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# ANNUAL REPORT 2005

Actionable Analytics.

Predictive Leads.

Exceptional Results.

# Angoss Software Corporation

Angoss provides best-in-class predictive analytics software systems that help sales, marketing and risk professionals make "Better Business Decisions. Every Day."™

### FundGuard™

Predictive leads target & prioritize best value advisors.
Accelerating growth in assets under management.
For mutual funds and wealth management companies.

### Telecom Marketing Analytics™

Strategic segmentation provides lists of best offer opportunities.
Maximizing value, for every customer.
For carriers, content and technology providers.

### Credit Risk Analytics™

Better risk | reward credit approval and collection decisions.
Real-time alerts and recovery strategies reduce losses.
For consumer and small business credit portfolio managers.

### Claims & Payments Analysis™

Claims verification automation and abuse flagging.
Speeding approvals, with higher impact, exceptions based review.
For claims and payments administrators and investigators.

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# President's Message to Shareholders

Enclosed is our Annual Report for 2005.

Angoss Software empowers people to make *"Better Business Decisions. Every Day."*™ Some of the world's leading financial services, telecom, life sciences, and retail organizations use Angoss data mining and predictive analytics solutions to grow revenues, while reducing risk and cost.

Angoss helps our clients use their own marketing, sales and other transactional data to discover the key drivers of customer behaviors, predict future trends and events, and act with confidence by making analytics results actionable for business users across their companies.

We are recognized as one of the world's most innovative data mining and predictive analytics software companies. Our mission builds on this tradition of industry leadership, by bringing new analytics capabilities that deliver actionable insight, revenue growth and performance improvement to more organizations.

During 2005, we achieved 9% revenue growth to over $6 million in revenues, with 29% growth in direct Angoss software and solution sales offset by disappointing partner sales which were down 94% from 2004 results.

Our growth resulted from continued expansion of our highly successful **KnowledgeSEEKER®** and **KnowledgeSTUDIO®** packaged software sales, and the successful introduction of expanded solutions such as **FundGuard™** and **Telecom Marketing Analytics™** combining our software with expanded implementation services to early adopting clients in the financial services and telecommunications industries.

Angoss solutions helped our clients achieve revenue growth this year. We provided a more disciplined, data driven approach to their marketing and sales activities, teams, supplier communities, distribution and channel partnerships, and to the business processes connecting all of them. Angoss predictive analytics solutions delivered significant, demonstrable return on investment to our customers. They also involved higher value, higher visibility projects, broader use of Angoss software, and a more comprehensive set of implementation services.

In short, we ended 2005 with an expanded set of predictive analytics solutions to support business growth, with what we believe is one of North America's best predictive analytics expert services teams to implement them, and with a marketing and sales organization that continues to improve its effectiveness.

As we move into 2006, our focus continues to be on expanding our direct revenues, with a solutions led business strategy targeting the industry segments and predictive analytics business opportunities - increasingly in sales and marketing areas - that we believe will drive the most immediate impact and long term value for our customers, and give us the best prospect of creating more value for our shareholders.

I look forward to meeting with shareholders at our annual meeting this year to review our accomplishments in 2005 and to discuss our outlook for 2006.

Yours truly,

Eric Apps

# 2005 Review

## 2005 Goals and Achievements

**Increase KnowledgeSEEKER® and KnowledgeSTUDIO® packaged software sales with marketers and risk managers at the world's largest and most successful financial services organization, deliver major new product releases.**

*We grew our **KnowledgeSEEKER®** and **KnowledgeSTUDIO®** user base with leading organizations in North American and European financial services and telecommunications verticals, while adding users at exciting new corporate customers such as Yahoo!, eBay and PayPal. We also added new financial services and telecom customers in dynamic growth markets, such as India and China. Our releases of **KnowledgeSEEKER®** 5 and **KnowledgeSTUDIO®** 5 were well received by both existing customers and prospects.*

**Introduce to the market four new Angoss predictive analytics solutions: FundGuard™, Telecom Marketing Analytics™, Credit Risk Analytics™, and Claims & Payments Analysis™.**

*We successfully brought our predictive analytics solutions to market, with initial clients achieving significant business value from our **FundGuard™** and **Telecom Marketing Analytics™** solutions. **FundGuard™** alone generated well over $200 million in incremental assets under management for initial clients during trial implementations. Deployment of these solutions continues to expand. Although adoption of our risk management solutions has been slower, we expect these solutions to become increasingly important to our customers.*

**Expand marketing, sales and services investments supporting our predictive analytics solutions offerings, while improving the efficiency of packaged software sales.**

*We improved our sales productivity, with a smaller sales organization delivering higher revenues through improved marketing initiatives, better sales efficiency, and better alignment of our sales teams with company goals.*

**Pursue higher average transaction value solutions with our clients, by focusing on business opportunities where we can deliver significant business value to them, with solutions that combine the market proven capabilities of Angoss software, with the uniquely differentiated capabilities of our expert services organization.**

*We made progress in extending our integrated software and expert services delivery model, providing higher value to our clients, enabling higher average transaction value per deal, and creating a stronger foundation for future growth.*

**Grow shareholder value by delivering improved revenue growth, and improved operating performance, focusing on cash flow generation and operating profitability.**

*Solutions led direct revenue growth combined with solid financial management of headcount and operating expenses, resulted in significantly improved operating performance of the Company, while retiring the first tranche of the preferred share financing we secured in 2003.*

## 2005 Business Highlights

### Delivering Fund Wholesalers Predictive Leads On RIM Blackberry™ Platform

Angoss excels in making predictive analytics actionable for business users. The Angoss **FundGuard**™ solution was successfully launched in 2005. **FundGuard**™ helps mutual fund managers drive growth in assets under management while reducing redemption risk. **FundGuard™** has already generated well over $200 million in incremental growth in assets under management with adopting clients during initial trial phases. Specifically designed for the mutual fund and wealth management industries, **FundGuard**™ uses advanced analytics, strategic segmentation, channel optimization, and sales territory and lead management tools to deliver improved sales force productivity with fast time to solution and low implementation cost.

**FundGuard**™ is now also enabling one Angoss client to further accelerate sales productivity and asset growth by delivering predictive leads to its sales teams through their **RIM Blackberry**™ wireless devices. We are partnering with third parties delivering sales force automation solutions on the Microsoft® platform, and leveraging the capabilities of the RIM Blackberry™ platform, to make prediction analytics actionable for sales and marketing professionals.

### Telecom Marketing Analytics™ Helps Telco Marketers Better Target SME Prospects

Angoss continues to expand use of its **Telecom Marketing Analytics**™ solution at two North American telecommunications clients. Angoss is helping these clients identify, target and win share in highest value consumer and small business market segments, with more targeted, relevant and impactful launches of new VOIP and solutions based offerings.

Specifically designed for the communications industry, Angoss **Telecom Marketing Analytics™** provides sales and marketing managers with advanced analytics, planning and forecasting tools enabling strategic segmentation and value assessment of consumer and small business markets, targeted lead generation with next offer analysis, optimization of sales force channel activities, improved product mix analysis and inventory forecasting, and reduced customer churn.

During 2006, we expect to expand this offering to additional North American customers, and to replicate our success in the telecommunications segment with the sales and marketing organizations of new clients in the networks, systems and content arenas.

### KnowledgeSEEKER® & KnowledgeSTUDIO® Growth Ahead of Industry Projections

Key differentiators in selecting Angoss predictive analytics software include usability, flexibility, scalability, interoperability, and total cost of ownership. Notable 2005 customer wins included continued expansion at many of North America's and Europe's largest financial services organizations and new customer relationships with leading on-line retailing brands.

During 2005, the Company continued to deliver growth in analytics software sales well in excess of reported industry growth rates, with strong positive customer reception for the Company's **KnowledgeSEEKER**® 5 and **KnowledgeSTUDIO**® 5 releases. The Company has also introduced a new software offering as part of our solutions portfolio, **StrategyBuilder**™. **StrategyBuilder**™ maintains our demonstrated lead in innovation and thought

leadership, making it even easier for marketers and risk managers to reduce time to strategy, and time to business value.

## 2005 Results Review

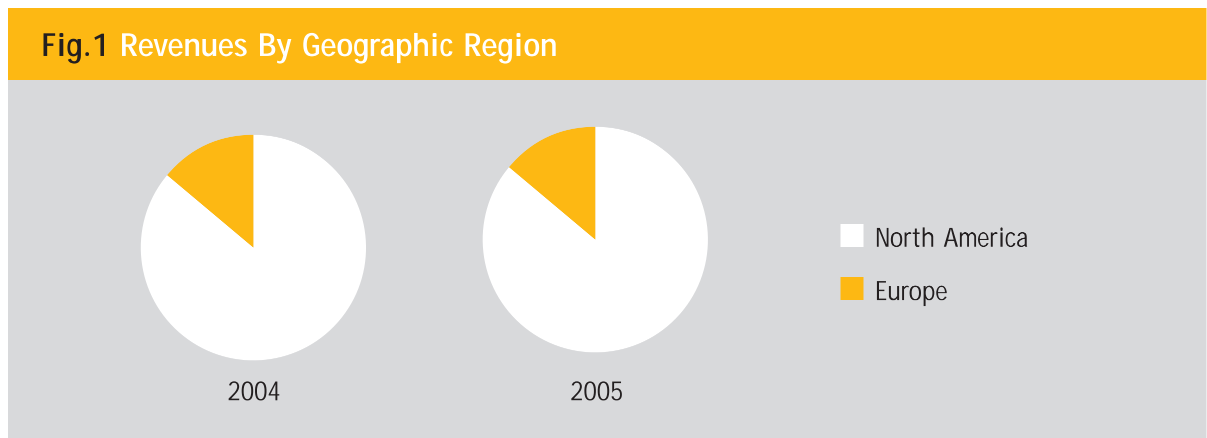
**Revenues By Geographic Region** *(See Fig.1)*

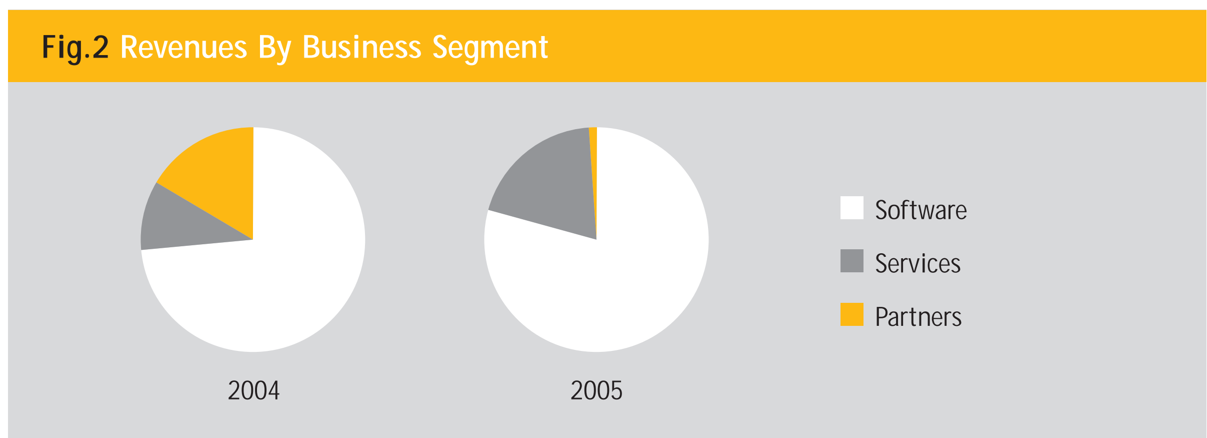
North America and European revenues both grew, while maintaining the same relative contributions to overall revenues. Outside of North America and Europe, Angoss has not had a meaningful sales presence, with the exception of local market affiliates of our global clients. We will be exploring opportunities to expand our direct investment in North American and European sales and expert services, while initiating more significant, mutually rewarding partnering relationships in other key markets during 2006.

**Revenues By Business Segment** *(See Fig.2)*

Growth in software and services revenues associated with direct solution sales, was offset by the loss of almost $1 million in partner originated revenues. This decline represented a drag on our quarterly direct year over year revenue growth. As a result of disappointing performance of partnerships, and broader technology industry consolidation trends, we are re-evaluating our partnering strategies.

Our focus is increasingly on developing direct sales and services delivery capabilities associated with our targeted solutions offerings in our North American and European markets. We expect partnerships to be less of a factor in our business growth during 2006 but hope to leverage partnership channels for our higher value solutions offerings once we have established them in the market place and are better positioned to support partners in those markets.



# 2006 Outlook

## 2006 Goals

The Company expects to continue to grow its market share as it increasingly positions **KnowledgeSEEKER®** and **KnowledgeSTUDIO®** as premium offerings for high-end users of advanced predictive analytics tools. The Company expects to continue to grow analytics software revenues ahead of IDC reported industry growth rates and will continue to focus on the premium user segment of this market.

We were also pleased with the progress made during 2005 in gaining market awareness and customer acceptance - particularly on the initial phases of our **FundGuard**™ and **Telecom Marketing Analytics**™ systems. The work of the Angoss team in all cases was exceptional, not from our standpoint, but from the standpoint of our clients, who acknowledged the value of the solutions provided. We also learned valuable lessons through sales cycles that did not result in closed business about areas where we can do better as we broaden our solutions portfolio to provide more compelling value propositions, deliver more powerful solutions, and ultimately close more business with faster sales cycles.

At the outset of 2005, we noted that solutions based business models tend to involve longer and more complex sales cycles before closing, longer timelines for deployment, and requirements driven implementations from proof of value projects through to fully deployed production systems.

Unlike packaged software sales where revenue is generally recognized in the period of sale against delivery of software media, solutions revenues tend to be recognized over the time period of implementations which may fall within or span quarterly reporting periods. However, on the positive side, as relationships mature and multi-phase implementations progress, more predictable revenue profiles tend to emerge.

As we move into 2006, we will be working to achieve the following goals:

- Maintain current growth rates in direct revenues in North America and Europe while delivering improved operating profitability, resulting in performance ahead of reported industry and peer group company growth rates.
- Continued expansion of **KnowledgeSEEKER®** and **KnowledgeSTUDIO®** packaged software sales to existing and new clients in the financial services vertical, and with expanded sales to early adopting customers in other industries, combined with continuous improvements in marketing effectiveness and sales team productivity.
- Continued expansion of our sales and marketing analytics solutions offerings combining Angoss predictive analytics software systems and related implementation services under the **FundGuard™**, **Telecom Marketing Analytics™**, and new solution brands - all designed to meet the needs of our clients for revenue generation and business growth through optimization of their sales and marketing activities.
- Continued expansion of our software products portfolio supporting our sales and marketing analytics solutions offerings, with the successful introduction of **StrategyBuilder™**, the next release of **KnowledgeSERVER®** and **Mining Manager™**, and new capabilities that help our clients continue to improve their marketing and sales activities and impacts.
- Evaluation of financing, business acquisition, distribution and other opportunities to extend our direct sales and solution delivery capability in the US and international markets to support broader sales of our high margin packaged software offerings, and continued expansion of our sales and marketing analytics solutions offerings with early adopting clients primarily in US and European markets.

## 2006 Outlook

Our business focus is encapsulated in our *"Discover. Predict. Act."*™ positioning statement. Organizations that successfully integrate predictive analytics systematically as an integral component of their customer life-cycle management activities - in marketing, sales and risk - will be the market leaders in finance, telecom, retailing and other sectors over the next decade.

Our company strategy and business development initiatives for 2006 continue to be focused on strengthening our strategic relationships with customers who have selected Angoss as a preferred predictive analytics platform for delivering actionable analytics and insight to their sales, marketing and risk management personnel.

Organizations within the financial services industry are well advanced in their use of predictive analytics and face unique issues and challenges to streamline, standardize and extend their predictive analytics capability. Angoss is actively working to address these challenges with innovative enhancements to our products under the Angoss **KnowledgeSTUDIO®** brand.

Outside the financial services sector, most organizations are looking for integrated, packaged predictive analytics systems that are designed to meet the specific business needs and challenges they face. Predictive analytics solutions meet these requirements. They are delivered on Angoss **FundGuard™, Telecom Marketing Analytics™**, **Mining Manager™** and other Angoss products, with a comprehensive suite of expert services, providing an open, standards based alternative for the delivery of this capability to business users.

Our experience in selling predictive analytics software and services across several industries has provided Angoss with an unique insight into both the opportunities and challenges all organizations face in successfully adopting and using predictive analytics to unlock insight from their data that can drive business value.

During 2005, we achieved significant success with certain of our solutions, but for others the sales cycles remain longer than we would like. We are applying the experiences we have developed this year to further refine, better position and extend our risk analytics solutions, for example, meet the needs of targets users.

All of our initiatives are oriented to delivering more highly focused, substantially higher value proposals to targeted clients in need of our industry specific predictive analytics solutions. We are pleased with the responses we have received to date from our clients and prospects and expect to see progress on these fronts during 2006.

## 2006 Risks

We believe that delivering higher value predictive analytics solutions is a natural evolution for our company. It reflects our experience and leverages our expertise.

While this transition creates opportunity, it also requires additional capabilities and resources, and involves changes in business strategy and operations that in certain areas may be significant. As a result of these factors, our predictive analytics solutions business may create new risks and unanticipated ones.

We have identified and discussed these risks in our discussion and analysis of operating results. See "Management's Discussion and Analysis of Operating Results and Financial Condition".

# Management's Discussion and Analysis of Operating Results and Financial Condition

Management's discussion and analysis of operating results and financial condition should be read in conjunction with the Angoss Software Corporation (the "Company" or "Angoss") fiscal 2005 audited consolidated financial statements (the "Financial Statements") that have been prepared by management in accordance with Canadian generally accepted accounting principles. All amounts are stated in Canadian dollars unless otherwise stated. The Company's financial year ends on November 30. All references to a "Fiscal Year" mean the twelve-month period commencing on December 1 and ending on November 30 of the following year. The financial data in the MD&A has been prepared by management in accordance with Canadian generally accepted accounting principles. This MD&A has been prepared with all information available up to and including January 26, 2006.

In December 2003, the Emerging Issues Committee of the CICA issued EIC-142, "Accounting for Revenue Arrangements with Multiple Deliverables" ("EIC-142"). EIC-142 addresses how to determine whether an arrangement involving multiple deliverables contains more than one unit of accounting. EIC-142 also addresses how arrangement consideration should be measured and allocated to the separate units of accounting in the arrangement. EIC-142 is applicable to the Company beginning December 1, 2004 and the Company has adopted EIC-142, on a retroactive basis with restatement of prior fiscal and interim periods. As a result of the application of this new accounting principle, each of the deficit and unearned revenue as at December 1, 2003 was increased by $735,582. In 2004, revenues were reduced by $301,129 with a corresponding increase in the net loss, deficit and unearned revenues as at November 30, 2004. In 2005, the effect of this change was to reduce

revenues by $133,194 with a corresponding increase in the net loss, deficit and unearned revenues as at November 30, 2005.

In accordance with the new CICA requirements, effective December 1, 2004, the Company has adopted, on a retroactive basis without restatement of prior periods and an adjustment to the opening deficit, the fair value of accounting for employee stock-based compensation and other stock-based payments. See note 3 to the Financial Statements for the twelve months ended November 30, 2005.

Some of the statements contained in this Annual Report including, without limitation, those relating to financial and business prospects and financial outlook of the Company, may be forward-looking statements which reflect management's expectations regarding the Company's future growth, results from operations, performance and business prospects and opportunities. Wherever possible, words such as "anticipate", "believe", "expect", "intend" and similar expressions have been used to identify these forward-looking statements. These statements reflect management's current beliefs and are based on information currently available to management. Forward-looking statements involve significant risk and uncertainties. A number of factors could cause actual results to differ materially from the results discussed in the forward-looking statements including but not limited to, changes in the general economic and market conditions.

Although forward-looking statements contained herein are based upon what management believes to be reasonable assumptions, the Company cannot assure that actual results will be consistent with these forward-looking statements. These forward-looking statements are made as of the date hereof and the Company assumes no obligation to update or revise them to reflect new events or circumstances until the effective date of the Company's future reports filed with the applicable securities regulatory authorities.

## Three Year Financial Information Comparison

*(See Fig.3 and Fig.4)*

## Results of Operations

**Revenue** *(See Fig.5)*

Angoss direct revenue is earned through the licensing of the right to use the Company's software products. License revenues are derived from the earned portion of direct sales of the initial software and the earned portion of software license renewals. Professional services revenue is earned from data mining consulting, engineering and implementation services associated with delivery of Angoss predictive analytics solutions. Interest income earned is generated on surplus cash.

**Fig.3 Three Year Financial Information Comparison**

| Stated in $ Canadian | 2005 (restated) | 2004 (restated) | 2003 (as published) |
|---|---|---|---|
| Revenue | **$ 6,289,017** | $ 5,772,365 | $ 4,541,717 |
| Gross margin | **6,271,297** | 5,722,999 | 4,513,801 |
| Sales and Marketing, General and Administration and Research and Development expenses | **5,964,587** | 6,072,107 | 4,867,339 |
| Income (loss) before the following | **306,710** | (349,108) | (353,538) |
| Foreign exchange losses, Special charges, Financing expenses, Amortization, Stock-based Compensation and Other income | **(432,990)** | (589,108) | (340,238) |
| (Loss) before income taxes | **(126,280)** | (938,216) | (693,776) |

## Fig.4 Three Year Financial Information Comparison

| Stated in $ Canadian | **2005 (restated)** | 2004 (restated) | 2003 (as published) |
|---|---|---|---|
| Future income tax recovery | **-** | 125,000 | 125,000 |
| Net (loss) for the year | **(126,280)** | (813,216) | (568,776) |
| Basic and diluted (loss) per share | **(0.00)** | (0.02) | (0.01) |
| Total assets | **4,189,019** | 4,530,308 | 4,962,789 |
| Total long term financial liabilities | **1,112,889** | 1,650,021 | 2,315,560 |
| Cash dividends declared per Preferred share | **$ 0.07** | $ 0.07 | $ 0.00 |

## Fig.5 Revenue

| | Twelve months ended November 30 | | |
|---|---|---|---|
| | **2005** | 2004 | % Change |
| Licenses | **$ 4,839,848** | $ 4,233,634 | 14.3% |
| Professional services | **1,335,971** | 552,713 | 141.7% |
| Angoss direct revenue | **6,175,819** | 4,786,347 | 29.0% |
| Partners | **57,765** | 944,672 | (93.9%) |
| Product revenue | **6,233,584** | 5,731,019 | 8.8% |
| Interest | **55,433** | 41,346 | 34.1% |
| Revenue | **$ 6,289,017** | $ 5,772,365 | 9.0% |
| Angoss license billings | | | |
| Initial software billings | **$ 3,110,874** | $2,743,257 | 13.4% |
| Renewal software billings | **$ 2,106,345** | $1,785,877 | 17.9% |

Partner revenue consists of licensee fees payable on the sale of Angoss product licenses by partners and professional services fees for implementation services provided to partners directly or as part of a partner's solution for a customer. Partner revenue is derived from partner software sales in accordance with the provisions of the applicable license agreement. Service revenue is earned through fees paid by clients and partners for data mining consulting, engineering and implementation services provided by Angoss to support direct sales, customization and integration with partner offerings, and partner software sales.

The annual license to use the Company's software provides the right to receive product corrections, unspecified upgrades during the license period and installation and technical support. Revenue from such licenses is deferred and recognized ratably over the one-year term of the license. Prior to the adoption of EIC-142, the revenue with respect to the initial one-year agreement was recognized on the delivery of the license. License renewals provide the licensee the right to use the software for an additional year as well as a further year of right to receive product corrections, unspecified upgrades and technical support over the renewal period. License renewal revenue is recognized ratably over the one-year renewal term.

The perpetual license to use the Company's software provides the right to receive product corrections and installation and technical support for one year. Revenue from such licenses is recognized on the delivery of the license.

Separate one-year maintenance agreements for product upgrades and support can be acquired by perpetual licensees and such revenue is recognized ratably over one year. For further information on revenue elements and related revenue recognition policies and procedures see notes 2 and 3 to the consolidated Financial Statements.

During 2005, earned license revenues increased 14.3%. New product license billings grew 13.4% lead by a 119.5% increase in **KnowledgeSEEKER®** sales as a result of the introduction of a new major release of that product.Renewal revenues increased by 4%. While **KnowledgeSTUDIO®** billings declined 1.9% in 2005, **KnowledgeSTUDIO®** billings are expected to increase in 2006 following the introduction of a new major release in late November 2005.

Professional service revenues increased 141.7% during 2005. The increase is attributable primarily to expanded sales of Angoss predictive analytics solutions that combine both software and associated implementation services. In general, these solutions have a higher component of expert services, particularly during initial implementation phases. Implementation services revenues are expected to continue to grow reflecting the Company's continuing expansion of predictive analytics solutions targeting industry specific vertical application requirements of customers.

During 2005, revenues derived from partners declined by 93.9%. Declines in reported partner revenues in 2005 resulted from lower reported sales of partner offerings incorporating Angoss products, as well as continuing changes in partners' personnel, resources and ownership as evidenced by the recent merger transactions involving the acquisition of both PeopleSoft Corporation and Siebel Systems by Oracle Corporation.

As a result of industry consolidation, declining partner-reported revenues, and an inability of partners to achieve expected budget targets for revenue generation during 2005; the Company reviewed its partnering strategy in the third quarter. As a result of these developments, the Company's licensing agreements with both PeopleSoft Corporation and Siebel Systems have been terminated and the Company is re-evaluating its partner channels strategies in general.

Following its third quarter termination of a licensing agreement with partner Siebel Systems, which preceded the announcement of the proposed merger of Siebel Systems with Oracle Corporation, and completion of a preliminary post-termination audit during the fourth quarter, the Company has initiated litigation proceedings. Matters in dispute include non-disclosure, non-reporting and non-payment by Siebel Systems of royalties due on distributions of its own and OEM partner software over the past several quarters using so-called enterprise license agreements, pool of funds' transactions and other undisclosed program bundles. Siebel Systems has disputed the Company's right to terminate the agreement. No provision has been made in 2005 results for any additional revenues resulting from the resolution or adjudication of such claims. The Company has declined the partner's proposals to settle matters in dispute.

The Company currently operates primarily in two geographic markets: North America and Europe. During 2005, 83.6% of revenue was generated in North America (including Australia) (2004 - 83.8%); 16.4% in Europe (2004 - 16.2%). The increase in the relative proportion of European revenues reflected expansion of the Company's direct sales efforts in Europe. As well, the decline of the US dollar impacted North American revenues. Product revenues from markets outside these geographic regions currently are not material to the Company's operations and are included in North American revenues. During 2003, the Company established a relationship with a local market representative for the Australian and New Zealand markets. During 2005, this market place generated 0.9% (2004 - 1.6%) of product revenues.

During 2005, the Company maintained its primary focus on the financial services industry. Approximately 66% of revenue in 2005 (2004 - 68%) was derived from clients in the financial services industry (comprising banking, insurance, brokerage, consumer credit and other financial services businesses). The balance of revenue was derived primarily from clients in the communications and life sciences industries.

### Cost of Goods Sold and Gross Margin

Cost of goods sold consists primarily of royalties and other direct production costs such as shipping, manuals and disks. Comparative cost of goods sold and gross margin are as follows: *(See fig.6)*

Gross margins were essentially unchanged during 2005. The Company, from time to time, licenses third party software components for integration into the Company's products. To the extent that such arrangements provide for the payment of royalties or other amounts included within the cost of goods sold by the Company, such transactions would impact on cost of goods sold.

### Costs and Expenses *(See fig.7)*

Costs and expenses consist of salary and benefit expenses ("compensation"), as well as sales and marketing, administrative and research and development expenses. Such costs and expenses decreased by 1.8% in 2005 over 2004 levels (a 24.8% increase in 2004 over 2003).

In 2005, compensation accounted for 71.8% (2004 - 73.3%) of operating expenses. Compensation costs decreased 3.9% in 2005 (2004 - 20.9% increase) reflecting adjustments to head count and compensation levels based upon performance. The increase in 2004 compensation levels reflected the investment in sales, services and development personnel. Increases in non-compensation operating expenses occurred primarily in the areas of sales and marketing.

### Sales and Marketing *(See fig.8)*

During 2005, sales and marketing ("S&M") expenses were $3,288,078, an increase of 0.4% over the same period in 2004.

Compensation is composed of salary, commissions, bonuses and benefit costs associated with direct sales, marketing and services personnel. Reductions in North American compensation costs in 2005 resulted from reductions in quota carrying sales representatives. European costs increased as a result of increased head-count. At November 30, 2005, 11 full-time people (2004 - 15) were assigned to this department in North America, including 5 quota carrying sales representatives (2004 - 8), 5 analytics services consultants (2004 - 5) and 1 sales support person (2004 - 2). In 2005, two additional people were paid based solely on sales performance. In Europe, 5 people (2004 - 5) were fully dedicated to this department and in 2004; the compensation associated with 1 additional person was allocated between General and Administration ("G&A") and S&M expenses.

## Fig.6 Cost of Goods Sold and Gross Margin

| | 2005 | | 2004 | |
|---|---|---|---|---|
| Cost of goods sold | **$ 17,720** | **0.28%** | $ 49,366 | 0.86% |
| Gross margin | **$ 6,271,297** | **99.72%** | $ 5,722,999 | 99.14% |

## Fig.7 Cost and Expenses

| | 2005 | 2004 |
|---|---|---|
| Sales and Marketing, General and Administration and Research and Development expenses ("operating expenses") | **$ 5,964,587** | $ 6,072,107 |

## Fig.8 Sales and Marketing

| | 2005 | | 2004 | |
|---|---|---|---|---|
| **Compensation** | | | | |
| North America | $ 1,876,765 | 57.1% | $ 2,051,420 | 62.7% |
| Europe | 701,194 | 21.3% | 585,586 | 17.9% |
| Consulting fees | - | - | 12,640 | 0.3% |
| | 2,577,959 | 78.4% | 2,649,646 | 80.9% |
| (Decrease) | (2.7%) | | | |
| **Other** | | | | |
| North America | 641,897 | 19.5% | 494,038 | 15.1% |
| Europe | 68,222 | 2.1% | 130,503 | 4.0% |
| | 710,119 | 21.6% | 624,541 | 19.1% |
| Increase | 13.7% | | | |
| | $ 3,288,078 | 100.0% | $ 3,274,187 | 100.0% |
| | 0.4% | | | |
| Total S&M expenditures as a % of revenue | 52.3% | | 56.7% | |

In 2005, other sales and marketing expenses increased 13.7% reflecting increased investment in product promotion, tradeshow attendance, direct marketing and other lead generation activities. In 2005, 34.6% (2004 - 15.2%) of other S&M expenses was invested in product promotion, lead generation and related marketing activities. In 2005, 33.4% (2004 - 41.0%) of other S&M expenses was devoted to travel and on-site customer visits associated with gathering client requirements and preparing analytical solutions proposals linked to those requirements. In 2005, 19.6% (2004 - 14.8%) of other S&M expenses was directly related to attendance at tradeshows. The balance of other S&M expenses (2005 - 12.4%; 2004 - 29.0%) was spent on consulting services paid to third parties who provided training and strategic sales and marketing services. These expenditure trends are expected to continue in 2006.

**General and Administration** *(See fig.9)*

During 2005, G&A expenses were $1,510,036, a decrease of 5.7% over the same period in 2004. G&A expenses declined from 27.7% of revenues in 2004 to 24.0% of revenues in 2005 reflecting lower G&A expenses combined with higher revenues in 2005.

In North America, changes in compensation reflect decreases in bonus compensation in 2005. At November 30, 2005, 5 full-time people were assigned to this department in North America (2004 - 5). In 2005, European administration services have been contracted to a third party on an as needed basis. In 2004, European compensation represented the cost of one additional person allocated between G&A and S&M.

Other G&A expenses are made up of four main components of which occupancy costs, professional fees and communication costs were 72.1% of other G&A expenses (2004 - 68.5%). Both the mix and amount of such expenses were consistent after taking into account the contracted increases in rent (in both North America and Europe), increased recruiting fees as well as other inflationary increases. The balance of other G&A expenses are ordinary course business expenses. In 2005, in North America, such expenses declined as a result of a reduction in the amount of provision against the Australia working capital loan (2005 - $57,582; 2004 - $97,736).

**Research and Development** *(See fig.10)*

All research and development ("R&D") costs have been expensed as incurred.

Research and development comprises all engineering, quality assurance, support and related personnel resources associated with solution delivery. All research and development is conducted in North America. As at November 30, 2005, there were 16 staff in R&D (2004 - 12).

Other development costs include training costs, supplies, subscriptions, software and other costs associated with R&D. The amount fluctuates from year to year depending upon the development cycle and the number of changes in personnel.

While 2005 compensation costs were down 1.5%, R&D head count increased throughout 2005 to support the release of KnowledgeSEEKER® 5.0, as well as new product development associated with the Company's predictive analytics solutions business. Product development activities are now substantially completed with respect to the Company's analyst tools offerings, and the Company expects to continue to reduce development costs, other than those costs directly related to delivering and configuring revenue-producing predictive

**Fig.9 General and Administration**

| | 2005 | | 2004 | |
|---|---|---|---|---|
| **Compensation** | | | | |
| North America | $ 506,595 | 33.6% | $ 566,760 | 35.4% |
| Europe | - | - | 35,429 | 2.2% |
| | 506,595 | 33.6% | 602,189 | 37.6% |
| (Decrease) | (15.9%) | | | |
| **Other** | | | | |
| North America and Australia | 804,676 | 53.2% | 834,986 | 52.2% |
| Europe | 198,765 | 13.2% | 163,875 | 10.2% |
| | 1,003,441 | 66.4% | 998,861 | 62.4% |
| Increase | 0.5% | | | |
| | $ 1,510,036 | 100.0% | $ 1,601,050 | 100.0% |
| (Decrease) | (5.7%) | | | |
| Total G&A expenditures as a % of revenue | 24.0% | | 27.7% | |

## Fig.10 Research and Development

| | 2005 | | 2004 | |
|---|---|---|---|---|
| Compensation | **$ 1,195,298** | **98.3%** | $ 1,213,011 | 97.3% |
| (Decrease) | **(1.5%)** | | | |
| All Other | **21,175** | **1.7%** | 33,859 | 2.7% |
| (Decrease) | **(37.5%)** | | | |
| Total expenditures before tax credit | **$ 1,216,473** | **100.0%** | $ 1,246,870 | 100.0% |
| (Decrease) | **(2.4%)** | | | |
| OITC | **(50,000)** | | (50,000) | |
| | **$ 1,166,473** | | $1,196,870 | |
| (Decrease) | **(2.5%)** | | | |
| Total R&D expenditures before tax credit as a % of revenue | **19.3%** | | 21.6% | |

analytics solutions, as a percentage of revenues. The decline in 2004 compensation resulted from the restructuring of R&D operations and reductions in staff levels at that time.

In 2005 and 2004, the Company recognized $50,000 on account of Ontario Incentive Tax Credits ("OITC"). As at November 30, 2005, accounts receivable include $189,000 (2004 - $150,000) on account of OITC's. This amount represents approximately 66% (2004 - 66%) of the amount management otherwise estimates to be collected on account of 2002 through 2005.

During 2005, the Company's development activities were directed primarily towards the development and release of **KnowledgeSEEKER®** 5.0, the continued extension of the Angoss predictive analytics platform to support solutions and the development of additional tools to support the delivery of higher value predictive analytics solutions on both a software licensing and managed service delivery basis. These initiatives included the following:

- Angoss Analytics Solutions - Development of extensions to the Angoss predictive analytics platform to support Credit Risk Reporting & Analytics, **FundGuard™**, Claims & Payments Analysis, Telecom Marketing Analytics and other planned predictive analytics solutions.
- **KnowledgeSTUDIO®** Enterprise - Migration of Angoss analytics tools, **KnowledgeSEEKER®**, **KnowledgeSTUDIO®**, **KnowledgeSERVER®**, and **Mining Manager™** to new client-server architectures based on Microsoft.Net client technologies and supporting client-server configurations for popular Windows and Unix server platforms. **KnowledgeSEEKER®** 5.0 was released in June 2005. **KnowledgeSTUDIO®** 5.0 was released in November 2005. Additional product releases are scheduled for 2006.
- Development and release of an improved product license management and delivery system.

### Amortization / Interest Accretion

Amortization in 2005 comprised amortization of capital assets (2005 - $109,487; 2004 - $88,544) and the amortization of financing fees (2005 - $17,152; 2004 - $17,151) associated with the issue of the preferred shares in 2003. Amortization of capital assets increased in 2005 as a result of the increased investment in such assets in 2004 and 2005.

The difference between the preferred share principal ($2,300,000) and the value allocated to the preferred shares ($1,989,500) at the date of issuance is accreted as interest expense (2005 - $90,003; 2004 - $99,510) over the term of the preferred shares. The effective interest rate, including dividends, for the liability component is 11.9%.

### Other Income

In 2005, proceeds from the settlement agreement with TRIFOX, net of collection fees, were $62,318 (2004 - $55,724). Repayment amounts are based upon TRIFOX revenue and are expected to continue for another five years at current levels of repayment. See note 13 to the 2005 Financial Statements.

### Special Charges

On November 30, 2004, the Company restructured its operations and terminated 9 employees to re-align its on-going operating costs. As at November 30, 2004, a provision of $113,489 was made for the termination and lay-off associated with these 9 employees - seven in research and development, one in sales and one in administration. As at November 30, 2004, the Company had paid a total of $108,413. As at November 30, 2005, all amounts had been paid.

### Foreign Exchange

The Company sells software and services in both United States dollars and other currencies while maintaining its primary base of business operations and source of operating expenses in Canada. These factors give rise to the risk that its income, cash flows and the value of assets held in United States dollars may be adversely impacted by fluctuations in foreign exchange rates. The Company uses both its natural hedge to mitigate the effects of such fluctuations, to the extent possible, and will, from time to time, enter into foreign exchange forward contracts to manage foreign exchange risk on US cash held as term deposits and license renewal billings.

The Company enters into foreign exchange forward contracts to minimize its exposure to fluctuations in foreign currency exchange rates. These derivative contracts do not qualify for hedge accounting and therefore the contracts are recorded at fair value at the consolidated balance sheet dates and with the corresponding gain/loss recorded in the consolidated statements of loss. The Company does not enter into foreign exchange forward contracts for speculative purposes.

As at November 30, 2005, the Company had one outstanding foreign exchange forward contract representing commitments to sell US$500,000 in exchange for Canadian dollars with a term to maturity of 30 days. As at November 30, 2005, the effective rate of exchange on the contract was $1.2100. As at November 30, 2005, a gain of $21,300 was recorded on the contract.

As at November 30, 2005, the $US to $Canadian and £UK to $Canadian exchange rates were $1.1674 and $2.0221, respectively (2004 - $1.1904 and $2.2703, respectively). For the twelve months ended November 30, 2005, the weighted average $US to $Canadian and £UK to $Canadian exchange rates were $1.2162 and $2.2109, respectively (2004 - $1.3074 and $2.3827, respectively).

## Summary of Quarterly Results

*(See fig.11)*

Revenues in any quarter are dependent on orders received and licenses renewed in that quarter. In addition, the timing and amount of the Company's revenues are affected by a number of factors that make estimation of operating results before the end of a quarter uncertain.

Sales and Marketing, General and Administration and Research and Development expenses are planned based upon anticipated revenues. During 2005, the Company increased the amount spent on direct marketing and continued traveling to customer sites. Increased marketing activity, travel and on-site customer visits with the expressed goal of better understanding our customer needs are expected to continue. In 2004, the Company engaged a third party consultant who had invested in the preferred share financing to provide strategic sales and marketing services. This contract ended in early 2005. In 2005, the Company continued to use various external consultants for strategic, advisory and operational purposes.

Financing expenses and amortization expense are consistent quarter to quarter. Foreign exchange gains (losses) are a continuing exposure for the Company. See the separate discussion outlining the Company's foreign exchange strategy. Other income relates to TRIFOX and such income was received at the end of the second and fourth quarters (see note 13 to the Financial Statements). There is no guarantee that such income will be received.

## Fig.11 Summary of Quarterly Results

| Unaudited (restated for the adoption of EIC-142) | 4th Quarter | | 3rd Quarter | | 2nd Quarter | | 1st Quarter | |
|---|---|---|---|---|---|---|---|---|
| (000's) | **2005** | 2004 | **2005** | 2004 | **2005** | 2004 | **2005** | 2004 |
| Revenues | **$1,685** | $1,519 | **$1,530** | $1,495 | **$1,668** | $1,510 | **$1,406** | $1,248 |
| Gross margin | **1,680** | 1,513 | **1,526** | 1,487 | **1,663** | 1,481 | **1,402** | 1,242 |
| Sales and Marketing, General and Administration and Research and Development expenses | **1,531** | 1,506 | **1,426** | 1,411 | **1,572** | 1,623 | **1,435** | 1,532 |
| Income (loss) before the following | **149** | 7 | **100** | 76 | **91** | (142) | **(33)** | (290) |
| Foreign exchange gains (losses), Special charges, Financing expenses, Amortization, Stock-based Compensation expense and Other income | **(116)** | (219) | **(223)** | (155) | **(97)** | (187) | **3** | (28) |
| Income (loss) before income taxes | **33** | (212) | **(123)** | (79) | **(6)** | (329) | **(30)** | (318) |
| Future income tax recovery | **-** | 125 | **-** | - | **-** | - | **-** | - |
| Net Income (loss) | **33** | (87) | **(123)** | (79) | **(6)** | (329) | **(30)** | (318) |
| Earnings (loss) per share | **$0.00** | $(0.00) | **$(0.00)** | $(0.00) | **$0.00** | $(0.01) | **$(0.00)** | $(0.01) |

## Liquidity and Capital Resources

Cash and cash equivalents as at November 30, 2005 Cash and cash equivalents as at November 30, 2005 were $1,820,148 (2004 - $2,721,348). At the year end, accounts receivable were $1,938,333 (2004 - $1,497,344). The decline in cash balances resulted from the purchase of capital assets (2005 - $210,630; 2004 - $142,625), payment of preferred dividends (2005 - $161,000; 2004 - $141,923), and the redemption of preferred shares (2005 - $575,000; 2004 - nil). The remainder of the decline resulted from the use of cash to invest in business expansion and support revenue growth.

Accounts payable and accrued liabilities as at November 30, 2005 were $625,917 (2004 - $578,808). The increase is primarily due to an increase in regular operating expenses.

As at November 30, 2005, the Company's net liquid assets (current assets less current liabilities (excluding deferred revenue)) were $2,555,544 compared to $3,012,353 as at November 30, 2004. The decrease resulted from the use of cash in operating, investing and financing activities offset by an increase in accounts receivable as a consequence of continuing growth. In November 2005, the Company redeemed the first tranche of the preferred shares ($575,000). The Company currently intends to finance future redemptions through operating cashflow.

As at November 30, 2005, deferred revenue, current and long-term, totalled $2,635,708 (2004 - $2,440,658). Unearned software revenues increased by 15.5% reflecting increased billings. These increases were offset by a reduction in the amount of unearned services. While the amount of unearned services declined (year over year – 43.3%), the value of signed services contracts for future delivery and related unbilled service contracts that are not reflected in either the consolidated balance sheet or consolidated statements of loss increased by 81.7%.

At November 30, 2005, the Company had share capital of $14,030,423 (2004 - $13,805,813) and a deficit of $14,896,444 (2004 - $14,641,098). The increase in share capital is attributable to the exercise of stock options at various times throughout 2005 (see note 7 to the Financial Statements). The increase in the 2005 deficit is attributable to the adoption of CICA Section 3870 without restatement plus the 2005 net loss of $126,280. On December 1, 2004, the Company increased the deficit by $129,066 and increased contributed surplus by the same amount. In 2004, the increase in deficit was attributable to a net loss of $813,216.

## Commitments and Obligations

### Repayable Contribution Agreement

On February 14, 2003, the Company entered into a Repayable Contribution Agreement with the National Research Council of Canada ("NRC"). Under the Agreement, the NRC contributed $246,600 for costs incurred in the direct performance of defined work undertaken by the Company. Starting in September 2004, the contributions are repayable quarterly at a rate of 1.07% of the prior quarter's revenue until the earlier of February 2006 or $369,900 has been repaid. If, as at February 2006, the payments are less than $246,000, payments will continue on the same basis until the earlier of full repayment of the original NRC contribution of $246,600 or September 2014. Based on revenues through November 2005, the Company has repaid $84,949 of the original contribution. As it is unlikely that revenues through February 2006 will be sufficient to trigger payments to the NRC in excess of the original contributions, the repayable contribution liability recognized in the Financial Statements is based on the original contribution of $246,600 less repayments through November 2005. In fiscal 2006, the Company estimates that it will repay $79,500.

### Class A Preferred Shares

In November 2003, the Company issued 2,300,000 Class A Preferred shares, Series 1 ("Series 1") and 3,450,000 warrants to acquire 3,450,000 common shares of the Company at $0.30 per common share for total proceeds of $2,300,000.

Terms and conditions attached to the Series 1 are as follows:

(i) non-voting;

(ii) bear a fixed, preferential, cumulative cash dividend at the rate of 7%, payable quarterly;

(iii) redeemable, at the option of the Company, in whole any time after November 14, 2005 with a minimum annual redemption of $575,000 commencing November 14, 2005; and

(iv) in the event the Company fails to pay a dividend or redeem the minimum annual amount, the entire amount outstanding at the time of default becomes due and payable immediately.

The dividend expense in 2005 was $160,450 (2004 – $161,000). The first redemption of the Series 1 in the amount of $575,000 was made in November 2005.

### Leases

The total future minimum annual lease payments under operating leases for premises and equipment are as follows: *(See fig. 12)*

Future minimum annual payments do not include the Company's share of premises business and realty taxes and other operating costs estimated to be $180,000 per year plus any inflationary adjustments that may be required under the terms of the lease. Premises in the United Kingdom are leased on a month-to-month basis. The estimated UK expense for 2006, not included above, is $94,000.

## Financial and Other Instruments

Foreign exchange forward contracts are discussed under Results of Operations - Foreign Exchange.

Cash and cash equivalents include such items as bankers' acceptances carried at cost with maturities at acquisition of 90 days or less. The carrying values of accounts receivable, accounts payable and accrued liabilities and license fees payable approximate their fair values due to the relatively short periods to maturity of these financial instruments. The aggregate

fair value of the Preferred shares, calculated at the current market rate of interest available to the Company for the same or similar financial instrument, approximates their current carrying value.

The Company manages its credit risk with respect to accounts receivable by dealing primarily with credit-worthy customers and, where feasible, by billing in advance of rendering services. As at November 30, 2005, two customers represented more than 24.7% of the outstanding receivable balance. As at November 30, 2004, one customer represented 10.8% of the outstanding receivable balance.

As at November 30, 2005, the allowance for doubtful accounts totalled $169,334 (2004 - $199,901), including a provision in general and administration expenses, of $155,318 against the Australia working capital loan (2004 - $97,736).

## Related Parties

As at November 30, 2005, annual and meeting fees payable to directors acting in their capacity as directors was $16,254 (2004 - $13,750). For the year ended November 30, 2005, directors' fee expense was $50,000 (2004 - $45,000).

During 2004, employee notes totalling $31,850 were forgiven.

As at November 30, 2005, officers, directors and employees of the Company hold 10.9% (2004 - 10.9%) of the outstanding Series 1 offering and warrants and received their pro-rata share of dividends and redemption proceeds paid in 2005. During 2004, a Director sold his interest in the Series 1 and warrants to a related third party.

## Outlook

During 2005 revenues increased 9.0%. The Company has continued to expand direct software license sales and the number of signed contracts providing for future implementation of predictive analytics solutions consistent with its strategy of pursuing direct revenue growth through the delivery of higher value predictive analytics systems combining Angoss software programs and associated implementation services. However, growth in direct software license and services revenues has been offset by declines in partner revenues in year-to-date results, and with particular impact in the third quarter on a comparables basis to the prior year. In addition, additional amounts may be included in revenues as a result of a review and reconciliation of partner-reported revenues with actual amounts due under the agreements.

The Company continues to focus on improving revenue growth and operating margin through the expansion of analyst software and predictive analytics solutions sales, while improving the productivity of existing sales and services personnel, continuing to expand marketing initiatives, maintaining an appropriate level of research and development relative to current and planned software offerings, and continuing to reduce general and administrative expenses.

In the context of the Company's overall objectives, the Company intends to continue to manage its business to enable the hiring of additional personnel in several areas to support its growth objectives, provided that profitability and cash flow objectives are met. During 2006, staff increases are expected to focus primarily on the hiring of additional qualified personnel in sales, services and solution delivery. This expansion is expected to occur in North America and in Europe.

**Fig.12** Leases

| | |
|---|---|
| 2006 | $ 154,623 |
| 2007 | 32,758 |
| 2008 | 7,724 |
| | $ 195,105 |

As a result of declining revenues from current partners, and broader industry consolidation trends that have impacted and are in future likely to continue to impact on OEM and reseller channel based software distribution models, the Company is also exploring alternatives to expand / improve distribution of its products, expand revenue sources, and enhance shareholder value.

### Competition

In selling its predictive analytic tools and applications, the Company competes on the basis of the usability, functionality, performance, reliability, and connectivity of its software. The significance of each of these factors varies depending upon the anticipated use of the software and the analytical training and expertise of the customer. To a lesser extent, the Company competes on the basis of price and thus maintains pricing policies to meet market demand.

Historically, the Company's success has been driven by highly usable interfaces, comprehensive analytical capabilities, efficient performance, consistent quality, connectivity capabilities, and widely recognized brand names. The Company considers its primary worldwide competitor in each of its targeted markets to be the larger and better-financed SAS Institute, although the Company believes that a significant percentage of the revenue of SAS is derived from offerings in areas other than predictive analytics.

In the market for data mining tools, the Company competes with offerings from SAS and SPSS, as well as from a large number of small organizations.

In the future, the Company may face competition from other new entrants into its markets. The Company could also experience competition from companies in other sectors of the broader market for business intelligence software, such as providers of OLAP and analytical application software, as well as from companies in other sectors of the broader market for enterprise applications, who could add enhanced analytical functionality to their existing products. Some of these potential competitors have significant capital resources, marketing experience, and research and development capabilities. New competitive offerings by these companies or other companies could have a material adverse effect on the Company.

### Intellectual Property

The Company attempts to protect its proprietary software with trade secret laws and internal non-disclosure safeguards, as well as copyrights and contractual restrictions on copying, disclosure and transferability that are incorporated into its software license agreements. The Company licenses its software only in the form of executable code, with contractual restrictions on copying, disclosures and transferability. The Company licenses its products to end-users and in order to activate the software, the end user must also receive from the Company a license key that is delivered separate from the software itself.

The source code for all of the Company's products is protected as a trade secret. The Company has also entered into confidentiality and non-disclosure agreements with its key employees. Despite these restrictions, the possibility exists for competitors or users to copy aspects of the Company products or to obtain information which the Company regards as a trade secret. The Company has applied for three patents with respect to its technology to date and is expecting to file a third patent with respect to products currently under development. However, judicial enforcement of copyright laws, patent laws and trade secrets may be uncertain, particularly outside of North America. Preventing unauthorized use of computer software is difficult, and software piracy is expected to be a persistent problem for the packaged software industry. These problems may be particularly acute in international markets.

The Company uses a variety of trademarks with its products. Management believes the following are material to its business:

- Angoss and the Angoss logo are registered trademarks used in connection with the Company's corporate branding;
- **KnowledgeSEEKER®**, **KnowledgeSTUDIO®**, **KnowledgeSERVER®** and **Mining Manager™** are registered trademarks and are used in connection with the product lines of the Company;
- Credit Risk Reporting & Analytics, **FundGuard™**, Claims & Payments Analysis and **Telecom Marketing Analytics™** are trademarks used in connection with the Company's industry specific predictive analytics solution; and
- "Discover. Predict. Act" and "Better Business Decisions. Every Day" are trademarks used in connection with the Company's corporate branding.

The Company has registered the trademarks in Canada and some of its trademarks in the United States and the United Kingdom.

Due to the rapid pace of technological change in the software industry, the Company believes that patent, trade secret, and copyright protection are less significant to its competitive position than factors such as the knowledge, ability, and experience of the Company's personnel, new research and development, frequent technology and product enhancements, name recognition and ongoing reliable technology maintenance and support.

The Company believes that its solutions, products, and trademarks and other proprietary rights do not infringe the proprietary rights of third parties. There can be no assurance, however, that third parties will not assert infringement claims in the future or that such claims will not have a material effect on the Company if they are decided adversely to the Company.

### Impacts of Fluctuations in Revenues

The Company's quarterly operating results fluctuate due to several factors, including:

- The cyclical nature of customer purchases of enterprise software systems and tools which impact on quarterly results;
- Purchasing schedules, budgets and spending patterns of its customers;
- Changes in foreign currency exchange rates;
- The timing of solution implementations;
- Changes in mix of product and solutions revenues; and
- General economic conditions.

In addition, to the extent that the Company is successful in expanding its analytical solutions business, the changing relative proportion of software and services revenues involved in analytical solution sales, as well as schedules for solution delivery and associated recognition of software and services revenues, will impact the timing of recording and reporting revenue on a quarterly basis.

The Company has historically operated with very little backlog because of its focus on sales of analytical tools that have generally been shipped as orders are received. As a result, revenues in any quarter are dependent on orders received and licenses renewed in that quarter. In addition, the timing and amount of the Company's revenues are affected by a number of factors that make estimation of operating results before the end of a quarter uncertain.

Although the Company endeavours to link operating expenses with revenue forecasts, many operating expenses are planned and fixed based on revenue expectations. If 2006 revenues fall below expectations, operating results may be adversely affected because the Company's expense levels are to a large extent based on these forecasts. Accordingly, the Company believes that quarter-to-quarter comparisons of its results of operations may not be meaningful and should not be relied upon as an indication of future performance. The Company cannot provide assurance that profitability will be achieved on a quarterly or annual basis in the future.

## Outstanding Share Data *(See fig.13)*

## Disclosure Controls

The Company's Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures are effective, based on their evaluation of the effectiveness of these controls and procedures as of the end of the period covered by this report.

## Other Information

Other information related to the Company can be found on SEDAR at www.SEDAR.com.

## Fig.13 Outstanding Share Data

| Share capital consists of the following: | Authorized # | Outstanding # | Conversion rate |
|---|---|---|---|
| Common Shares | Unlimited | 39,499,723 | - |
| Preferred Shares | 2,300,000 | 1,725,000 | - |
| Warrants – 1 warrant is convertible to 1 Common share | | 3,450,000 | $ 0.30 |
| Warrants – 1 warrant is convertible to 1 Common share | | 380,000 | $ 0.25 |
| Options – 1 option is convertible to 1 Common share | 5,700,000 | 4,165,747 | At rates varying from $ 0.12 to $ 0.50 per option |

*Additional information about the Company's share capital is detailed in notes 6 and 7 to the Financial Statements.*

# Management's Responsibility for Financial Reporting and Auditor's Report

## Management's Responsibility for Financial Reporting

The accompanying consolidated financial statements of **Angoss Software Corporation** and all information in the Annual Report are the responsibility of management and have been reviewed and approved by the Board of Directors. The Company maintains appropriate processes to ensure that relevant and reliable financial information is produced. Consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles. Significant accounting policies which management believes are appropriate for the Company are described in the notes to the consolidated financial statements.

The Board of Directors carries out its responsibility for the consolidated financial statements and other financial information in this Annual Report principally through its Audit Committee currently consisting of three members, all of whom are unrelated, non-management Directors. The Audit Committee meets periodically with management and with the external auditors to discuss the results of audit examinations with respect to the adequacy of internal accounting controls and to review and discuss the consolidated financial statements and financial reporting matters.

Ernst & Young LLP, Chartered Accountants, were appointed as the Company's external auditors by the Company's shareholders to independently audit the consolidated financial statements in accordance with Canadian generally accepted auditing standards and to express to the shareholders their opinion on the consolidated financial statements.

Eric Apps
President

Lon Vining
Chief Financial Officer

January 27, 2006.

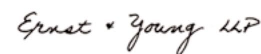
## Auditors' Report

To the Shareholders of
**Angoss Software Corporation**

We have audited the consolidated balance sheets of **Angoss Software Corporation** as at November 30, 2005 and 2004 and the consolidated statements of (loss), deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material mis-statement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at November 30, 2005 and 2004 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.



Toronto, Canada,
January 27, 2006.

Ernst & Young LLP
Chartered Accountants

# Consolidated Balance Sheets

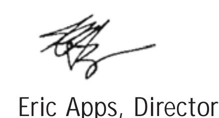
## Angoss Software Corporation
## Consolidated Balance Sheets

| As at November 30<br>(stated in Canadian dollars) | 2005 | 2004<br>*[note 3]* |
|---|---|---|
| **ASSETS**<br>**Current**<br>Cash and cash equivalents *[note 4]* | **$ 1,820,148** | $ 2,724,348 |
| Accounts receivable *[notes 4 and 12]* | **1,938,333** | 1,497,344 |
| Prepaid expense | **103,506** | 65,575 |
| **Total current assets** | **3,861,987** | 4,287,267 |
| Deferred financing fees | **50,739** | 67,891 |
| Capital assets, net *[note 5]* | **276,293** | 175,150 |
| Total assets | **$ 4,189,019** | $ 4,530,308 |
| **LIABILITIES AND SHAREHOLDERS' DEFICIENCY**<br>**CURRENT**<br>Accounts payable and accrued liabilities<br>*[notes 4 and 14]* | **$ 625,917** | $ 578,808 |
| Dividends payable on Preferred shares *[note 6]* | **26,026** | 26,576 |
| Current redeemable portion of repayable contribution *[note 12]* | **79,500** | 94,530 |
| Current portion of Preferred shares *[note 6]* | **575,000** | 575,000 |
| Current portion of deferred revenue *[note 3]* | **2,635,708** | 2,429,058 |
| **Total current liabilities** | **3,942,151** | 3,703,972 |
| Repayable contribution *[note 12]* | **82,151** | 134,286 |
| Deferred revenue *[note 3]* | **–** | 11,600 |
| Preferred shares, net of currently redeemable portion *[note 6]* | **1,030,738** | 1,515,735 |
| **Total liabilities** | **5,055,040** | 5,365,593 |
| Commitments and contingencies<br>*[notes 15 and 16]* | | |
| **Shareholders' deficiency**<br>Share capital *[note 7]* | **14,030,423** | 13,805,813 |
| Deficit *[note 3]* | **(14,896,444)** | (14,641,098) |
| **Total shareholders' deficiency** | **(866,021)** | (835,285) |
| | **$ 4,189,019** | $ 4,530,308 |

*See accompany notes*

On behalf of the Board:

John Gardener, Director


Eric Apps, Director

# Consolidated Statements of Loss

## Angoss Software Corporation
## Consolidated Statements of Loss

| Years ended November 30<br>(stated in Canadian dollars) | 2005 | 2004<br>*[note 3]* |
|---|---|---|
| **Revenue** *[notes 2, 8 and 11]* | $ 6,289,017 | $ 5,772,365 |
| Cost of goods sold | 17,720 | 49,366 |
| | 6,271,297 | 5,722,999 |
| **Costs and expenses**<br>Sales and marketing | 3,288,078 | 3,274,187 |
| General and administration *[note 4]* | 1,510,036 | 1,601,050 |
| Research and development expenditures, net *[note 12]* | 1,166,473 | 1,196,870 |
| | 5,964,587 | 6,072,107 |
| Income (loss) before the following | 306,710 | (349,108) |
| Other income *[note 13]* | 62,318 | 55,724 |
| Special charges *[note 14]* | – | (125,646) |
| Amortization of capital assets | (109,487) | (88,544) |
| Amortization of deferred financing fees | (17,152) | (17,151) |
| Interest accretion on Preferred shares *[note 6]* | (90,003) | (99,510) |
| Dividend expense on Preferred shares *[note 6]* | (160,450) | (161,000) |
| Foreign exchange loss, net *[note 4]* | (52,204) | (152,981) |
| Stock option expense *[notes 3 and 7]* | (66,012) | – |
| (Loss) before income taxes | (126,280) | (938,216) |
| Future income tax recovery *[note 9]* | – | 125,000 |
| Net (loss) for the year | $ (126,280) | $ (813,216) |
| Basic and diluted (loss) per share *[note 7]* | $ 0.00 | $ (0.02) |
| **Weighted average number of common shares outstanding** *[note 7]*<br>Basic | 39,474,069 | 39,221,687 |
| Diluted | 39,474,069 | 39,221,687 |

*See accompanying notes*

# Consolidated Statements of Deficit

## Angoss Software Corporation
## Consolidated Statements of Deficit

| Years ended November 30<br>(stated in Canadian dollars) | **2005** | 2004<br>*[note 3]* |
|---|---|---|
| **Deficit, beginning of year as previously reported** | **$ (13,604,387)** | $ (13,092,300) |
| Cumulative adjustment for adoption of EIC-142 *[note 3]* | **(1,036,711)** | (735,582) |
| Deficit, beginning of year as restated | **(14,641,098)** | (13,827,882) |
| Cumulative adjustment for stock-based compensation *[note 3]* | **(129,066)** | – |
| Net (loss) for the year | **(126,280)** | (813,216) |
| Deficit, end of year | **$ (14,896,444)** | $ (14,641,098) |

*See accompanying notes*

# Consolidated Statements of Cash Flows

# Angoss Software Corporation
## Consolidated Statements of Cash Flows

| Years ended November 30<br>(stated in Canadian dollars) | 2005 | 2004<br>*[note 3]* |
|---|---|---|
| **OPERATING ACTIVITIES** | | |
| Net (loss) for the year | **$ (126,280)** | **$ (813,216)** |
| Adjustments to reconcile net (loss) to cash provide by (used in) operating activities | | |
| Future income tax | – | (125,000) |
| Amortization of capital assets | **109,487** | 88,544 |
| Amortization of deferred financing fees | **17,152** | 17,151 |
| Interest accretion on preferred shares | **90,003** | 99,510 |
| Stock-based compensation and advisory services | **70,761** | 100,101 |
| | **161,123** | (632,910) |
| **Changes in assets and liabilities** | | |
| Increase in accounts receivable | **(440,989)** | (79,210) |
| (Increase) decrease in prepaid expenses | **(37,931)** | 11,710 |
| Increase in accounts payable and accrued liabilities | **47,109** | 317,904 |
| Increase (decrease) in deferred revenue | **195,050** | (33,354) |
| (Decrease) increase in dividends payable on Preferred shares | **(550)** | 19,077 |
| **Cash used in operating activities** | **(76,188)** | (396,783) |
| **INVESTING ACTIVITIES** | | |
| Purchase of capital assets | **(210,630)** | (142,625) |
| **Cash used in investing activities** | **(210,630)** | (142,625) |
| **FINANCING ACTIVITIES** | | |
| Repayment of preferred shares | **(575,000)** | – |
| Repayment of repayable contribution | **(67,165)** | (17,784) |
| Issuance of common shares on exercise of options | **24,783** | 20,281 |
| **Cash (used in) provided by financing activities** | **(617,382)** | 2,497 |
| **Net decrease in cash and cash equivalents during the year** | **(904,200)** | (536,911) |
| Cash and cash equivalents, beginning of year | **2,724,348** | 3,261,259 |
| **Cash and cash equivalents, end of year** | **$ 1,820,148** | $ 2,724,348 |
| **Supplemental cash flow information** | | |
| Dividends on Preferred shares | **$ 161,000** | $ 141,923 |

*See accompanying notes*

# Notes to Consolidated Financial Statements

## 1. Description of Business

Angoss Software Corporation ("Angoss" or the "Company") develops and licenses data mining and predictive analytics software solutions. Modellers and business analysts in the banking, insurance, telecommunications, health care and pharmaceuticals, retail, manufacturing and technology industries use Angoss solutions.

Angoss solutions are based on a common suite of integrated technologies. They consist of (i) analyst tools used for data analysis and modelling; (ii) a scoring and decisioning server used for deploying data mining models to operational systems; (iii) web-based task automation, collaboration and model management tools used to develop template-based pre-packaged predictive analytics applications; and (iv) developer tools, used for automating data mining tasks, integrating data mining functionality with enterprise systems and creating intelligent analytic applications

Angoss products are sold directly and by licensees as integrated and embedded components of their application suites. Angoss supports its software through a professional services organization that offers implementation services for Angoss offerings and complementary data mining and predictive analytics capability on a project and outsourcing basis.

## 2. Basis of Presentation

These consolidated financial statements of Angoss have been prepared by management in accordance with Canadian generally accepted accounting principles ["GAAP"].

In the opinion of management, all adjustments considered necessary for the presentation of the Company's financial position, results of operations and cash flows have been included.

The significant accounting policies are as follows:

### Basis of Consolidation

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Angoss Software Limited, incorporated in the United Kingdom, Angoss Software International (U.S.A.), Inc., incorporated under the laws of the State of Wyoming, U.S.A., and the Angoss Incentive Trust ["AIT"], a business trust governed by the laws of Ontario. All significant intercompany accounts and transactions have been eliminated upon consolidation.

### Cash and Cash Equivalents

Cash and cash equivalents include such items as bankers' acceptances carried at cost with remaining maturities at acquisition of 90 days or less.

### Financial Instruments

The fair values of financial instruments approximate their carrying values except as otherwise disclosed in these consolidated financial statements.

### Deferred Financing Costs

Costs incurred in connection with securing the Preferred share financing have been deferred and are being amortized over the term of the Preferred shares.

### Capital Assets

Capital assets are initially recorded at cost. Amortization is provided at rates designed to amortize the cost of capital assets over their estimated useful lives at the following rates and methods:

Computer equipment: Straight-line over three years

Duplication equipment: 30% declining balance

Equipment under capital lease: Straight-line over lease term

Office furniture and equipment: 20% declining balance

Computer software: Straight-line over two years

Leasehold improvements: Straight-line over lease term

### Revenue Recognition

Revenue consists of the sale of specific Company products and their related license revenue (sold solely on an annual basis and renewable annually), services revenue, partner revenue and interest income earned.

License revenue is earned through the licensing of the right to use the Company's software products. The annual license to use the Company's software provides the right to receive product corrections, unspecified upgrades during the license period and installation and technical support. The perpetual license to use the Company's software provides the right to receive product corrections and installation and technical support. Separate maintenance agreements for product upgrades can be acquired by perpetual licensees. Services revenue is earned through fees for data mining consulting, engineering and user-training services. License and services revenue is also earned through partners that have licensed Angoss products for distribution to their clients. Generally, license revenue earned through partners is based on the Company's share of the revenue earned by the partners from their sales of the Company's products to their customers. Services revenue earned from partners is based on their use of the Company's services.

The Company does not recognize revenue for agreements with rights of return, refundable fees, cancellation rights or acceptance clauses until such rights to return, refund or cancel have expired or acceptance has occurred.

When the Company's software and related license are sold with other services, the Company allocates the total fee to the various elements based on the relative fair values of the elements specific to the Company. The Company determines the fair value of each element in the arrangement based on vendor-specific objective evidence ["VSOE"] of fair value. For software licenses with a fixed number of licenses, VSOE of fair value is based on the price charged when sold separately,

which is in accordance with the Company's standard price list. The Company's standard price list specifies prices applicable to each level of volume purchased and is applicable when the products are sold separately.

Revenue allocated to licensed software is recognized when persuasive evidence of an agreement exists, delivery of the product has occurred, no significant obligations by the Company with regard to implementation remain, and collection of a fixed or determinable fee is probable. The Company considers all payments outside the Company's normal payment terms, including all amounts due in excess of one year, to not be fixed and determinable, and such amounts are recognized as revenue when the fee is collected. For software arrangements where the Company is obligated to perform professional services for implementation, the Company does not consider delivery to have occurred or customer payment to be probable of collection until no significant obligations with regard to implementation remain. Generally, this would occur when substantially all service work has been completed in accordance with the terms and conditions of the customer's implementation requirements but may vary depending on factors such as an individual customer's payment history or order type [e.g., initial versus follow-on].

Revenue allocated to data mining consulting, engineering and user-training elements is recognized as the services are performed.

Renewal and maintenance agreements are sold solely on an annual basis and are generally priced based on a percentage of the current product list price. Revenue from renewal and maintenance agreements is recognized ratably over the term of the agreement, which is one year.

Deferred revenue includes amounts received from customers in excess of revenue recognized.

### Leases

Leases are classified as capital or operating leases. A lease that transfers substantially all of the benefits and risks incidental to the ownership of property is classified as a capital lease. At the inception of a capital lease, an asset and an obligation are recorded at an amount equal to the lesser of the present value of the minimum lease payments and the property's fair value at the beginning of the lease. Assets recorded under capital leases are amortized on a straight-line basis over the term of the lease that is the estimated useful life of the assets. All other leases are accounted for as operating leases wherein rental payments are expensed as incurred.

### Research and Development

Research costs are expensed in the year incurred. Development costs are expensed in the year incurred unless the development project meets Canadian generally accepted accounting criteria for deferral and amortization.

### Foreign Currency Translation

Accounts of integrated subsidiary operations which are stated in currencies other than Canadian dollars are translated as follows:

- Monetary assets and liabilities - at year-end rates;
- Non-monetary assets - at historical rates; and
- Revenue and expenses - at the average exchange rate for the year, except that the amortization of capital assets is translated at the same exchange rate as the asset to which it relates.

Exchange gains and losses on translation are included in net (loss) for the year.

The monetary assets and liabilities of the Company that are denominated in foreign currencies are translated at the rate of exchange in effect at the consolidated balance sheet dates. Revenue and expenses are translated at rates of exchange prevailing on the transaction dates. Exchange gains or losses on translation are included in net (loss) for the year.

The Company enters into foreign exchange forward contracts to minimize its exposure to fluctuations in foreign currency exchange rates. These derivative contracts do not qualify for hedge accounting and therefore the contracts are recorded at fair value at the consolidated balance sheet dates and with the corresponding gain/loss recorded in the consolidated statements of net (loss). The Company does not enter into foreign exchange forward contracts for speculative purposes.

### Income Taxes

The Company uses the liability method of tax allocation for income taxes. Under the liability method of tax allocation, future tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using substantively enacted tax rates and laws that are expected to be in effect when the differences are expected to reverse.

### Use of Estimates

The preparation of the consolidated financial statements in accordance with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Actual amounts may differ from those estimates.

### Earnings (Loss) per Share

Earnings (loss) per share are calculated based on net income (loss) attributable to common shareholders. Basic earnings per share are calculated using the weighted average number of common shares outstanding during the year. The computation of diluted earnings per share assumes the basic weighted average number of common shares outstanding during the year is increased to include the number of additional common shares that would have been outstanding if the dilutive potential common shares had been issued. The dilutive effect of warrants and stock options is determined using the treasury stock method.

### Stock-Based Compensation

The Company adopted the CICA Handbook Section 3870 "Stock-based Compensation and Other Stock-based payments" ("Section 3870")which establishes standards for the recognition, measurement and disclosure of stock-based compensation and other stock-based payments. Section 3870 requires the fair value based method of accounting be applied to all stock-based payments to non-employees and to employee awards that are direct awards of stock that call for settlement in cash or other assets. Until November 30, 2004, the Section permitted the Company to continue its policy of recording no compensation expense for the granting of stock options to employees with the addition of pro-forma information. In accordance with the new CICA requirements, effective December 1, 2004, the Company has adopted, on a retroactive basis without restatement of prior periods and an adjustment to the opening deficit, the fair value method of accounting for employee stock-based compensation and other stock-based payments. The effect of the retroactive adoption of this accounting policy was to increase each of the deficit and contributed surplus as at December 1, 2004 by $129,066 respectively.

## 3. Changes in Accounting Policy

### Revenue Arrangements with Multiple Deliverables

In December 2003, the Emerging Issues Committee of the Canadian Institute of Chartered Accountants ("CICA") issued EIC-142, "Accounting for Revenue Arrangements with Multiple Deliverables" ("EIC-142"). EIC-142 addresses how to determine whether an arrangement involving multiple deliverables contains more than one unit of accounting. EIC-142 also addresses how arrangement consideration should be measured and allocated to the separate units of accounting in the arrangement. EIC-142 is applicable to the Company's fiscal year beginning December 1, 2004 and the Company has adopted EIC-142 on a retroactive basis with restatement of prior fiscal and interim periods. As a result of the application of this new accounting policy, each of the deficit and deferred revenue as at December 1, 2003 was increased by $735,582. In 2004, revenue was reduced by $301,129 with a corresponding increase in the net loss, deficit and deferred revenue as at November 30, 2004. In 2005, the effect of this change was to reduce revenue by $133,194 with a corresponding increase in the net loss, deficit and deferred revenue as at November 30, 2005.

## 4. Financial Instruments

### Credit Risk

The Company manages its credit risk with respect to accounts receivable by dealing primarily with credit-worthy customers and, where feasible, by billing in advance of rendering services. As at November 30, 2005, two customers represented more than 24.7% of the outstanding accounts receivable balance. As at November 30, 2004, one customer represented 10.8% of the outstanding accounts receivable balance.

The Company has entered in an agreement with a customer, Angoss Software Australia Pty. Ltd. ("Australia"), wherein the Company is entitled to receive up to a 50% interest in the revenue generated by Australia. In exchange for its interest, the Company has granted Australia the exclusive right to represent and distribute the Company's software, services and related solutions. The Company's share of the revenue is recognized as earned by Australia and is re-invested in Australia as a non-interest bearing working capital loan. Subject to certain terms and conditions, the agreement otherwise expires on December 1, 2006.

As at November 30, 2005, the allowance for doubtful accounts totalled $169,334 [2004 - $199,901], including a provision in general and administration expenses of $155,318 against the Australia working capital loan [2004 - $97,736].

### Currency Risk

The Company sells software and services in both Canadian and foreign currencies that give rise to the risk that its earnings and cash flows may be adversely impacted by fluctuations in foreign exchange. Certain purchases of services and equipment are also made in non-Canadian currencies. The Company uses its natural hedge to mitigate, to the extent possible the impact of foreign exchange fluctuation, and will, from time to time, enter into foreign exchange forward contracts to manage foreign exchange risk on US cash held as term deposits and anticipated future license renewal billings.

As at November 30, 2005, the Company had one (2004 - two) outstanding foreign exchange forward contract representing commitments to sell US$500,000 (2004 - US$1,000,000) in exchange for Canadian dollars at a weighted average rate of $1.2100 (2004 - $1.2100) and a weighted average remaining contractual life of 30 days (2004 - 303 days). The spot US dollar to Canadian dollars exchange rate as at November 30, 2005 was $1.1674 (2004 - $1.1904).

These contracts do not qualify for hedge accounting treatment and are recorded at their fair value at the close of each reporting period with the gain or loss being included in foreign exchange gain (loss) on the consolidated statements of (loss). During 2005, a gain of $21,300 (2004 - $19,600) was recorded on these contracts in the consolidated statements of (loss).

As at November 30, 2005, 66.3% (2004 - 66.8%) of cash and cash equivalents and 74.5% (2004 - 64.8%) of accounts receivable are denominated in foreign currencies. As at November 30, 2005, 30.0% (2004 - 21.9%) of accounts payable and accrued liabilities are denominated in foreign currencies.

### Fair Value

The carrying values of accounts receivable and accounts payable and accrued liabilities approximate their fair values due to the relatively short periods to maturity of these financial instruments. The aggregate fair value of the Preferred shares, calculated at the current market rate of interest available to the Company for the same or similar financial instrument, approximates its current carrying value.

## 5. Capital Assets

Capital Assets consists of the following: *(See fig.14)*

## 6. Preferred Shares *(See fig.15)*

### Series 1

In November 2003, the Company issued 2,300,000 Class A Preferred shares, Series 1 ("Series 1") and 3,450,000 warrants to acquire 3,450,000 common shares of the Company at $0.30 per common share for total proceeds of $2,300,000. In November 2005, 575,000 of the Series 1 were redeemed for $575,000. The annual redemption is 575,000 Series 1 for $575,000.

In accordance with CICA recommendations, a portion of the Series 1 has been allocated to shareholders' equity as the Series 1 contains both a liability and an equity element arising from the warrants attached. The method used to determine the equity component of the Series 1 is detailed in note 7 - Warrants. The difference between the Series 1 principal ($2,300,000) and the value allocated to the Preferred shares ($1,989,500) on the issue date is accreted as an interest expense over the term of the Series 1. The effective interest rate, including dividends, for the liability component is 11.9%.

The carrying value of the Series 1 is determined as follows: *(See fig.16)*

## Fig.14 Capital Assets *[See note 5]*

| | | 2005 | |
|---|---|---|---|
| Capital assets consist of the following: | Cost | Accumulated Amortization | Net Book Value |
| Computer equipment | **$ 815,220** | **$ 633,824** | **$ 181,396** |
| Duplication equipment | **7,431** | **6,985** | **446** |
| Equipment under capital lease | **229,079** | **229,079** | **–** |
| Office furniture and equipment | **197,743** | **153,756** | **43,987** |
| Computer software | **341,844** | **291,380** | **50,464** |
| Leasehold improvements | **228,796** | **228,796** | **–** |
| | **$ 1,820,113** | **$ 1,543,820** | **$ 276,293** |

| | | 2004 | |
|---|---|---|---|
| | Cost | Accumulated Amortization | Net Book Value |
| Computer equipment | $ 687,323 | $ 572,038 | $ 115,285 |
| Duplication equipment | 7,431 | 6,794 | 637 |
| Equipment under capital lease | 229,079 | 229,079 | – |
| Office furniture and equipment | 169,842 | 145,011 | 24,831 |
| Computer software | 287,012 | 252,615 | 34,397 |
| Leasehold improvements | 228,796 | 228,796 | – |
| | $ 1,609,483 | $ 1,434,333 | $ 175,150 |

## Fig.15 Preferred Shares *[See note 6]*

| | **2005** | 2004 |
|---|---|---|
| **Authorized**<br>Unlimited Class A Preferred shares, issuable in series | | |
| **Issued**<br>7% Class A Preferred shares, Series 1<br>November 30, 2005 - 1,725,000 | $ 1,605,738 | – |
| November 30, 2004 - 2,300,000 | – | $ 2,090,735 |

**Fig.16 Preferred Shares - Series 1** *[See note 6]*

| | 2005 | 2004 |
|---|---|---|
| Stated value of Series 1 issued | **$ 1,725,000** | $ 2,300,000 |
| Less amount allocated to warrants | **(310,500)** | (310,500) |
| Amount allocated to Series 1 | **1,414,500** | 1,989,500 |
| Add cumulative interest accretion expense | **191,238** | 101,235 |
| Total liability | **1,605,738** | 2,090,735 |
| Less current portion to be redeemed | **(575,000)** | (575,000) |
| Long-term liability | **$ 1,030,738** | $ 1,515,735 |

During 2005, the interest accretion on Series 1 was $90,003 (2004 - $99,510) and the dividend expense was $160,450 (2004 - $161,000).

In 2003, the legal and financial advisor fees associated with the issue, $85,757, were deferred and amortized over five years from the date of issue. The financial advisor invested $50,000 of the fees it received in a private placement of common shares *[note 7]* completed in conjunction with the financing.

Terms and conditions attached to the Series 1 are as follows:

(i) non-voting;

(ii) a fixed, preferential, cumulative cash dividend at the rate of 7%, payable quarterly;

(iii) redeemable, at the option of the Company, in whole any time after November 14, 2005 with a minimum annual redemption of $575,000 commencing November 14, 2005; and

(iv) in the event the Company fails to pay a dividend or redeem the minimum annual amount, the entire amount outstanding at the time of default becomes due and payable immediately.

## 7. Share Capital

Share capital consists of the following: *(See fig.17)*

### Issued Common Shares

During 2005, the Company issued 186,251 common shares on the exercise of stock options at prices ranging from $0.12 to $0.15 per common share, for a total of $24,783.

During 2004, the Company issued 133,542 common shares on the exercise of stock options at prices ranging from $0.15 to $0.20 per common share, for a total of $20,281.

Direct awards of stock to employees have been accounted for in accordance with the fair value method of accounting for stock-based compensation. During 2004, the Company issued 100,000 common shares to an officer as part of an employment contract (2005 - nil). The fair value of the common shares is based on the market price ($0.20 per common share) on the date the contract was signed. Accordingly, the fair value of $20,000 on the awarded common stock was charged to operations, with an offsetting credit to share capital.

### Warrants

During 2004, the Company issued 380,000 warrants to purchase 380,000 common shares of the Company at $0.25 per share in connection with a consulting services contract (2005 - nil). As at November 30, 2005, all warrants had vested (2004 - 285,000). The warrants expire December 10, 2008. As at November 30, 2005, no

## Fig.17 Share Capital *[See note 7]*

| | 2005 | 2004 |
|---|---:|---:|
| **Authorized**<br>Unlimited common shares<br>Preferred shares *[note 6]* | | |
| **Issued**<br>Common shares<br>November 30, 2005 - 39,499,723 | **$ 13,471,845** | |
| November 30, 2004 - 39,313,472 | | $ 13,447,062 |
| Warrants<br>3,450,000 at $0.30 | **310,500** | 310,500 |
| 380,000 at $0.25 | **49,400** | 44,651 |
| | **359,900** | 355,151 |
| Contributed surplus *[note 3]* | **198,678** | 3,600 |
| | **$ 14,030,423** | $ 13,805,813 |

warrants had been exercised. Principals of the consulting company were investors in the Series 1 financing *[note 6]* and have also provided consulting services *[note 10]*. The total fair value assigned to the warrants, $49,400, has been expensed. During 2005, of the value assigned to 95,000 warrants (2004 - 285,000), $4,749 (2004 - $44,651) was expensed.

The amount expensed in each of 2004 and 2005 approximates the value of the services provided in each year. The fair value of the warrants was estimated at the date of their issuance using the Black-Scholes option pricing model with the following assumptions:
*(See fig.18)*

## Fig.18 Warrants 2004 *[See note 7]*

| | |
|---|---:|
| Weighted average risk-free interest rate | 4.0% |
| Dividend yield | 0.0% |
| Weighted average volatility factors of the expected market price of the Company's common shares | 55.6% |
| Weighted average expected life of the warrants (in years) | 2.5 |

On November 14, 2003, the Company issued 3,450,000 warrants to purchase 3,450,000 common shares of the Company at $0.30 per share in connection with the issuance of Series 1 on that date *[note 6]*. The warrants expire November 13, 2008. As at November 30, 2005, no warrants had been exercised. The fair value of the warrants, $310,500, was estimated at the date of their issuance using the Black-Scholes option pricing model with the following assumptions: *(See fig.19)*

On February 25, 2002, the Company issued 100,000 warrants to purchase 100,000 common shares of the Company at US$0.35 per share in connection with a licensing agreement signed on that date. The warrants are not exercisable until the software has been released and expires five years thereafter. As at November 30, 2005, the software had not been released. No value has been assigned to the warrants.

### Stock-Based Compensation Plans

At November 30, 2005, the Company has two active stock-based compensation plans, which are described below.

*Employee Share Purchase Plan*

On April 23, 2002, shareholders of the Company approved the adoption and implementation by the Company, in its capacity as trustee, of an employee share purchase plan ["ESPP"] for eligible employees. Under the ESPP such employees are entitled to elect to receive common shares of the Company on account of up to 15% of their base and bonus compensation otherwise payable determined annually. These shares may, at the option of the trustee, be acquired in the market or from treasury based on the prevailing market prices of the common shares at the time of such purchase. As at November 30, 2005, no shares had been acquired [2004 - nil].

*Stock Option Plan*

The Company may grant to employees, officers, directors and consultants options to acquire up to 5,700,000 common shares of the Company. The exercise price of each option equals the market price of the Company's common shares on the date of the grant and an option's maximum term is five years. Vesting terms and conditions are determined by the Board of Directors at the time of the grant. A summary of the Company's Stock Option Plan as at November 30, 2005 and 2004 and changes during the years ended on those dates is presented below: *(See fig.20)*

As at November 30, 2005, non-executive directors of the Company have been granted a total of 425,000 options to acquire 425,000 common shares of the Company at prices ranging from $0.13 to $0.20 per share. As at November 30, 2004, non-executive directors of the Company have been granted a total of 312,500 options to acquire 312,500 common shares of the Company at prices ranging from $0.13 to $0.20 per share.

The following table summarizes information about the stock options outstanding as at November 30, 2005: *(See fig.21)*

### Employees and Directors

On December 1, 2004, the Company adopted the CICA's recommendations in Section 3870, "Stock-based Compensation and Other Stock-based Payments" and has recorded the fair value of all options granted in the consolidated statements of (loss). Upon adopting Section 3870, the Company elected to retroactively adjust the deficit without restatement. On December 1, 2004, the Company increased the deficit by $129,066 and increased contributed surplus by the same amount *[note 3]*. Employee stock based compensation expense for 2005 was $66,012.

**Fig.19 Warrants 2003** *[See note 7]*

| | |
|---|---|
| Weighted average risk-free interest rate | 4.2% |
| Dividend yield | 0.0% |
| Weighted average volatility factors of the expected market price of the Company's common shares | 55.0% |
| Weighted average expected life of the warrants (in years) | 2.5 |

## Fig.20 Stock Option Plan *[See note 7]*

| | 2005 | | 2004 | |
|---|---|---|---|---|
| | Options | Weighted average exercise price | Options | Weighted average exercise price |
| Outstanding, beginning of year | **3,192,434** | **$ 0.22** | 4,669,639 | $ 0.20 |
| Granted | **1,790,000** | **0.16** | 1,882,500 | 0.18 |
| Exercised | **(186,251)** | **0.13** | (133,542) | 0.15 |
| Cancelled | **(1,774,692)** | **0.24** | (3,226,163) | 0.18 |
| **Outstanding, end of year** | **3,021,491** | **0.19** | 3,192,434 | 0.22 |
| **Options vested, at end of year** | **1,995,380** | **$ 0.20** | 2,752,188 | $ 0.22 |

## Fig.21 Stock Options *[See note 7]*

| Exercise price | Options outstanding | Remaining Contractual life [months] | Options vested |
|---|---|---|---|
| $0.12 | 60,000 | 27 | 60,000 |
| 0.13 | 1,157,247 | 43 to 55 | 848,080 |
| 0.15 | 238,000 | 19 | 238,000 |
| 0.16 | 686,944 | 50 | – |
| 0.19 | 232,500 | 30 | 232,500 |
| 0.20 | 180,800 | 1 to 13 | 180,800 |
| 0.28 | 30,000 | 38 | 30,000 |
| 0.32 | 100,000 | 38 | 70,000 |
| 0.33 | 120,000 | 7 | 120,000 |
| 0.35 | 66,000 | 5 | 66,000 |
| 0.50 | 150,000 | 3 | 150,000 |
| | 3,021,491 | | 1,995,380 |

During 2005, the Company granted 1,790,000 options to acquire 1,790,000 common shares of the Company at prices ranging from $0.13 to $0.16 per share. The value of each option is estimated on the date of the grant using the Black-Scholes option pricing model and recorded as an expense ratably over the vesting period of the option. The fair value for these options was estimated at the date of grant using the Black-Scholes option pricing model with the following assumptions: *(See fig.22)*

**Non-Employees**

Stock and stock option awards granted to non-employees have been accounted for in accordance with the fair value method of accounting for stock-based compensation. Accordingly, the fair value of the options at the date of grant is accrued and charged to operations. During 2004, the value assigned to 30,000 options granted to non-employees was $3,600. The fair value of these options was estimated at the date of grant using the Black-Scholes option pricing model with the following assumptions: *(See fig.23)*

**Stated Capital**

The legal stated value of the Company's common shares differs from the carrying value reflected in these consolidated financial statements. As at November 30, 2005, the legal stated capital of the common shares is $19,302,449 (2004 - $19,277,666).

The legal stated value of the Company's warrants differs from the carrying value reflected in these consolidated financial statements. The legal stated capital of the warrants is $0.02.

**Earnings (Loss) per Share**

In accordance with the CICA's Section 3500, "Earnings Per Share", earnings (loss) per share are computed by dividing net income (loss) available to common shareholders by the weighted average number of common shares outstanding during the year. Loss per share, for the years presented, were calculated using the weighted average number of common shares outstanding during each year as follows: *(See fig.24)*

During 2005 and 2004, all warrants and stock options were excluded from the calculation of diluted loss per share because the effect would have been anti-dilutive.

## 8. Major Customers

During 2005 and 2004, no single customer accounted for more than 10% of revenue.

**Fig.22 Employees and Directors** *[See note 7]*

| | |
|---|---|
| Weighted average risk-free interest rate | 3.0% to 3.02% |
| Dividend yield | 0.0% |
| Weighted average volatility factors of the expected market price of the Company's common shares | 59.3% to 59.8% |
| Weighted average expected life of the options (in years) | 2.5 to 3.0 |

### Fig.23 Non-Employees *[See note 7]*

| | |
|---|---|
| Weighted average risk-free interest rate | 4.0% |
| Dividend yield | 0.0% |
| Weighted average volatility factors of the expected market price of the Company's common shares | 55.6% |
| Weighted average expected life of the options (in years) | 2.5 |

### Fig.24 Earnings (Loss) Per Share *[See note 7]*

| | 2005 | 2004 |
|---|---|---|
| Basic (loss) per share<br>Net (loss) | **$ (126,280)** | $ (813,216) |
| Weighted average number of common shares outstanding | **39,474,069** | 39,221,687 |
| Basic and diluted (loss) per share | **$ (0.00)** | $ (0.02) |

## 9. Income Taxes

### Future Income Taxes

Future income taxes reflect the net tax effect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's future tax assets and liabilities as at November 30 are as follows: *(See fig.25)*

For Canadian tax purposes, the Company has non-capital losses of $280,000 that can be applied against future years' taxable income. The Company also has unclaimed SR&ED deductions of $3,624,000 that can be used to offset taxable income, and $1,257,000 in investment tax credits that can be applied against income taxes payable in the future.

For US tax purposes, the Company has net operating losses of $200,000 that have a 15-year carry forward period. These losses expire during 2006 through 2017.

For UK tax purposes, the Company has tax losses of $2,502,000 that may be carried forward indefinitely.

The Company has determined that the realization is not more likely than not and therefore a valuation allowance against future income tax assets has been recorded.

### Future Income Tax Recovery

The reconciliation of income taxes computed at the statutory tax rates to income tax expense is as follows: *(See fig.26)*

### Loss Carryforwards

As at November 30, 2005, the Company's non-capital losses and federal investment tax credits for Canadian tax purposes expire as follows: *(See fig.27)*

Furthermore, the Company has capital losses of $426,000 for Canadian tax purposes that have no expiry date. These losses have not been recognized in the consolidated financial statements.

November 30, 2005 (in Canadian dollars unless otherwise indicated)

**Fig.25 Future Income Taxes** *[See note 9]*

| | 2005 | 2004 |
|---|---|---|
| **Future Tax Assets**<br>Non-capital loss carryforward benefit | | |
| North America | $ 171,000 | $ 517,000 |
| Europe | 500,000 | 558,000 |
| Investment tax credit carry forward, net | 980,000 | 841,000 |
| Undeducted SR&ED pool inducements | 1,309,000 | 1,116,000 |
| Book deductions in excess of tax deductions | 666,000 | 598,000 |
| | 3,626,000 | 3,630,000 |
| Valuation reserve | (3,626,000) | (3,630,000) |
| | – | – |
| **Future Tax Liabilities**<br>Tax deductions in excess of accounting | – | – |

**Fig.26 Future Income Tax Recovery** *[See note 9]*

| | 2005 | 2004 |
|---|---|---|
| Tax at combined federal and provincial tax rate | 45,612 | $ 343,575 |
| Use of future tax assets not previously recognized | (41,008) | (234,154) |
| Permanent differences | (23,452) | 18,334 |
| Lower effective tax rates outside Canada | 18,848 | (2,755) |
| Future income tax recovery | – | $ 125,000 |

## 10. Related Party Transactions

As at November 30, 2005, annual and meeting fees payable to directors acting in their capacity as directors was $16,254 (2004 - $13,750). During 2005, directors' fee expense was $50,000 (2004 - $45,000).

During 2004, employee notes totalling $31,850 were forgiven.

In December 2003, the Company entered into a contract with a consulting company whose principals were investors in the Series 1 offering. On signing the contract the consulting company received warrants

**Fig.27** Loss Carryforwards *[See note 9]*

| | Tax losses | Investment tax credits |
|---|---|---|
| 2006 | – | 106,000 |
| 2007 | 36,000 | 56,000 |
| 2008 | 9,000 | 123,000 |
| 2009 | – | 188,000 |
| 2010 | 235,000 | 173,000 |
| 2011 | – | 12,000 |
| 2012 | – | 170,000 |
| 2013 | – | 182,000 |
| 2014 | – | 154,000 |
| 2015 | – | 93,000 |
| | $ 280,000 | $ 1,257,000 |

*[note 7]*. During 2005, the Company expensed consulting fees totalling nil (2004 - $105,172).

As at November 30, 2005 and 2004, officers, directors and employees of the Company hold 10.9% of each of the outstanding Series 1 offering and warrants and received their pro-rata share of dividends. During 2004, a director sold his interest in each of the Series 1 and warrants to a related third party.

## 11. Information by Geographic Area

The Company operates within one dominant industry segment, the development and sale of computer software products. *(See fig.28)*

## 12. Research and Development

### Repayable Contribution

On February 14, 2003, the Company entered into a Repayable Contribution Agreement with the National Research Council of Canada ("NRC"). Under the agreement, the NRC contributed $246,600 for costs incurred in the direct performance of defined work undertaken by the Company. Starting in September 2004, the contributions are repayable quarterly at a rate of 1.07% of the prior quarter's revenue until the earlier of February 2006 or $369,900 has been repaid. If, as at February 2006, the payments are less than $246,000, payments will continue on the same basis until the earlier of full repayment of the original NRC contribution of $246,600 or September 2014. Based on revenue through November 2005, the Company has repaid $84,949 of the original contribution. As it is unlikely that revenue through February 2006 will be sufficient to trigger payments to the NRC in excess of the original contributions, the repayable contribution liability recognized in these consolidated financial statements is based on the original contribution of $246,600 less repayments through November 2005.

### Ontario Innovation Tax Credit

Research and development expenditures for the years ended November 30, 2005 and 2004 are recorded net of the Ontario Innovation Tax Credit ("OITC") as outlined below. *(See fig.29)*

## Fig.28 Information by Geographic Area *[See note 11]*

| 2005 | North America and Australia | Europe | Eliminations | Consolidated |
|---|---|---|---|---|
| **Revenue**<br>Customers | $ 5,200,838 | $ 1,032,746 | – | $ 6,233,584 |
| Interest income | 55,051 | 382 | – | 55,433 |
| Intercompany | 75,746 | – | (75,746) | – |
| | $ 5,331,635 | $ 1,033,128 | $ (75,746) | $ 6,289,017 |
| Income (loss) before income taxes | $ (178,323) | $ 52,043 | – | $ (126,280) |

| 2004 | North America and Australia | Europe | Eliminations | Consolidated |
|---|---|---|---|---|
| **Revenue**<br>Customers | $ 4,793,614 | $ 937,405 | – | $ 5,731,019 |
| Interest income | 40,784 | 562 | – | 41,346 |
| Intercompany | 63,953 | – | (63,953) | – |
| | $ 4,898,351 | $ 937,967 | $ (63,953) | $ 5,772,365 |
| Income (loss) before income taxes | $ (876,444) | $ (61,772) | – | $ (938,216) |

| Capital assets | North America | Europe | Eliminations | Consolidated |
|---|---|---|---|---|
| November 30, 2005 | $ 242,734 | $ 33,559 | – | $ 276,293 |
| November 30, 2004 | $ 147,726 | $ 27,424 | – | 175,150 |

## Fig.29 Ontario Innovation Tax Credit *[See note 12]*

| | 2005 | 2004 |
|---|---|---|
| Total research and development expenditures | $ 1,216,473 | $ 1,246,870 |
| Less OITC | (50,000) | (50,000) |
| Research and development expenditures, net | $ 1,166,473 | $ 1,196,870 |

## 13. Other Income

In May 2000, the Company settled an outstanding proceeding with TRIFOX, Inc. ("TRIFOX"). The settlement provided for an initial cash payment of US$250,000 (all of which was received) and ongoing semi-annual payments in aggregate totalling US$520,000, of which US$164,977 (2004 - $230,124) remains outstanding. These remaining payments are linked to the revenue of TRIFOX and are collateralized by way of a US$824,886 Secured Promissory Note to be drawn down pro-rata based on the payments received. The Company is also entitled to receive additional cash consideration in certain circumstances and to participate, at its option, in certain future financing transactions involving TRIFOX. TRIFOX's payment obligations can be prepaid on an agreed net present value basis, and are collateralized by a first ranking General Security Agreement, Stock Pledge Agreement, Copyright Security Agreement, Limited Recourse Guaranty Agreement and a Source Code Escrow Agreement. In connection with the settlement, both companies have also entered into Mutual Final Releases of claims on all matters relating to litigation between the parties.

The balance of the amount receivable, after deducting collection expenses (21.37% of amounts received), will be recorded in Company income when the amount is otherwise due. To date, all amounts from TRIFOX have been received in accordance with the settlement agreement.

## 14. Special Charges

On May 31, 2004, the Company restructured its operations and terminated nine employees to re-align its on-going operating costs. As at May 31, 2004, a provision of $125,646 was made for the termination and lay-off associated with these nine employees - seven in research and development, one in sales and one in administration. As at November 30, 2004, the Company had paid a total of $108,413. As at November 30, 2005, all amounts had been paid.

## 15. Commitments

### Operating Leases

The total future minimum annual lease payments under operating leases for premises and equipment are as follows: *(See fig.30)*

Future minimum annual payments do not include the Company's share of premises business and realty taxes and other operating costs estimated to be $180,000 per year plus any inflationary adjustments that may be required under the terms of the lease. Premises in the UK are leased on a month-to-month basis. The estimated UK expense for 2006, not included above, is $94,000.

## 16. Contingencies

In the ordinary course of its business activities, the Company may be contingently liable with respect to litigation and other claims made by or on behalf of current or former employees, agents, customers, suppliers, partners, contractors or other persons, as well as federal, state, local and municipal taxation and other governmental and regulatory authorities. Management believes that adequate provision has been recorded in the accounts where required with respect to such claims, based on such considerations as the nature and scope of its business operations, the basis of such claims and remedies available to the Company with respect to them, the reasonableness and likelihood of such claims, exposure

**Fig.30 Operating Leases** *[See note 15]*

| | |
|---|---|
| 2006 | $154,623 |
| 2007 | 32,758 |
| 2008 | 7,724 |
| | $ 195,105 |

estimates for such claims, the Company's past experience with respect to such claims, and similar factors. It is reasonably possible that management estimates of such claims may differ materially from the amounts recorded in the consolidated financial statements.

## 17. Comparative Consolidated Financial Statements

The comparative consolidated financial statements have been reclassified from statements previously presented to conform to the presentation of the current year consolidated financial statements.

# Corporate Information

### Independent Auditors

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Canada

### Corporate Banker

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M5G 2E9
Canada

### Registrar and Transfer Agent

Computershare Trust Company of Canada
Toronto, Calgary, Montreal, Vancouver

### Exchange

The Toronto Venture Exchange
Trading Symbol: ANC

Quotes available at www.tsx.com

### Annual and Special Meeting

Angoss shareholders and other interested parties are invited to attend the Corporation's annual and special meeting.

**Date**
April 18th, 2006

**Time**
4:30pm EST

**Location**
TSX Broadcast and Conference Centre
130 King Street West
Toronto, Ontario
M5X 1J2
Canada

Copies of this report and other information are available from:

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## Client Needs Driven Implementation Methodology

The Angoss implementation methodology reflects a decade of providing predictive analytics systems to advanced users with the world's largest financial services organizations.

By tailoring these best practices to industry and client specific needs Angoss predictive analytics systems ensure that results are actionable, can be deployed systematically, and deliver exceptional, measurable return on investment.