

Kudelski Group

Notes to the consolidated financial statements

1. Summary of significant accounting policies

(A) Basis of preparation

The consolidated financial statements of the Kudelski Group ("Group" or "company") are prepared in accordance with the International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB) and its predecessor organization, the International Accounting Standards Committee (IASC). IFRS 1, First-time Adoption of International Financial Reporting Standards, is applied in preparing these financial statements. These consolidated financial statements are the first Kudelski Group financial statements prepared in accordance with IFRS.

The policies set out below are consistently applied to all the years presented.

Consolidated financial statements of Kudelski Group until December 31, 2004 had been prepared in accordance with Swiss GAAP FER, which differ in certain respects from IFRS. When preparing the Group consolidated financial statements 2005, management has amended certain accounting, valuation and consolidation methods applied in the Swiss GAAP FER financial statements to comply with IFRS. The comparative figures in respect of 2004 are restated to reflect these adjustments.

Reconciliations and descriptions of the effects of the transition from Swiss GAAP FER to IFRS on the Group's equity and its net income are provided in note 42.

These consolidated financial statements were prepared under the historical cost convention, except for items to be recorded at fair value.

The preparation of the consolidated financial statements in conformity with IFRS 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 financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. See note 2 for areas involving a higher degree of judgment and significant estimates.

The annual closing date of the individual financial statements of all Group companies is December 31.

(B) Group accounting

(a) Subsidiaries

Subsidiaries are all entities over which the Group has the power to govern the financial and operating policies, generally implying an ownership of more than one half of the voting rights, unless they are held on a temporary basis. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries also comprise companies in which the Group does not own, directly or indirectly, more than one half of the voting rights but exercises significant power to govern their financial and operating policies and bears an over-proportional responsibility for the main risks.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date on which control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets of the subsidiary acquired is recorded as goodwill.

Kudelski Group

Notes to the consolidated financial statements

Inter-company transactions, balances and unrealized gains on transactions between Group companies are eliminated. Unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

(b) Joint ventures

The Group's interest in jointly controlled entities are accounted for by proportionate consolidation.

The Group combines its share of the joint ventures' individual income and expenses, assets and liabilities and cash flows on a line-by-line basis with similar items in the Group's financial statements.

The Group recognizes the portion of gains or losses on the sale of assets by the Group to the joint venture that is attributable to the other venturers. The Group does not recognize its share of profits or losses from the joint venture that result from the Group's purchase of assets from the joint venture until it resells the assets to an independent party. However, a loss on the transaction is recognized immediately if the loss provides evidence of a reduction in the net realizable value of current assets, or an impairment loss. Accounting policies of joint ventures have been changed where necessary to ensure consistency with the policies adopted by the Group.

(c) Associates

Associates are entities over which the Group has significant influence but which is neither a subsidiary nor a joint-venture to the Group. Significant influence is the power to participate in the financial and operating policy decisions of the associate but not to control those policies. It is presumed to exist when the Group holds at least 20% of the associate's voting power.

Investments in associates are accounted for using the equity method of accounting and are initially recognized at cost.

Unrealized gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates. Unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

(C) Foreign currencies

The consolidated financial statements of the Group are expressed in Swiss francs (CHF), which is the company's presentation currency.

The local currency is generally used as the reporting currency throughout the world. In the respective entity financial statements, monetary assets and liabilities denominated in foreign currencies are translated at the rate prevailing at the balance sheet date. Transactions are recorded using the approximate exchange rate at the time of the transaction. All resulting foreign exchange transaction gains and losses are recognized in the subsidiary's income statement.

Income, expense and cash flows of the consolidated companies have been translated into CHF using average exchange rates. The balance sheets are translated using the year-end exchange rates. Translation differences arising from movements in the exchange rates used to translate equity, long-term internal financing deemed as net investment in a foreign operation and net income are allocated to reserves.

(D) Revenue recognition

Revenue includes the fair value from the sale of goods and services, net of value-added tax, rebates and discounts and after eliminating sales within the Group.

(a) Sale of goods

Sale of goods is recognized when delivery to the customer has occurred, the significant risks and rewards have been transferred to the buyer and collection of the related receivables is reasonably assured. Sale of goods may include delivery of complete systems comprising hardware, software, specific developments, an initial batch of smart-cards, licenses and other services.

(b) Services rendered

Revenue for services rendered includes various types of services such as system integration, specific developments and customization, maintenance, training as well as revenues from complete security solutions generating recurring service revenues.

Complete security solutions may comprise hardware, software, specific developments, licenses, smartcards, maintenance and other services according to the specific arrangements contracted with the client. Assets made available to clients under such contracts are initially recognized in the balance sheet at cost under fixed assets as they remain the Group property. Revenue is recognized when contractually earned and is usually dependent on the client's number of subscribers or number of smartcards made available. Cost in connection with the depreciation of the assets made available to clients is recognized over the shorter of the duration of the contract and the useful lives of those assets. It is shown under depreciation in the income statement. It is also subject to periodic impairment reviews. Other costs (such as maintenance, services and security efforts) relating to those contracts are recognized when incurred. When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognized immediately.

Revenue from system integration, specific developments and customization is recognized under the percentage of completion method. The stage of completion is measured by reference to the contract costs incurred and the effective hours worked up to the balance sheet date as a percentage of total estimated costs and total estimated hours worked for each contract.

Revenue from maintenance and training is recognized when earned (maintenance revenue is allocated over the contractual period).

(c) Royalties and licenses

Royalty income is recognized when earned. If the relevant license agreement contains certain performance obligations, the revenue is considered earned when the obligation has been performed.

For software license arrangements that do not require significant modifications or customizations of the underlying software, the Group recognizes new software license revenue when: (1) The company enters into a legally binding arrangement with a customer for the license of software; (2) it delivers the products; (3) customer payment is deemed fixed or determinable and free of significant contingencies or uncertainties; and (4) collection is probable.

(d) Interest income

Interest income is recognized as earned unless collectibility is in doubt.

(E) Derivative financial instruments

Derivative financial instruments, including foreign exchange forward contracts, options and interest rate swaps, are initially recognized in the balance sheet at cost and are subsequently re-measured at their fair value. The method of recognizing the resulting gain or loss is dependent on whether the derivative is designated to hedge a specific risk and qualifies for hedge accounting.

The Group designates certain derivatives which qualify as hedges for accounting purposes as either a hedge of the fair value of recognized assets or liabilities or an unrecognized firm commitment (fair value hedge) or as a hedge of a forecasted transaction (cash flow hedge). The Group documents at the inception of the transaction the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives designated as hedges to specific assets, liabilities or cash flows. The Group also documents its assessment, both at the hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values of hedged items.

(a) Derivatives that do not qualify for hedge accounting

Certain derivatives transactions, while providing effective economic hedging under the Group's risk management policy, do not qualify for hedge accounting under the specific rules of IAS 39. Changes in the fair value of any derivative instruments that do not qualify for hedge accounting under IAS 39 are recognized immediately in the income statement as part of other finance income/(expense), net.

(b) Fair value hedge

Changes in the fair value of derivatives that are designated and qualify as fair value hedges and that are highly effective are recorded in the income statement, along with any changes in the fair value of the hedged asset or liability that is attributable to the hedged risk.

(c) Cash flow hedge

Changes in the fair value of derivatives that are designated and qualify as cash flow hedges and that are highly effective are recognized in equity. Where the forecasted transaction results in the recognition of an asset or a liability, the gains and losses previously included in equity are included in the initial measurement of the asset or liability. Otherwise, amounts recorded in equity are transferred to the income statement and classified as revenue or expense in the same period in which the forecasted transaction affects the income statement.

The instruments that may be used include forward foreign exchange contracts, currency swaps as well as zero cost option strategies with terms generally not exceeding six months. The derivative financial instruments are entered into with high credit quality financial institutions, consistently with specific approval, limit and monitoring procedures.

(F) Taxes

Taxes reported in the consolidated income statements include current and deferred taxes on profit, as well as non reimbursable withholding taxes and tax adjustments relating to prior years. Income tax is recognized in the income statement, except to the extent that it relates to items directly taken to equity, in which case it is recognized in equity. Taxes on income are accrued in the same periods as the revenues and expenses to which they relate.

Deferred taxation is the tax attributable to the temporary differences that appear when taxation authorities recognize and measure assets and liabilities with rules that differ from those of the consolidated accounts. Deferred taxes are calculated using the comprehensive liability method at the substantially enacted rates of tax expected to prevail when the temporary differences reverse. Any changes of the tax rates are recognized in the income statement unless related to items directly recognized in equity.

Deferred tax liabilities are recognized on all taxable temporary differences excluding non deductible goodwill. Deferred tax assets are recognized on all deductible temporary differences provided that it is probable that future taxable income will be available.

Deferred income tax liability have not been recognized for withholding tax and other taxes that would be payable on the unremitted earnings of certain subsidiaries. Such amounts are either permanently reinvested or do not generate any taxation due to the application of tax relief.

(G) Tangible fixed assets

(a) General

All property, plant and equipment is shown at cost, less subsequent depreciation and impairment, except for land, which is shown at cost less impairment. Cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repair and maintenance expenditures are charged to the income statement during the financial period in which they are incurred. Financing costs associated with the construction of tangible fixed assets are not capitalized.

Depreciation is calculated on a straight-line basis over the useful life, according to the following schedule:

Buildings

	Useful life in years
Buildings	20 – 33
Buildings improvements	4 – 8

Technical equipment and machinery

	Useful life in years
Machinery and measurement instruments	4 – 7
Digital material and equipment	4 – 5
Computers and information networks	4
Fixed assets made available to clients	2 – 10

Other equipment

	Useful life in years
Office furniture and equipment	5 – 7
Vehicles	4 – 5

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date. An asset's carrying amount is impaired immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Gains and losses on disposal or retirement of tangible fixed assets are determined by comparing the proceeds received with the carrying amounts and are included in the consolidated income statements.

(b) Leased tangible fixed assets

Assets acquired under long-term finance leases are capitalized and depreciated in accordance with the Group's policy on property, plant and equipment. The financial commitments resulting therefrom are reported as other current and long-term liabilities. Rentals payable under operating leases are charged to the income statement as incurred.

(c) Fixed assets made available to clients

The Group makes equipment as well as smart cards available to clients within the scope of complete security solutions. The assets given to these clients remain the property of the Group and are initially recognized at cost and disclosed in the balance sheet under technical equipment and machinery. These assets are depreciated over the shorter of the duration of the contract and the economic life of the individual components and the related expense is disclosed under depreciation.

(H) Intangible assets

(a) Goodwill

Arising after January 1, 2004

Goodwill represents the excess of the acquisition cost over the fair value of the Group's share of net identifiable assets acquired at the date of acquisition. Goodwill is allocated to cash-generating units for the purpose of impairment testing. Goodwill on acquisition of subsidiaries and joint-ventures is included in intangible assets. Goodwill on acquisition of associates is included in investments in associates. Goodwill is at least annually tested for impairment and carried at cost less accumulated impairment losses. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Arising before January 1, 2004

Goodwill resulting from business combinations occurred before January 1, 2004 has been written off directly to equity following the Group's previous accounting policies and has not been reinstated. It is not transferred to the income statement when impaired or disposed of.

(b) Research and development

Research and development expenses are fully charged to the income statement. The Group considers that economic uncertainties inherent in the development of new products preclude it from capitalizing development costs, except for those developments related to the deployment of complete security solutions provided to certain customers and paid for by those customers in a rental agreement. In such cases, these specific developments are capitalized under the fixed assets made available to clients and amortized using the straight-line method over their estimated useful lives of 4 to 5 years.

(c) Computer software

Acquired computer software licenses are capitalized on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortized using the straight-line method over their estimated useful lives (three to four years). Costs associated with developing or maintaining computer software programs are recognized as an expense as incurred.

(I) Financial assets

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

(a) Financial assets at fair value through profit or loss

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management. Derivatives are also categorized as held for trading unless they are designated as hedges. Assets in this category are classified as current assets if they are either held for trading or are expected to be realized within 12 months of the balance sheet date.

(b) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable. They are included in current assets, except for maturities greater than 12 months after the balance sheet date. These are classified as long-term assets. Loans and receivables are included in trade and other receivables in the balance sheet.

Purchases and sales of investments are recognized on settlement date. Investments are initially recognized at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Investments are derecognized when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership.

Financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables are carried at amortized cost using the effective interest method. Realized and unrealized gains and losses arising from changes in the fair value of the "financial assets at fair value through profit or loss" category are included in the income statement in the period in which they arise.

The fair values of quoted investments are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, and option pricing models refined to reflect the issuer's specific circumstances.

(J) Inventories

Inventories are stated at the lower of cost and net realizable value. Cost is determined using the weighted average cost method.

The cost of work in progress and manufactured finished goods comprises direct production costs and an appropriate proportion of production overheads and factory depreciation. Net realizable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

Furthermore, inventories which are no longer part of production and sales plans are directly written off from the gross value of inventories.

(K) Trade accounts receivable

Trade accounts receivables are carried at invoiced amounts, less adjustments for doubtful receivables. A provision for impairment is made for doubtful receivables based on a review of all material outstanding amounts at the reporting date.

(L) Cash and cash equivalents

Cash and cash equivalents include cash in hand and highly liquid investments with original maturities of three month or less. This position is readily convertible to known amounts of cash. Bank overdrafts are shown within short-term financial debt in current liabilities on the balance sheet.

(M) Marketable securities

Marketable securities consist of equity and debt securities which are traded in liquid markets. The Group has classified all its marketable securities as financial assets at fair value through profit or loss. All purchases and sales of marketable securities are recognized on the trade date, which is the date on which the Group commits to purchase or sell the asset.

(N) Convertible bonds

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

The fair value of the liability component of convertible bonds is determined using a market interest rate for an equivalent straight bond at inception. This amount is recorded as a liability on an amortized cost basis until extinguished on conversion or maturity of the bond. The remainder of the proceeds is allocated to the conversion option. Issuance costs are allocated on a proportional basis to the liability component and are expensed over the convertible bond life.

(a) Convertible bond with cash settlement alternative
If the convertible bonds issued entitle the issuer to deliver cash upon exercise of the conversion option (cash settlement alternative), the conversion option is recorded as a liability and is subsequently measured at fair value using the Black & Scholes option pricing model. Changes in fair values of the conversion option are recognized in the income statement as other finance income/(expense), net.

(b) Convertible bond without cash settlement alternative
If the convertible bonds issued do not entitle the issuer to deliver cash upon exercise of the conversion option, the equity component is measured at inception and is allocated to the reserves.

(O) Provisions

Provisions are recognized when the Group has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Restructuring provisions comprise lease termination penalties and employee termination payments. Provisions are not recognized for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognized even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

(P) Contingent consideration

The purchase consideration for selected Group acquisitions may include contingent components, which depend on the future financial performance of the company acquired ("earn-out clause"). It is based on the management's best estimate of the final consideration payable and is subject to a yearly review.

Where a portion of the contingent consideration for an acquisition is deferred to a date more than one year after the end of the current financial year, that portion is discounted to its present value and disclosed within other long term liabilities.

(Q) Employee benefits

(a) Pension obligations

The Group operates a number of defined benefits and defined contribution plans, the assets of which are generally held in separate trustee-administered funds. The pension plans are generally funded by payments from employees and by the relevant Group companies, taking into consideration the recommendations of independent qualified actuaries. For defined benefit plans, the Group companies provide for benefits payable to their employees on retirement by charging current service costs to income.

The liability in respect of defined benefit pension plans is the present value of the defined benefit obligation at the balance sheet date minus the fair value of plan assets, together with adjustments for actuarial gains/losses and past service costs. Defined benefit obligation is in all material cases calculated annually by independent actuaries using the projected unit credit method, which reflects services rendered by employees to the date of valuation, incorporates assumptions concerning employees' projected salaries and uses interest rates of highly liquid corporate bonds which have terms to maturity approximating the terms of the related liability. Actuarial gains and losses arising from experience adjustments, amendments to the pension plan and changes in actuarial assumptions in excess of the greater of 10% of the value of plan assets or 10% of the defined benefit obligation are charged or credited to income over the average working life of the related employees.

The Group's contributions to the defined contribution plans are charged to the income statement in the year to which they relate.

(b) Other long-term employee benefits

Other long-term employee benefits represent amounts due to employees under deferred compensation arrangements mandated by certain jurisdictions in which the Group conducts its operations. Benefits cost is recognized on an accrual basis in the personnel expenses.

(c) Employee Share Plan (ESP)

The Group put in place an employee share purchase program which allows certain employees to buy a specific number of shares at preferred conditions and with a blocking period of 3 years. The difference between the fair value of these shares and the employees' payments for the shares is expensed in the income statement at subscription date. The fair value of the shares transferred is determined based on the market price of the shares adjusted to account for the estimated value effect of the blocking period.

(d) Employee Stock Option Plan (ESOP)

The Group put in place an equity settled stock option plan for the members of the Board of Directors, the management and certain expert employees within the Group. The plan includes options with vesting periods of 3, 4 and 5 years and which may be exercised during a period of one year from the end of the vesting period.

Options are measured at fair value at the grant date using the Black & Scholes model adjusted to account for the estimated value impact of the exercise period. The determined fair value is then expensed in the income statement over the vesting period. An adjustment for future forfeited options is included in the calculation.

(e) Profit sharing and bonus plan

The Group recognizes a liability and an expense for bonuses and profit sharing where contractually obliged or where there is a past practice that has created a constructive obligation. In addition, the Board of Directors may grant free shares to certain employees. These shares may be subject to a blocking period of up to 5 years and are expensed in the income statement at their fair value at grant date taking into account the estimated value reduction due to the blocking period.

(f) Other employee benefits

Salaries, wages, social contributions and other benefits are recognized on an accrual basis in the employee benefits expense in the year in which the employees render the associated services.

(R) Treasury shares

Treasury shares are deducted from equity at acquisition cost. Gains or losses on the sale or cancellation of treasury share are recognized in the retained earnings.

(S) Dividends

Dividends are recorded in the Group's financial statements in the period in which they are approved by the Group's shareholders.

(T) New accounting standards and IFRIC interpretations

Certain new standards, amendments and interpretations to existing standards have been published that are mandatory for the Group's accounting periods beginning on or after 1 January 2006 or later periods but which the Group has not early adopted:

- IAS 19 (amendment), Employee Benefits (effective from January 1, 2006). The Group does not intend to change the accounting policy adopted for recognition of actuarial gains and losses and does not participate in any multi-employers plans. Therefore adoption of this amendment will only impact the format and extent of disclosures. The Group will apply this amendment for annual period beginning after January 1, 2006.
- Following changes in IAS 39 and in IFRS 4, and IFRS 6 are not relevant for the Group's operations:
 - IAS 39 (Amendment), Cash Flow Hedge Accounting of Forecast Intragroup Transactions (effective from 1 January 2006).
 - IAS 39 (Amendment), The Fair Value Option (effective from 1 January 2006).
 - IAS 39 and IFRS 4 (Amendment), Financial Guarantee Contracts (effective from 1 January 2006).
 - IFRS 6, Exploration for and Evaluation of Mineral Resources (effective from 1 January 2006).
- IFRS 7, Financial Instruments: Disclosures, and a complementary amendment to IAS 1, Presentation of Financial Statements – Capital Disclosures (effective from 1 January 2007). IFRS 7 introduces new disclosures to improve the information about financial instruments. It requires the disclosure of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk and market risk, including sensitivity analysis to market risk. The amendment to IAS 1 introduces disclosures about the level of an entity's capital and how it manages capital. The Group is currently assessing the impact of IFRS 7 and the amendment to IAS 1 and will apply IFRS 7 and the amendment to IAS 1 from annual periods beginning January 1, 2007.
- Following IFRICs are not relevant to the Group's operations:
 - IFRIC 4, Determining whether an Arrangement contains a Lease (effective from January 1, 2006).
 - IFRIC 5, Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds (effective from January 1, 2006).
 - IFRIC 6, Liabilities arising from Participating in a Specific Market – Waste Electrical and Electronic Equipment (effective from December 1, 2005).
 - IFRIC 7, Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies (effective March 1, 2006).
 - IFRIC 8, Scope of IFRS 2 (effective May 1, 2006).

2. Critical accounting estimates and judgements

The Group's principal accounting policies are set out in note 1 of the Group's consolidated financial statements and conform to International Financial Reporting Standards (IFRS). Significant judgments and estimates are used in the preparation of the consolidated financial statements which, to the extent that actual outcomes and results may differ from these assumptions and estimates, could affect the accounting in the areas described in this section.

Complete security solutions generating recurring service revenues

As defined in note 1 D, the Group provides complete security solutions generating recurring service revenues by making assets available to clients, whereby depreciation is recognized over the shorter of the duration of the contract and the useful life of such assets. Depending on the contract terms with each client, the Group may replace the assets made available to the client for security or economic reasons. Early replacement due to technical obsolescence would affect the profitability of the Group by resulting in an impairment of the assets made available to the client.

Deferred tax assets

The Group is subject to income tax in numerous jurisdictions. Significant judgment is required in determining the portion of tax losses carried forward which can be offset against future taxable profit (note 15). In order to assess whether there is any future benefit, forecasts are made of the future taxable profits by legal entity. Actual outcomes could vary significantly from forecasts of future profits and could therefore modify significantly the deferred tax asset and the income taxes captions.

Litigation and product liability provisions

A number of Group subsidiaries can be subject to litigation and product liability claims arising out of the normal conduct of their businesses. As a result, claims could be made against them that might not be covered by existing provisions or by external insurance coverage. Management believes that the outcomes of such actions, if any, would not be material to the Group's financial condition but could be material to future results of operations in a given period.

Retirement benefit plans

The Group sponsors pension and other retirement plans in various forms covering employees who meet eligibility requirements. Several statistical and other factors that attempt to anticipate future events are used in calculating the expense and liability related to the plans. These factors include assumptions about the discount rate, expected return on plan assets and rate of future compensation increases, as determined by Group management within certain guidelines. In addition, the Group's actuarial consultants use statistical information such as withdrawal and mortality rates for their estimates. The actuarial assumptions used (note 26) may differ materially from actual results due to changing market and economic conditions, higher or lower withdrawal rates or longer or shorter life spans of participants. The Group has recorded in compliance with IFRS 1 the initial differences as of January 1, 2004 between assumed and actual income and expense as a liability in its balance sheet and uses the corridor approach in order to recognize its unrecorded gains and losses.

3. Segment information

Primary segments

A business segment is a group of assets and operations engaged in providing products and services subject to risks and returns that are different from those of other business segments.

Operating divisions

The Group is divided operationally on a worldwide basis into two divisions, Digital Television and Public Access. These divisions, which are also based on internal management structures, are best described as follows:

The Digital TV division provides open conditional access solutions allowing digital TV and content providers to operate a wide range of high value-added pay TV services on a secure platform.

The Public Access division provides access control systems and ticketing services for ski lifts, car parks, stadiums, concert halls and important events as well as multifunctional cards for universities and corporations.

Corporate

Income and expenses relating to Corporate include the costs of Group headquarters and the items of income and expense which are not directly attributable to specific divisions.

The primary segment information

	Operating division Digital Television 2005	Operating division Digital Television 2004	Operating division Public Access 2005	Operating division Public Access 2004
in CHF'000				
Revenues				
External sales	492 162	417 826	194 940	179 727
Inter-segment sales	4 162	1 999	1 684	1 587
Total revenues	496 324	419 825	196 624	181 314
Income statement				
Operating income (EBIT)	125 432	107 731	9 971	-3 257
Interest expense and other Finance income/(expense), net				
Share of results of associates			2 663	1 315
Income before tax				
Income tax expense				
Net income for the year				
Balance sheet				
Assets				
Segment assets	435 133	431 265	176 230	145 758
Investments in associates			7 559	5 399
	435 133	431 265	183 789	151 157
Liabilities				
Segment liabilities	108 495	96 659	113 367	108 657
Other information				
Capital expenditure	40 211	56 684	8 780	8 979
Depreciation and amortization	-31 897	-23 368	-7 759	-7 590
Impairment losses		-2 749		

Corporate 2005	Corporate 2004	Eliminations 2005	Eliminations 2004	Total 2005	Total 2004
				687 102	597 553
		-5 846	-3 586	-	-
		-5 846	-3 586	687 102	597 553
-14 261	-12 253			121 142	92 221
				-31 091	5 937
				2 663	1 315
				92 714	99 473
				-5 942	-5 973
				86 772	93 500
308 194	97 470			919 557	674 493
				7 559	5 399
308 194	97 470			927 116	679 892
314 761	194 717			536 623	400 033
	48			48 991	65 711
-35	-22			-39 691	-30 980
				-	-2 749

Expenses, assets and liabilities relating to Corporate include the costs, assets and liabilities of Group headquarters and the items of expenses, assets and liabilities which are not directly attributable to specific divisions.

Kudelski Group

Notes to the consolidated financial statements

Secondary segments

A geographical segment provides products or services within a particular economic environment that is subject to risks and returns that are different from those segments operating in other economic environments.

Sales

	Digital TV 2005	Digital TV 2004	Public Access 2005	Public Access 2004	Total 2005	Total 2004
in CHF'000						
Europe	244 247	198 021	171 232	164 933	415 479	362 954
Americas	184 431	172 444	13 925	7 983	198 356	180 427
Asia, Oceania and Africa	63 484	47 361	9 783	6 811	73 267	54 172
	492 162	417 826	194 940	179 727	687 102	597 553

Sales are allocated based on where the client is located.

Other geographical information

	Europe	Others	Total
in CHF'000			
Total assets as of December 31			
– 2005	861 346	65 770	927 116
– 2004	628 515	51 377	679 892
Capital expenditures for:			
– 2005	47 950	1 041	48 991
– 2004	64 336	1 375	65 711

Assets and capital expenditures are allocated based on location of the entity owning the assets.

Revenue categories

	2005	2004
in CHF'000		
Sale of goods	493 031	403 774
Services rendered	147 995	162 640
Royalties and licenses	46 076	31 139
	687 102	597 553

4. Other operating income

	2005	2004
in CHF'000		
Income received for costs incurred in maintaining system security	7 750	–
Gain on sale of a subsidiary	35	4 437
Loss on fixed assets sales proceeds	-226	–
Others	2 512	4 141
	10 071	8 578

5. Other operating expenses

		2005	2004
in CHF'000			
Development and engineering expenses		24 383	16 571
Travel, entertainment and lodging expenses		18 780	18 087
Legal and consultancy expenses		17 189	18 679
Administration expenses		14 279	13 019
Building and infrastructure expenses		13 835	12 957
Marketing and sales expenses		9 091	12 569
Taxes other than income tax		3 739	3 886
Change in provisions		2 037	2 066
Insurance, vehicles and others		5 589	8 373
		108 922	106 207

6. Depreciation, amortization and impairment

	Notes	2005	2004
in CHF'000			
Land and buildings	12	2 093	2 243
Equipment and machines	12	33 252	26 820
Total depreciation and impairment of tangible fixed assets		35 345	29 063
Patents, software and other	13	4 346	4 666
Total amortization and impairment on intangible fixed assets		4 346	4 666
Depreciation, amortization and impairment		39 691	33 729

7. Interest expense

	Notes	2005	2004
in CHF'000			
Interest expense:			
- Convertible bond 2002-2009	30	10 449	12 651
- Convertible bond 2005-2012	25	2 576	-
- Other and bank charges		1 152	1 364
Loss on the repurchase of the convertible bond 2002-2009		6 513	-
		20 690	14 015

8. Other finance income/(expense), net

	Notes	2005	2004
in CHF'000			
Interest income		7 300	4 266
Change in fair value of the convertible bond 2002-2009 conversion option		2 064	14 105
Net (gains)/losses on foreign exchange related derivative financial instruments not qualifying for hedge accounting		-6 663	4 153
Net foreign exchange transaction (gains)/losses	10	-13 156	7 818
Fair value adjustment of financial asset at fair value through profit or loss		-	-10 500
Others		54	110
		-10 401	19 952

9. Income tax expenses

	Notes	2005	2004
in CHF'000			
Current income tax		-10 337	-8 866
Deferred income tax	15	4 852	3 524
Other taxes		-457	-632
		-5 942	-5 973

Other taxes include non reimbursable withholding taxes.

The tax on the Group's profit before tax differs from the theoretical amount that would arise using the weighted average tax rate applicable to profits of the consolidated companies as follows:

	2005	2004
in CHF'000		
Profit before taxes	92 714	99 473
Tax calculated at domestic tax rates applicable to profits in the respective countries	-21 746	-16 004
Income not subject to income tax	7 672	10 109
Utilization of previously unrecognized tax losses	6 932	8 071
Write off deferred taxes	-1 766	-9 737
Expenses not deductible for tax purposes	-385	-286
Prior year income taxes	-	-1 331
Non-reimbursable withholding tax	-457	-632
Other	3 808	3 835
Tax expense	-5 942	-5 973

Profit before tax includes the full profit before tax of a joint venture company which taxes are paid by its shareholder since its is a tax transparent company. As a result 100% of the profit before taxes of this company is included although the Group only recognizes 50% of the taxes on this profit due to the special tax arrangements. The tax impact which is included in others amounts to kCHF 3 735 (2004: kCHF 3 974).

The weighted average applicable tax rate was 23.45% (2004: 15.81%). The increase in tax rate is mainly attributable to two elements: a) material financial profits on zero tax companies in 2004 and b) change in the profitability of the subsidiaries on one hand in the respective countries and on the other hand in the respective entities with special tax holidays.

10. Net foreign exchange result

The exchange differences accounted for in the income statement are as follows:

	2005	2004
in CHF'000		
Sales	6 742	-1 031
Cost of material	-1 380	-606
Other finance income/(expense) net	-13 156	7 818
Total exchange differences	-7 794	6 181

11. Earnings per share (EPS)

Basic earnings per share

Basic earnings per share are calculated by dividing the net income attributable to shareholders by the weighted average number of shares outstanding during the year.

The number of outstanding shares is calculated by deducting the average number of shares purchased and held as treasury shares from the total of all issued shares.

	2005	2004
in CHF'000		
Net income attributable to bearer shareholders	71 785	76 257
Net income attributable to registered shareholders	7 068	7 528
Total net income	78 853	83 785
Weighted average number of bearer shares outstanding	47 025 780	46 898 894
Weighted average number of registered shares outstanding	46 300 000	46 300 000

	2005	2004
in CHF		
Bearer shares	1.5265	1.6260
Registered shares	0.1527	0.1626

Diluted earnings per share

The diluted earnings per share calculation takes into account all potential dilutions to the earnings per share arising from the convertible bonds and options on Kudelski SA shares.

	2005	2004
in CHF'000		
Net income attributed to equity holders of the company	78 853	83 785
Elimination of interest expense on convertible debt*	–	–
Tax impact on above adjustments	–	–
Net income used to determine earnings per share	78 853	83 785
Of which:		
– Attributable to bearer shareholders	71 813	76 282
– Attributable to registered shareholders	7 040	7 503
	78 853	83 785
Weighted average number of bearer shares outstanding	47 025 780	46 898 894
Effect of dilutive potential bearer share:		
– Share options	201 041	174 700
– Convertible bond*	–	–
Weighted average number of bearer shares for the purpose of diluted earnings per share	47 226 821	47 073 594
Weighted average number of registered shares for the purpose of diluted earnings per share	46 300 000	46 300 000

	2005	2004
in CHF		
Bearer shares	1.5206	1.6205
Registered shares	0.1521	0.1620

* Shares equivalent of 3 341 254 (2004: 2 835 327) relating to the convertible bonds were excluded from the calculation of diluted earnings per share as they were anti-dilutive.

12. Tangible fixed assets

	31.12.2005	31.12.2004
in CHF'000		
Land and buildings	59 524	38 535
Equipment and machines	75 768	89 136
	135 292	127 671

Land and buildings

	Land	Buildings	Building improve- ments	Cons- truction in progress	Total
in CHF'000					
Gross values at cost					
As of January 1, 2004	8 807	29 650	8 723	74	47 254
Additions	2 300	1 914	491	8 311	13 016
Disposals and retirements	-	-1 824	-153	-	-1 977
Change in scope of consolidation	-	-	-462	-	-462
Currency translation adjustment	-	-63	-32	-	-95
Reclassification	-	-114	114	-	-
As of January 1, 2005	11 107	29 563	8 681	8 385	57 736
Additions	81	4 814	272	18 326	23 493
Disposals and retirements	-	-	-666	-	-666
Currency translation adjustment	-	-11	45	-	34
Reclassification and others	-	-	7	-114	-107
As of December 31, 2005	11 188	34 366	8 339	26 597	80 490
Accumulated depreciation and impairment					
As of January 1, 2004	-	-11 542	-6 511	-	-18 053
Systematic depreciation	-	-1 068	-1 175	-	-2 243
Recovery of depreciation on disposals and retirements	-	774	153	-	927
Change in scope of consolidation	-	-	111	-	111
Currency translation adjustment and others	-	42	14	-	56
Reclassification	-	35	-35	-	-
As of January 1, 2005	-	-11 759	-7 443	-	-19 202
Systematic depreciation	-	-1 605	-488	-	-2 093
Recovery of depreciation on disposals and retirements	-	-	350	-	350
Currency translation adjustment	-	3	-24	-	-21
As of December 31, 2005	-	-13 361	-7 605	-	-20 966
Net book values as of December 31, 2004	11 107	17 804	1 239	8 385	38 535
Net book values as of December 31, 2005	11 188	21 005	734	26 597	59 524
Useful life in years		20 – 33	4 – 8		

Leased land and buildings included in the table above amount to:

	31.12.2005	31.12.2004
in CHF'000		
Leased land and buildings	8 737	8 737
Accumulated depreciation	-6 885	-6 429
Net book value	1 852	2 308

	31.12.2005	31.12.2004
in CHF'000		
Fire insurance value of buildings	53 252	46 859
Corporate buildings on land whose owner has granted a permanent and specific right of use	4 027	4 287

Equipment and machines

	Technical equipment and machinery	Other equipment	Total
in CHF'000			
Gross values at cost			
As of January 1, 2004	112 100	8 128	120 228
Additions	44 955	2 326	47 281
Disposals and retirements	-13 422	-1 393	-14 815
Change in scope of consolidation	-739	-99	-838
Currency translation adjustment	-422	-107	-529
Reclassification and others	-951	240	-710
As of January 1, 2005	141 520	9 096	150 615
Additions	19 212	1 441	20 653
Disposals and retirements	-4 277	-225	-4 502
Change in scope of consolidation	-52	-	-52
Currency translation adjustment	634	222	856
Reclassification and others	-725	864	139
As of December 31, 2005	156 312	11 397	167 709
Accumulated depreciation and impairment			
As of January 1, 2004	-40 987	-5 043	-46 030
Systematic depreciation	-22 684	-1 447	-24 131
Impairment	-2 681	-8	-2 689
Recovery of depreciation on disposals and retirements	8 800	1 247	10 047
Change in scope of consolidation	410	35	445
Currency translation adjustment	338	64	402
Reclassification and others	705	-229	476
As of January 1, 2005	-56 099	-5 381	-61 480
Systematic depreciation	-31 517	-1 735	-33 252
Impairment	-	-	-
Recovery of depreciation on disposals and retirements	3 179	201	3 380
Change in scope of consolidation	2	-	2
Currency translation adjustment	-443	-139	-582
Reclassification and others	375	-384	-9
As of December 31, 2005	-84 503	-7 438	-91 941
Net book values as of December 31, 2004	85 421	3 715	89 136
Net book values as of December 31, 2005	71 809	3 959	75 768
Useful life in years	2 – 10	4 – 7	

The technical equipment and machinery comprise assets made available to clients and generating recurring service revenue. Customers carry the property risks related to such assets.

	31.12.2005	31.12.2004
in CHF'000		
Fire insurance value		
Equipment	58 530	52 568

13. Intangible assets

in CHF'000	Know-How	Patents, software and other	Total
Gross values at cost			
As of January 1, 2004	5 000	25 850	30 850
Additions	–	6 457	6 457
Disposals and retirements	–	-1 074	-1 074
Change in scope of consolidation	–	-231	-231
Currency translation adjustment	–	-18	-18
Reclassification and others	–	-117	-117
As of January 1, 2005	5 000	30 867	35 867
Additions	–	4 812	4 812
Disposals and retirements	–	-190	-190
Change in scope of consolidation	–	-302	-302
Currency translation adjustment	–	10	10
As of December 31, 2005	5 000	35 198	40 198
Accumulated depreciation and impairment			
As of January 1, 2004	-5 000	-10 941	-15 941
Systematic amortization	–	-4 662	-4 662
Impairment	–	-4	-4
Recovery of amortization on disposal and retirements	–	369	369
Change in scope of consolidation	–	203	203
Currency translation adjustments	–	18	18
Reclassification and others	–	15	15
As of January 1, 2005	-5 000	-15 002	-20 002
Systematic amortization	–	-4 347	-4 347
Recovery of amortization on disposal and retirements	–	175	175
Change in scope of consolidation	–	14	14
Currency translation adjustments	–	-7	-7
Reclassification and others	–	9	9
As of December 31, 2005	-5 000	-19 156	-24 156
Net book values as of December 31, 2004	–	15 866	15 866
Net book values as of December 31, 2005	–	16 041	16 041
Useful life in years		4 – 8	

14. Investments in associates

	2005	2004
in CHF'000		
As of January 1	5 399	5 119
Share of profit	2 663	1 315
Dividend received	-503	-1 005
Exchange differences	-	-30
As of December 31	7 559	5 399

The Group's interests in its principal associates, all of which are unlisted, were as follows:

Name of associate	Principal activity	Interest held 2005	Interest held 2004
Digital Elektronik GmbH, Austria	Manufacture of Electronics products	25%	25%
APT-SkiData Ltd, United Kingdom	Sales of Physical Access products	26%	26%
SkiData Parking Systems	Sales of Physical Access products	26%	26%

Summarized financial information of the Group's associates

	31.12.2005	31.12.2004
in CHF'000		
Total assets	52 802	42 031
Total liabilities	22 725	20 570
Net assets	30 077	21 461
Group's share of associates' net assets	7 559	5 399

	2005	2004
in CHF'000		
Revenue	76 781	51 967
Result of the period	10 545	5 261
Group's share of associates' result for the period	2 663	1 315

15. Deferred income taxes

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority.

The offset amounts are as follows:

	31.12.2005	31.12.2004
in CHF'000		
Deferred tax asset	27 255	21 026
Deferred tax liabilities	-2 899	-1 792
	24 356	19 234

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

	Notes	2005	2004
in CHF'000			
At January 1		19 234	15 834
Exchange differences		270	-124
Income statement (expense)/income	9	4 852	3 524
At December 31		24 356	19 234

The movement in deferred tax assets and liabilities during the year, without taking into consideration the offsetting of balances within the same tax jurisdiction, is as follows:

	01.01.2005	Charged to income statement	Exchange differences	31.12.2005
in CHF'000				
Deferred tax assets associated with:				
– Intangibles	7 407	965		8 372
– Employee benefits	2 391	386		2 777
– Tax losses	6 990	2 828		9 818
– Provisions	715	3 371		4 086
– Inter-company profit elimination	4 232	-1 289	272	3 215
– Others	963	-664		299
Total deferred tax asset (gross)	22 698	5 597	272	28 567
Deferred tax liabilities associated with:				
– Affiliates and allowances for Group companies	-2 386	-968		-3 354
– Provisions and accelerated tax depreciation	-1 046	191	-2	-857
– Others	-32	32		–
Total deferred tax liability (gross)	-3 464	-745	-2	-4 211
Net deferred tax asset/(liability)	19 234	4 852	270	24 356

And for the past year:

in CHF'000	01.01.2004	Charged to income statement	Exchange differences	31.12.2004
Deferred tax assets associated with:				
– Intangibles	5 534	1 873		7 407
– Employee benefits	1 974	416	1	2 391
– Tax losses	6 299	691		6 990
– Provisions	1 181	-497	31	715
– Inter-company profit elimination	2 784	1 561	-113	4 232
– Others	120	894	-51	963
Total deferred tax asset (gross)	17 892	4 938	-132	22 698
Deferred tax liabilities associated with:				
– Affiliates and allowances for Group companies	-1 957	-438	9	-2 386
– Provisions and accelerated tax depreciation	-62	-983	-1	-1 046
– Others	-39	7		-32
Total deferred tax liability (gross)	-2 058	-1 414	8	-3 464
Net deferred tax asset/(liability)	15 834	3 524	-124	19 234

At the balance sheet date, the Group has unused tax losses and temporary differences of CHF 248.0 million (2004: CHF 222.9 million) available for offset against future profits. A deferred tax asset has been recognized in respect of CHF 113.0 million (2004: CHF 87.0 million) of such losses.

No deferred tax asset has been recognized in respect of the remaining CHF 135.0 million (2004: CHF 135.8 million) due to the unpredictability of future profits streams. The amount of unused tax losses carry forward which has not been capitalized as deferred tax assets, with their expiry dates, is as follows:

in millions of CHF	2005	2004
One year	0.9	0.7
Two years	1.8	0.9
Three years	1.6	1.8
Four years	45.0	12.3
Five years	30.5	53.3
More than five years	55.2	66.8
Total	135.0	135.8

Tax losses are capitalized if it is probable that future taxable profits will arise to utilize the losses.

16. Financial assets and other non current assets

in CHF'000	31.12.2005	31.12.2004
Financial assets at fair value through profit or loss	10 044	6 748
Loans	11 590	11 238
Others	2 340	1 605
	23 974	19 591

Financial assets at fair value through profit or loss consist in investments for which the fair value is determined using either the market value or a future discounted cash flow method.

The effective interest rate on loans was 6% (2004: 6%). Others mainly consist of guarantee deposits.

Kudelski Group

Notes to the consolidated financial statements

17. Inventories

	31.12.2005	31.12.2004
in CHF'000		
Raw materials	10 074	9 557
Work in progress	7 086	5 121
Finished goods	34 264	61 436
	51 424	76 114

Write-downs of inventories recognized as an expense amount to kCHF 888 (2004: kCHF 439).

Changes in inventories of finished goods and work in progress included in cost of material are kCHF -27 755 (2004: kCHF 25 746).

18. Trade accounts receivable

	31.12.2005	31.12.2004
in CHF'000		
Trade accounts receivable	178 306	173 928
Trade accounts receivable related parties	6 252	5 877
Provision for impairment	-11 950	-11 359
	172 608	168 446

Provisions recognized for the impairment of trade receivables amount to kCHF -2 302 (2004: kCHF -983).

19. Other current assets

	31.12.2005	31.12.2004
in CHF'000		
Loans – short term portion	1 733	3 758
Other receivables	22 664	17 334
Prepaid expenses	13 129	9 852
Accrued income	10 930	7 875
	48 456	38 819

20. Financial assets at fair value through profit or loss

	Notes	31.12.2005	31.12.2004
in CHF'000			
Financial assets held for trading:			
– Marketable securities		9 822	8 776
– Derivative financial instruments	33	–	466
		9 822	9 242

21. Cash and cash equivalents

	31.12.2005	31.12.2004
in CHF'000		
Cash at bank and in hand	68 784	33 838
Short term deposits	365 901	163 880
	434 685	197 718

The effective interest rate on short-term bank deposit was 2.3% (2004: 2.2%); these deposits have an average maturity of 30 days.

22. Share capital

Issued and fully paid share capital

	31.12.2005	31.12.2004
in CHF'000		
47 052 914/46 929 580 bearer shares, at CHF 10 each	470 529	469 296
46 300 000 registered shares at CHF 1 each	46 300	46 300
	516 829	515 596

The Bearer Shares have been listed on the main market of the SWX since 2 August 1999 (ticker: KUD, security number: 1 226 836; ISIN CH0012268360) and traded on virt-x

since 2001. They are included in the SMI (Swiss Market Index) since October 1, 2000. The Registered Shares are not listed nor traded on any stock exchange.

Authorized share capital

	31.12.2005	31.12.2004
in CHF'000		
3 768 164/3 768 164 bearer shares, at CHF 10 each	37 682	37 682
3 200 000 registered shares at CHF 1 each	3 200	3 200
Authorized share capital as of December 31	40 882	40 882

The Board of Directors is authorized to increase the share capital in one or more stages until May 26, 2006 for the purpose of acquiring companies or parts of companies.

Conditional share capital

	31.12.2005	31.12.2004
in CHF'000		
Conditional share capital as of January 1	68 342	68 988
Increase of conditional share capital	47 500	-
Employee share purchase plan	-105	-126
Shares allotted to employees	-1 128	-520
Conditional share capital as of December 31	114 609	68 342

The shareholders of Kudelski SA met in an Extraordinary General Meeting on September 30, 2005 and approved an increase of the conditional share capital of up to a total amount of CHF 100 million, through the issue of 10 million bearer shares of a nominal value of CHF 10, to be issued as and when rights are exercised to convert the bonds of Kudelski SA and its subsidiaries.

Furthermore, the ordinary 2005 General Assembly approved an increase of the conditional share capital for the exercise of options or the subscription of shares by employees up to a maximum amount of CHF 15 841 760 consisting of 1 584 176 bearer shares of a nominal value of CHF 10.

23. Treasury shares

	Number of bearer shares	Book value in CHF'000
As of January 1, 2004, December 31, 2004 and 2005	20 155	380

No transaction occurred during the last two financial years.

24. Long term financial debt

	Notes	31.12.2005	31.12.2004
in CHF'000			
Bank loans		1 172	2 077
Financial lease obligations		1 860	2 867
CHF 350 million 1.625% unsubordinated convertible bond 2005/2012	25	311 426	–
		314 458	4'944

The fixed interest rate paid in 2005 and 2004 for bank loans is 2%.

25. Convertible bond 2005/2012

On October 5, 2005, Kudelski Financial Services Holding SCA issued a CHF 350 million unsubordinated convertible bond due 2012, convertible into bearer shares of Kudelski SA. This bond has a denomination of CHF 5 000 nominal amount with an initial conversion price of CHF 67.76 per bearer shares of Kudelski SA with a nominal value of CHF 10.

Bondholders may request conversion at any time from January 1, 2006 until September 12, 2012. The bond is callable at par value after October 5, 2010, subject to a 110% provisional call hurdle. If not converted prior to the date of maturity, the bonds will be redeemed at par value. Interest expense on the liability component of the bond is calculated on the effective yield basis using an effective rate of 3.2%. The convertible bond is recognized in the consolidated balance sheets as of December 31, as follows:

	31.12.2005	31.12.2004
in CHF'000		
Face value of convertible bond issued on October 5, 2005	350 000	–
Transactions costs	-5 719	–
Equity conversion component	-34 087	–
Liability component on initial recognition on October 5, 2005	310 194	–
Interest expense	2 576	–
Interest paid	–	–
Interest accrued (short term portion)	-1 343	–
Liability component as of December 31, 2005	311 426	–

Transaction costs amounted to kCHF 6 337 of which kCHF 618 were allocated to the equity component of the convertible bond.

The above interest expense includes the following:

	2005	2004
in CHF'000		
Base interest (1.625%)	1 343	–
Allocation of the equity conversion component	1 040	–
Effective interest expense (effective yield rate of 3.2%)	2 383	–
Allocation of transaction costs	193	–
Interest expense	2 576	–

26. Employee benefits liabilities

In addition to the social security plans mandated by the law, the Group sponsors an independent pension plan in Switzerland. All employees in Switzerland are covered by this plan, which is a defined benefit plan according to IAS 19. In certain locations abroad, the Group is subject to termination and jubilee benefits treated as defined benefit plans according to IAS 19.

Plan assets have been estimated at market fair value. Liabilities have been calculated according to the "Projected Unit Credit" method.

The following table sets forth the status of the pension plans and the amount that is recognized in the balance sheet at December 31, 2005 and December 31, 2004:

	31.12.2005	31.12.2004
in CHF'000		
Fair value of plan assets	55 886	45 667
Defined benefit obligation	-81 006	-66 937
Funded status	-25 120	-21 270
Unrecognized gains/(losses)	-11 040	-9 104
Recognized employee benefits liability	-14 080	-12 166

The actual return on plan assets amounts to kCHF 4 203 for the year 2005.

According to IAS 19, the following amount is recorded as net pension cost in the income statement of the financial years 2005 and 2004:

	2005	2004
in CHF'000		
Service cost	-8 677	-5 499
Interest cost	-2 134	-1 771
Expected return on plan assets	2 283	1 922
Employees contributions	2 897	1 785
Amortization of losses	101	224
Net pension cost	-5 530	-3 339
Exchange rate difference	-	20
Employer contributions	3 616	2 105

Kudelski Group

Notes to the consolidated financial statements

Movement during the year in the employee benefit liabilities recognized in the balance sheet for post-employment defined benefit plans were as follows:

	2005	2004
in CHF'000		
As of January 1	12 166	10 932
Net pension cost	5 530	3 339
Contribution paid	-3 616	-2 105
As of December 31	14 080	12 166

The main assumptions used for the calculation of the pension cost and the defined benefit obligation for the years 2005 and 2004 are as follows:

	31.12.2005	31.12.2004
Switzerland		
Discount rate	2.75%	3.10%
Rate of future increase in compensations	2.00%	2.00%
Rate of future increase in current pensions	1.00%	1.00%
Expected long-term rate of return on plan assets	5.00%	5.00%
Abroad		
Discount rate	4.51%	4.48%
Rate of future increase in compensations	3.32%	3.24%

27. Provisions for other liabilities and charges

in CHF'000	Legal fee and lawsuit	Risk on contract and warranty	Other	Total 2005	Total 2004
As of January 1	11 215	6 689	3 090	20 994	27 978
Additional provisions	412	–	–	412	4 643
Unused amounts reversed	–	–	–	–	-1 194
Used during the year	-6 555	-4 826	-3 090	-14 471	-10 125
Exchange differences	–	–	–	–	-308
As of December 31	5 072	1 863	–	6 935	20 994
Thereof:					
– Short-term	207	1 863	–	2 070	16 334
– Long-term	4 865	–	–	4 865	4 660
	5 072	1 863	–	6 935	20 994

Legal fee and lawsuit

A number of Group companies are the subject of litigation arising out of the normal conduct of their business, as a result of which claims could be made against them.

Such claims, in whole or in part, might not be covered by insurance. The provisions for legal fee and lawsuit are valued according to the best management estimate principle.

28. Other long-term liabilities

in CHF'000	31.12.2005	31.12.2004
Contingent consideration (earn-out) – long-term portion	3 168	5 990
Loans granted by third parties	866	1 690
Loans granted by related parties	253	253
	4 287	7 933

The loans granted by third parties have a nil interest rate.

29. Short term financial debt

in CHF'000	Notes	31.12.2005	31.12.2004
Short term bank borrowings		16 103	22 077
Short term financial lease obligations		1 088	1 146
Other short term financial liabilities		1 343	1 863
USD 325 million 2.25% unsubordinated convertible bond 2002/2009	30	–	188 892
		18 534	213 978

The average effective interest rate paid in 2005 for short term bank borrowings is 2.49% (2004: 2.83%).

The effective lease interest rate for 2005 and 2004 was between 2.8% and 3.7% depending of the lease term.

30. Convertible bond 2002/2009

On January 31, 2002, Kudelski Financial Services Holding SCA issued a convertible bond with an aggregate principal amount of USD 325 million. This convertible bond was issued in denominations of USD 1 000 at par value, with interest at 2.25% payable semi-annually and final redemption in January 2009 at 105.79, representing a yield to maturity of 3%. The conversion price was set at CHF 100. The issuer could redeem all of the bonds at any time after January 31, 2005 and before January 31, 2007.

On September 6, 2005 the issuer and Kudelski SA announced that they would tender for cash the remaining USD 157 928 000 convertible bond. As a result, holders of a total of USD 149 297 000 have tendered at a price of USD 1 020 per USD 1 000 principal amount. On November 9, 2005, the issuer called for the redemption of the remaining portion of the convertible bond with a redemption date of December 12, 2005 at a price of USD 1 030.41 per USD 1 000 principal amount. As of December 12, 2005 the bond was delisted and fully repaid.

The convertible bond is recognized in the consolidated balance sheets as of December 31, as follows:

	2005 USD'000	2005 CHF'000	2004 CHF'000
Face value of convertible bond as of January 1	172 928	197 138	214 431
Carrying value as of January 1, of			
– Conversion option	-9 754	-11 119	-17 295
– Reconstitution of the redemption value	4 046	4 611	3 296
– Transaction costs	-1 524	-1 738	-2 796
Liability component as of January 1	165 696	188 892	197 636
Interest expense	7 688	9 708	11 745
Interest paid	-2 996	-3 784	-4 825
Transaction cost allocated	586	740	906
Cash reimbursement	-176 061	-225 170	–
Gain on repurchase	-2 023	-2 573	–
Impairment of conversion option and transaction costs	7 110	9 085	–
Exchange rate (gain)/loss	–	23 102	-16 570
Liability component as of December 31	–	–	188 892

Transaction and issuing costs of kUSD 7 832 have been deducted from the carrying value of the liability and equity components upon initial recognition.

The above figures assumed an early redemption on January 31, 2007; therefore the initial transaction and issuing costs were allocated over the period up to this date on a straight line basis.

The above interest expense includes the following:

	2005 USD'000	2005 CHF'000	2004 CHF'000
Interest expense	2 996	3 784	4 825
Reconstitution of the redemption value	1 111	1 402	1 720
Amortization of the conversion option	3 581	4 522	5 200
	7 688	9 708	11 745

Interest expense on the bond is calculated using the effective interest method by applying the effective interest rate of 5.895% to the liability component.

As the convertible bond entitles the issuer to deliver cash upon exercise of the conversion option (cash settlement alternative), the conversion option is treated as a derivative financial instrument (note 33).

31. Trade accounts payable

	31.12.2005	31.12.2004
in CHF'000		
Trade accounts payables – third parties	75 652	63 638
Trade accounts payables – related parties	7 448	10 400
	83 100	74 038

32. Other Current liabilities

	31.12.2005	31.12.2004
in CHF'000		
Accrued expenses	46 467	32 374
Deferred income	7 686	5 284
Payable to pension fund	995	569
Other payables	11 768	14 396
	66 916	52 623

33. Derivative financial instruments

	31.12.2005	31.12.2005	31.12.2004	31.12.2004
	Assets	Liabilities	Assets	Liabilities
in CHF'000				
Convertible bond – conversion option	–	–	–	2 064
Zero cost options on currencies	–	1 760	466	–
Total current portion	–	1 760	466	2 064
Total	–	1 760	466	2 064

Convertible bond – conversion option

The conversion option related to the 2002 convertible bond is treated as a derivative financial instrument (see note 30). The initial measurement has been deducted from the liability component of the convertible bond. Subsequent measurement is the fair value of the financial instrument and differences resulting thereto are recognized in other finance income/(expense), net. Fair value is determined using the Black & Scholes option model.

Zero cost options on currencies

Short-term derivatives on currencies are entered into to cover exposure in foreign currencies. They did nevertheless not meet the criteria for hedge accounting. The notional amounts of the outstanding zero cost options on currencies as of December 31, 2005 are kCHF 37 250 and kCHF 59 650 as of December 31, 2004.

34. Cash flows arising from divestments of subsidiaries

The following is a summary of the cash flow impact of the divestments of subsidiaries:

	2005 Disposal	2004 Disposal
in CHF'000		
Financial fixed assets	–	1
Intangible fixed assets	288	–
Tangible fixed assets	50	745
Net working capital	-37	-3 773
Long term debt	–	-772
Cash and cash equivalent	25	160
Fair value of net asset disposed of	326	-3 639
Minority interest disposed of	-161	–
Gain on disposal of subsidiaries	35	4 514
Contingent consideration adjustment ("earn-out")	–	2 225
Total sale proceeds	200	3 100
Disposal consideration not paid as of December 31	–	-3 100
Consideration received from prior year disposed of subsidiaries	3 100	–
Cash and cash equivalent disposed of	-25	-160
Net Cash inflow/(outflow) on disposals	3 275	-160

35. Principal Shareholders

	Voting rights 31.12.2005	Voting rights 31.12.2004	Shareholdings 31.12.2005	Shareholdings 31.12.2004
Kudelski Family Pool	57%	64%	22%	34%

According to information available to the Board of Directors at December 31, 2005, there were no other individual shareholders with more than 5% of the voting rights.

36. Research and development

The following amounts were recognized as expenses and charged to the income statement:

	2005	2004
in CHF'000		
Research and development	165 563	141 481

37. Dividend

The dividend paid in 2005 was kCHF 10 321 which correspond to a dividend of CHF 0.20 per bearer share and CHF 0.02 per registered share. No dividend was paid during 2004.

For the current year, the Board of Directors propose a dividend of CHF 0.30 per bearer share and CHF 0.03 per registered share. This dividend is subject to the approval of shareholders at the Annual General Meeting and has not been included as a liability in these financial statements. The total estimated dividend to be paid is kCHF 15 499 and may fluctuate upon exercise of option and conversion rights.

38. Employee share participation plan

Employee stock option plan

In April 2003 the Kudelski Group set up a stock option plan for the members of the Board of Directors, the management and certain expert employees. The Board of Directors and

executive management determined the modalities and the conditions governing the grant of options. The following options were granted:

Year of grant	Number of options	Vesting	Maturity	Ratio	Exercise price
2003	125 000	01.04.2006	01.04.2007	1 : 1	20
2003	125 000	01.04.2007	01.04.2008	1 : 1	20
2003	125 000	01.04.2008	01.04.2009	1 : 1	20
2005	1 000	01.04.2007	01.04.2008	1 : 1	20
2005	1 000	01.04.2008	01.04.2009	1 : 1	20

The following table summarizes the change in options held:

	Options 2005	Strike price 2005	Options 2004	Strike price 2004
in CHF'000				
In circulation on January 1	358 303	20	375 000	20
of which exercisable	-	-	-	-
New rights issued	2 000	20	-	-
Rights exercised	-	-	-	-
Rights forfeited	-3 163	20	-16 697	20
In circulation on December 31	357 140	20	358 303	20
of which exercisable	-	-	-	-

The expense charged against the income statement for the financial year 2005 amounts to kCHF 659 (2004: kCHF 659).

The expense assumes a departure rate based on the fact that some beneficiaries will not be able to exercise.

Employee share plan (ESP)

As of financial year 2004, the Group set up a plan to allow employees of certain Group companies to buy shares, giving them preferential conditions to buy Kudelski SA bearer

shares. All such shares purchased and the additional shares and options obtained through this plan are subject to a three-year blocking period.

	Shares 2005	Options 2005	Shares 2004	Options 2004
Shares underwritten by employees	9 135	-	10 804	-
Bonus shares and options from ESP	1 407	420	1 840	321
Total employee share plan	10 542	420	12 644	321

	2005	2005	2004	2004
in CHF'000				
Amount paid by employee	264	-	289	-
Booked corporate charges (excluding social charges)	89	7	90	8
	353	7	379	8

Shares issued for employees

In 2005, 112 792 bearer shares of Kudelski SA (2004: 52 000) were delivered to employees for no consideration, of which 85 000 include a five year blocking period

(2004: 52 000). The total expense recognized in the income statement amounts to kCHF 3 193 (2004: kCHF 1 442).

Kudelski Group

Notes to the consolidated financial statements

39. Related parties

(a) Trading transactions

Transaction between the Group and its subsidiaries, which are related parties of the Group have been eliminated on consolidation and are not disclosed in this note.

During the year, Group entities entered into the following significant trading transactions with related parties that are not member of the Group, associates or joint ventures:

	Sale of goods and services 2005	Sale of goods and services 2004	Purchase of goods and services 2005	Purchase of goods and services 2004	Amounts owed to related parties 31.12.05	Amounts owed to related parties 31.12.04	Amounts owed by related parties 31.12.05	Amounts owed by related parties 31.12.04
In CHF'000								
Easyplex software GmbH				1 278	–	347	–	–
Total not member of the Group	–	–	–	1 278	–	347	–	–
Digital-Elektronik GmbH	316	463	31 012	31 705	7 204	7 189	71	48
APT-SkiData Ltd	8 562	7 240	–	–	–	–	3 599	2 348
SkiData Parking System	5 712	5 792	–	–	–	–	2 576	2 606
Total associated companies	14 590	13 495	31 012	31 705	7 204	7 189	6 246	5 002
Mediacrypt SA	35	–	817	1 092	277	498	5	4
Total joint ventures	35	–	817	1 092	277	498	5	4

Easyplex provides engineering services for SkiData. Since 2005 it is no longer a related party. Digital Elektronik is the main supplier of access control material for SkiData. APT SkiData and SkiData Parking Ltd are sales representatives companies for SkiData Group.

(b) Key management compensation

	2005	2004
in CHF'000		
Salaries and other short-term employee benefits	7 951	6 972
Termination benefits	–	152
Share-based payments	3 485	2 688
	11 436	9 812

Management compensation includes share and cash-based payments granted for the year but not yet executed at the closing date.

40. Commitments and contingencies

Operating lease commitments

The future aggregate minimum lease payments under operating leases are as follows:

	2005	2004
in CHF'000		
Within one year	1 163	1 877
In the second to fifth year inclusive	1 288	2 263
	2 451	4 140

41. Financial risk management

(a) Market risk

The Group is exposed to market risk, primarily related to foreign exchange, interest rates and the market value of investments assets and equity securities. Management actively monitors these exposures. The objective is to minimize, where deemed to be appropriate, fluctuations in earning flows associated with changes in foreign exchange, interest rates and the market value of investments in financial assets and securities. To manage the volatility relating to these exposures and to enhance the yield on investments in financial assets, the Group uses derivative financial instruments. The Group does not use financial derivatives for trading or speculative reasons, or for purposes unrelated to normal business activities. Any loss in value on a financial derivative would normally be offset by an increase in the value of the underlying transaction.

The Group does not enter into any financial transactions containing a risk that cannot be quantified at the time the transaction is concluded; i.e. it does not sell assets short. The Group only sells existing assets or hedges transactions and future transactions (in the case of anticipatory hedges) it knows it will have in the future based on past experience. In the case of liquid funds, it writes options on assets it has, or on positions it wants to acquire, and for which it has the required liquidity. The Group therefore expects that any loss in value for these instruments would be generally offset by increases in the value of the hedged transactions.

(b) Foreign exchange risk

The Group conducts business in a variety of countries using a variety of foreign currencies. However, the Group prepares its consolidated financial statements in CHF. It is therefore exposed to foreign exchange risk arising from various currency exposures, primarily with respect to the US Dollar (USD) and the Euro (EUR). Foreign exchange risk arises from future commercial transactions, recognized assets and liabilities and net investments in foreign operations. In order to manage the foreign exchange risk arising from future commercial transactions and certain assets and liabilities, the Group uses forward contracts and foreign currency zero cost option contracts to hedge certain anticipated foreign currency revenues.

Until November 2005, The Group had a USD denominated convertible bond liability. This foreign currency liability was not fully offset by a corresponding USD asset amount as it was used as a natural hedge for long-term USD cash flows.

Net investments in Kudelski affiliates with a functional currency other than the Swiss Franc are of long-term nature: the Group does not hedge such foreign currency translation exposures.

(c) Interest rates

The Group manages its exposure to interest rate risk through a mix of fixed rate debt and variable rate debt in its total debt portfolio. To manage this mix, the Group may enter into interest rate swap agreements, in which it exchanges periodic payments based on a notional amount with agreed upon fixed and variable interest rates.

However, at the end of 2005, the Group had no such swap agreement.

(d) Counterparty risk

Counterparty risk includes issuer risk on debt securities, settlement risk on derivative and money market transactions, and credit risk on cash and fixed term deposits. Issuer risk is limited by buying debt securities, which are at least A rated.

Settlement and credit risk is reduced by entering into transactions with counterparties that are usually at least A rated banks or financial institutions. Exposure to these risks and compliance with the risk parameters approved by the Board of Directors is closely monitored. The Group does not expect any losses due to non-performance by these counterparties. The diverse portfolio of investments limits the exposure to any single counterparty or sector.

(e) Equity prices

The Group is not exposed to equity price risks.

(f) Commodities

The Group has very limited exposures to price risk related to anticipated purchases of certain commodities used as raw materials in its business. A change in commodity prices may alter the gross margin, but due to the limited exposure to any single raw material, a price change is unlikely to have a material unforeseen impact on the Group's earnings.

42. Transition to IFRS

(A) Basis of transition to IFRS

The Group's financial statements for the year ended December 31, 2005 are the first annual financial statements that comply with IFRS. In preparing these financial statements in accordance with IFRS, the Group has applied the mandatory exceptions and certain of the exemptions from full retrospective application of IFRS.

(B) Exemptions from full retrospective application elected by the Group

(a) Business combination exemptions

The Group has applied the business combination exemptions in IFRS 1. It has not restated business combinations that took place prior to January 1, 2004. The Group did not recognize goodwill in its IFRS balance sheet since in Swiss GAAP FER it was recognized as a deduction from equity. Adjustments resulting from the subsequent resolution of a contingency affecting the purchase consideration are recognized in retained earnings.

(b) Fair value as deemed cost

The Group has elected to measure an item of property at fair value as at January 1, 2004. The application of this exemption is detailed in note (a) to the reconciliation of equity and income statement.

(c) Employee benefits exemption

The Group has elected to recognize all cumulative actuarial gains and losses as at January 1, 2004. The application of this exemption is detailed in note (f) to the reconciliation of equity and income statement.

(d) Cumulative translation difference exemption

The Group has elected to set the previously accumulated translation differences to zero as at January 1, 2004.

(e) Designation of previously recognized financial instruments

The Group has designated certain existing financial assets as financial assets at fair value through profit or loss on January 1, 2004.

(C) Reconciliation of equity and income statement

The tables below detail the impact of the conversion of the financial statements from Swiss GAAP FER to IFRS. They reconcile the equity at January 1, 2004, at December 31, 2004 and the income statement for 2004.

Swiss GAAP FER balance sheet figures have been reclassified to be comparable with the IFRS balance sheet. Deferred income tax assets have been reclassified from current to non-current assets according to IAS 12 resulting in an increase of kCHF 11 586 for January 1, 2004 and of kCHF 13 193 for December 31, 2004 in non-current assets and a similar reduction in current assets compared to the financial statements approved by the 2004 general assembly. Furthermore the 2002 convertible bond has been reclassified from non-current liabilities to current liabilities resulting in an increase of kCHF 214 637 for January 1, 2004 and of kCHF 199 746 for December 31, 2004 in current liabilities and a similar decrease in non-current liabilities. This reclassification was necessary since the Group does not have an unconditional right to defer settlement of the liability from the cash settlement alternative.

Under Swiss GAAP FER, joint venture entities were fully integrated within the scope of consolidation. As not all control requirements for full consolidation were fulfilled under IFRS, the companies Mediacypt AG, Nagra-Futuris SA and Nagra Thomson Licensing SA are now consolidated using the proportionate consolidation. Using the proportionate consolidation for these companies impacts several balance sheet and income statement items. For clarity reasons, the impact of proportionate consolidation is disclosed as a separate column named "joint venture impact" in the reconciliations below.

Reconciliation of equity at January 1, 2004

	Notes	Swiss GAAP FER	Effect of transition to IFRS Joint venture impact	Effect of transition to IFRS Other changes	IFRS
in CHF'000					
Tangible fixed assets	a	104 848	-4	-1 443	103 401
Intangible assets	b	34 915	-	-20 005	14 910
Investments in associates		5 119	-	-	5 119
Deferred income taxes	g	11 586	-	5 818	17 404
Financial assets and other non-current assets		27 668	-200	-	27 468
Total non-current assets		184 136	-204	-15 630	168 302
Inventories		49 940	-	-	49 940
Trade accounts receivable	c	157 328	9	-2 680	154 657
Other current assets		37 517	-10	-	37 507
Financial assets at fair value through profit or loss	c	906	-	2 036	2 942
Cash and cash equivalents		236 201	-320	-	235 881
Total current assets		481 892	-321	-644	480 927
Total assets		666 028	-525	-16 274	649 229
Share capital		514 949	-	-	514 949
Reserves	i	-323 910	-	-25 697	-349 607
Treasury shares		-380	-	-	-380
Equity attributable to equity holders of the parent	i	190 659	-	-25 697	164 962
Minority interest	h	15 194	-746	2 332	16 780
Total equity	i	205 853	-746	-23 365	181 742
Long-term financial debt		7 035	-	-	7 035
Deferred income tax liabilities		1 569	-	-	1 569
Employee benefits liabilities	f	1 872	-	9 078	10 950
Provisions for other liabilities and charges		18 901	-	-	18 901
Other long-term liabilities		15 122	128	-	15 250
Total non-current liabilities		44 499	128	9 078	53 705
Short-term financial debt	d	261 941	-	-17 001	244 940
Trade accounts payable		68 448	158	-	68 606
Other current liabilities	f	62 139	-69	-1 337	60 733
Current income taxes		3 249	3	-	3 252
Advances received from clients		10 436	1	-	10 437
Provision for other liabilities and charges		9 463	-	-	9 463
Derivative financial instruments	e	-	-	16 351	16 351
Total current liabilities		415 676	93	-1 987	413 782
Total liabilities		460 175	221	7 091	467 487
Total equity and liabilities		666 028	-525	-16 274	649 229

Reconciliation of equity at December 31, 2004

	Notes	Swiss GAAP FER	Effect of transition to IFRS Joint venture impact	Effect of transition to IFRS Other changes	IFRS
in CHF'000					
Tangible fixed assets	a	129 122	-8	-1 443	127 671
Intangible assets	b	41 105	-	-25 239	15 866
Investments in associates		5 399	-	-	5 399
Deferred income taxes	g	13 193	-	7 833	21 026
Financial assets and other non-current assets		19 586	5	-	19 591
Total non-current assets		208 405	-3	-18 849	189 553
Inventories		76 115	-1	-	76 114
Trade accounts receivable	c	170 044	-949	-649	168 446
Other current assets		39 135	-316	-	38 819
Financial assets at fair value through profit or loss	c	8 776	-	466	9 242
Cash and cash equivalents		198 897	-1 179	-	197 718
Total current assets		492 967	-2 445	-183	490 339
Total assets		701 372	-2 448	-19 032	679 892
Share capital		515 596	-	-	515 596
Reserves	i	-234 153	-	-23 749	-257 902
Treasury shares		-380	-	-	-380
Equity attributable to equity holders of the parent	i	281 063	-	-23 749	257 314
Minority interest	h	21 721	-4 319	5 143	22 545
Total equity	i	302 784	-4 319	-18 606	279 859
Long-term financial debt		4 944	-	-	4 944
Deferred income tax liabilities		1 792	-	-	1 792
Employee benefits liabilities	f	3 075	-	9 095	12 170
Provisions for other liabilities and charges		4 660	-	-	4 660
Other long-term liabilities		7 680	253	-	7 933
Total non-current liabilities		22 151	253	9 095	31 499
Short-term financial debt	d	224 936	-104	-10 854	213 978
Trade accounts payable		71 566	2 472	-	74 038
Other current liabilities	f	53 942	-588	-731	52 623
Current income taxes		4 395	-26	-	4 369
Advances received from clients		5 130	-2	-	5 128
Provision for other liabilities and charges		16 468	-134	-	16 334
Derivative financial instruments	e	-	-	2 064	2 064
Total current liabilities		376 437	1 618	-9 521	368 534
Total liabilities		398 588	1 871	-426	400 033
Total equity and liabilities		701 372	-2 448	-19 032	679 892

Reconciliation of Income Statement for 2004

	Notes	Swiss GAAP FER	Effect of transition to IFRS Joint venture impact	Effect of transition to IFRS Other changes	IFRS
in CHF'000					
Revenues	j	601 287	-41	-3 693	597 553
Other operating income	k	17 759	–	-9 181	8 578
Cost of material		-192 720	-1 077	–	-193 797
Employee benefits expense	l	-178 661	249	-1 765	-180 177
Other operating expenses		-106 528	321	–	-106 207
Operating income before interest, taxes, depreciation, amortization and impairment		141 137	-548	-14 639	125 950
Depreciation, amortization and impairment	b	-39 638	3	5 906	-33 729
Operating income (EBIT)		101 499	-545	-8 733	92 221
Interest expense	m	-8 820		-5 194	-14 015
Other finance income/(expense), net	n	-1 516	35	21 433	19 952
Share of results of associates		1 315	–	–	1 315
Income before tax		92 477	-510	7 506	99 473
Income tax expense	g	-8 017	24	2 020	-5 973
Net income for the year	i	84 460	-486	9 526	93 500
Attributable to:					
– Equity holders of the company	i	77 195	–	6 590	83 785
– Minority interest	h	7 265	-486	2 936	9 715
		84 460	-486	9 526	93 500

Notes to the reconciliation of equity at January 1, 2004,
December 31, 2004, and Income Statement for the year 2004

a) Tangible fixed assets

The change in connection with tangible fixed assets is due to a building measured at its fair value and used as deemed cost.

	01.01.2004	31.12.2004
in CHF'000		
Initial fair value adjustment through reserves	-1 443	-1 443

b) Intangible assets and depreciation, amortization and impairment

Intangible assets under Swiss GAAP FER included kCHF 20 005 for capitalized developments of new products that are transferred to retained earnings since they do not qualify for recognition as intangible asset under IFRS.

	01.01.2004	31.12.2004
in CHF'000		
Initial net balance not recognized	-20 005	-25 239
Of which adjusted through:		
Retained earnings	-20 005	-20 005
Currency translation adjustment	-	-18
Net income:		
- 2004 capitalized development under Swiss GAAP FER (note k)	-	-13 618
- 2004 depreciation recognized under Swiss GAAP FER	-	5 906
- Carrying value of capitalized developments of a disposed of company (note k)	-	2 496
	-20 005	-25 239

The Group has disposed of affiliates in 2004, which had capitalized development in its Swiss GAAP FER balance sheet. As developments were not recognized in the opening balance sheet, the carrying value of these developments has been reclassified in the income statement as a gain on sale of subsidiary.

c) Trade accounts receivable and Financial assets at fair value through profit or loss

Under Swiss GAAP FER, hedge accounting was applied to derivative instruments hedging accounts receivable. These derivatives do not qualify for hedge accounting under IFRS since they are not effective during the whole life of the coverage. They are classified as financial asset at fair value through profit and loss and valued at fair value under IFRS.

	01.01.2004	31.12.2004
in CHF'000		
Hedge value disclosed under trade accounts receivable under Swiss GAAP FER	-2 680	-649
Fair value of the derivative financial instruments	2 036	466
	-644	-183
Of which adjusted through:		
Retained earnings	-644	-644
Net income: "revenues" (note j)	-	461
	-644	-183

d) Short term financial debt

Under Swiss GAAP FER, the 2002/2009 convertible bond was treated as a debt instrument. Under IFRS, it is treated as a compound financial instrument in compliance with IAS 39.

	01.01.2004	31.12.2004
in CHF'000		
Value adjustment of the liability component of the 2002/2009 convertible bond	-17 001	-10 854
Of which adjusted through:		
Retained earnings	-17 001	-17 001
Interest expense – allocation of the equity conversion component and transaction costs (note m)	-	5 194
Other finance income/(expense), net – exchange difference (note n)	-	953
	-17 001	-10 854

The difference includes the equity portion of the convertible bond at January 1 respectively December 31, 2004 under IFRS as well as the corresponding allocation of the issuance costs.

e) Derivative financial instruments

The 2002/2009 convertible bond has a cash alternative settlement option. IAS 32 prescribes that the conversion option be classified as a fair value instrument through profit or loss and disclosed as a liability.

	01.01.2004	31.12.2004
in CHF'000		
Fair value of the conversion option	16 351	2 064
Of which adjusted through:		
Retained earnings	16 351	16 351
Other finance income/(expense), net – fair value adjustment (note n)	-	-14 105
Other finance income/(expense), net – exchange difference (note n)	-	-182
	16 351	2 064

Kudelski Group

Notes to the consolidated financial statements

f) Employee benefits liabilities and other current liabilities

Under IFRS, employee benefits liabilities are adjusted as follows:

	01.01.2004	31.12.2004
in CHF'000		
Employee benefits according to IAS 19	10 950	12 170
less:		
Liability according to Swiss GAAP FER 16 included in:		
– employee benefits obligations	-1 872	-3 075
– other current liabilities	-1 337	-731
	7 741	8 364
Of which adjusted through:		
Retained earnings	7 741	7 741
Reversal of modification of purchase accounting under Swiss GAAP FER	–	-476
Currency translation impact	–	-6
Employee benefits expenses – additional IAS 19 expense (note I)	–	1 105
	7 741	8 364

g) Deferred income taxes and income tax expense

The above changes increase the deferred tax asset as follows:

	01.01.2004	31.12.2004
in CHF'000		
Intangible assets	3 647	5 624
Derivative financial instruments	120	20
Employee benefits IAS 19	2 051	2 194
Currency Translation	–	-5
	5 818	7 833
Of which adjusted through:		
Retained earnings	5 818	5 818
Currency translation	–	-5
Income tax expense	–	2 020
	5 818	7 833

h) Minority interest

Under Swiss GAAP FER, the Group applied the entity concept method to determine the minority interest. Under this method, the Group recognized minority interest on the elimination of an internal profit in joint venture companies. A difference of kCHF 2 332 results from the cancellation of internal profit on inventory in IFRS. Minority interests reconciles as follows:

	01.01.2004	31.12.2004
in CHF'000		
Initial net balance not recognized	-2 332	-2 332
Impact 2004	–	-2 936
Currency translation	–	125
	-2 332	-5 143

i) Equity

Adjustments to retained earnings/equity as of January 1, and December 31, 2004 are as follows:

	Equity adjustments 01.01.04	Income statement impact 2004	Retained earnings impact 2004	Currency translation impact 2004	Total equity adjust. 31.12.04
in CHF'000					
Tangible fixed assets (note a)	-1 443	-	-	-	-1 443
Intangible assets (note b)	-20 005	-5 216	-	-18	-25 239
Derivative financial instruments (note c)	-644	461	-	-	-183
Convertible bond (note d)	17 001	-6 147	-	-	10 854
Conversion option (note e)	-16 351	14 287	-	-	-2 064
Employee benefits – IAS 19 (note f)	-7 741	-1 105	476	6	-8 364
Deferred tax asset (note g)	5 818	2 020	-	-5	7 833
Stock option plan expense (note l)	-	-659	659	-	-
Impact of Goodwill not recycled (note n)	-	3 466	-3 466	-	-
Impact of change in functional currency (note n)	-	2 419	-	-2 419	-
Adjustments to equity attributable to equity holders of the parent	-23 365	9 526	-2 331	-2 436	-18 606
Minority interest (note h)	-2 332	-2 936	-	125	-5 143
Adjustments to total equity	-25 697	6 590	-2 331	-2 311	-23 749

j) Revenues

Under IFRS, revenues are adjusted as follows:

	2004
in CHF'000	
Change in fair value of derivative financial instruments (note c)	461
Reclassification to other finance income/(expense), net (note n)	-4 154
	-3 693

As derivative financial instruments did not qualify for hedge accounting under IFRS, they are reclassified in other finance income/(expense), net. Furthermore, derivative financial instruments are valued at their fair value and the difference impacting the profit and loss account is shown in note c.

k) Other operating income

Under IFRS, other operating income is adjusted reflecting a different accounting of the developments of new products:

	2004
in CHF'000	
Change in connection with intangible assets (note b)	-13 618
Carrying value of development of a sold company under Swiss GAAP FER (note b)	2 496
Reclassification of the remaining profit on the sale of subsidiaries (note n)	1 941
	-9 181

Kudelski Group

Notes to the consolidated financial statements

l) Employee benefits expense

Under IFRS, employee benefits are adjusted as follows:

	2004
in CHF'000	
IAS 19 impact (note f)	-1 105
Stock option plan expense	-659
	-1 765

Stock option expenses were fully recognized at grant date in 2003 under Swiss GAAP FER. However, under IFRS stock option expenses are recognized pro rata over the vesting period. Hence, the charge of kCHF 659 corresponds to this pro rata allocation of expenses.

m) Interest expense

Under IFRS, interest expense is adjusted as follows:

	2004
in CHF'000	
Impact of the convertible bond treated as a compound financial instrument (note d)	-5 194

n) Other finance income/(expense), net

Under IFRS, other finance income/(expense), net is adjusted as follows:

	2004
in CHF'000	
Reclassification of derivative financial instrument (note j)	4 154
Fair value change of conversion option (note e)	14 105
Goodwill on sale proceeds not recycled through income statement	3 466
Reclassification of the remaining profit on the sale of subsidiaries under other operating income (note k)	-1 941
Impact of change in functional currency – Exchange difference (note e)	182
Impact of change in functional currency – Exchange difference (note d)	-953
Impact of change in functional currency – Currency translation impact	2 419
	21 433

Functional currencies of two companies were changed to meet IAS 21 requirements. Thus, translation differences impact the income statement in IFRS as opposed to the currency translation adjustment reserve as in Swiss GAAP FER. In Swiss GAAP FER, goodwill of a company disposed of was recycled in the income statement. Using the business combination exemption of IFRS 1, it is no longer deducted from the income statement.

Reconciliation of material adjustments to the cash flow statement for 2004

kCHF 4824 of interest paid on the 2002 convertible bond have been reclassified from financing to operating activities. Developments costs of kCHF 13618 have been reclassified from investing to operating activities (note b).

There are no other material differences between the cash flow statement presented under IFRS and the cash flow statement presented under Swiss GAAP FER.

43. Additional information

31.12.2005 31.12.2004

in CHF'000

Guarantee in favor of third parties	13 209	12 990
Current assets pledged to secure own commitments	964	1 353

44. Principal currency translation rate

		Year end rates used for the consolidated balance sheets 2005	Year end rates used for the consolidated balance sheets 2004	Average rates used for the consolidated income and cash flow statements 2005	Average rates used for the consolidated income and cash flow statements 2004
1	USD	1.31	1.14	1.25	1.24
1	GBP	2.26	2.19	2.26	2.27
1	EUR	1.55	1.55	1.55	1.54
100	MYR	34.70	30.00	32.90	32.70
100	SEK	16.50	17.10	16.20	16.90
1	SGD	0.79	0.70	0.75	0.75
100	KRW	0.13	0.11	0.12	0.11

45. Events subsequent to the Balance sheet date

These consolidated financial statements have been approved for issue by the Board of Directors on February 23, 2006.

On December 5, 2005 the Group entered into a sale agreement with a consortium of investors to dispose of the Ticketcorner Group. The Group retains a 28% stake of the acquiring vehicle.

The disposal was completed on February 17, 2006, on which date control of Ticketcorner Group passed to the acquirers. The net consideration for the equity sold was CHF 71.1 million consisting of a cash payment of CHF 53.6 million plus a loan of CHF 17.5 million granted to the vehicle company acquiring the Ticketcorner Group. Furthermore, the acquirer has reimbursed the CHF 10 million loan granted by the Group to Ticketcorner and committed to an earn-out payment of up to CHF 15.5 million.

46. Principal operating companies

Company	Place of incorporation	Activity		Share Capital	% held 2005	% held 2004
Digital Television						
Nagravision SA	CH Cheseaux	Solutions for Digital TV and audio products	■	kCHF 12 000	100	100
NagraCard SA	CH Cheseaux	Secure smartcards	■	kCHF 100	100	100
NagraID SA	CH Chaux-de-Fonds	Smartcard production	■	kCHF 4 000	100	100
Nagra France Sàrl	FR Paris	Solutions for Digital TV and audio products	■	kEUR 32 833	100	100
Nagra USA, Inc.	US Nashville	Sales and support	■	kUSD 10	100	100
Nagravision Asia Pte Ltd	SG Singapore	Services	■	kSGD 100	100	100
Quative Ltd	UK London	IPTV solutions	■	kGBP 1	100	–
NagraStar LLC	US Englewood	Smartcards and Digital TV support	■	kUSD –	50	50
Nagra Plus	CH Cheseaux	Analog TV	■	kCHF 2 000	50	50
Nagra Thomson Licensing SA	FR Paris	Intellectual property management	■□	kEUR 240	50	50
Public Access						
Nagra Public Access AG	CH Zug	Holding in Public Access	■	kCHF 15 000	100	100
SkiData AG	AT Gartenau	People and car access systems	■	kEUR 3 634	100	100
Ticketcorner AG	CH Rümlang	Event distribution and ticketing	■	kCHF 2 000	100	100
polyright	CH Sion	Multifunction chipcard system	■	kCHF 5 000	100	100
Corporate						
Kudelski SA	CH Cheseaux	Holding, parent company of the Group	■	kCHF 516 829	100	100
Kudelski Financial Services Holding SCA	LU Luxemburg	Finance, convertible bearing company	■	kCHF 37 050	100	100

■ Full consolidation method applied

■□ Joint-venture accounting applied