since February 2006 the share price has consistently been above €2.00.

The annual meeting of shareholders approved on June 10, 2005 a €449,713 capital increase implemented in August 2005. The new shares were issued for the then CEO, Uwe Ahrens, who in return waived a loan claim against *aap* Implantate AG.

In September 2005 a further capital increase involved the issue of 1,460,857 shares. From September 12 to 27, 2005 the new shares were offered for sale to existing shareholders at an issue price of €1.60 and a ratio of 21 to 2. In other words, each shareholder was entitled

to buy two new shares for every 21 old shares held. There was no rights trading and the new shares were entitled to profits for the full financial year 2005. The new shares were admitted to the Prime Standard segment of the Frankfurt Stock Exchange's regulated market on September 30, 2005. They are listed as Security No. 506 660 (ISIN DE0005066609) and have been traded on the stock market since October 6, 2005.

This capital increase was guaranteed in advance and in full by existing *aap* shareholders. All shares offered but not taken up were either acquired by this group, which included executive officers of the company, or allocated to institutional investors and employees.

Due to the capital the company accrued €2.3 million before transaction costs. It was spent partly on funding the acquisition of Osartis and ADC and on boosting existing business.

Group sales revenues improved by 16% on the year to €13.367 million (previous year: €11.530 million). Adjusted for the effect of the ADC and Osartis acquisitions, Group sales revenues would have totaled €13.098 million, equivalent to 14% year-on-year growth. *aap*'s earnings position also improved significantly on the year. EBITDA was up 93% to €2.326 million, taking the EBITDA margin to 17% (previous year: 10%). EBIT too was up on the year to €855K (previous year: €-316K).

2004 earnings before taxes included the effect of the 2004 balance sheet restructuring. Adjusted for this extraordinary effect, EBT improved from €-1.259 million in 2004 to €-1.081 million in the year under review.

Due to high existing loss carryovers, the *aap* Group paid hardly any taxes last financial year. Taxes shown in the consolidated financial statements are mainly the result of reducing previously capitalized deferred taxes on loss carryovers. Earnings after taxes were €655K (previous year: €-140K), and DVFA/SG earnings per share €0.04 (previous year: €-0.07).

The Group's operative cash flow (before investment and financing activity) increased by €2.851 million to €718K (previous year: €-2.133 million). The €1.950 million in positive cash flow achieved by means of financing activity consisted mainly of a capital increase in cash from the issue of 1.5 million shares in September and October 2005. Operative cash flow and cash flow from financing activity totaling €2.466 million were used for investments.

aap will for the foreseeable future be paying no dividends, given that cash and cash equivalent held are being invested fully in building up and enlarging the company.

aap Implantate AG is the *aap* Group's parent company. Within the Group there are currently four operative companies: *aap* Implantate AG, *aap* Biomaterials GmbH & Co. KG (previously Coripharm GmbH & Co. KG), Osartis GmbH & Co. KG, and ADC GmbH & Co. KG.

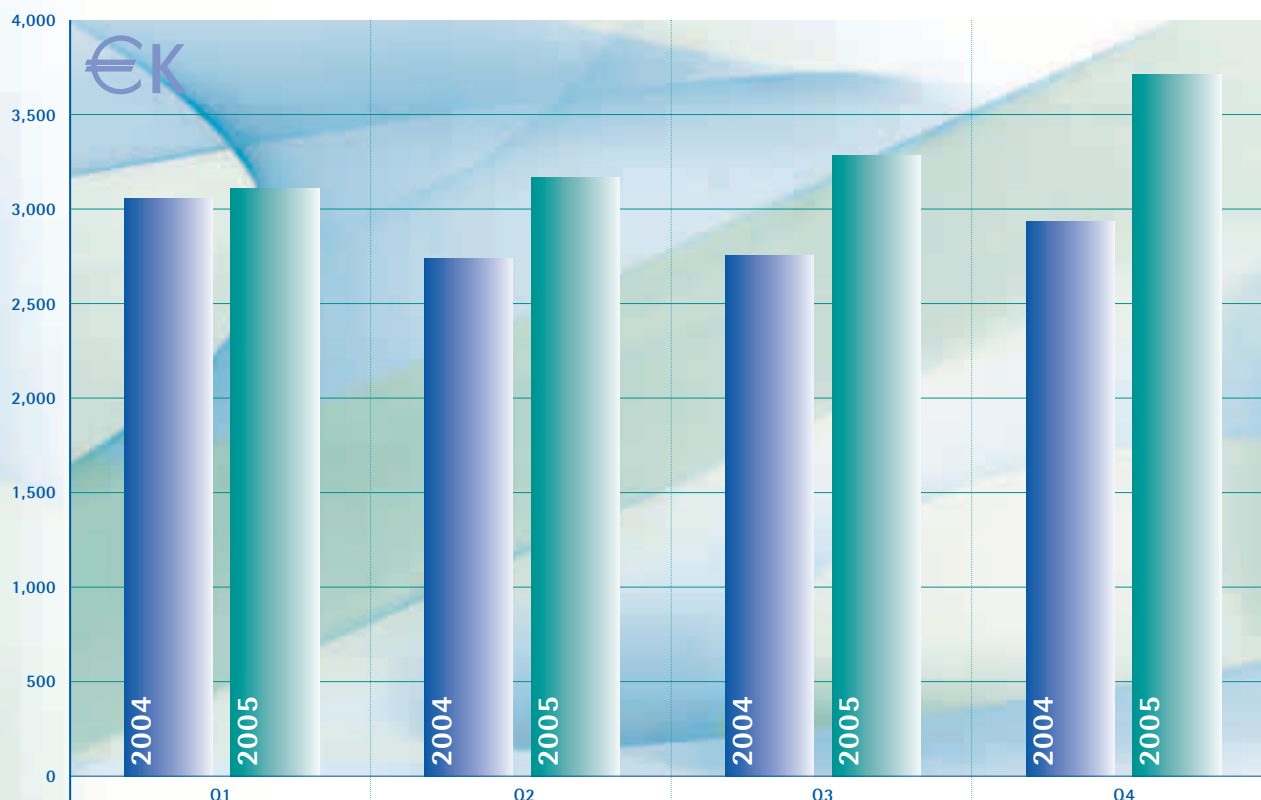
Where the structure of the consolidated financial statements is concerned please note that the consolidation entity has changed on the year due to two acquisitions. With effect from October 1, 2005 the remaining 51% holding in Osartis GmbH & Co. KG, Elsenfeld, and 54% of ADC GmbH & Co. KG was acquired. Since October 1, 2005 both companies have been incorporated accordingly in *aap*'s consolidated financial statements.

Osartis GmbH & Co. KG and ADC Advanced Dental Care GmbH & Co. KG are being integrated into *aap* Biomaterials GmbH & Co. KG, which in future will handle all of the Group's biomaterials activities (bone cements, infection care and bone & tissue regeneration).

Sales and Results Development at Group Level

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aap Implantate AG Company and Group Management Report 2005



Sales 2004 vs 2005 at Group Level by Quarters

In financial year 2005 *aap* sales were up 16% on the year to €13.367 million from €11.530 million. This positive trend was due mainly to organic growth but also to the two acquisitions, Osartis and ADC. With these acquisitions organic year-on-year growth would have been 14% and sales revenues would have totaled €13.098 million.

While sales in the first quarter of 2005 were only slightly up on the year due export sales delays and extraordinarily high sales in 2004, *aap* was able to report sales growth in all of the following reporting periods. In the fourth quarter alone, with the first-time consolidation of Osartis and ADC, *aap* achieved 27% year-on-year growth.

The increase in inventories of finished and unfinished products to €883K from €-172K the previous year is mainly due to new large OEM projects getting under way in both lines of business and a result of laying in stocks

and building up endoprosthesis, a line of business in which the customary consignment purchasing is highly capital-intensive.

Given *aap's* depth of value added in trauma/joint reconstruction, *aap* manufactures produce many of the instruments and instrument kits itself along with the tools and equipment to manufacture the implants. These costs, totaling €520K in the reporting period, are charged to capital in the balance sheet and will be depreciated over their likely service life.

In keeping with IFRS, *aap* as a research-intensive company also capitalizes development costs incurred for development projects that are on the brink of either completion or market launch (2005: €865K, 2004: €555K). The increase on 2004 is due to an enormous increase in development expenditure (on employees, external projects and prototypes) with a view to launching a number of new products over the next 18 months.

Other operating income totaling €1.473 million (previous year: €1.993 million) includes, in addition to investment and research grants and a revaluation of the AEQU-OS GmbH holding, the retransfer of reserves no longer needed and of claim waivers in connection with the full takeover of Osartis.

aap was able to reduce its **cost of materials** ratio by nearly 5%. This trend is set to continue in financial year 2006. In view of a significant improvement in the sales mix, with low-margin commercial sales being replaced by sales of products manufactured in-house and with a corresponding depth of value added, such as biomaterials, *aap* anticipates in the medium term a cost of materials ratio of less than 25%.

Personnel costs at *aap* continued to increase as planned, both organically and due to acquisitions, to €5.423 million from €4.059 million. With 35 new hirings in nearly all operative areas (sales, marketing, development OEM development and OEM production), taking the payroll to 139, the 35% personnel cost ratio will only be reduced slightly in 2006. In 2005, *aap* was able to recruit a large number of proven industry experts for the company and thereby to improve the Group's operative capability substantially.

The reduction in **other operating expenses** to €4.633 million from €4.937 million was due mainly to the end of special restructuring effects totaling €1.0 million that

were included under this heading in 2004. Sales-related rental and logistics expenses increased especially as a result of starting work on new OEM orders, expanding sales, and due to the acquisitions.

Depreciation of fixed assets was on a par with the previous year. In the years ahead *aap* anticipates falling ratios but a slight increase in depreciation in absolute terms.

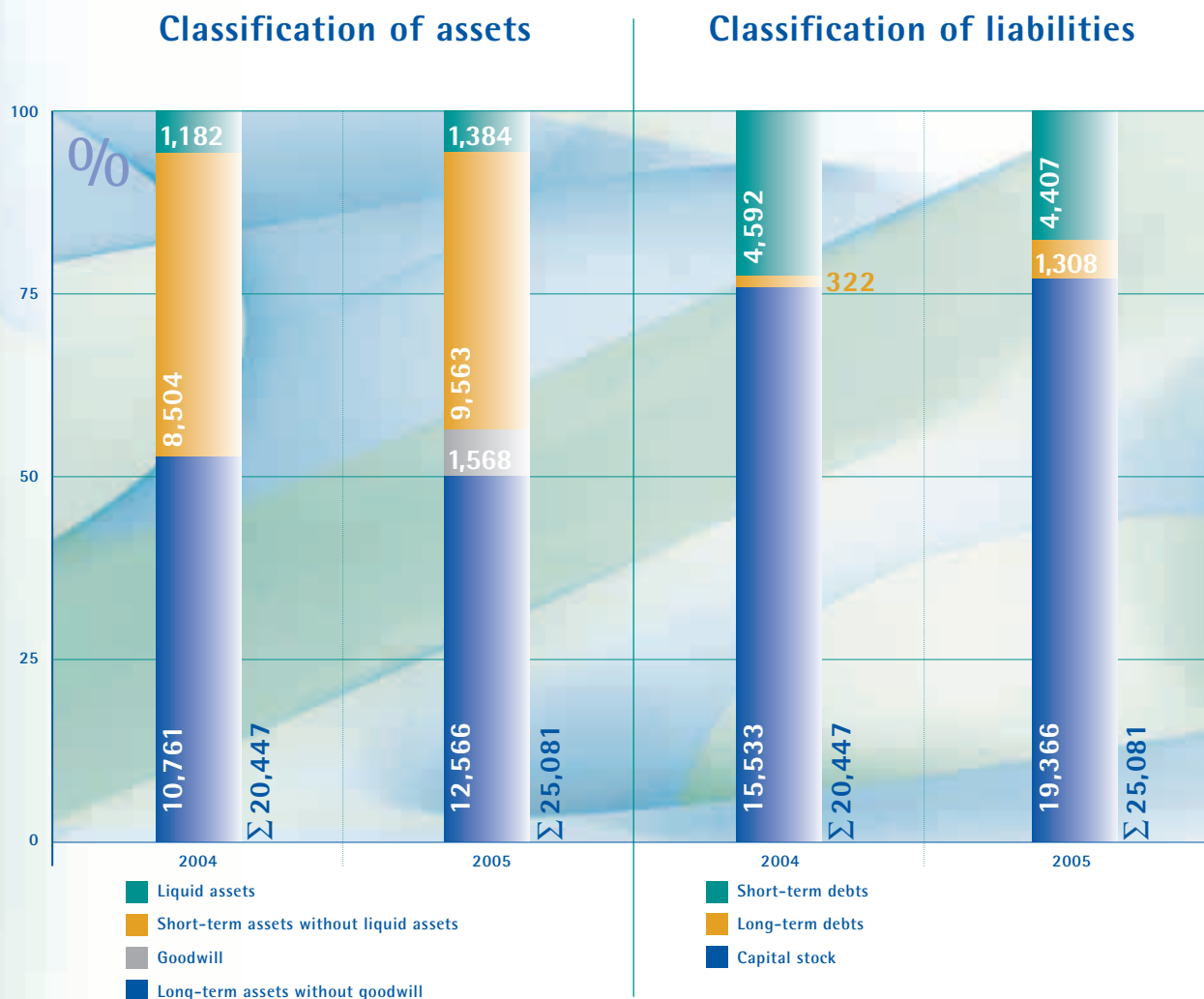
With the positive sales trend, *aap* was able to increase EBITDA to €2.326 million from €1.203 million, leading to a change in EBITDA margin from 10% in 2004 to 17% in 2005. The operating result – EBIT – also increased substantially to €855K from €-316K.

As for earnings from investments in affiliates, the pro rata results until September 30, 2005 of the holdings in OSARTIS GmbH & Co. KG and Neue Magnetodyn GmbH based on the equity method were carried as €239K (previous year: €-110K).

As a consequence, *aap's* earnings from ordinary business activity were €1.081 million after €-1.259 million the previous year.

Income tax is listed at €421K, but actual payments were not due on account of enormous loss carryovers. Earnings after taxes and minority interests were €651K after €-135K the year before.

The development of key items in the consolidated balance sheet to December 31, 2005 compared with the year before is summarized in the following charts.



The Group's cash and cash equivalent amounted to €1.384 million at December 31, 2005. In addition, aap had an overdraft facility of €500K (from Q1 2006: €1.0 million) at its disposal, of which €465K had been taken up on the balance sheet cutoff date.

In connection with the initial consolidation of the two acquisitions, the build-up of inventories and receivables for the new OEM orders, and sales-related increases in general, short-term assets increased by €1.261 million to €10.947 million (previous year: €9.686 million).

The increase in long-term assets was a result of boosting capacity for new large orders, of investing in a new

processing center for osteosynthesis production, and of additionally capitalized development work taking into account depreciation totaling €1.348 million. Goodwill, stated at €1.568 million, resulted from the takeovers of Osartis and ADC. Both were acquired in view of their earning power.

Major changes in the balance sheet picture resulted from the acquisition of Osartis and ADC (including contributions that will lead to a capital increase of 379,000 shares), the start of new production orders and the corresponding increase in current assets, plus the other capital increases undertaken in 2005.

Despite organic and acquisition-related growth, *aap* increased its equity ratio yet again (from 76% in 2004 to 79% in 2005, including shares that have still to be issued for the purchase of ADC). That laid the groundwork for further growth and for further outside funding, albeit exercised with restraint.

aap was also able to improve the due date structure of its liabilities. The proportion of short-term debt, excluding the contributions made to carry out the capital increase agreed, showed a further decline to €3.782 million from €4.592 million.

Liquidity Position

aap regards the liquidity position as sufficient for current business and to ensure organic growth. It is not enough to cover the cost of acquisitions. The share of equity required for that had to be raised by means of a capital increase.

Sales and Results Development at *aap* Implantate AG

Most of the sales increase at the *aap* Group of Companies was at *aap* Biomaterials. *aap* Implantate AG took a €500K falls in commercial sales of bone cement, as announced, that neutralised growth in other areas.

The €461K increase in inventories was due primarily to consignment stocks of hip and knee systems held in the endoprosthesis line of business. Inventories were also built up to improve the service level for osteosynthesis products.

Capitalized goods and services for own account totaling €571K consisted mainly of instruments held in consignment and of production tools made in-house.

Other operating income amounting to €1.181 million included inter-company contributions, investment grants and development subsidies, revaluation of the

AEQUOS GmbH holding and of guaranty obligations, and income from the retransfer of reserves.

Given that the financial statements of *aap* Implantate AG include a variety of Group functions (sales, administration, R&D, trade fairs, cost of business premises), the personnel expenses block and other operating costs both showed above-average increases. The Group view is, however, what counts here.

Group financing is undertaken via *aap* Implantate AG, which took over high claims against *aap* Biomaterials from the 2004 balance sheet restructuring.

That is why *aap* Implantate AG earns high interest income accordingly. The result of *aap* Implantate AG's ordinary business activities on the basis of German commercial law regulations was improved to €-797K from €-1.192 million.

Balance Sheet Development *aap* Implantate AG

aap Implantate AG's balance sheet increased to €21.631 million from €19.394 million. The main reasons for this increase were the September 2005 capital increase and the takeover of Osartis and ADC that it financed, and investment in trauma production equipment.

The conversion of Uwe Ahrens' €736K shareholder's loan into equity in July 2005 and the September 2005 capital increase in cash (totaling €2.3 million before transaction costs) led to a further equity quota increase at *aap* Implantate AG to 82% in 2005 from 77% in 2004.

Subsidiaries

● *aap* Biomaterials GmbH & Co. KG ●

With effect from January 1, 2006 the *aap* Implantate AG subsidiary Coripharm GmbH & Co. KG, Dieburg, was renamed *aap* Biomaterials GmbH & Co. KG. This company handles all of the Group's bone cement and biomaterials activities. At the same time the employees and trading activities of Mebio GmbH, which had been merged with *aap* Implantate AG were transferred to *aap* Biomaterials. In the first half of 2006 *aap* plans to merge Osartis with *aap* Biomaterials.

● Osartis GmbH & Co. KG ●

aap Implantate AG took over Osartis in full with effect from October 1, 2006. Osartis, which has excellent development and production know-how and holds the product rights for the innovative bone replacement material Ostim® in the trauma, orthopedics and spinal column area, had run into financial difficulties. By means of various claim waivers negotiated by *aap* the balance sheet was restructured before and after the 100% takeover of the company.

Osartis is to be merged with *aap* Biomaterials GmbH & Co. KG in the first half of 2006.

Strategic participations

● ADC Advanced Dental Care GmbH & Co. KG ●

aap acquired a 54% majority shareholding in ADC with effect from October 1, 2005 in return for shares in *aap* Implantate AG. ADC is a development and sales company that holds product rights for Ostim® in the dental sector.

● AEQUOS Endoprothetik GmbH ●

aap Implantate AG holds an 11.2% participation in AEQUOS Endoprothetik GmbH. AEQUOS owns and sells the innovative AEQUOS® knee system partly developed and manufactured by *aap* Implantate AG.

In February 2006 a new group of investors undertook a substantial financial commitment in AEQUOS, which will use the funding received to improve further on its successful start in 2005, to hire new employees in sales and marketing, and to take forward clinical trials of the system in Europe and the United States.

● Neue Magnetodyn GmbH ●

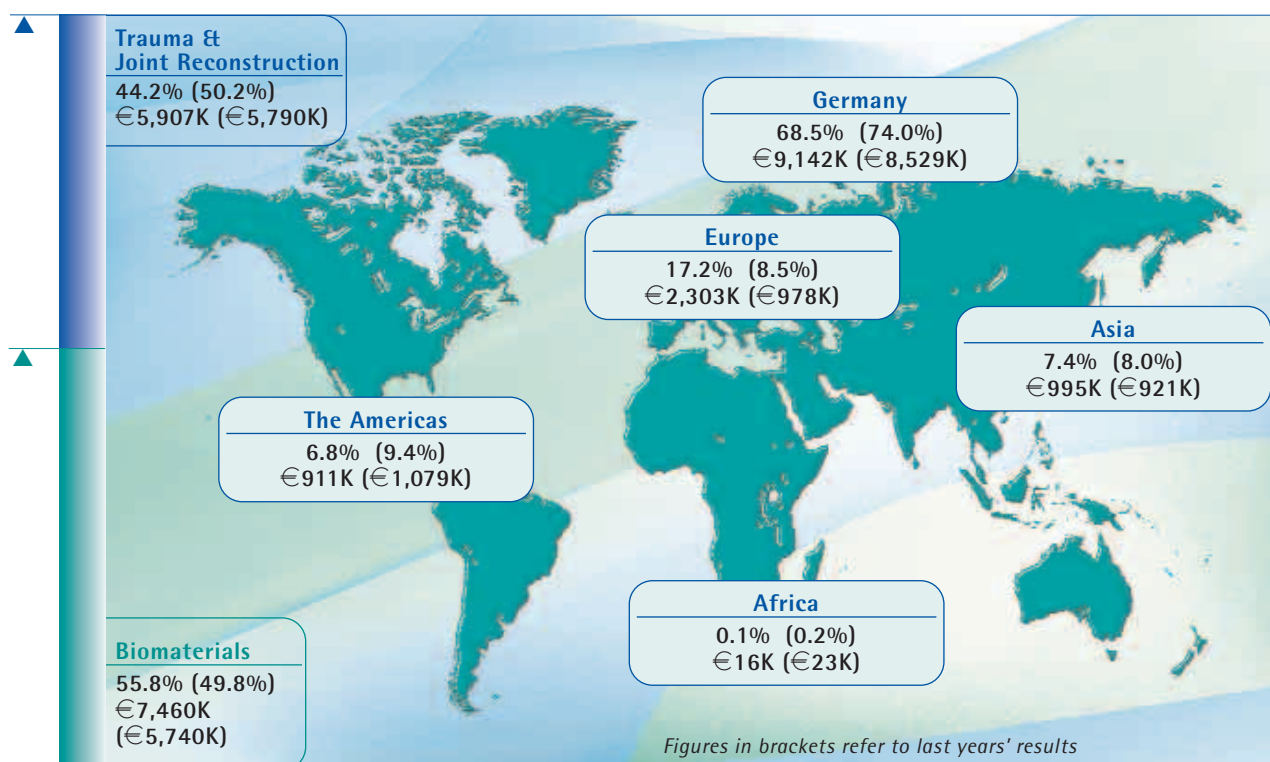
The 30% participation in GEOT (Gesellschaft für Elektro-Osteotherapie) held until 2005 was converted by the company's merger with Neue Magnetodyn GmbH into a 7.1% shareholding in that company.

Products, Markets and Sales

aap's previous lines of business (osteosynthesis, endoprosthesis and orthobiology) were adjusted to the company's new structure from January 1, 2006 at the year's end and in the reporting schema. aap now has two lines of business, Trauma/Joint Reconstruction (aap T/O) and Biomaterials (aap Biomaterials). Sales in the former con-

sist of the combined sales of the former osteosynthesis and endoprosthesis lines, but without bone cements and without cementing techniques. The latter are now shown along with biomaterials in the new Biomaterials line of business. The company's legal structure shall follow these divisions from around mid-2006.

Sales Distribution at Group Level



Sales 2004 vs 2005 at Group Level by Region and Lines of Business

Trauma & Joint Reconstruction includes fracture-healing products for all main skeletal regions along with shoulder, hip and knee joint replacements. In 2005 the sales decline of previous years in this area was brought to a halt and modest, 2% growth was achieved (to €5.907 million compared with €5.790 million in 2004). However, the figures are still not satisfactory. On the one hand aap has deliberately dispenses with unprofitable trauma export orders while on the other the annualized consequences of customers lost in the first half of 2004 and cost pressure in the German hospitals sector have come to light.

Main performers in Trauma are cannulated screws and standard osteosynthesis with a marked trend toward titanium products. Shoulder fractures, with the modular Trauma Shoulder System and the AC Plates System, make a major contribution toward sales. The fastest-growing product group was the anatomic stable-angle plates launched in the course of 2005. By launching new product systems in 2006, making use of its high name recognition level in Germany and by expanding its international sales network aap intends in the years ahead a return to double-digit growth.

aap gained new international customers and distribution partners in Spain, Austria, Korea, the Czech Republic and Russia and signed a number of framework contracts with buying groups in Germany. Sales in China will, in contrast, be down on previous years in 2006.

aap also increased **Joint Replacement** sales with the VarioFit® variable hip system and the AEQUOS® knee system developed and manufactured for AEQUOS GmbH. Further strong sales growth is anticipated for both systems in 2006. Sales of *aap*'s Mebio knee system have in contrast declined. The instrument kit is being modernized to counteract this trend. The VarioFit® hip system was extended to include the VarioCup® PressFit hip socket and is to be placed on the market in summer 2006.

Biomaterials, with the bone cements, infection care, and bone & tissue regeneration product areas, developed successfully both organically and as a result of the Osartis and ADC acquisitions. In spite of the end of the Palacos® distribution contract, leading to a fall in sales of more than €500K, *aap* was able in 2005 to boost Biomaterials sales by 30% to €7.460 million from €5.740 million. Without the two acquisitions, sales would have been €7.192 million and sales growth 25%.

In these fast-growing niche markets *aap* is a world technology leader. Along with its own sales, *aap* is successfully enlarging OEM development and production and has blue chip customers such as Smith & Nephew, Biomet Europe and Heraeus.

New OEM bone cement partnerships begun in 2005 and increasing expansion of the Group's in-house biomaterials distribution network will ensure above-average growth rates in the years ahead.

From the second half of 2006 *aap* Biomaterials will be launching new products to extend the existing portfolio.

With the exception of U.S. business, which was influenced negatively by the cessation of trauma activities with the existing sales partner and by the FDA's warning letter in 2004, *aap* posted sales growth in all regions. Strong growth in international business, especially with OEM customers in the Biomaterials segment, enabled *aap* to reduce further its dependence on the German market. In spite of ongoing cost pressure in the German healthcare sector and cancellation of the Palacos® distribution contract *aap* was also able by stepping up sales activities to achieve a further increase in German sales. In 2006 the proportion of international business will show a further marked increase. *aap* signed new sales agreements with international partners in all lines of business and will thereby be able to establish internationally the products it has newly launched in Germany (Variofit®, WSP, Ostim®, PerOssal®).

Sales Distribution at *aap* Implantate AG

aap Implantate AG's sales were roughly on a par with the previous year at €10.136 million, of which 83% was in Germany.

aap Implantate AG's main line of business, accounting for 58% (previous year: 56%) was Trauma & Joint Reconstruction. While T&O sales were increased by 3% to €5.898 million (previous year: €5.701 million), Biomaterials sales were down 8% to €4.238 million (previous year: €4.580 million).

Most of *aap* Implantate AG's international sales in financial year 2005 were in Asia (€958K; previous year: €927K), followed by Europe with €565K (previous year: €810K).

Sales and Marketing Activities

After last year's increase in field sales, the focus in 2005 was on strengthening product management and marketing.

A number of marketing-relevant measures were undertaken to ensure further growth in the years ahead:

- Consistent implementation of the new corporate design
- An enhanced presence at all major national and international trade fairs
- Conclusion of framework agreements with German buying groups
- A stronger clinical presence with studies and user observation and implementation in workshops, publications and speeches

Along with field sales for the Joint Reconstruction and Trauma product areas, *aap* has built up a group of bio-materials specialists to look after innovative products that need explaining in Germany.

Internationally, *aap* presented its newly launched products VarioFit®, WSP, Ostim® and PerOssal® at Arab Health in Dubai and Hospitalar in Sao Paulo. Nationally, *aap* was represented with a new trade fair concept designed to appeal to the emotions at the first Joint Orthopedics/Accident Surgery Congress and at Medica 2005.

The proportion of international business will continue to increase strongly in 2006, and *aap* has also boosted International Sales significantly. In all lines of business *aap* has signed new sales contracts with international partners, so it should be able to establish internationally the products that it has newly launched in Germany.

Production

30 *aap* has three production locations in Germany. They are Berlin, Dieburg and Obernburg. In Berlin *aap* Implantate AG manufactures osteosynthesis and endoprosthesis products and instruments for Trauma and Joint Reconstruction. Dieburg is the central production location for bone cements. Biomaterials are manufactured in Obernburg and Dieburg.

In 2005 *aap* stepped up bone cement production in Dieburg by hiring 15 new employees. *aap* today is one of the three leading world manufacturers of these niche products.

In Berlin, *aap* Implantate AG took new automatic production machinery into service, thereby increasing significantly its previously limited production capacity for high-precision endoprosthesis, especially AEQUOS®, and anatomic stable-angle plates. *aap* Implantate AG sees depth of value added and the resulting flexibility as one of the most important competitive factors. *aap* Implantate AG continuously trains skilled employees of its own to ensure long-term availability of production skills.

Quality Management

In most of the world's markets official registrations and approvals are a prerequisite for marketing medical devices. Since the products of *aap* are designed as a matter of principle to be marketed internationally, the quality management system is based on the requirements of internationally harmonized standards and on European regulations. That is why the *aap* Group is regularly audited and certified to ensure that its products can carry and be sold with the CE mark.

All *aap* companies are certificated to the DIN EN ISO 13485 standard for medical devices and the EU directive 93/42/EEC. *aap* Implantate AG is also certificated voluntarily to EN ISO 9001:2000 and operates a vali-

dated environmental management system. In business activity all relevant environmental protection regulations are observed. Neither production nor *aap* products pose any direct or indirect risks to the environment.

After the FDA's warning letter received in July 2004, *aap* Implantate AG interrupted sales of trauma products in the United States. In the first quarter of 2006, the company will be re-audited, and depending on the result of the re-audit sales in the United States may then be resumed. Approval procedures for the biomaterials portfolio are currently under way in a number of Asian countries. *aap* is also preparing to submit Ostim® and PerOssal® for approval in the United States.

Employees

On December 31, 2005 the Group had 139 employees on its payroll, including 123 full- and 16 part-time employees (previous year: 109, including 99 full-time and 16 part-time employees).

The marked payroll growth results from the increase in production of bone cements, the takeovers of Osartis and ADC, and the further increase in sales and marketing.

In financial year 2005, trainees included on average 134 people were employed by the Group. Personnel expenses in the reporting period totaled €5.423 million, equiv-

alent to a labor cost ratio of 41% of Group sales revenues (previous year: 35%).

The number of *aap* Implantate AG employees at December 31, 2005 was 103, of which 96 are full-time and 7 are part-time employees (previous year: 100, including 91 full- and 9 part-time employees).

The number of trainees at *aap* Implantate AG continues to be very high. 11% of employees are trainees on the production side.

Research and Development

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Group of Companies

aap invested heavily in research and development in the financial year 2005, and 13% of its employees (18 employees) are assigned to R&D.

aap has a fourfold R&D focus in line with its product portfolio:

- Osteosynthesis
- Endoprosthetics
- Bone cements and cementing techniques
- Biomaterials

As a matter of principle all products are developed in close collaboration with medical users, and frequently on their initiative. Given that the aap product pipeline is subject to close observation by the competition, the following comments can only be general in character.

aap Implantate AG - Trauma & Joint Reconstruction

Since March 2005 the development department in Berlin has been managed by a new head with many years of expe-

rience in orthopedics and osteosynthesis. To ease and accelerate routine work significantly, all workplaces were equipped with powerful new 3D CAD software at the beginning of July.

Development in Trauma & Joint Reconstruction concentrated mainly on completing the new stable-angle humerus and radius plate, testing a new knee instrument kit and expanding the VarioFit® hip system.

All new developments were completed on schedule and went into series production after successful clinical trials.

Biomaterials

Along with the start of production of a totally new bone cement family as an OEM project with significant participation by the R&D team, development activity focused on new bone cement, infection care and bone & tissue regeneration products. Over the next 18 months aap will be placing on the market a variety of new products in all three areas of competence. It will market some of them itself and others in collaboration with sales or OEM partners.

Events of special Importance

Bone Cement Production Agreement with international Orthopedics Group

On March 31, 2005 *aap* signed a multi-year contract with Biomet Europe to manufacture the Biomet bone cement family. Outside of the U.S., Biomet Europe is the world market leader in bone cements for anchoring endo-prosthetics.

Cancellation of Palacos® Distribution Contract for Germany

On April 8, 2005 *aap* was served notice by Essex Chemie AG, Switzerland, of cancellation of the long-term supply contract for Palacos® bone cement. *aap* is considering legal action against Essex.

The cancellation cost *aap* a decline in sales revenues from the distribution of bone cement to the level notified.

Distribution Contract signed with Biomet for Refobacin® Bone Cement in Germany

As of August 30, 2005, *aap* became Biomet Deutschland GmbH's new official bone cement distribution partner.

That enabled *aap* to supply its own bone cement customer with one of the best-quality products on the market and thereby to offset in part the fall in sales resulting from the Palacos® cancellation.

Capital Increase against Cash Contribution

aap Implantate AG undertook in September 2005 a capital increase, issuing 1.46 million new shares at €1.60 each. All were placed in full, giving the company a cash boost of €2.3 million before transaction costs. The cash was used for two acquisitions in the biomaterials sector and for expanding operative business.

Full Takeover of Osartis GmbH & Co. KG, 54% Acquisition of ADC GmbH & Co. KG

With effect from October 1, 2005 *aap* acquired the remaining 51% of Osartis GmbH & Co. KG stock and 54% of ADC GmbH & Co. KG. Osartis is a research and manufacturing company specialized in biomaterials. ADC is a sales company for biomaterials in the dental sector. The product portfolio of the acquisitions includes Ostim®, an innovative bone replacement material that *aap* distributes.

Risk Report

The risk report applies in equal measure to the Group of Companies and to aap Implantate AG.

Risk Management System

In its operative business the *aap* Group is naturally exposed to a large number of risks that are inseparably associated with entrepreneurial activity.

Risk management is an integral part of management at *aap* and is based on three basic components:

- **Certificated Quality Management:** Clearly structured and documented processes in quality management and quality control are a precondition for marketing medical devices. The aim is risk prevention. The quality assurance system in use at *aap* was certificated by DEKRA (*aap* Implantate AG), TÜV (Coripharm GmbH & Co. KG) and LGA Bayern (Osartis GmbH & Co. KG).
- **Controlling Instruments:** Controlling at *aap* briefs the Management Board, Supervisory Board and decision makers in a regular and timely manner on the company's economic position and the status of potential risks by means of key figures and ratios.
- **Risk Management System:** To identify and assess risks and take suitable counter-measures, *aap* has developed a risk management system that is currently in the course of implementation. A key part of this system is regular recording, systematization and evaluation of possible risks, the likelihood that they will occur and the damage that they might cause. Full implementation in organizational processes in all divisions of the company is planned by 2007.

Market, Competition, New Products and Technologies

Competition in the market for medical technology in general and for orthopedic and biological implants in particular will continue to increase. That is why there is a fundamental risk of *aap* failing, in comparison with its competitors, to react in time to market trends with new products or adaptations to existing products. That could have negative repercussions on the company's asset, earnings and financial position and lead to deterioration of its market position.

aap faces up to this risk actively by investing heavily in research and development and by means of constant market and technology screening.

Government intervention in the healthcare system may also have a negative effect on the Group's sales volume and earnings position. *aap* counteracts this risk by continuous internationalization of sales and intensive observation of the German healthcare system with a view to anticipating negative developments and counteracting them.

The German hospital landscape, which is *aap*'s main customer category is currently in a state of flux. On the customer side concentration is caused by mergers into hospital groups and buying groups, with decisions on purchasing being transferred from the physician to the procurement department.

aap is counteracting this trend actively by signing framework agreements with buying groups and by taking special care of hospital chains.

Product Approvals

Strict approval requirements apply in medical technology and healthcare, differing from country to country. Rejection or postponement of approval applications for the company's products such as the delay in FDA reapproval for the United States could have a negative effect on *aap*'s future sales and profits.

To identify such developments in good time and be able to react suitably to them, the company keeps a very close eye on developments in this area and monitors approval procedures in great detail as a part of the quality management system that it implements.

Dependence on Customers and Suppliers

aap buys in various products as commercial merchandise (around 23% of total sales), but this proportion is scheduled to decrease in the years ahead. This partnership naturally involves a greater dependence on these suppliers' quality and readiness to deliver. *aap* takes precautions against this risk to the best of its availability by means of strategic cooperation with a few qualified suppliers.

In 2005 the company's three biggest customers accounted for 19% of *aap*'s sales revenues. OEM sales revenues are scheduled to increase in the years ahead as well. If one of them were to cease to be a customer or to become insolvent, the Group's earnings and financial position could be endangered. Given the size of these OEM partners, we feel that this is most unlikely.

aap counteracts this risk by a careful and balanced choice of its major customers for stability and financial strength and by intensive customer relationship care.

Patents and intellectual Property

aap is not aware of any material breaches of patents or other third-party industrial property rights. It cannot, however, be ruled out that third parties might at a future date claim damages from *aap* for breach of industrial property rights. A breach of this kind might delay the shipment of products. If it lost the case, *aap* might be required to pay fees or sign license agreements. In this way a suit filed against *aap* for breach of industrial property rights could have a lasting negative effect on the Group's asset, finance and earnings position.

Product Liability Risk

aap's products are determined for use in and, in some instances, permanent placement in the human body. Due to differences in healing properties and in the quality of the doctors that use them, a malfunction of the products can never be ruled out entirely. No significant product liability claims have yet been made against *aap*, but they cannot be ruled out in the future.

aap takes precautions against possible product liability suits by a high quality control and by taking out product liability insurance cover. There can, however, be no ruling out the possibility that the existing insurance cover might not be sufficient to meet potential claims, especially in the United States.

Legal Risks

No legal action against *aap* is currently in progress.

Further Statements as per § 315 Section 2 No. 2
of the German Commercial Code

36 Risks posed by changes in price cannot be ruled out entirely. *aap* counters this risk by seeking to switch sales to higher-margin products that it develops and manufactures itself. Its success in doing so is reflected by the gross margin trend (70% in 2005 compared with 65% in 2004).

Active management of receivables minimizes risks arising from possible default on trade receivables. In addition, *aap* regularly makes sufficient risk provision for default. In all, however, the risk can be considered

extremely slight. Losses of receivables totaled €28K in the reporting year.

Funding situation of *aap* Implantate AG and Group can be deemed satisfactory. On the balance sheet date, 31, December 2005, cash and cash equivalents held by *aap* totaled €1.384 million. Since January 2006 the Company has had a €1.0 million overdraft facility at its disposal. *aap* is subject to no major payment flow fluctuations.

aap does not take out foreign currency cover because the risk is minimal at present. In the future, however, hedging may be required if, for example, more business is dollar-denominated.

Supplementary Report

On March 3, 2006 *aap* announced the conclusion of a new sales partnership with Heraeus Kulzer, a Heraeus Group company. Heraeus will in future market *aap*'s

Ostim® bone replacement material worldwide in the dental sector. After a one-year startup period this partnership should exceed a €1 million sales volume.

Forecast Report

Following the first full financial year since balance sheet restructuring and the financial and operational commitment of a group of investors, *aap* can draw up a balance sheet that is predominantly positive.

The Group has been operatively stabilized, its key functions are performed by experienced specialists, heavy investment in sales and marketing is beginning to pay dividends, and a large number of promising development projects has been initiated.

aap has been able to increase its existing technology and innovation leadership in various interesting niches (for example bone cements and synthetic biomaterials) and above all to convert this lead into commercial successes by means of OEM partnerships.

The intention is to set up by mid-2006 a holding structure consisting of a management holding company (with a central board and a shared services center for Finance, IT, Administration and Investor Relations) and two operating companies (*aap* Trauma/Joint Reconstruction and *aap* Biomaterials). *aap* Implantate AG itself will then no longer have an operative role. Its profits will in future be indirect, generated by its participation in the two above-mentioned companies and earnings from services provided.

The growth initiatives initiated are starting to take effect. Sales growth in recent quarters will increase and continue, as evidenced at Group level by the roughly 30% sales growth in the first quarter of 2006, leading in the course of the year to a marked increase in profits.

With the professionalization of its German and international sales structure and a wider network of OEM partners *aap* will be able over the next 18 months to launch different products in all areas (bone replacement, bone cement, trauma and joint reconstruction) with a prospect of high initial acceptance and corresponding growth rates.

With the acquisition and integration of Osartis and ADC, *aap* has shown that the Group is stable enough for growth by acquisition. Its high equity ratio and access to the capital market underscore what is financially feasible. *aap* will continue to analyze acquisition opportunities actively, but its focus will be on integration capability and risk limitation.

That still leaves much to do, of course. The focus in 2006 will be on extending *aap*'s clinical and regulatory competence, rebuilding the sales structure for the U.S. market and the trauma market position in Europe, and accelerating development projects – in short, in further professionalization of the entire organization to make it a high-value enterprise.

Berlin, March 28, 2006

The Management Board

Oliver Bielenstein
Member of the Board

Bruke Seyoum Alemu
Member of the Board

ANNUAL FINANCIAL STATEMENT

of the Group

Consolidated Income Statement according to IFRS

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Consolidated Annual Financial Statement

	Notes	2005	2004
		€K	€K
1. Sales revenues	(1)	13,367	11,530
2. Changes in inventories of finished goods and work in progress		883	-172
3. Production of own fixed assets capitalized		1,384	1,213
4. Other operating income	(2)	1,473	1,993
5. Cost of materials			
a) Cost of raw materials, supplies, and of purchased materials		-4,327	-4,242
b) Cost of purchased services		-393	-123
		-4,720	-4,365
6. Personnel expenses	(3)		
a) Wages and salaries		-4,620	-3,414
b) Social security and other pension costs		-803	-645
		-5,423	-4,059
7. Depreciation of fixed intangible and tangible assets	(4)	-1,471	-1,519
8. Other operating expenses	(5), (8)	-4,633	-4,937
9. Investment income	(6)	239	-110
10. Income from loans of financial assets	(7)	0	1
11. Other interest and similar income	(7)	39	30
12. Depreciation on financial assets	(7)	0	-294
13. Other interest and similar expenses	(7)	-57	-570
14. Results from ordinary activities		1,081	-1,259
15. Extraordinary income		0	7,418
16. Extraordinary expenses		0	-4,874
17. Extraordinary result		0	2,544
18. Income tax	(9)	-421	-1,424
19. Other taxes		-5	-1
20. Net profit/loss		655	-140
21. Share of interest held by parties outside the Group		-4	5
22. Loss carryover from previous year		-23,927	-23,335
23. Consolidated balance sheet loss		-23,276	-23,470

Consolidated Cash Flow Statement according to IFRS

	Notes	2005	2004
		€K	€K
1.	Net profit/loss for the year (B.2)	655	-140
2.	Extraordinary income without effect on payments from the debt waiver (F.9)	-250	-7,379
3.	Extraordinary expenditure without effect on payments	0	4,875
		-250	-2,504
4.	Depreciation of fixed assets including accounting at equity	1,231	1,629
5.	Depreciation on financial assets	0	294
6.	Decrease in provisions	-285	-1,073
7.	Losses of the disposal of fixed asset items	214	9
8.	Write-ups of equity investment	-213	0
9.	Decrease in inventories, trade receivables and other assets	-393	1,896
10.	Decrease in trade accounts payable and other liabilities	-267	-2,120
11.	Income from retransfer of special item for investment allowances	26	-124
12.	Inflow/outflow of funds from current business activity (H.19)	718	-2,133
13.	Amounts paid out for capital investment	-2,398	-1,200
14.	Payments for the purchase of subsidiaries	-41	0
15.	Amounts paid out for investment in financial assets	-27	-30
16.	Outflow of funds from investment activity	-2,466	-1,230
17.	Inpayments from capital increases and shareholder contributions	2,337	9,739
18.	Equity procurement transaction costs	-45	-340
19.	Inpayments from the take-up of loans	738	836
20.	Payments to redeem loans and dormant equity holdings	-1,080	-5,775
21.	Inflow of funds from investment activity	1,950	4,460
22.	Financial resources at start of period	1,182	85
23.	Exchange rate-related changes	0	0
24.	Financial resources at end of period	1,384	1,182

Consolidated Balance Sheet according to IFRS

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Consolidated Annual Financial Statement

ASSETS	Notes	Dec. 31, 2005	Dec. 31, 2004
		€K	€K
A. Non-current Assets	(11)		
I. Intangible Assets			
1. Industrial property rights and similar rights and values		1,478	1,484
2. Goodwill		1,568	0
3. Capitalized development costs		4,539	3,191
		7,585	4,675
II. Tangible Assets			
1. Land and buildings		781	864
2. Technical plant and machinery		1,737	1,523
3. Other fixtures and fittings, tools and equipment		1,258	1,011
4. Prepayments made		9	0
		3,785	3,398
III. Financial Assets			
1. Investments balanced at equity		0	173
2. Other investments	(20), (22)	388	0
3. Other lendings		0	30
		388	203
IV. Deferred taxes	(12)	2,376	2,485
B. Current Assets			
I. Inventories	(13)		
1. Raw materials and supplies		1,077	907
2. Work in progress		1,196	678
3. Finished goods and goods for resale		4,652	4,368
		6,925	5,953
II. Accounts receivable and other assets	(14)		
1. Trade accounts receivable		1,524	965
2. Accounts receivable due from companies in which an equity interest is held		168	546
3. Other assets		946	1,040
		2,638	2,551
III. Checks, Cash in Hand and on Deposit with Deutsche Bundesbank, Postal Giro Balances, Cash in other Banking Accounts		1,384	1,182
Total		25,081	20,447

T€ corresponds to €K.

LIABILITIES AND SHAREHOLDERS' EQUITY	Notes	Dec. 31, 2005	Dec. 31, 2004
		€K	€K
A. Shareholders' equity	(15)		
I. Subscribed Capital		16,519	14,609
II. Additional paid-in capital		25,198	24,080
III. Revenue Reserve			
1. Legal reserve		42	42
2. Other revenue reserve		273	272
IV. Revaluation Reserve		608	0
V. Consolidated retained earnings		-23,276	-23,470
VI. Adjustment item for interests held by parties outside the Group		2	0
		19,366	15,533
B. Non-current Liabilities (above 1 year)	(17), (18)		
1. Non-current provisions		271	138
2. Advances from customers		650	0
3. Special items for investment grants		187	110
4. Capital lease obligations		0	3
5. Other non-current liabilities		200	71
		1,308	322
C. Current Liabilities (up to 1 year)	(17)		
1. Other short-term provisions	(16)	777	904
2. Short-term tax provisions		2	87
3. Due to banks		579	826
4. Advanced payments received		600	0
5. Trade accounts payable		925	1,308
6. Contributions made to implement the capital increase agreed		625	0
7. Special items for investment grants		89	0
8. Accounts payable due to related parties		10	202
9. Current portion of capital lease obligation		3	66
10. Other current liabilities		797	1,199
		4,407	4,592
Total		25,081	20,447

Contingent liabilities €0 (previous year: €21K).

T€ corresponds to €K.

Consolidated Schedule of Assets according to IFRS

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Consolidated Annual Financial Statement

	HISTORICAL COST OF ACQUISITION				
	STATUS AS AT 1.1.2005	CHANGES IN THE CONSOLIDATION ENTITY	ADDITIONS	RETIREMENTS	STATUS AS AT 12.31.2005
	€K	€K	€K	€K	€K
A. Non-current Assets					
I. Intangible Assets					
1. Industrial property rights and similar rights and values	17,235	1	230	0	17,466
2. Goodwill	4,018	1,568	0	0	5,586
3. Capitalized development costs	5,022	1,002	865	0	6,889
	26,275	2,571	1,095	0	29,941
II. Tangible Assets					
1. Land and buildings	1,747	25	0	0	1,772
2. Technical plant and machinery	5,861	260	606	0	6,727
3. Other fixtures and fittings, tools and equipment	4,297	146	764	555	4,652
4. Prepayments made	0	0	9	0	9
	11,905	431	1,379	555	13,160
III. Financial Assets					
1. Investments balanced at equity	679	-679	0	0	0
2. Other investments	0	184	27	0	211
3. Other lendings	294	0	0	0	294
4. Loans to companies in which an equity interest is held	30	-30	0	0	0
	1,003	-525	27	0	505
Total	39,183	2,477	2,501	555	43,606

	HISTORIC COST OF ACQUISITION			
	STATUS AS AT 1.1.2004	ADDITIONS	RETIREMENTS	STATUS AS AT 12.31.2005
	€	€	€	€
A. Fixed assets				
I. Intangible Assets				
1. Industrial property rights and similar rights and values	17,193,512	44,865	3,711	17,234,666
2. Goodwill	4,018,037	0	0	4,018,037
3. Capitalized development costs	4,467,809	554,500	0	5,022,309
	25,679,358	599,365	3,711	26,275,012
II. Tangible Assets				
1. Land and buildings	1,746,609	0	0	1,746,609
2. Technical plant and machinery	5,657,957	202,768	0	5,860,725
3. Other fixtures and fittings, tools and equipment	3,980,186	398,319	81,669	4,296,836
	11,384,752	601,087	81,669	11,904,170
III. Financial Assets				
1. Participations	679,300	0	0	679,300
2. Loans to companies in which an equity interest is held	0	30,000	0	30,000
3. Other lendings	293,363	959	0	294,322
	972,663	30,959	0	1,003,622
Total	38,036,773	1,231,411	85,380	39,182,804

	CUMULATIVE DEPRECIATION					BOOK VALUES		
	STATUS AS AT 1.1.2005	CHANGES IN THE CONSOLIDATION ENTITY	DEPRECIATION FISCAL YEAR	RETIREMENTS	STATUS AS AT 12.31.2005	WRITE-UPS FISCAL YEAR	STATUS AS AT 12.31.2005	STATUS AS AT 12.31.2004
	€K	€K	€K	€K	€K	€K	€K	€K
	15,751	1	236	0	15,988	0	1,478	1,484
	4,018	0	0	0	4,018	0	1,568	0
	1,831	279	240	0	2,350	0	4,539	3,191
	21,600	280	476	0	22,356	0	7,585	4,675
	883	13	95	0	991	0	781	864
	4,338	121	531	0	4,990	0	1,737	1,523
	3,286	110	369	371	3,394	0	1,258	1,011
	0	0	0	0	0	0	9	0
	8,507	244	995	371	9,375	0	3,785	3,398
	506	-266	-240*	0	0	0	0	173
	0	155	0	0	155	332	388	0
	294	0	0	0	294	0	0	0
	0	0	0	0	0	0	0	30
	800	-111	-240	0	449	332	388	203
	30,907	413	1,231	371	32,180	332	11,758	8,276

* Positive results of equity investments carried at equity.

T€ corresponds to €K.

	CUMULATIVE DEPRECIATION				BOOK VALUES		
	STATUS AS AT 1.1.2004	DEPRECIATIONS FISCAL YEAR	EXTRAORDINARY ADJUSTMENTS	RETIREMENTS	STATUS AS AT 12.31.2005	STATUS AS AT 12.31.2005	STATUS AS AT 12.31.2005
	€	€	€	€	€	€	€
	11,640,713	439,358	3,674,705	3,709	15,751,067	1,483,599	5,552,799
	4,018,036	0	0	0	4,018,036	1	1
	1,305,699	146,249	379,058	0	1,831,006	3,191,303	3,162,110
	16,964,448	585,607	4,053,763	3,709	21,600,109	4,674,903	8,714,910
	788,088	94,602	0	0	882,690	863,919	958,521
	3,847,240	490,700	0	0	4,337,940	1,522,785	1,810,717
	3,010,265	347,852	0	72,333	3,285,784	1,011,052	969,921
	7,645,593	933,154	0	72,333	8,506,414	3,397,756	3,739,159
	395,887	110,479	0	0	506,366	172,934	283,413
	0	0	0	0	0	30,000	0
	0	294,322	0	0	294,322	0	293,363
	395,887	404,801	0	0	800,688	202,934	576,776
	25,005,928	1,923,562	4,053,763	76,042	30,907,211	8,275,593	13,030,845

Movement in Equity and Shares of other Shareholders according to IFRS

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Consolidated Annual Financial Statement

	SUBSCRIBED CAPITAL	CAPITAL RESERVE	R E V E N U E R E S E R V E S	
			LEGAL REVENUE RESERVE	OTHER REVENUE RESERVES
	€K	€K	€K	€K
Status as at 12.31.2002/01.01.2003	4,765	24,543	42	272
Capital Increase	105	95	-	-
Transaction Costs	-	-218	-	-
Net Loss for the Year	-	-	-	-
Status as at 12.31.2003/01.01.2004	4,870	24,420	42	272
Capital Increase	9,739	-	-	-
Retransfer arising from the Dissolution of <i>aap</i> Implants Inc.	-	-	-	-
Transaction Costs	-	-340	-	-
Net Loss for the Year	-	-	-	-
Status as at 12.31.2004/01.01.2005	14,609	24,080	42	272
Capital Increase Aug. 29, 2005	450	286	-	-
Capital Increase Sept. 30, 2005	1,460	877	-	-
Transaction Costs	-	-45	-	-
Initial Consolidation	-	-	-	-
Revaluation of other equity investments	-	-	-	-
Changes in the consolidation entity	-	-	-	1
Net Profit for the Year	-	-	-	-
STATUS AS AT 12.31.2005	16,519	25,198	42	273

T€ corresponds to €K.

	REVALUATION RESERVE	BALANCE SHEET LOSS/PROFIT	SHARES OWNED BY THE GROUP	SHARES OWNED BY THE OTHER SHAREHOLDERS	TOTAL
	€K	€K	€K	€K	€K
	0	-7,639	21,983	-269	21,714
	-	-	200	-	200
	-	-	-218	-	-218
	-	-15,417	-15,417	-5	-15,422
	0	-23,056	6,548	-274	6,274
	-	-	9,739	-	9,739
	-	-279	-279	279	0
	-	-	-340	-	-340
	-	-135	-135	-5	-140
	0	-23,470	15,533	0	15,533
	-	-	736	-	736
	-	-	2,337	-	2,337
	-	-	-45	-	-45
	-	-457	-457	-2	-459
	118	-	118	-	118
	490	-	491	-	491
	-	651	651	4	655
	608	-23,276	19,364	2	19,366

Notes to the Consolidated Financial Statements

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A. Company Data

● Company Name, Domicil ●

aap Implantate AG, Berlin

● Head Office ●

Lorenzweg 5, 12099 Berlin, Germany

● Commercial Register ●

The Company is registered at the Berlin-Charlottenburg district court as HRB 64083 and was entered into the court's commercial register on September 10, 1997.

● Stock Market Listing ●

aap Implantate AG has been listed on the regulated market since May 10, 1999 and traded in the Frankfurt Stock Exchange's Neuer Markt segment under Security ID number 506 660. On May 16, 2003, the Company was admitted to the market's Prime Standard segment, which has further regulatory requirements.

● Incorporation by modifying Conversion ●

The Company was incorporated by means of modifying conversion of aap Ahrens, Ahrens & Partner GmbH & Co. Betriebs KG on January 1, 1997.

● Type of Business ●

aap Implantate AG is a medical sector enterprise. The Group's business activity consists of the research, development, manufacture and sale of implants, medical instruments, bone cements and replacement materials.

B. General Information

● 1. Basic Principles ●

The consolidated financial statements of aap Implantate AG, Berlin, to December 31, 2005 are drawn up in accordance with the International Financial Reporting Standards 2005 as applied in the European Union and with the commercial law provisions of § 315 a Section 1 of the German Commercial Code (HGB). The International Financial Reporting Standards consist of the IFRS newly issued by the International Accounting Standards Board (IASB), the International Accounting Standards (IAS), and the interpretations by the International Financial Reporting Interpretations Committee (IFRIC) and the Standing Interpretations Committee (SIC). The IFRS that had come into binding force on the balance sheet date were

applied in the consolidated financial statements.

The consolidated financial statements of aap Implantate AG to December 31, 2005 are based on the financial statements of the companies in the Group. These were drawn up applying uniform accounting and valuation methods as used by the parent company in accordance with the HGB and the German Stock Corporation Act (Aktengesetz). The transfer to IFRS was effected at individual company level.

The consolidated balance sheet and the consolidated profit and loss statement are structured in accordance with the IFRS. The consolidated profit and loss account was drawn up using the total costs method.

The consolidated financial statements were denominated in euros. Unless otherwise specified, all amounts are shown in thousands of euros (€K).

These annual financial statements for the financial year 2005 are based on a reporting period from January 1 to December 31, 2005.

● 2. Cash Flow Statement ●

The consolidated cash flow statement was drawn up as per IAS in accordance with the indirect method. It is structured by payment flows from business, investment and financial activities. Effects of exchange rate fluctuations are shown separately. Net funds as shown in the cash flow statement tally with the net funds total shown in the balance sheet.

Cash and cash items consist of cash in hand and with banks. There are no restraints on disposal. Inflow and outflow of funds from the acquisition of consolidated companies are listed separately under cash flow from investment activity.

C. Consolidation Principles

● 1. Consolidated Entity ●

The consolidated financial statements include, in addition to the parent company aap Implantate AG, all the subsidiaries in which aap Implantate AG directly or indirectly holds a controlling interest. Associated companies are included in the accounts on the basis of the equity method. Participating interests are listed at H (20) below.

aap Implantate AG, Berlin
Parent Company

	Holding	
	2005	2004
aap Biomaterials GmbH & Co. KG, Dieburg*	100%	100%
aap Biomaterials Verwaltungs GmbH, Dieburg**	100%	100%
Osartis GmbH & Co. KG, Elsenfeld	100%	49%
OSARTIS Verwaltungs GmbH, Elsenfeld	100%	49%
ADC Advanced Dental Care GmbH & Co. KG, Elsenfeld	54%	-
ADC Advanced Dental Care Verwaltungs GmbH, Elsenfeld	51%	-

* Formerly Coripharm GmbH & Co. KG

** Formerly Coripharm Verwaltungs GmbH

● 2. Acquisitions/Changes in Participations ●

By the terms of a contract dated September 21, 2005, aap Implantate AG acquired the remaining 51% in OSARTIS GmbH & Co. KG, Elsenfeld, and OSARTIS Verwaltungs GmbH, Elsenfeld, for a purchase price of €33K, including incident acquisition costs. The purchase price was paid in cash in the financial year 2005. Both companies are now wholly owned by aap Implantate AG. Due to the change in status from associated company to subsidiary, a change from equity accounting to full consolidation seemed advisable. In accordance with IFRS 3, assets of participating interest were totally revalued at the time when full control was gained with the exception of goodwill, for which the original valuation still stands. The €490K increase in undisclosed reserves was included in the revaluation reserve. Changes in value booked in accordance with the equity method before full control was gained were canceled.

In the course of the financial year, 54% of ADC Advanced Dental Care GmbH & Co. KG, Elsenfeld, and 51% of Advanced Dental Care Verwaltungs GmbH, Elsenfeld, was acquired. The purchase price, including incidental acquisition costs, was €670K, of which €37K was paid in cash. The remainder was paid in the form of an issue of 379,000 new bearer shares. The share price at the time of the transaction was €1.67.

Initial consolidation of the company took place at the time of acquisition on October 1, 2005. €28K in negative differential amounts arising from the capital consolidation is booked as other operating income at F (2). The balance from company acquisitions includes the following assets and liabilities:

	€K
Intangible assets	2,290
Fixed assets	186
Inventories	157
Receivables and other assets, including deferred tax credits	407
Cash and cash equivalents	29
Long-term debt	541
Short-term debt	1,381

From the time of acquisition, sales by the companies acquired totaled €269K in 2005.

Influences arising from the change in consolidation entity are shown in the notes insofar as they are of any special importance.

During the financial year GEOT Gesellschaft für Elektro-Osteo-Therapie mbH, Munich, was merged with Neue Magnetodyn GmbH, Munich. In return for its shareholding in GEOT Gesellschaft für Elektro-Osteo-Therapie mbH, aap Implantate AG received a nominal €4K interest in Neue Magnetodyn GmbH, equivalent to a 7.12% participation. On the change in status to a simple participation, equity accounting was discontinued. The €33K book value of the shares held at the time of the change in status was taken as a new basis for the cost of acquisition.

● **3. Reporting Date of the Consolidated Financial Statements** ●

The financial year of the companies included is the calendar year. Accordingly, the consolidated financial statements were prepared to December 31, 2005.

● **4. Accounting and Valuation Method** ●

The financial statements of the companies included in the consolidated financial statements were drawn up applying uniform accounting and valuation methods as used by the parent company.

Consolidated companies draw up their financial statements in their national currency, the euro (€), as the functional currency in which they do most of their business.

● **5. Capital Consolidation** ●

Financial statements for mergers are prepared on the basis of the purchase method. Capital consolidation is thereby undertaken at the time of purchase by netting out the purchase price against the revalued net assets of the subsidiaries acquired.

Subsidiaries' allowable assets, debts and contingent liabilities are stated at their full market value irrespective of the minority interest. Intangible assets are shown separately from goodwill insofar as they can be separated from the company and result from a contractual or other right. No initial restructuring reserves are created in the course of purchase price allocation. Any positive remaining differential amounts are capitalized as goodwill. Negative differential amounts arising from initial consolidation are retransferred with effect on results. Capitalized goodwill is not depreciated according to schedule but submitted to an impairment test annually and whenever there are indications of an impairment of value.

Income and expenditure of companies acquired are included in the consolidated financial statements from the time of acquisition.

● **6. Debt Consolidation** ●

Intra-group receivables and liabilities are offset. Any balancing differences that arose in the reporting period were recorded as affecting earnings.

● **7. Consolidation of Earnings** ●

In the context of earnings consolidation, internal sales and intra-group income and expenses are offset. Interim results are eliminated insofar as they are of minor significance.

D. Accounting and Valuation Methods

Intangible assets are shown at acquisition costs less planned depreciation. All intangible assets have an ascertainable useful life and were therefore depreciated according to schedule.

Development costs are capitalized as intangible assets if a newly developed product or process can be clearly demarcated, is technically realizable and if the company plans to use it itself or to market it. Further prerequisites for capitalization are the likelihood of deriving future economic benefit and a reliable valuation of the asset. Capitalized development costs are depreciated according to schedule in a straight line over their useful life, as a rule between 5 and 10 years from the date they were put to use. Research costs are recorded as expenses in the period in which they were incurred.

Tangible fixed assets are valued at cost of acquisition or production and, where depreciable, taking into account scheduled depreciation. The production costs of tangible fixed assets include the full costs. Costs of borrowing are not capitalized as part of acquisition or production costs.

Movable assets up to a value of €410.00 are written down in full in the year of acquisition. Fixed tangible assets rented by financial leasing are capitalized at current market value or at the lower cash value of the lease installments and depreciated in a straight line over their foreseeable service life.

Intangible assets and fixed tangible assets are depreciated off schedule if the sum obtainable for the asset is less than the book value. Assets are written up if and when the reason for any previous non-scheduled depreciation no longer applies. The resulting increase in book value may not exceed the depreciated cost of acquisition or production. Goodwill is not written up.

In accordance with equity accounting, **holdings in associated companies** are first netted out against acquisition costs, and subsequently against updated pro rata net assets. Stated goodwill is shown in the participation's book value. There is no scheduled depreciation of goodwill. The book values of participations are increased or decreased annually by the pro rata results of the associated companies. Book values are written down off schedule if the sum achievable is less than the book value.

Other holdings listed under **financial investments** come in the "available for disposal" category. They are valued both on first inclusion in the balance sheet and in subsequent periods at market value insofar as the market value can be ascertained reliably. Initial valuation is on the day of fulfillment. Unrealized profits or losses are shown under equity. On disposal, the profit or loss affects results. If there are objective, substantial indications that an asset's value has been impaired, it will be depreciated with effect on results.

Deferred taxation results from time differences and differing valuations in IFRS and tax balance sheets of individual companies and from consolidation. Deferred tax credits include tax reduction entitlements arising from the anticipated use of existing loss carryovers in subsequent years the realization of which is sufficiently assured. Deferred taxes are assessed on the basis of the tax rates in force or anticipated at the time of realization.

Inventories are valued at cost of acquisition or production or at net sale value. Production costs are full costs calculated on the basis of ordinary employment. In detail, production costs include in addition to directly attributable costs appropriate proportions of

essential production overheads. These include material and manufacturing overheads and production-related administrative costs as well as straight-line depreciation of production plant and equipment. Loan capital costs are not capitalized as part of acquisition or production costs.

Valuation is based on the FIFO assumed sequence of consumption.

Inventory risks arising from diminished usability are taken account of by means of appropriate write-downs. Lower values on the reporting date due to lower net losses on disposal are stated.

Production orders for specific customers are reported in the balance sheet applying the percentage of completion method. The sum to be capitalized is shown under receivables. The stage of performance is determined according to expenses incurred and project phases that have been demonstrably completed. The pro rata contractual proceeds are shown under sales revenues as proceeds from orders.

Receivables and other assets are shown in the balance sheet at cost of acquisition less essential value adjustments in line with the actual risk of default. Interest-free receivables with a term of more than one year are reported at cash value. Foreign currency receivables are translated at the exchange rate at the time of first posting. Translation differences are reported with effect on results.

Investment allowances and investment grants received are carried as liabilities under the heading special investment allowances items. They are written down, with the resulting effect on earnings, in a straight line in accordance with the useful economic life of the assets they helped to acquire.

The **revaluation reserve** contains unrealized profits and losses from changes in market value of financial assets that are available for disposal. These profits or losses do not affect results.

Provisions are set up if a liability to a third party arising from a past event exists, if a claim is likely and if the foreseeable level of provision required can be estimated reliably. Provisions are stated at the settlement amount that is likeliest to be determined and are not netted out against claims to reimbursement.

Liabilities are stated at market value on first mention. In subsequent years they are valued at their updated cost of acquisition. Liabilities from financial leasing agreements are carried as liabilities at their market value. Where the cash value of minimum leasing payments is lower than the market value, the cash value will count. Foreign currency liabilities are translated at the repayment exchange rate when the liability was incurred. Translation difference are reported with effect on results.

Contingent liabilities are possible or existing liabilities based on past events that are not likely to involve an outflow of funds. They are not recorded in the balance sheet. There were no contingent liabilities on the balance sheet date.

Sales revenues are realized when due delivery or performance has been rendered and the risk has been transferred to the customer. This does not apply to order-related income that results from applying the percentage-of-completion method. Customer discounts and rebates and returned goods are taken into account in the appropriate period in line with the sales revenues on which they are based.

Discretion must be exercised in applying accounting and evaluation methods to, for example, long-term assets that are up for disposal. It must here be determined whether the assets are saleable in the current condition and their disposal is highly likely. In this case the assets and, if applicable, attendant debts must be stated and evaluated as assets or debts held for disposal.

For some items, drawing up the consolidated financial statements entails making estimates and assumptions that affect the statement and level of assets, debts and contingent liabilities and of income and expenses reported. Actual amounts may diverge from these estimated values. These assumptions and estimates relate inter alia to the forward-looking premises assumed in connection with the impairment test for goodwill, to assessments on deriving future economic benefit from a development project, and to the likelihood of realizing tax carryovers. All such assumptions and estimates are based on circumstances and assessments on the balance sheet date and on the future business development anticipated for the enterprise, taking into account realistic expectations of future development of its economic environment. Insofar as these framework conditions develop differently, the assumptions and, if necessary, book values of the assets and debts affected will be adjusted accordingly.

On the basis of facts known when the consolidated financial statements were being compiled, no material change in the assumptions and estimates needs to be assumed, so no adjustment of the book values of the stated assets and debts is to be expected in financial year 2006.

E. Changes in Accounting and Valuation Methods

The International Accounting Standards Board (IASB) has both made changes to existing International Financial Reporting Standards and adopted new IFRS standards that have been mandatory since January 1, 2005. The following IFRS standards were used for the first time in the reporting period:

IAS 1 (2003)	Presentation of financial statements
IAS 2 (2003)	Inventories
IAS 8 (2003)	Accounting policies, changes in accounting estimates, and errors
IAS 10 (2003)	Events after the balance sheet cutoff date
IAS 16 (2003)	Fixed tangible assets
IAS 17 (2003)	Leasing relationships
IAS 21 (2003)	Effects of exchange rate changes
IAS 24 (2003)	Related party disclosures
IAS 27 (2003)	Consolidated and separate individual financial statements to IFRS
IAS 28 (2003)	Holdings in associated companies
IAS 33 (2003)	Earnings per share
IAS 36 (2004)	Value impairment of assets
IAS 38 (2004)	Intangible assets
IAS 39 (2004)	Stating and evaluating financial instruments
IFRS 3	Mergers

Initial use of these standards had no material influence on the consolidated financial statements compared with the previous procedure. Taking considerations of materiality into account, no adjustment of figures for previous years was necessary.

F. Notes on the Profit and Loss Statement

• (1) Sales Revenues •

	2005	2004		2005	2004
	€K	€K		€K	€K
By region			By lines of business		
Germany	9,143	8,529	Trauma & Joint Reconstruction	5,907	5,790
Other European countries	2,302	978	Biomaterials	7,460	5,740
Asia	995	921			
The Americas	911	1,079			
Afrika	16	23			
Total	13,367	11,530	Total	13,367	11,530

• (2) Other Operating Income •

	2005	2004
	€K	€K
Proceeds of restructuring	561	0
Revaluation of assets	325	181
Retransfer of provisions	161	1,316
Private car use	123	89
Income unrelated to accounting period	66	102
Income from write-back of special item for investment allowances and grants	54	124
Income from expense allowances	61	50
Insurance claims settled	36	6
Negative differential amount from capital consolidation	29	0
Current asset disposals	12	12
Other	45	113
Total	1,473	1,993

€100K of the revaluation of assets relates to guaranty claims against contributing shareholders (cf G (14)). Some of these claims are covered by the assignment to *aap* Implantate AG of shares held by these shareholders. The revaluation corresponds to the market price of the shares on the balance sheet date. Income totaling €214K relates to the participation in AEQUOS Endoprothetik GmbH. The increase in this company's enterprise value took concrete shape as a result of capitalization measures undertaken in the year under review.

• (3) Personnel Expenses •

	2005	2004
	€K	€K
Wages and salaries	4,620	3,414
Social insurance contributions and expenses for old-age provision and for support	803	645
	5,423	4,059

Average headcount over the year	2005	2004
Wage-earners	54	47
Salary-earners	67	57
	121	104

• (4) Depreciation •

Scheduled depreciation of tangible assets totaled €995K (previous year: €933K) and of intangible assets €476K (previous year: €586K).

There were no extraordinary write-downs in 2005 (previous year: €4.054 million).

● (5) Other Operating Expenses ●

	2005	2004
	€K	€K
Cost of premises	777	573
Advertising and travel expenses	766	592
Other costs	671	310
Freight charges, packaging material, cost of delivery	531	415
Consulting fees	369	722
Patent fees, other fees	214	249
Leasing	243	174
Vehicle costs	234	157
Repairs and maintenance	199	157
Insurance, subscriptions, fiscal/public charges	187	234
Office requisites, telephone, faxes, postage	176	162
Asset disposals	184	342
Expenses unrelated to accounting period	57	72
Losses and value reductions arising from accounts receivable	24	751
Currency differences	1	27
	4,633	4,937

● (6) Result of Participating Interests ●

This includes the pro rata result of participating interests in GEOT Gesellschaft für Elektro-Osteo-Therapie mbH and OSARTIS GmbH & Co. KG drawn up using the equity

accounting method for the period up to June 30, 2005 and September 30, 2005 respectively and amounting to €239K (previous year: €-111K, cf C (2)).

● (7) Financial Result ●

	2005	2004
	€K	€K
Income from other loans	0	1
Other interest and similar income	39	30
Depreciation of financial assets	0	-294
Other interest and similar expenditure		
▪ Interest on long-term loans	-27	-318
▪ Interest on current debts to banks	-26	-149
▪ Interest paid to sleeping partners	0	-85
▪ Write-back of financial costs	-3	-11
▪ Other interest expenses	-1	-7
	-57	-570
	-18	-833

● (8) Exchange Rate Differences ●

Exchange rate differences affecting the operating result in the accounting period were

	2005	2004
	€K	€K
Income from exchange rate differences	4	36
Cost of exchange rate differences	-1	-27
	-3	-9

● (9) Taxes on Income ●

Income tax expenses to IFRS (cf G. 12) can be translated to the theoretical tax expense as follows. This is based on a tax rate of 39% (previous year: 39%) comprising German corporate income tax, plus solidarity surcharge, and trade tax.

Income tax expenses to IFRS include €1K in actual income tax.

	2005	2004
	€K	€K
Earnings before tax	1,076	1,284
Theoretical tax expense (income) 39% (previous year: 39%)	-419	-499
Tax effects on		
Realization of negative differential amounts from capital consolidation	11	0
Results/Depreciation of companies with balance sheets drawn up on the basis of equity accounting	93	-43
Permanent differences	-144	-1,093
Equity capital transaction costs	29	216
Non-tax-deductible expenses and additional trade tax	-11	-36
Differences in tax rate	17	0
Tax-free income	2	32
Total adjustments	-3	-924
Income tax expenses to IFRS	-422	-1,423
Effective tax rate in %	39%	111%

● (10) Earnings per Share
as per IAS 33 ●

Undiluted earnings per share are calculated by dividing the earnings from the shares for the period by the average weighted number of shares.

	2005	2004
Result for the period in €K	651	-140
Number of shares ('000s)	15,237	8,522
Earnings per share in €	0.04	-0.02

Diluted earnings per share correspond in financial year 2005 to the undiluted earnings per share.

	2005	2004
Result for the period in €K	651	-140
Number of shares ('000s)	15,237	8,686
Earnings per share in €	0.04	-0.02

G. Notes on the Balance Sheet

● (11) Non-current Assets ●

For movement in long-term fixed assets please see the consolidated schedule of assets attached. Of the additions shown in the financial year, self-made assets accounted for €865K and additions resulting from changes in the consolidation entity accounted for €2.472 million.

1. Intangible Assets (excluding Development Costs)

Intangible assets acquired in return for payment are depreciated pro rata in a straight line from the historic cost of acquisition.

Useful economic life is as follows:

	Years
Industrial property rights and similar rights and values	3 - 20

No extraordinary depreciation was undertaken in the year under review (previous year: €3.675 million).

2. Development Costs

In the reporting period development costs totaling €865K (previous year: €555K) were capitalized. They include €40K in directly attributable loan capital costs determined on the basis of the Group's average financing cost rate of 3.57%. Development costs relate essentially to the following projects:

Bone cement with antibiotic
HF cement
CS pellets – absorbable bone replacement
Angle-stable plates
Dynamic hip nail

In addition, €546K in research and further development costs (previous year: €348K) was carried as expenses. Depreciation in the reporting period totaled €240K (previous year: €525K), of which nil (previous year: €379K) was extraordinary depreciation.

3. Tangible Assets

Tangible assets are depreciated in a straight

line from historic cost of acquisition or cost of production.

Useful economic life is, on average, as follows:

	Years
Land and buildings	50
Technical plant and machinery	5 - 10
Other plant, office and business equipment	5 - 10

The book value of leased tangible assets on December 31, 2005 was €74K (previous year: €753K).

4. Financial Assets

Participating interests	2005		2004	
	€K	%	€K	%
1. Neue Magnetodyn GmbH, München (GEOT Gesellschaft für Elektro-Osteo-Therapie mbH, Munich)	32	7.12	23	30.0
2. AEQUOS Endoprothetik GmbH, Munich	356	11.2	0	11.9
3. Cybernetic Vision AG Health Monitoring Technologies, Berlin	0	5.69	0	5.69
Loans to companies with which <i>aap</i> has a participation relationship	0		30	
Total	388		53	

● (12) Deferred Taxes ●

Tax accruals carried as assets totaling €2,376 million (previous year: €2,485 million) include the following capitalized tax credit entitlements arising, according to the present business plan, from the anticipated utilization of existing loss carryovers in the years ahead:

	2005	2004
	€K	€K
Corporate income tax, including solidarity surcharge	2,145	2,176
Trade tax	1,450	1,368
	3,595	3,544

There is a sufficient degree of certainty that these loss carryovers will be realized.

Deferred tax credit claims totaling €390K (previous year: €355K) relate to items that

are offset directly against equity. Deferred tax liabilities totaling €1.765 million (previous year: €1.571 million) result from consolidation (elimination of interim results and debt consolidation including currency differences) and from temporary differences between tax values and amounts stated for balance sheet items in accordance with IFRS.

To calculate trade earnings tax, the IFRS result for the year was taken as the starting point and trade earnings were calculated by means of trade tax additions and deductions. Trade tax is charge at roughly 17% after taking tax deductibility into account. Deferred corporate income tax was determined on the

basis of a tax rate of 25% plus a 5.5% solidarity surcharge on corporate income tax due. Deferred tax credits arising in connection with consolidation were calculated on the basis of an average tax rate of 39% for the Group.

In accordance with IAS 1.27a, the allocation of capitalized deferred taxes was changed from the previous year. It is now shown under item A, long-term assets. The previous year's total, €2.485 million, was reallocated accordingly.

● (13) Inventories ●

To state inventories at net sale value, value adjustments totaling €48K (previous year: €6K) were undertaken in the year under review. Value markdowns amounting to €2,464 million (previous year: €2,596 million) were made. There were no extraordinary markdowns (previous year: €640K).

● (14) Accounts receivable and other Assets ●

	12.31.2005	Of which due in more than 1 Year	12.31.2004	Of which due in more than 1 Year
	€K	€K	€K	€K
Trade receivables				
Based on percentage of completion	103	0	91	0
Of which already paid	0	0	-75	0
Other receivables	1,421	0	949	0
	1,524	0	965	0
Claims against other companies with which <i>aap</i> has a participation relationship	168	0	546	387
Other assets				
Tax refund claims	136	0	229	0
Warranty claims	646	0	548	0
Other	164	4	263	2
	946	4	1,040	2
	2,638	4	2,551	389

Claims arising from percentage of completion relate to a production order from AEQUOS Endoprothetik GmbH for customer-specific implants. Costs incurred by December 31, 2005 totaled €76K. No prepayments were made. The claim for breach of warranty is against the contributing partners of holdings in Corimed Kundenorientierte Medizinprodukte GmbH, Coripharm Medizinprodukte-Verwaltungs-GmbH and Coripharm Medizinprodukte GmbH & Co. KG. Claims totaling €100K were added.

Other assets consist of €4K in discounts (previous year: €2K).

● (15) Equity ●

Capital Stock

On December 31, 2005 the company's capital stock amounted to €16,519,157 and was divided into 16,519,157 individual bearer shares.

The General Meeting held on June 10, 2005 resolved to increase the company's capital stock to €15,058,300 from €14,608,587 by issuing 449,713 new bearer shares, each with an arithmetical share of €1 in the company's capital stock. The capital increase was undertaken in return for the contribution by Mr. Uwe Ahrens of a claim with a nominal value of €736K.

The capital increase was recorded in the Commercial Register on August 29, 2005.

A General Meeting resolution adopted on June 10, 2005 authorized the Management Board to increase the company's capital stock by June 10, 2010 on one or more occasions by up to €7,300,000 in cash or investment in kind and to lay down the terms and conditions for the share issue.

On the basis of this authorization the Management Board agreed on September 7, 2005 to increase the company's capital by €1,460,857 to €16,519,157 by issuing 1,460,857 bearer shares, each with an arithmetical share of €1 in the capital stock.

The new shares were offered to shareholders as an indirect rights issue in a ratio of 21 to 2. The issue and purchase price was €1.60 per share.

The capital increase was recorded in the Commercial Register on September 30, 2005.

By the terms of Management Board decision on December 14, 2005, approved on the same day by the Supervisory Board, the company's capital stock was to be increased from Approved Capital by €379,000 to €16,898,157 from €16,519,157 by issuing 379,000 new bearer shares, each with an arithmetical share of €1 in the capital stock. The share issue excluded a rights entitlement for shareholders and was to be paid for investment in kind. The contribution in question was partnership shares with a nominal value of €54,000 in ADC Advanced Dental Care GmbH & Co. KG, Elsenfeld, entered into the Commercial Register of the Aschaffenburg district court with the registration number HRA 3954, and a partnership share with a nominal value of €12,500 in ADC Advanced Dental Care Verwaltungs GmbH, Elsenfeld, entered into the Commercial Register of the Aschaffenburg district court with the registration number HRB 8174. The shares are entitled to profits from January 1, 2005.

The capital increase has yet to be registered. It is shown under short-term debts as a special item on contributions made to implement the capital increase agreed (cf G 17).

The statutory reserve at the end of the financial year amounted to €41,703.95 and, together with the capital reserve, exceeded one tenth of the capital stock.

Transaction Costs

Transaction costs totaling €45K (previous year: €340K) were carried in the balance sheet as a deduction from equity.

Conditional Capital

The General Meeting held on May 29, 2001 approved a conditional capital increase of €96,000 by the issue of up to 96,000 individual bearer shares. The new shares are entitled to profits from the beginning of the financial year in which they are issued. The conditional capital is solely for the purpose of granting stock options to employees and management of the company or of an associated company as follows:

- 17.1% to board members of the company and associated companies
- 25% senior executives
- 57.9% to employees of the company and of associated companies

Stock options are granted in accordance with the provisions laid down in the 2001 stock option plan. Subscription rights could have been granted until January 12, 2006. The Company made no use of this option and the conditional capital was not utilized.

Authorized Capital

The General Meeting held on June 10, 2005 authorized the Management Board to increase the company's capital stock by June 10, 2010 on one or more occasions by up to €7,300,000 in cash or investment in kind and to lay down the terms and conditions of the share issue. Subject to Supervisory Board approval, subscription rights for existing shareholders may be ruled out

- to balance residual amounts,
- if the capital increase in cash does not exceed 10 % of the capital stock and the issue price of the new shares is not substantially lower than the market price (§ 186 Section 3 Sentence 4 German Stock Corporation Act, AktG),
- to issue shares in return for contributions as part of an acquisition of companies, parts of companies or participations in companies (including conversions by the terms of the Conversion Act)
- to issue shares to strategic partners,
- to serve conversion or subscription rights held by holders of stock options, convertible bonds, stock warrants and/or participation certificates,
- to issue shares to employees and directors of the company and to employees and management of associated companies as part of a stock option plan,
- in payment for consulting services,
- to issue shares to lenders in place of interest payments in cash or in addition thereto (so-called equity kickers), especially in connection with mezzanine financing,
- to repay loans or other liabilities.

Please see the schedule of equity.

• (16) Short-term Provisions •

	As at 01.01.2005	Addition based on changes in the consoli- dation entity 10.01.2005	Consumption	Retransfer	Additions	As at 12.31.2005
	€K	€K	€K	€K	€K	€K
Provisions for taxation	87	0	87	0	2	2
Other provisions						
Commitments to employees	157	213	344	20	162	168
Bonuses paid	50	0	50	0	94	94
Commission	10	0	9	1	26	26
Licenses	147	0	54	40	38	91
Cost of annual financial statements, audit costs	130	8	97	31	116	126
Employers' liability insurance	28	2	26	2	35	37
Bills outstanding	178	3	154	12	201	216
Legal costs and risks	30	0	0	30	0	0
Other uncertain provisions	140	0	140	0	0	0
Warranties	34	0	0	25	9	18
	991	226	961	161	683	778

All of the stated reserves have terms of up to one year.

• (17) Liabilities •

Times to maturity of liabilities, broken down by balance sheet heading, are as follows:

Time to maturity	12.31.2005 Total	Up to 1 Year	1-5 Years	More than 5 Years	Previous year
	€K	€K	€K	€K	€K
Amounts owed to banks	850	579	271	0	964
Prepayments received	1,250	600	650	0	0
Trade receivables	925	925	0	0	1,308
Contributions made to implement the capital increased agreed (G (15))	625	625	0	0	0
Special investment grant item	276	89	187	0	110
Liabilities to associated company	10	10	0	0	202
Financial leasing liabilities	3	3	0	0	69
Other liabilities	997	797	200	0	1,271
Of which:					
(Social security-related)	(153)	(153)	(0)	(0)	(108)
(Taxes)	(192)	(192)	(0)	(0)	(113)
	4,936	3,628	1,308	0	3,924

Of long-term liabilities (time to maturity > 1 year) totaling €1.308 million, €271K (previous year: €141K) was subject to interest. The average interest charge was around 2.75% (previous year: 6.9%).

With recourse to a €465K overdraft facility all present and future trade receivables were assigned to Deutsche Bank AG, Berlin.

The contributions made relate to the capital increase in kind agreed on December 14, 2005 involving the issue of 379,000 shares. The shares were valued at the market price on the transaction date (G 15 and C 2).

H. Other Information

• (18) Reporting on Financial Instruments •

The *aap* Group holds only primary financial instruments. On the assets side they consist mainly of participating interests, receivables and cash assets. Financial assets that are available for disposal are stated at market value, other financial assets at the depreciated cost of acquisition. Market values are established on the basis of acknowledged evaluation methods.

On the liabilities side the primary financial instruments consist mainly of liabilities stated at cost of acquisition. Holdings of primary financial instruments are shown in the balance sheet. The level of financial assets corresponds to the maximum risk of default. Where default risks are apparent, they are covered by value adjustments.

For details see figures at C. 2.

• (19) Cash Flow Statement •

The inflow of funds from current business activities includes inter alia:

Interest income €15K (previous year: €12K)
Interest expenses €44K (previous year: €498K)

Income tax paid totaled €87K (previous year: nil); income tax refunded was nil (previous year: nil).

• (20) Participating Interests •

I. Allied Companies (§ 271 Section 2 HGB)

This information relates to the annual financial statements according to IFRS.

II. Participation Interests

This information relates to preliminary management analyses to December 31, 2005 according to the German Commercial Code (HGB).

Insolvency proceedings were initiated on December 1, 2000 in respect of the assets of Cybernetic Vision AG and have yet to be concluded.

• (21) Other Financial Commitments •

Other financial commitments as defined by § 285 Section 3 HGB result from rental agreements totaling €3.427 million, of which €619K is due within a year, while €2.515 million is due within two to five years and €293K in more than five years.

Further financial commitments from leasing agreements total €438K, of which €266K is due in 2006 and €172K in 2007 and 2008.

Minimum lease payments	Financial leasing Nominal value	Cash value	Operate Leasing Nominal value
	€K	€K	€K
Payable within 1 year	3	3	263
Payable in 1 to 5 years	0	0	172
Payable after more than 5 years	0	0	0
	3	3	435

Commitments arising from financial leasing relate mainly to an installment purchase agreement for production machinery. The operational leasing agreements relate to short-term contracts for cars and in some cases provide for options to extend or buy.

Contingent liabilities up to a total of €284K exist for a period up to 2012.

Name	Domicile	Participation	Equity	Result
		%	€K	€K
1. <i>aap</i> Biomaterials GmbH & Co. KG*	Dieburg	100	-1,152	180
2. <i>aap</i> Biomaterials Verwaltungs-GmbH**	Dieburg	100	38	2
3. OSARTIS GmbH & Co. KG	Elsfeld	100	-1,129	924
4. OSARTIS Verwaltungs GmbH	Elsfeld	100	26	1
5. ADC Advanced Dental Care GmbH & Co. KG	Elsfeld	54	-8	6
6. ADC Advanced Dental Care Verwaltungs GmbH	Elsfeld	51	16	0

*Formerly Coripharm GmbH & Co. KG/**Formerly Coripharm Verwaltungs GmbH

Name	Domicile	Participation	Equity	Result
		%	€K	€K
7. Neue Magnetodyn GmbH	Munich	7.12	-	-20
8. AEQUOS Endoprothetik GmbH	Munich	11.2	-	-544
9. Cybernetic Vision AG Health Monitoring Technologies	Berlin	5.96	-	-

● (22) Related Enterprises and Persons ●

Related enterprises are *aap* GmbH, Neue Magnetodyn GmbH and AEQUOS Endoprothetik GmbH. In financial year 2005 business was conducted that led to the following items in the accounts:

<i>aap</i> GmbH	Neue Magnetodyn GmbH	AEQUOS Endoprothetik GmbH
€K	€K	€K
Trade receivables	168	103
Earnings	10	290
Liabilities/loans	-10	

Transactions are undertaken on market terms and conditions.

In accordance with a resolution adopted by the annual meeting of shareholders on June 10, 2005, Mr. Uwe Ahrens waived the loan he made to the company in 2000 totaling

€736K in return for 449,713 new shares. No interest was incurred in the year under review (previous year: €34K).

● (23) Management Board, Supervisory Board ●

Members of the company's Management Board in the year under review were:

Mr. Uwe Ahrens,
Dipl.-Ing., Berlin, (until Sept. 30, 2005)
Mr. Bruke Seyoum Alemu,
Dipl.-Ing., Berlin,
Mr. Oliver Bielenstein,
lic. oec. HSG, Berlin

Management remuneration totaled:

Mr. Uwe Ahrens €126,860.55
Mr. Bruke Seyoum Alemu €138,181.68
Mr. Oliver Bielenstein €123,059.20

The company has taken out D&O insurance cover for the management. Premiums paid in 2005 totaled €27,956.

Members of the Management Board hold the following supervisory board and advisory board directorships:

Mr. Uwe Ahrens:
bmp AG Venture Capital & Network Management, Berlin

Members of the company's Supervisory Board are:

Mr. Jürgen W. Krebs,
Business Management Specialist,
Kilchberg near Zurich, Switzerland
(Chairman)
Herr Rubino Di Girolamo,
Business Management Specialist,
Oberägeri near Zug, Switzerland
(Vice Chairman)
Herr Prof. Dr. Dr. med. Reinhard Schnettler,
University Professor, Giessen

The Supervisory Board members were elected for the full terms of office permitted under the company statute, until the end of the

General Meeting that resolves to approve the Supervisory Board's actions for the year 2007. Dr. Wolfgang Hohensee, Frankfurt am Main, was elected as a substitute for all three Supervisory Board members.

Supervisory Board remuneration in the financial year totaled €28K and consists of the following:

Mr. Jürgen W. Krebs €12,500
Mr. Rubino Di Girolamo €9,375
Prof. Dr. Dr. med.
Reinhard Schnettler €6,250

No payments were made and €2K was offset.

Members of the Supervisory Board hold the following Supervisory Board directorships in addition to their work on behalf of *aap* Implantate AG:

Mr. Jürgen W. Krebs
Merval Holding AG,
(Administrative Board President)
Reviderm AG
Mr. Rubino Di Girolamo
Deepblue Holding AG
(Administrative Board President)

Supervisory Board and Management Board members held the following shares:

	Shares		Options	
	2005	2004	2005	2004
Supervisory Board				
Jürgen W. Krebs	2,941,200	2,800,000	0	0
Rubino Di Girolamo	1,347,142	1,230,000	0	0
Prof. Dr. Dr. med. Reinhard Schnettler*	68,094	68,094	0	0
Management Board				
Uwe Ahrens (in his capacity as CEO until Sept. 30, 2005)	1,666,949	1,358,436	0	0
Bruke Seyoum Alemu	35,000	26,520	0	0
Oliver Bielenstein	484,548	469,889	0	0

* Prof. Dr. Dr. med. Reinhard Schnettler is entitled to a further 98,000 shares from the capital increase in kind in connection with the acquisition of shares in ADC.

● (24) Auditor's Fees ●

Auditor's fees stated as expenses in the financial year totaled:

a) For auditing the annual financial statements €45,000.00
b) Other certificates or evaluation services €34,822.85

● (25) Statement on the German Corporate Governance Code ●

aap Implantate AG has issued a declaration of compliance with the German Corporate Governance Code in accordance with § 161 German Stock Corporation Act (AktG) and made it available to shareholders.

● (26) Publication ●

The company's Management Board will on March 30, 2006 approve for publication these consolidated financial statements to December 31, 2005.

Berlin, March 28, 2006

The Management Board



Oliver Bielenstein
Management Board



Bruke Seyoum Alemu
Management Board

Auditor's Certification

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Consolidated Annual Financial Statement

We have audited the consolidated financial statements drawn up by *aap* Implantate Aktiengesellschaft, comprising the balance sheet, profit and loss statement, statement of changes in equity, flow of funds statement and notes to the consolidated financial statements, and the report on the situation of the Company and the Group for the financial year January 1, 2005 to December 31, 2005.

Drawing up the financial statements and the report on the situation of the Company and the Group in accordance with IFRS as applied in the EU and with the additional commercial law provisions of § 315 a Section 1 of the German Commercial Code (HGB) is the responsibility of *aap* Implantate Aktiengesellschaft's Management Board. Our task is to pass judgment, on the basis of our audit, on the consolidated financial statements and the report on the situation of the *aap* Implantate Aktiengesellschaft Company and Group.

We carried out our audit of the financial statements drawn up in accordance with § 317 HGB with due regard for the German principles of proper auditing laid down by the Institute of Auditors (IDW). These state that the audit is to be planned and executed in such a way as to be able to identify with a sufficient degree of certainty inaccuracies and infringements that have a material effect on the picture of the assets, financial and earnings position conveyed by the consolidated financial statements, taking into account the principles of proper accounting and the situation report for the *aap* Implantate Aktiengesellschaft Company and Group. In determining audit activities, knowledge about the company's business activities and economic and legal environment is taken into account, as are expectations of possible errors.

As a part of the audit, the effectiveness of the accounting-related internal audit system and the evidence provided for the information given in the consolidated financial statements and in the report on the situation of the *aap* Implantate Aktiengesellschaft Company and Group are assessed mainly on the basis of random checks.

The audit comprises assessing the annual financial statements of the companies included in the consolidated annual report, delimitation of the consolidation entity, the accounting principles applied and the fundamental assessments made by the Management Board, as well as forming an opinion on the overall picture presented in the financial statements and in the report on the situation of the *aap* Implantate Aktiengesellschaft Company and Group. We are of the opinion that our audit forms a sufficiently sound basis for our judgment.

Our audit led to no objections.

In our opinion, based on what we learnt in the course of the audit, the consolidated financial statements comply with IFRS as applied in the EU and with the additional commercial law provisions of § 315 a Section 1 of the German Commercial Code and convey, with due regard to these regulations, a picture of the Group's assets, financial and earnings position that is in accordance with the actual circumstances. The report on the situation of the Company and the Group tallies with the consolidated financial statements, conveys an accurate idea of the company's situation and accurately describes the risks of future development.

Berlin, March 30, 2006

Dr. Röver & Partner KG
Wirtschaftsprüfungsgesellschaft
Steuerberatungsgesellschaft

Helmut Schuhmann
Auditor

Bettina Grothe
Auditor

ANNUAL FINANCIAL STATEMENT

of *aap* Implantate AG

Balance Sheet

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Annual Financial Statement of aap Implantate AG

ASSETS	Notes	Dec. 31, 2005	Dec. 31, 2004
		€K	€K
A. Non-current assets	(4)		
I. Intangible assets			
1. Industrial property rights and similar rights and values		354	500
2. Goodwill		0	0
3. Prepayments made		10	0
		364	500
II. Tangible assets			
1. Land and buildings		493	500
2. Technical plant and machinery		1,428	1,242
3. Other fixtures and fittings tools and equipment		874	841
		2,795	2,583
III. Financial assets	(5)		
1. Shares in related parties	(15)	1,282	820
2. Loans to related parties		6,006	5,393
3. Investments	(15)	341	100
		7,629	6,313
B. Current assets	(6)		
I. Inventories			
1. Raw materials and supplies		656	648
2. Work in progress		685	806
3. Finished goods and goods for resale		4,806	4,435
		6,147	5,889
II. Accounts receivable and other assets			
1. Trade accounts receivable		796	724
2. Accounts receivable due to related parties	(15)	1,682	1,145
3. Accounts receivable due from companies in which an equity interest is held	(15)	168	145
4. Other assets		734	941
		3,380	2,955
III. Checks, cash on hand and on deposit with Deutsche Bundesbank, postal giro balances, in other banking accounts		1,274	1,141
C. Prepayments and accrued income	(7)	42	14
Total		21,631	19,395

LIABILITIES AND SHAREHOLDERS' EQUITY	Notes	Dec. 31, 2005	Dec. 31, 2004
		€K	€K
A. Shareholders' equity	(8)		
I. Subscribed Capital		16,520	14,609
II. Additional paid-in capital		12,012	10,849
III. Revenue Reserve			
1. Legal Reserve		42	42
2. Other revenue reserves		219	219
		261	
IV. Accumulated deficit		-11,503	-10,703
		17,290	15,016
B. Contributions made to implement the capital increase agreed	(8)	379	0
C. Special reserve with an equity portion		220	73
D. Accrued expenses			
1. Provisions for taxation		0	85
2. Other provisions	(9)	633	800
		633	885
E. Liabilities	(10)		
1. Due to banks		850	964
2. Advanced payment received		1,250	75
3. Trade accounts payable		572	943
4. Accounts payable due to related parties		0	15
5. Accounts payable due from companies in which an equity interest is held		10	193
6. Other liabilities			
thereof taxes: €145K (previous year: €103K)			
Thereof social security: €115K (previous year: €97K)		427	1,231
		3,109	3,422
Total		21,631	19,395

Liabilities arising from contingencies €0K (previous year: €0K).

Thereof due to related companies €0K (previous year: €0K).

T€ corresponds to €K.

Income Statement

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Annual Financial Statement of aap Implantate AG

	Notes	2005	2004
		€K	€K
1. Sales revenues	(11)	10,136	10,281
2. Increase in finished goods, inventories and work in progress		461	-72
3. Capitalized cost of self-constructed assets		571	714
4. Total operating performance		11,168	10,923
5. Other operating income	(13)	1,181	1,908
6. Cost of materials		-4,392	-4,212
a) Cost of raw materials, consumables and supplies and of purchased materials		-240	-100
b) Cost of purchased services		-4,632	-4,312
7. Personnel expenses	(12)		
a) Wages and salaries		-3,801	-2,933
b) Social security and other pension costs		-637	-551
		-4,438	-3,484
8. Depreciations			
a) of fixed intangible and tangible assets and capitalized start-up and business expansion expenses		-923	-958
b) of current assets to the extent that it exceeds normal company depreciation		0	-88
9. Other operating expenses	(13)	-3,588	-4,775
10. Investment income		0	142
11. Other interest and similar income			
- thereof from affiliated companies: €458K (Previous year: €113K)		475	127
12. Amortization of financial assets and investments classified as current assets		0	-294
13. Other interest and similar expenses		-40	-381
14. Result of ordinary business activities		-797	-1,191
15. Extraordinary income		0	5,464
16. Extraordinary expenses		0	-2,681
17. Extraordinary result		0	2,783
18. Taxes on income		0	-63
19. Other taxes		-2	-1
20. Net loss/income for the year		-799	1,528
21. Loss carryover		-10,704	-12,232
22. Balance sheet loss		-11,503	-10,703

I. Notes to the Financial Statements

• (1) General •

The financial statements as of December 31, 2005 are drawn up in conformity with German Commercial Code (Handelsgesetzbuch, HGB) regulations.

General regulations §§ 238 to 263 for all traders and supplementary regulations for large corporations according to §§ 264 seq. have been observed.

The Income Statement is drawn up using the total costs method.

The Income statement is laid out in conformity with §§ 266 and 275 German Commercial Code (HGB).

• (2) Consistency of presentation •

Unlike in previous years, the shares in Osartis GmbH & Co. KG and Osartis Verwaltungs GmbH are no longer shown as shares in undertakings with which the company is linked by virtue of participation, but as shares in affiliated undertakings.

Lendings to and receivables from these companies are therefore shown as being to and from affiliated undertakings. As agreed with the affiliated undertakings, in this financial year lendings existing in the previous year are partly reported under receivables from affiliated undertakings. The previous year's figures, including in the schedule of fixed assets, have been reclassified accordingly.

• (3) Accounting and valuation methods •

Intangible assets acquired for a consideration are reported at cost of acquisition and depreciated according to schedule.

Tangible fixed assets are valued at cost of acquisition or production and, where depreciable, taking into account scheduled depreciation.

Capitalized goods and services for own account were valued at cost of production. The extent of production costs corresponds to the amount reported for finished products.

Movable assets are depreciated in a straight line over the shortest useful life permitted under tax regulations. Assets with an acquisition cost of less than €410 are depreciated fully in the year of accession (§ 6 sub-

section 2 German Income Tax Act [Einkommensteuergesetz, EStG]) and treated as disposals.

Disposals are charged off at acquisition cost less accrued depreciation at the time of retirement.

Shares in associated companies and participating interests are reported at acquisition cost or at the lower values attributable to them. **Lendings** subject to interest are reported in the balance sheet at nominal value.

Inventories are valued at cost of acquisition or production or at the value attributable on the balance-sheet date. **Raw materials and supplies** were valued at cost prices, observing the strict principle of the lower of cost or market in accordance with § 253 sub-section 3 of the German Commercial Code (Handelsgesetzbuch, HGB).

Inventories are valued at cost of acquisition or production or at the value attributable on the balance-sheet date. **Raw materials and supplies** were valued at cost prices, observing the strict principle of the lower of cost or market in accordance with § 253 sub-section 3 of the German Commercial Code (Handelsgesetzbuch, HGB).

In order to follow the principle of the lower of cost of market as required by § 253 sub-section 3 HGB, write-downs were undertaken to reflect limited usability.

Receivables and other assets are valued at face value or at the lower value on the reporting date in accordance with § 253 sub-section 3 clause 2 HGB. Interest-free receivables with a residual term of more than one year are reported at cash value. The general credit risk is taken account of by a flat-rate deduction of 3% from all receivables for which no individual adjustments have been made.

Investment allowances are carried as liabilities under the heading **special investment allowance items**. They are written down in a straight line, with the resulting effect on earnings, in accordance with the useful economic life of the assets they helped to acquire.

Stock options granted to employees and management were reported in accordance with the position paper of the German Standardization Council (DSR) both as personnel expenses and as a transfer to capital reserves as per § 272 sub-section 2 item 2 HGB.

Transfer to capital reserves was undertaken over a performance period corresponding to the contractually agreed lock-up period of two years. Stock options issued were valued at the time of issue on the basis of the Black/Scholes option pricing model.

In creating **provisions**, appropriate account was taken of recognizable risks and uncertain liabilities. They are set at the value that prudent commercial judgment deems necessary.

Liabilities are reported at the repayment amount. Liabilities were translated into foreign currency at the repayment exchange rate when the liability was incurred or at the higher buying rate on the balance sheet date.

Contingent liabilities are possible for existing commitments based on past events that are not likely to involve an outflow of funds. They are not recorded in the balance sheet. No contingent liabilities existed on the balance-sheet date.

II. Notes to the Balance Sheet and the Income Statement

• (4) Expenses for expanding business operations and fixed assets •

For movements in fixed assets in 2005, see the schedule of fixed assets.

• (5) Financial assets •

Shares in affiliated undertakings

The shares in CORIPHARM Medizinprodukte GmbH & Co. KG, CORIPHARM Medizinprodukte Verwaltungs GmbH, CORIMED Kundenorientierte Medizinprodukte GmbH, Osartis GmbH & Co. KG and Osartis Verwaltungs GmbH transferred to the Company on October 1, 2000 were reported at the nominal value of the registered shares in *aap* Implantate AG to be issued to the transferring parties plus the cash payment made. Acquisition costs were reduced because of a contractual entitlement to purchase price reductions due to breaches of warranty.

The shares in ADC Advanced Dental Care GmbH & Co. KG and der ADC Advanced Dental Care Verwaltungs GmbH that were transferred to the Company on October 1, 2005 were reported at the nominal value of the registered shares in *aap* Implantate AG to be issued to the transferring parties plus expenses incidental to acquisition.

● (6) Current assets ●

Amounts receivable from allied undertakings include receivables from the current financial year and loans to assist liquidity.

Other assets includes a breach of warranty claim amounting to €646K against the contributing partners of the shares in CORIPHARM Medizinprodukte GmbH & Co. KG, CORIPHARM Medizinprodukte Verwaltungs-GmbH and CORIMED Kundenorientierte Medizinprodukte GmbH.

● (7) Accruals and deferrals ●

Inter alia, discounts totaling €2K are shown.

● (8) Equity ●

The Company's capital stock on December 31, 2005 was €16,519,157.00. It was divided into 16,519,157 individual bearer shares.

By resolution of the Annual Meeting of Shareholders held on June 10, 2005, the Company's capital stock was increased from €14,608,587.00 to €15,058,300.00 by issuing 449,713 new bearer shares, each with an arithmetical share of €1.00 in capital stock. The capital increase was effected in return for contributions of investment in kind.

The capital increase was recorded in the commercial register on August 29, 2005.

By resolution of the Annual Meeting of Shareholders held on June 10, 2005, the Management Board was authorized to increase the Company's capital stock on one or more occasions by up to a total of €7,300,000.00 in return for contributions in cash or investment in kind and when doing so to specify the terms of the share issue.

On the basis of this authorization, the Management Board on September 7, 2005 resolved to increase capital stock by €1,460,857.00 to €16,519,157.00 by issuing 1,460,857 bearer shares, each with an arithmetical share of €1.00 in the capital stock. The new registered shares were offered to Company shareholders for subscription in a ratio of 21:2 by way of direct subscription rights. The issue amount and subscription price per new registered share was €1.60.

This capital increase was recorded in the commercial register on September 30, 2005.

By resolution of the Management Board dated December 14, 2005, as approved by the Supervisory Board on February 14, 2005, the Company's capital stock was increased by €379,000.00 from €16,519,157.00 to €16,898,157.00 from Authorized Capital. This was effected by issuing 379,000 new bearer shares with an arithmetical share in capital stock of €1.00 per share. These shares were issued ruling out shareholders' sub-

scription rights in return for contributions in kind. The contributions in kind were certain limited partner's shares with a total nominal value of €54,000.00 in ADC Advanced Dental Care GmbH & Co. KG, which is headquartered in Elsenfeld and registered in the commercial register of Aschaffenburg district court, registration number HRA 3954, along with a participating interest with a nominal value of €12,500.00 in ADC Advanced Dental Care Verwaltungs GmbH, which is headquartered in Elsenfeld and registered in the commercial register of Aschaffenburg district court, registration number HRB 8174. These shares are entitled to participate in profits from January 1, 2005.

This capital increase has not yet been registered. It is reported under the special item "payments made to effect the resolved capital increase."

The statutory reserve totaled €41,703.95 at the end of the financial year and, together with capital reserve, exceeded one tenth of capital stock.

Conditional capital

The Annual Meeting of Shareholders held on May 29, 2001 approved a conditional increase of up to €96,000.00 in capital stock by the issue of up to 96,000 individual bearer shares. New shares are entitled to share in profit from the start of the financial year during which they were issued. The conditional capital is solely for the purpose of awarding stock options to employees and management of the Company or of an affiliated undertaking, as follows:

2001

- 17.1% to board members and senior executives of the company and affiliated undertakings
- 25% to senior executives
- 57.9% to employees of the Company and of affiliated undertakings

Stock options are granted in accordance with the relevant provisions of the 2001 stock option plan. The opportunity to issue subscription rights existed until January 12, 2006. The Company did not take advantage of this opportunity. The conditional capital was not used.

Authorized Capital

The General Meeting held on June 10, 2005 authorized the Management Board to increase the company's capital stock by June 10, 2010 on one or more occasions by up to €7,300,000 in cash or investment in kind and to lay down the terms and conditions of the share issue. Subject to Supervisory Board approval, subscription rights for existing shareholders may be ruled out

- a) to balance residual amounts,
- b) if the capital increase in cash does not exceed 10% of the capital stock and the issue price of the new shares is not substantially lower than the market price (§ 186 Section 3 Sentence 4 German Stock Corporation Act, AktG),
- c) to issue shares in return for contributions as part of an acquisition of companies, parts of companies or participations in companies (including conversions by the terms of the Conversion Act)
- d) to issue shares to strategic partners,
- e) to serve conversion or subscription rights held by holders of stock options, convertible bonds, stock warrants and/ or participation certificates,
- f) to issue shares to employees and directors of the company and to employees and management of associated companies as part of a stock option plan,
- g) in payment for consulting services,
- h) to issue shares to lenders in place of interest payments in cash or in addition thereto (so-called equity kickers), especially in connection with mezzanine financing,
- i) to repay loans or other liabilities.

Please see the schedule of equity.

● (9) Provisions ●

Please see provisions for movements in other provisions during the financial year.

● (10) Liabilities ●

Please see liabilities for times to maturity of liabilities, broken down by balance-sheet heading.

● (11) Sales revenues ●

Sales revenues are apportioned to geographically defined markets, as follows:

	2005	2004
	€K	€K
Germany	8,521	8,570
European Union	558	775
Other countries	1,275	1,123
Sales deductions	-218	-187
	10,136	10,281

● (12) Breakdown of personnel by category: ●

	2005	2004
Average number of employees:	92	93
of which		
Blue-collar workers	39	46
Salaried employees	53	47
Full-time	88	87
Part-time	4	6
Casual	0	0
	92	93
Administration	15	27
Sales	35	19
Production	38	44
Development	4	3
	92	93

● (13) Income and expenditure unrelated to the accounting period ●

In the financial year, earnings of €61K unrelated to the accounting period were accrued, mainly due to a release from commitments.

Expenses unrelated to the accounting period during the financial year totaled €35K and relate mainly to the relinquishment of a bonus claim dating from financial year 2004.

● (14) Auditor's fees ●

Auditors' fees posted as expenses in the financial year were as follows:

- for auditing the financial statements (individual financial statement and consolidated financial statement) €45,000.00
- other certification or appraisal services €34,822.85

III. Other Information

● (15) Participating interests ●

I. Affiliated undertakings (§ 271 sub-section 2 HGB)

Name	Domicile	Holding %	Equity €K	Result €K
1. <i>aap</i> Biomaterials GmbH & Co. KG (previously: CORIPHARM GmbH & Co. KG)	Dieburg	100	-4,486	562
2. <i>aap</i> Biomaterials Verwaltungs GmbH (previously: Coripharm Verwaltungs-GmbH)	Dieburg	100	38	2
3. Osartis GmbH & Co. KG	Elsfeld	100	-1,079	1,061
4. Osartis Verwaltungs GmbH	Elsfeld	100	26	0
5. ADC Advanced Dental Care GmbH & Co. KG	Elsfeld	54	-8	6
6. ADC Advanced Dental Care Verwaltungs GmbH	Elsfeld	51	16	0

II. Participations

Name	Domicile	Holding %	Equity €K	Result €K
7. Neue Magnetodyn GmbH	Munich	7.12	-	-20
8. AEQUOS Endoprothetik GmbH (previously HJS Gelenk-System GmbH)	Munich	11.20	-	-544
9. Cybernetic Vision AG Health Monitoring Technologies	Berlin	5.96	-	-

This information relates to managerial analyses as at December 31, 2005.

GEOT Gesellschaft für Elektro-Osteo-Therapie mbH was merged with Neue Magnetodyn GmbH with effect from January 1, 2005.

On December 1, 2000, insolvency proceedings were initiated in respect of the assets of Cybernetic Vision AG Health Monitoring.

● (16) Other financial commitments ●

Other financial commitments as defined by § 285 No. 3 German Commercial Code (HGB) arise from rental agreements totaling €2,415,000 of which €416K falls due within one year, while €1,706,000 is payable within two to five years and €293K in more than five years.

Leasing agreements give rise to other financial commitments totaling €407K, of which €235K is payable in 2006 and €172K in 2007 to 2008.

● (17) Management Board, Supervisory Board ●

The members of the Company's Management Board in the year under review were:

Mr. Uwe Ahrens,
Dipl.-Ing., Berlin,
(until September 30, 2005)

Mr. Bruke Seyoum Alemu,
Dipl.-Ing., Berlin

Mr. Oliver Bielenstein,
Lic. oec. HSG, Berlin

Management remuneration was as follows:

<u>Mr. Uwe Ahrens</u>	€126,860.55
<u>Mr. Bruke Seyoum Alemu</u>	€138,181.68
<u>Mr. Oliver Bielenstein</u>	€123,059.20

The Company took out D&O insurance for the management. Premiums in 2005 totaled €27,956.00.

Members of the Management Board hold the following supervisory board directorships:

Mr. Uwe Ahrens
bmp AG Venture Capital &
Network Management, Berlin

The members of the Company's Supervisory Board in the year under review were:

Mr. Jürgen W. Krebs
Business Management Specialist,
Kilchberg near Zurich, Switzerland
(Chairman)

Mr. Rubino di Girolamo
Business Management Specialist,
Oberägeri near Zug, Switzerland
(Vice-Chairman)

Mr. Prof. Dr. Dr. med. Reinhard Schnettler
University Professor, Giessen

The Supervisory Board members were elected for the full term of office permitted under the Company's statute, until the end of the General Meeting that resolves to approve their actions in fiscal 2007. Dr. Wolfgang Hohensee, Frankfurt am Main was elected as a substitute for all three supervisory board members.

Supervisory Board remuneration in the financial year totaled €29,000, broken down as follows:

Mr. Jürgen W. Krebs €12,500

Mr. Rubino di Girolamo €9,375

Prof. Dr. Dr. med. Reinhard Schnettler €6,250

There were no disbursements. The sum of €2K was offset.

Members of the Supervisory Board hold the following Supervisory Board directorships in addition to their work for aap Implantate AG:

Mr. Jürgen W. Krebs

Merval Holding AG,
Reviderm AG
(Chairman, Board of Director)

Mr. Rubino di Girolamo

Deepblue Holding AG
(President, Board of Directors)

The members of the Supervisory Board hold the following shares:

	Shares		Options	
	2005	2004	2005	2004
Supervisory Board				
Jürgen W. Krebs	2,941,200	2,800,000	0	0
Rubino di Girolamo	1,347,142	1,230,000	0	0
Prof. Dr. Dr. med. Reinhard Schnettler*)	68,094	68,094	0	0
Management Board				
Uwe Ahrens (in his capacity as chairman until September 30, 2005)	1,666,949	1,358,436	0	0
Bruke Seyoum Alemu	35,000	26,520	0	0
Oliver Bielenstein	484,548	469,889	0	0

*) Following the real capital increase in connection with the acquisition of shares in ADC KG, Prof. Dr. Dr. med. Reinhard Schnettler is entitled to a further 98,000 further shares.

● (18) German Corporate Governance Code Declaration ●

The Company has issued a statement on its application of the German Corporate Governance Code as prescribed by § 161 German Stock Corporation Act (AktG) and has made it accessible to shareholders.

Berlin, March 28, 2006

The Management Board

Oliver Bielenstein
Management Board

Bruke Seyoum Alemu
Management Board

Development of Capital Stock

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	Subscribed capital	Capital reserve	Revenue Reserves		Balance sheet loss	Total
	€K	€K	Legal €K	Other €K	€K	€K
As at 01.01.2004	4,870	10,849	42	219	-12,114	3,866
Loss carryover resulting from merger	-	-	-	-	-118	-118
Capital increase	9,739	-	-	-	-	9,739
Net income for the year	-	-	-	-	1,528	1,528
As at 12.31.2004/01.01.2005	14,609	10,849	42	219	-10,704	15,015
First capital increase	450	286	-	-	-	736
Second capital increase	1,461	877	-	-	-	2,338
Net income for the year	-	-	-	-	-799	-799
As at 12.31.2005	16,520	12,012	42	219	-11,503	17,290

Conditional capital: €96K (previous year: €96K)

Schedule of Provisions

	As at 01.01.2005	Take-up	Retransfer	Transfer	As at 12.31.2005
	€K	€K	€K	€K	€K
Commitments to employees	149	124	19	148	154
Bonuses and commission	40	39	1	101	101
Unpaid invoices	292	187	53	226	278
Financial statements and audit	114	85	29	100	100
Warranties	25	0	25	0	0
Provision for impending losses	0	0	0	0	0
Litigation risks and costs	10	0	10	0	0
Contingent liabilities	170	169	1	0	0
Share listing	0	0	0	0	0
	800	604	138	575	633

T€ corresponds to €K.

Schedule of Fixed Asset Movements

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Annual Financial Statement of aap Implantate AG

HISTORICAL COSTS

	AS AT 01.01.2005	ADDITIONS	DISPOSALS	REBOOKINGS	AS AT 12.31.2005
	€K	€K	€K	€K	€K
A. Start-up and business expansion expenses	639	0	0	0	639
B. Fixed assets					
I. Intangible assets					
1. Industrial property rights and similar rights and values	3,520	47	0	0	3,568
2. Goodwill	51	0	0	0	51
3. Prepayments made	0	10	0	0	10
	3,571	57	0	0	3,629
II. Tangible assets					
1. Land and buildings	873	0	0	0	873
2. Plant and machinery	5,943	595	0	0	6,538
3. Other fixtures and fittings, tools and equipment	2,823	559	568	0	2,814
	9,639	1,154	568	0	10,225
III. Financial assets					
1. Shares in affiliated companies	820	462	0	0	1,282
2. Loans to affiliated companies	5,393	801	188	0	6,006
3. Investments	184	27	0	0	211
4. Loans to companies in which an equity interest is held	294	0	0	0	294
5. Other loans	0	0	0	0	0
	6,691	1,290	188	0	7,793
TOTAL	20,540	2,501	756	0	22,286

T€ corresponds to €K.

ACCUMULATED DEPRECIATION					BOOK VALUES		
	AS AT 01.01.2005	DEPRECIATIONS FISCAL YEAR	DISPOSALS	AS AT 12.31.2005	WRITE-UPS 2005	AS AT 12.31.2005	AS AT 12.31.2004
	€K	€K	€K	€K	€K	€K	€K
	639	0	0	639	0	0	0
	3,021	193	0	3,214	0	354	499
	51	0	0	51	0	0	0
	0	0	0	0	0	10	0
	3,072	193	0	3,265	0	364	499
	373	7	0	380	0	493	500
	4,701	409	0	5,110	0	1,428	1,242
	1,981	314	355	1,940	0	874	842
	7,055	730	355	7,430	0	2,795	2,584
	0	0	0	0	0	1,282	820
	0	0	0	0	0	6,006	5,393
	84	0	0	84	214	341	100
	294	0	0	294	0	0	0
	0	0	0	0	0	0	0
	378	0	0	378	214	7,629	6,313
	11,144	923	355	11,712	214	10,788	9,396

Schedule of Liabilities

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Annual Financial Statement of aap Implantate AG

	12.31.2005	Due within		
	Total	up to 1 year	1-5 years	more than 5 years
	€K	€K	€K	€K
Due to banks	850	579	271	0
Advances from customers	1,250	600	650	0
Accounts payable	572	572	0	0
Due to affiliated companies	0	0	0	0
thereof accounts payable	0	0	0	0
Due to companies in which an equity interest is held	10	10	0	0
Other liabilities	427	427	0	0
Thereof leasing	3	3	0	0
taxes	145	145	0	0
social security	115	115	0	0
	3,109	2,188	921	0

With recourse to a €465K overdraft facility all present and future trade receivables were assigned to Deutsche Bank AG, Berlin.

T€ corresponds to €K.

Auditor's Certification

We have audited the financial statements of *aap* Implantate Aktiengesellschaft for the financial year January 1 to December 31, 2005, comprising the balance sheet, profit and loss statement and notes, including the accounting and the report on the situation of the company and the group. Accounting and drawing up the financial statements and report on the situation of the *aap* Implantate Aktiengesellschaft company and group in accordance with German commercial law are the responsibility of the Company's legal representatives. Our task is to pass judgment, on the basis of our audit, on the financial statements, including the accounting, and on the report on the situation of the *aap* Implantate Aktiengesellschaft company and group.

We conducted our audit of the financial statements drawn up in accordance with § 317 of the German Commercial Code (HGB) with due regard for the German principles of proper auditing laid down by the Institute of Auditors (IDW). These state that the audit is to be planned and executed in such a way as to be able to identify with a sufficient degree of certainty inaccuracies and infringements that have a material effect on the picture of the asset, financial and earnings position conveyed by the financial statements, taking into account the principles of proper accounting, and by the situation report for the *aap* Implantate Aktiengesellschaft company and group. In determining audit activities, knowledge about the company's business activities and economic and legal environment is taken into account, as are expectations of potential errors.

As part of the audit, the effectiveness of the accounting-related internal audit system and the evidence provided for the information given in the accounts, the financial statements and the report in the situation of the *aap* Implantate Aktiengesellschaft company and group are assessed mainly on the basis of random checks.

The audit comprises an assessment the accounting principles applied and the material assessments made by the legal representatives along with an appraisal of the overall picture presented in the financial statements and in the report on the situation of the *aap* Implantate Aktiengesellschaft company and group. We are of the opinion that our audit forms a sufficiently sound basis for our judgment.

Our audit led to no objections.

In our opinion, based on what we learned in the course of the audit, the financial statements meet the legal requirements and, taking into account the principles of proper accounting, convey a picture of the company's asset, financial and earnings situation that accords with the actual circumstances. The report on the situation of the *aap* Implantate Aktiengesellschaft company and group tallies with the financial statements, generally conveys an accurate picture of the company's situation and accurately describes the opportunities and risks of future development.

Berlin, March 29, 2006

Dr. Röver & Partner KG
Wirtschaftsprüfungsgesellschaft
Steuerberatungsgesellschaft

Helmut Schuhmann
Auditor

Bettina Grothe
Auditor

Results adjusted to DVFA/SG according to IFRS

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Annual Financial Statement of the Group

	2005	2004
	€K	€K
1. Net loss/income for the year	655	-140
2. Adjustments according to DVFA/SG	0	-422
3. Consolidated DVFA/SG result	655	-562
4. Payable to third parties	-4	0
5. Consolidated DVFA/SG result for aap Implantate AG stockholders	651	-562
	€	€
Consolidated DVFA/SG earnings per share for aap Implantate AG stockholders	0,04	-0,07

Results adjusted to DVFA/SG according to IFRS

	2005	2004
	€K	€K
1. Net loss/income for the year	655	-140
2. Depreciations on fixed assets	1,471	1,519
3. Depreciation on special item for investment allowances	27	-124
4. Adjustments according to DVFA/SG	0	-422
5. Consolidated DVFA/SG cash earnings	2,153	833
6. Payable to third parties	-4	0
7. DVFA/SG cash earnings for aap Implantate AG stockholders	2,149	833
	€	€
DVFA/SG cash earnings per share for aap Implantate AG stockholders	0,14	0,10

T€ corresponds to €K.

Report by the Supervisory Board

For *aap* Implantate AG the focus of financial year 2005 was on safeguarding and enlarging the company. It was, above all, a year that saw the acquisition of new large customers in the development and manufacture of bone cements and cementing techniques (Biomet Europe, Heraeus Medical) and the signing of a distribution agreement for the new Biomet bone cements. The loss of the previous commercial business in Palacos® bone cement was thereby more than offset.

Enlargement of the Group's structure was achieved by acquiring the remaining 51% of the previous minority holding in Osartis and 54% of ADC – Advanced Dental Care, Elsenfeld, in return for 379,000 *aap* shares. The Osartis takeover was made possible by a smaller-scale capital increase in the early fall of 2005. We should like to take this opportunity of thanking existing and new shareholders for having taken the company forward in this way.

After the longstanding Management Board chairman Uwe Ahrens stepped down on September 30, 2005, the company was represented most successfully by its two directors Bruke Seyoum Alemu and Oliver Bielenstein. We thank Mr. Ahrens for his meritorious service since the founding of the company.

The Supervisory Board performed its statutory duties and duties laid down in the articles of incorporation, closely following and monitoring the running of the group by the Management Board. In addition to monthly reports inter the Supervisory Board receives inter alia a weekly cash and debt position and daily sales information. Outside of regular meetings, Supervisory Board members are briefed regularly by the Management Board and offer advice in numerous one-on-one talks on important company and group matters.

Last financial year the focus of consultations was on the following issues:

- Acquiring Biomet as a new major customer and the accompanying major increase in OEM activity in developing and manufacturing bone cement
- Ensuring the availability of a bone cement for the company to sell in Germany
- Regaining credit lines with banks and implementing the capital increase last fall to ensure growth opportunities for the company
- Reorganizing Management Board areas of responsibility and strengthening organizational structures at both locations after Uwe Ahrens stepped down as Management Board chairman
- Acquiring two biomaterials companies.

The Supervisory Board was briefed regularly and fully by the Management Board orally and in writing on the economic and financial position, the group's development and, above all, on matters of operating activities and their implementation and further development, and on all other important business transactions. The Supervisory Board discussed this information intensively with the Management Board and made the decisions required of it by law and by the articles of incorporation.

In the reporting year the Supervisory Board held five ordinary meetings and one extraordinary meeting. All Supervisory Board members attended all meetings. As in the previous year Prof. Dr. Dr. Schnettler here deserves special thanks for his support and his contribution in terms of medical technology know-how.

The annual financial statements and consolidated financial statements and the combined management report of *aap* Implantate AG and the group for financial year

2005 were audited by accountants Dr. Röver & Partner KG, Berlin, as instructed by the Supervisory Board and received their unqualified audit certificate. The consolidated financial statements were drawn up in accordance with International Financial Reporting Standards (IFRS). The auditor confirmed that the consolidated financial statements and consolidated management report complied with IFRS as applicable in the EU and with the additional commercial law requirements of § 315a of the German commercial code (HGB). The annual financial statement and management report, consolidated financial statement and consolidated management report and the auditor's reports were submitted to the Supervisory Board. They were discussed in detail. The auditor who signed the auditor's report attended the Supervisory Board's discussion of the documents submitted, reported to the Supervisory Board on the fundamental audit findings and was on hand to answer questions.

The Supervisory Board reviewed the annual financial statement and management report and the consolidated financial statement and consolidated management report. The findings of its review did not lead to objections being raised. The Supervisory Board endorsed the financial statement for the year ending December 31, 2005, which is thereby approved.

A special report on the IT system was commissioned in the fall and submitted to the company in February 2006 with good results and a number of suggested improvements.

The Supervisory Board would like to thank all employees, including those who have left the company, and members of the Management Board for their work in the year under review, and their families for the understanding shown for what, at times, was a high workload handled by their partners.

We would also like to take this opportunity of thanking our customers, suppliers and banks for their confidence and accommodation, plus a special thank you to the Advisory Board members for their contributions and their support, especially on matters of product development.

We face further challenges in 2006. They will mainly be in the structural processing of high growth, the further expansion of operative business, and the integration of Osartis and ADC and possible further acquisitions in both segments. The signing in February 2006 of a long-term distribution contract for the product Ostim in the dental sector with Heraeus Kulzer, a leading European provider in the dental sector, is a further successful step in the company's progress after reconstruction in 2004.

Berlin, March 30, 2006

The Supervisory Board

Legal Note

These annual financial statements include forward-looking statements. These statements include forecasts for the company's products, sales revenues and results, *aap*'s plans for financial year 2006 in respect of research and development activities, the expansion of sales and expectations in respect of reaching certain product development milestones. These statements are based on assessments made by the Management, on assumptions made by *aap* and on information that is currently available to the company. A number of factors that the compa-

ny cannot foresee with certainty could lead to the actual results, including *aap*'s financial, sales and earnings position, differing materially from those explicitly or implicitly assumed for the statements.

Forward-looking statements are only valid as of the date when they are made. The company does not intend and assumes no obligation to update forward-looking statements or adjust them to future events or developments.



© **aap Implantate AG**
Lorenzweg 5 • 12099 Berlin
Germany
Fon +49 30 75019-0
Fax +49 30 75019-222
customer.service@aap.de
www.aap.de

Errors and omissions excepted.

Design, Illustrations and Composing:
deSIGN graphic | Wolfram Passlack, Berlin

Foto Page 4:
Idris Kolodziej, Berlin

▶ **aap Implantate AG**
Lorenzweg 5 • 12099 Berlin
Germany
Fon +49 30 75019-0
Fax +49 30 75019-222
customer.service@aap.de
www.aap.de

▶ **aap Biomaterials GmbH & Co. KG**
Lagerstraße 11-15 • 64807 Dieburg
Germany
Fon +49 6071 929-0
Fax +49 6071 929-100
biomaterials@aap.de
www.aap.de

▶ **OSARTIS**
GmbH & Co. KG
Industrie Center Oberburg
63784 Oberburg
Germany
Fon +49 6022 812002
Fax +49 6022 812004
info@osartis.de
www.osartis.de