Consolidated Annual Financial Statement 2005

Content

Key Figures Overview of the *aap* Group of Companies

SELECTED PROFIT AND LOSS STATEMENT DATA		
	1.1.-12.31.2005	**1.1.-12.31.2004**
Sales	€13,367K	€11,530K
Total Output	€15,634K	€12,571K
Special Factors*	€0	€2,544K
Net Profit/Loss	€655K	€-140K
Operating Income	€860K	€-315K
EBITDA	€2,326K	€1,203K
EBIT	€855K	€-316K
EBT	€1,076K	€-1,260K
DVFA/SG Earnings	€655K	€-561K
DVFA/SG Earnings per Share	€0.04	€-0.07
DVFA/SG Cash Earnings	€2,153K	€833K
DVFA/SG Cash Earnings per Share	€0.14	€0.10
SECTED BALANCE SHEET DATA		
	12.31.2005	**12.31.2004**
Long-term Assets	€14,134K	€10,761K
Short-term Assets	€10,947K	€9,686K
Total Assets	€25,081K	€20,447K
Shareholder's Equity	€19,366K	€15,533K
Non-current Liabilities	€1,308K	€322K
Current Liabilities	€4,407K	€4,592K
Equity Ratio	77%	76%
Employees	139	109

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

Foreword by the Board of Management

Ladies and Gentlemen,

Dear Shareholders,

Dear Employees and Business Partners,

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

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

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

Along with the successful establishment of new development, production and distribution partnerships with Biomet and Heraeus in bone cements and cementing techniques, a sector in which *aap* is one of the world's leading providers, *aap* was able to expand into the innovative biomaterials sector (bone cements, infection care and bone & tissue regeneration) by means of two acquisitions (Osartis, ADC). Both companies are now successfully integrated and will contribute in 2006 toward the growth and success of the *aap* Group.

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

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

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

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

Oliver Bielenstein

Bruke Seyoum Alemu

aap Implantate AG Company and Group Management Report 2005

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

Share and Stock Market

aap Implantate AG Share Price Development

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

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

In September 2005 a further capital increase involved the issue of 1,460,857 shares. From September 12 to 27, 2005 the new shares were offered for sale to existing shareholders at an issue price of €1.60 and a ratio of 21 to 2. In other words, each shareholder was entitled to buy two new shares for every 21 old shares held. There was no rights trading and the new shares were entitled to profits for the full financial year 2005. The new shares were admitted to the Prime Standard segment of the Frankfurt Stock Exchange's regulated market on September 30, 2005. They are listed as Security No. 506 660 (ISIN DE0005066609) and have been traded on the stock market since October 6, 2005.

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

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

Finance

Group sales revenues improved by 16% on the year to €13.367 million (previous year: €11.530 million). Adjusted for the effect of the ADC and Osartis acquisitions, Group sales revenues would have totaled €13.098 million, equivalent to 14% year-on-year growth.

aap's earnings position also improved significantly on the year. EBITDA was up 93% to €2.326 million, taking the EBITDA margin to 17% (previous year: 10%). EBIT too was up on the year to €855K (previous year: €-316K).

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

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

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

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

Structure of the Consolidated Financial Statements

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

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

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

Sales and Results Development at Group Level

In financial year 2005 *aap* sales were up 16% on the year to €13.367 million from €11.530 million. This positive trend was due mainly to organic growth but also to the two acquisitions, Osartis and ADC.

With these acquisitions organic year-on-year growth would have been 14% and sales revenues would have totaled €13.098 million.

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

Sales 2004 vs 2005 at Group Level by Quarters

The increase in **inventories** of finished and unfinished products to €883K from €-172K the previous year is mainly due to new large OEM projects getting under way in both lines of business and a result of laying in stocks and building up endoprosthetics, a line of business in which the customary consignment purchasing is highly capital-intensive.

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

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

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

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

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

The reduction in **other operating expenses** to €4.633 million from €4.937 million was due mainly to the end of special restructuring effects totaling €1.0 million that were included under this heading in 2004. Sales-related rental and logistics expenses increased especially as a result of starting work on new OEM orders, expanding sales, and due to the acquisitions.

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

With the positive sales trend, *aap* was able to increase EBITDA to €2.326 million from €1.203 million, leading to a change in EBITDA margin from 10% in 2004 to 17% in 205. The operating result – EBIT – also increased substantially to €855K from €-316K.

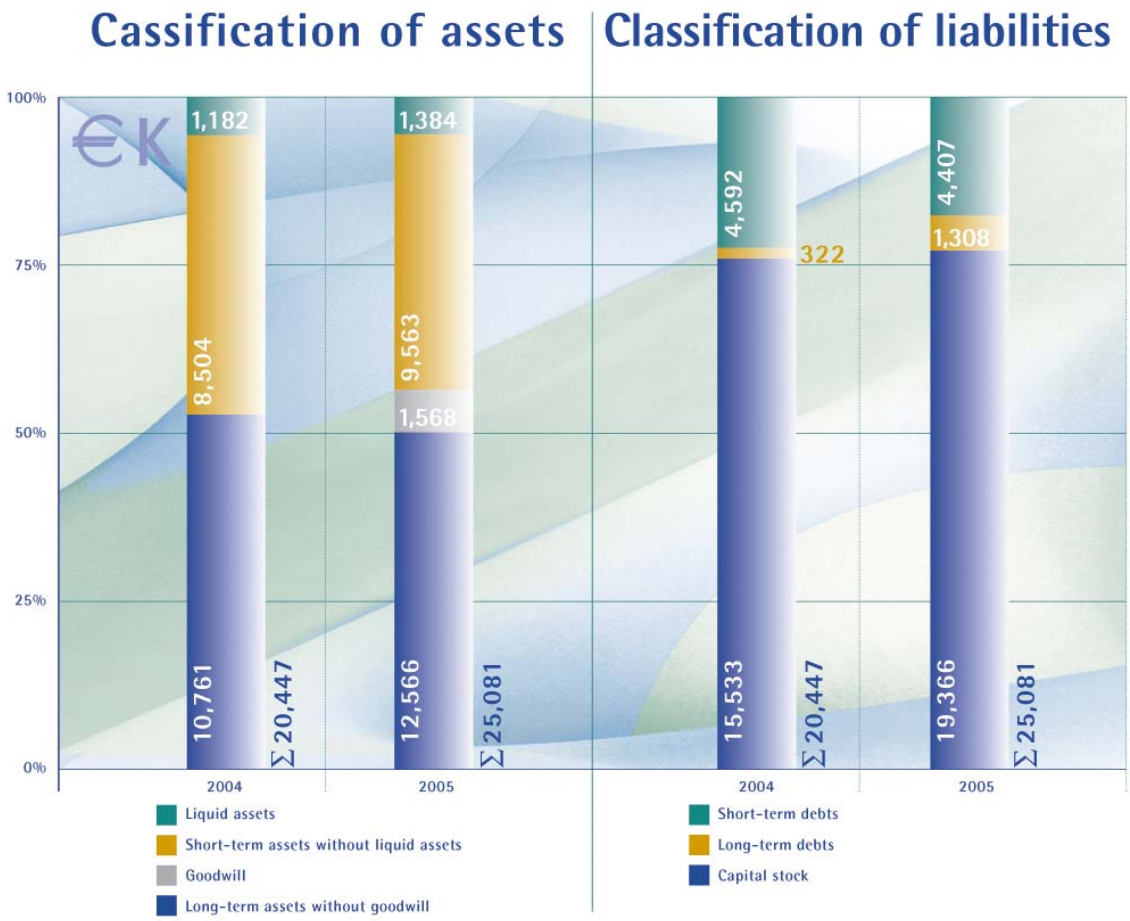
As for earnings from investments in affiliates, the pro rata results until September 30, 2005 of the holdings in OSARTIS GmbH & Co. KG and Neue Magnetodyn GmbH based on the equity method were carried as €239K (previous year: €-110K).

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

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

Balance Sheet Development at Group Level

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



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

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

The increase in long-term assets was a result of boosting capacity for new large orders, of investing in a new processing center for osteosynthesis production, and of additionally capitalized development work taking into account depreciation totaling €1.348 million. Goodwill, stated at €1.568 million, resulted from the takeovers of Osartis and ADC. Both were acquired in view of their earning power.

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

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

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

Liquidity Position

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

Sales and Results Development at aap Implantate AG

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

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

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

Other operating income amounting to €1.181 million included inter-company contributions, investment grants and development subsidies, revaluation of the AEQUOS GmbH holding and of guaranty obligations, and income from the retransfer of reserves.

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

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

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

Balance Sheet Development at aap Implantate AG

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

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

Subsidiaries

aap Biomaterials GmbH & Co. KG

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

Osartis GmbH & Co. KG

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

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

Strategic Participations

ADC Advanced Dental Care GmbH & Co. KG

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

AEQUOS Endoprothetik GmbH

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

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

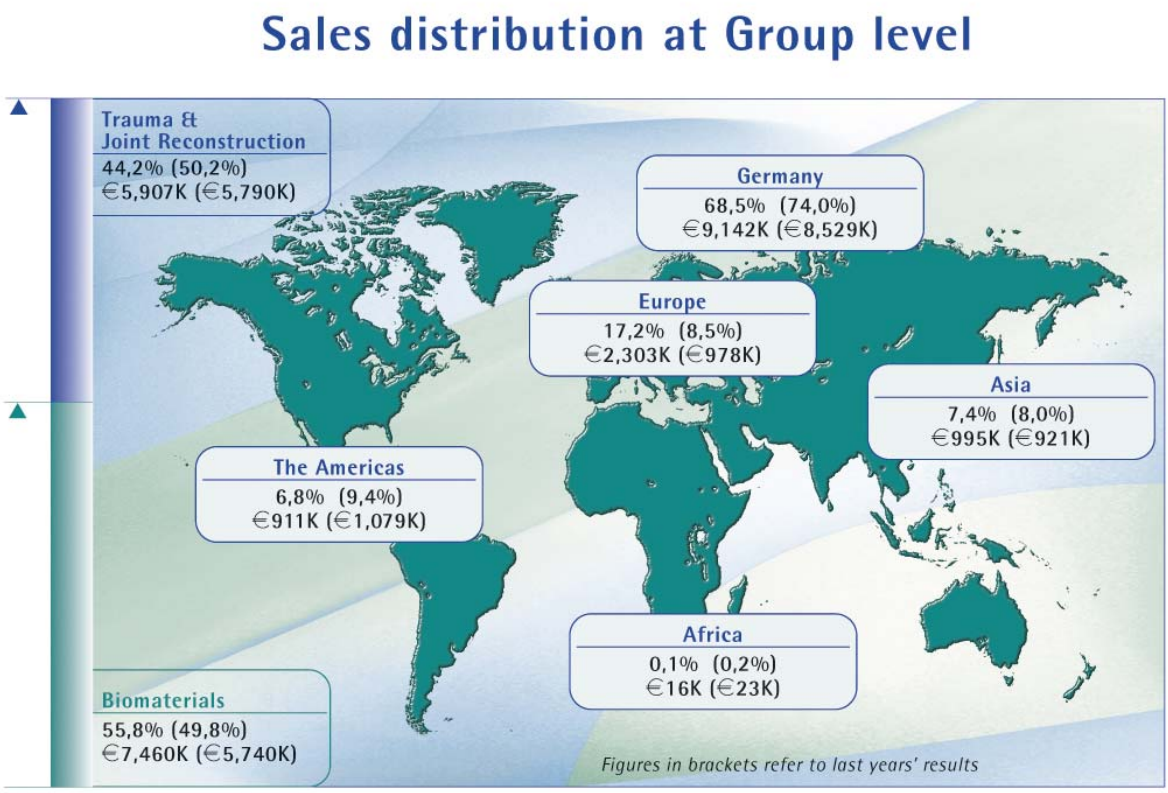
Neue Magnetodyn GmbH

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

Products, Markets and Sales

aap's previous lines of business (osteosynthesis, endoprosthetics and orthobiology) were adjusted to the company's new structure from January 1, 2006 at the year's end and in the reporting schema. *aap* now has two lines of business, Trauma/Joint Reconstruction (*aap* T/O) and Biomaterials (*aap* Biomaterials). Sales in the former consist of the combined sales of the former osteosynthesis and endoprosthetics lines, but without bone cements and without cementing techniques. The latter are now shown along with biomaterials in the new Biomaterials line of business. The company's legal structure shall follow these divisions from around mid-2006.

Sales Distribution at Group Level



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

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

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

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

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

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

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

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

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

With the exception of U.S. business, which was influenced negatively by the cessation of trauma activities with the existing sales partner and by the FDA's warning letter in 2004, *aap* posted sales growth in all regions.

Strong growth in international business, especially with OEM customers in the Biomaterials segment, enabled *aap* to reduce further its dependence on the German market. In spite of ongoing cost pressure in the German healthcare sector and cancellation of the Palacos® distribution contract *aap* was also able by stepping up sales activities to achieve a further increase in German sales.

In 2006 the proportion of international business will show a further marked increase. *aap* signed new sales agreements with international partners in all lines of business and will thereby be able to establish internationally the products it has newly launched in Germany (Variofit®, WSP, Ostim®, PerOssal®).

Sales Distribution at aap Implantate AG

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

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

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

Sales and Marketing Activities

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

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

- Consistent implementation of the new corporate design

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

Along with field sales for the joint reconstruction and trauma product areas, *aap* has built up a group of biomaterials specialists to look after innovative products that need explaining in Germany.

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

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

Production

aap has three production locations in Germany. They are Berlin, Dieburg and Obernburg. In Berlin *aap* Implantate AG manufactures osteosynthesis and endoprosthetics products and instruments for trauma and joint reconstruction. Dieburg is the central production location for bone cements. Biomaterials are manufactured in Obernburg and Dieburg.

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

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

Quality Management

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

All *aap* companies are certificated to the DIN EN ISO 13485 standard for medical devices and the EU directive 93/42/EEC. *aap* Implantate AG is also certificated voluntarily to EN ISO 9001:2000 and operates a validated environmental management system. In business activity all relevant environmental protection regulations are observed. Neither production nor *aap* products pose any direct or indirect risks to the environment.

After the FDA's warning letter received in July 2004, *aap* Implantate AG interrupted sales of trauma products in the United States. In the first quarter of the company will be re-audited, and depending on the result of the re-audit sales in the United States may then be resumed.

Approval procedures for the biomaterials portfolio are currently under way in a number of Asian countries. *aap* is also preparing to submit Ostim® and PerOssal® for approval in the United States.

Employees

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

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

In financial year 2005, trainees included on average 134 people were employed by the Group. Personnel expenses in the reporting period totaled €5.423 million, equivalent to a labor cost ratio of 41% of Group sales revenues (previous year: 35%).

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

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

Research and Development

Group of Companies

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

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

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

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

aap Implantate AG - Trauma/Joint Reconstruction

Since March 2005 the development department in Berlin has been managed by a new head with many years of experience in orthopedics and osteosynthesis. To ease and accelerate routine work significantly, all workplaces were equipped with powerful new 3D CAD software at the beginning of July.

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

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

Biomaterials

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

Events of special Importance

Bone Cement Production Agreement with international Orthopedics Group

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

Cancellation of Palacos® Distribution Contract for Germany

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

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

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

As of August 30, 2005, *aap* became Biomet Deutschland GmbH's new official bone cement distribution partner. That enabled *aap* to supply its own bone cement customer with one of the best-quality products on the market and thereby to offset in part the fall in sales resulting from the Palacos® cancellation.

Capital Increase against Cash Contribution

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

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

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

Risk Report

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

Risk Management System

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

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

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

Market, Competition, New Products and Technologies

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

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

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

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

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

Product Approvals

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

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

Dependence on Customers and Suppliers

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

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

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

Patents and intellectual Property

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

Product Liability Risk

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

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

Legal Risks

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

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

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

Active management of receivables minimizes risks arising from possible default on trade receivables. In addition, *aap* regularly makes sufficient risk provision for default. In all, however, the risk can be considered extremely slight. Losses of receivables totaled €28K in the reporting year.

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

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

Supplementary Report

On March 3, 2006 *aap* announced the conclusion of a new sales partnership with Heraeus Kulzer, a Heraeus Group company. Heraeus will in future market *aap*'s Ostim® bone replacement material worldwide in the dental sector. After a one-year startup period this partnership should exceed a €1 million sales volume.

Forecast Report

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

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

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

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

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

With the professionalization of its German and international sales structure and a wider network of OEM partners *aap* will be able over the next 18 months to launch different products in all areas (bone

replacement, bone cement, trauma and joint reconstruction) with a prospect of high initial acceptance and corresponding growth rates.

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

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

Berlin, March 28, 2006

The Management Board

Oliver Bielenstein Bruke Seyoum Alemu

Consolidated
Annual Financial Statement

Consolidated Income Statement according to IFRS for the Period January 1 to December 31, 2005

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

All figures in € K

Consolidated Balance Sheet according to IFRS at December 31, 2005

Assets			Notes	2005		2004
A.		Long-term Assets	(11)			
	I.	Intangible Assets				
		1. Concessions, industrial property rights and similar rights and values, and licenses thereto		1,478		1,484
		2. Goodwill		1,568		0
		3. Capitalized services rendered for own account		4,539		3,191
					7,585	4,675
	II.	Tangible Assets				
		1. Land and leasehold rights and buildings, including buildings on third-party land		781		864
		2. Plant and machinery		1,737		1,523
		3. Other fixtures and fittings, tools and equipment		1,258		1,011
		4. Prepayments made		9		0
					3,785	3,398
	III.	Financial Assets				
		1. Investments balanced at equity		0		173
		2. Other Investments	(20), (22)	388		0
		3. Loans to companies in which an equity interest is held		0		30
					388	203
	IV.	Prepayments and accrued Income	(12)		2,376	2,485
B.		Short-term Assets				
	I.	Inventories	(13)			
		1. Raw materials and supplies		1,077		907
		2. Work in progress		1,196		678
		3. Finished goods and goods for resale		4,652		4,368
					6,925	5,953
	II.	Accounts receivable and other Assets	(14)			
		1. Accounts receivable (trade debtors)		1,524		965
		2. Due from undertakings with which the company is linked by virtue participating interests		168		546
		3. Other assets		946		1,040
					2,638	2,551
	III.	Checks, Cash in Hand and on Deposit with Deutsche Bundesbank, Postal Giro Balances, Cash in other Banking Accounts			1,384	1,182
					25,081	20,447

Liabilities			Notes	2005		2004
A.		Capital Stock	(15)			
	I.	Subscribed Capital		16,519		14,609
	II.	Capital Reserve		25,198		24,080
	III.	Revenue Reserve				
		1. Legal reserve		42		42
		2. Other revenue reserve		273		272
	IV.	Revaluation Reserve		608		0
	V.	Consolidated Balance Sheet Profit		-23,276		-23,470
	VI.	Adjustment item for interests held by parties outside the Group		2		0
					19,366	15,533
B.		Long-term Liabilities (above 1 year)	(17), (18)			
		1. Long-term provisions		271		138
		2. Advances from customers		650		0
		3. Special items for investment grants		187		110
		4. Due to banks		0		3
		5. Other long-term liabilities		200		71
					1,308	322
C.		Short-term Liabilities (up to 1 year)	(17)			
		1. Other short-term provisions	(16)	777		904
		2. Short-term tax provisions		2		87
		3. Due to banks		579		826
		4. Advances from customers		600		0
		5. Accounts payable		925		1,308
		6. Contributions made to implement the capital increase agreed		625		0
		7. Special items for investment grants		89		0
		8. Due to undertakings with which the company is linked by virtue of participating interests		10		202
		9. Short-term financial leasing liabilities		3		66
		10. Other short-term liabilities		797		1,199
					4,407	4,592
					25,081	20,447

All figures in € K

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

Consolidated Cash Flow Statement according to IFRS

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

All figures in € K

Consolidated Schedule of Assets at December 31, 2005 according to IFRS

					Historical Cost of Acquisition					Cumulative Depreciation				Book Values	
			Status as at 01.01.2005	Changes in the Consolidation Entity	Additions	Retire-ments	Status as at 12.31.2005	Status as at 01.01.2005	Changes in the consolidation entity	Depreciation Fiscal Year	Retire-ments	Status as at 12.31.2005	Write-ups Fiscal Year	Status as at 12.31.2005	Status as at 12.31.2004
A.		Long-term Assets													
	I.	Intangible Assets													
		1. Industrial property rights and similar rights and values	17,235	1	230	0	17,466	15,751	1	236	0	15,988	0	1,478	1,484
		2. Goodwill	4,018	1,568	0	0	5,586	4,018	0	0	0	4,018	0	1,568	0
		3. Capitalized development costs	5,022	1,002	865	0	6,889	1,831	279	240	0	2,350	0	4,539	3,191
			26,275	2,571	1,095	0	29,941	21,600	280	476	0	22,356	0	7,585	4,675
	II.	Tangible Assets													
		1. Land and buildings	1,747	25	0	0	1,772	883	13	95	0	991	0	781	864
		2. Technical plant and machinery	5,861	260	606	0	6,727	4,338	121	531	0	4,990	0	1,737	1,523
		3. Other fixtures and fittings, tools and equipment	4,297	146	764	555	4,652	3,286	110	369	371	3,394	0	1,258	1,011
		4. Prepayments made	0	0	9	0	9	0	0	0	0	0	0	9	0
			11,905	431	1,379	555	13,160	8,507	244	995	371	9,375	0	3,785	3,398
	III.	Financial Assets													
		1. Participations carried at equity	679	-679	0	0	0	506	-266	-240*	0	0	0	0	173
		2. Other participations	0	184	27	0	211	0	155	0	0	155	332	388	0
		3. Other lendings	294	0	0	0	294	294	0	0	0	294	0	0	0
		4. Loans to companies in which an equity interest is held	30	-30	0	0	0	0	0	0	0	0	0	0	30
			1,003	-525	27	0	505	800	-111	-240	0	449	332	388	203
		Total	39,183	2,477	2,501	555	43,606	30,907	413	1,231	371	32,180	332	11,758	8,276

All figures in € K

* positive results of equity investments carried at equity

Movement in Equity and Shares of other Shareholders from January 1, 2001 to December 31, 2005 according to IFRS

	Subscribed Capital	Capital Reserve	Revenue Reserves		Revaluation reserve	Balance Sheet Loss/Profit	Shares owned by the Group	Shares owned by the other Shareholders	Total
			Legal Revenue Reserve	Other Revenue Reserves					
Status as at 12.31.2002/01.01.2003	4,765	24,543	42	272	0	-7,639	21,983	-269	21,714
Capital Increase	105	95					200		200
Transaction Costs		-218					-218		-218
Net Loss for the Year						-15,417	-15,417	-5	-15,422
Status as at 12.31.2003/01.01.2004	4,870	24,420	42	272	0	-23,056	6,548	-274	6,274
Capital Increase	9,739						9,739		9,739
Retransfer arising from the Dissolution of *aap* Implants Inc.						-279	-279	279	0
Transaction Costs		-340					-340		-340
Net Loss for the Year						-135	-135	-5	-140
Status as at 12.31.2004/01.01.2005	14,609	24,080	42	272	0	-23,470	15,533	0	15,533
Capital Increase Aug. 29, 2005	450	286					736		736
Capital Increase Sept. 30, 2005	1,460	877					2,337		2,337
Transaction Costs		-45					-45		-45
Initial Consolidation						-457	-457	-2	-459
Revaluation of other equity investments					118		118		118
Changes in the consolidation entity				1	490		491		491
Net Profit for the Year						651	651	4	655
Status as at 12.31.2005	16,519	25,198	42	273	608	-23,276	19,364	2	19,366

All figures in € K

Notes to the Consolidated Financial Statements to December 31, 2005 in Accordance with IFRS

A. Company Data

Company Name, Domicile

aap Implantate AG, Berlin

Head Office

Lorenzweg 5, 12099 Berlin, Germany

Commercial Register

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

Stock Market Listing

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

Incorporation by modifying Conversion

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

Type of Business

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

B. General Information

1. Basic Principles

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

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

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

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

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

2. Flow of Funds Statement

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

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

C. Consolidation Principles

1. Consolidated Entity

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

aap Implantate AG, Berlin — Parent Company

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

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

2. Acquisitions/Changes in Participations

By the terms of a contract dated September 21, 2005, *aap* Implantate AG acquired the remaining 51% in OSARTIS GmbH & Co. KG, Elsenfeld, and OSARTIS Verwaltungs GmbH,

Elsenfeld, for a purchase price of €33,000, including incident acquisition costs. The purchase price was paid in cash in financial year 2005. Both companies are now wholly owned by *aap* Implantate AG. Due to the change in status from associated company to subsidiary, a change from equity accounting to full consolidation seemed advisable. In accordance with IFRS 3, assets of participating interest were totally revalued at the time when full control was gained with the exception of goodwill, for which the original valuation still stands. The €490K increase in undisclosed reserves was included in the revaluation reserve. Changes in value booked in accordance with the equity method before full control was gained were canceled.

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

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

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

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

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

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

3. Reporting Date of the Consolidated Financial Statements

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

4. Accounting and Valuation Method

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

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

5. Capital Consolidation

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

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

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

6. Debt Consolidation

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

7. Consolidation of Earnings

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

D. Accounting and Valuation Methods

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

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

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

include the full costs. Costs of borrowing are not capitalized as part of acquisition or production costs.

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

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

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

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

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

Inventories are valued at cost of acquisition or production or at net sale value. Production costs are full costs calculated on the basis of ordinary employment. In detail, production costs include in addition to directly attributable costs appropriate proportions of essential production overheads. These include material and manufacturing overheads and production-related administrative costs as well as straight-line depreciation of production plant and equipment. Loan capital costs are not capitalized as part of acquisition or production costs.

Valuation is based on the FIFO assumed sequence of consumption.

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

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

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

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

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

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

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

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

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

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

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

Insofar as these framework conditions develop differently, the assumptions and, if necessary, book values of the assets and debts affected will be adjusted accordingly.

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

E. Changes in Accounting and Valuation Methods

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

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

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

F. Notes on the Profit and Loss Statement

(1) Sales Revenues

	2005	2004
	€ K	€ K
By region		
Germany	9,143	8,529
Other European countries	2,302	978
Asia	995	921
The Americas	911	1,079
Africa	16	23
Total	13,367	11,530

	2005	2004
	€ K	€ K
By lines of business		
Trauma & Joint Reconstruction	5,907	5,790
Biomaterials	7,460	5,740
Total	13,367	11,530

(2) Other Operating Income

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

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

(3) Personnel Expenses

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

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

(4) Depreciation

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

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

(5) Other Operating Expenses

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

(6) Result of Participating Interests

This includes the pro rata result of participating interests in GEOT Gesellschaft für Elektro-Osteo-Therapie mbH and OSARTIS GmbH & Co. KG drawn up using the equity accounting method for the period up to June 30, 2005 and September 30, 2005 respectively and amounting to €239K (previous year: €-111K, cf C (2)).

(7) Financial Result

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

(8) Exchange Rate Differences

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

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

(9) Taxes on Income

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

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

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

(10) Earnings per Share as per IAS 33

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

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

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

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

G. Notes on the Balance Sheet

(11) Long-term Fixed Assets

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

1. Intangible Assets (excluding Development Costs)

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

Useful economic life is as follows:	Years
Industrial property rights and similar rights and values	3 - 20

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

2. Development Costs

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

- Bone cement with antibiotic
- HF cement
- CS pellets – absorbable bone replacement
- Stable-angle plates
- Dynamic hip pin

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

3. Tangible Assets

Tangible assets are depreciated in a straight line from historic cost of acquisition or cost of production.

Useful economic life is, on average, as follows:	Years
Land and buildings	50
Technical plant and machinery	5 - 10
Other plant, office and business equipment	5 - 10

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

4. Financial Assets

Participating interests		2005		2004	
		€ K	%	€ K	%
1.	Neue Magnetodyn GmbH, Munich (GEOT Gesellschaft für Elektro-Osteo-Therapie mbH, Munich)	32	7.12	23	30.0
2.	AEQUOS Endoprothetik GmbH, Munich	356	11.2	0	11.9
3.	Cybernetic Vision AG Health Monitoring Technologies, Berlin	0	5.69	0	5.69
Loans to companies with which *aap* has a participation relationship		0		30	
Total		388		203	

(12) Deferred Taxes

Tax accruals carried as assets totaling €2.376 million (previous year: €2.485 million) include the following capitalized tax credit entitlements arising, according to the present business plan, from the anticipated utilization of existing loss carryovers in the years ahead:

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

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

Deferred tax credit claims totaling €390K (previous year: €355K) relate to items that are offset directly against equity. Deferred tax liabilities totaling €1.765 million result from consolidation (elimination of interim results and debt consolidation including currency differences) and from temporary differences between tax values and amounts stated for balance sheet items in accordance with IFRS.

To calculate trade earnings tax, the IFRS result for the year was taken as the starting point and trade earnings were calculated by means of trade tax additions and deductions. Trade tax is charge at roughly 17% after taking tax deductibility into account. Deferred corporate income tax was determined on the basis of a tax rate of 25% plus a 5.5% solidarity surcharge on corporate income tax due. Deferred tax credits arising in connection with consolidation were calculated on the basis of an average tax rate of 39% for the Group.

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

(13) Inventories

To state inventories at net sale value, value adjustments totaling €48K (previous year: €6K) were undertaken in the year under review. Value markdowns amounting to €2.464 million (previous year: €2.596 million) were made. There were no extraordinary markdowns (previous year: €640K).

(14) Accounts receivable and other Assets

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

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

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

(15) Equity

Capital Stock

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

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

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

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

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

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

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

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

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

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

Transaction Costs

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

Conditional Capital

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

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

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

Authorized Capital

The General Meeting held on June 10, 2005 authorized the Management Board to increase the company's capital stock by June 10, 2010 on one or more occasions by up to €7,300,000 in

cash or kind and to lay down the terms and conditions of the share issue. Subject to Supervisory Board approval, subscription rights for existing shareholders may be ruled out

a) to balance residual amounts,

b) if the capital increase in cash does not exceed 10% of the capital stock and the issue price of the new shares is not substantially lower than the market price (§ 186 Section 3 Sentence 4 AktG),

c) to issue shares in return for contributions as part of an acquisition of companies, parts of companies or participations in companies (including conversions by the terms of the Conversion Act)

d) to issue shares to strategic partners,

e) to serve conversion or subscription rights held by holders of stock options, convertible bonds, stock warrants and/or participation certificates,

f) to issue shares to employees and directors of the commpany and to employees and management of associated companies as part of a stock option plan,

g) in payment for consulting services,

h) to issue shares to lenders in place of interest payments in cash or in addition thereto (so-called equity kickers), especially in connection with mezzanine financing,

i) to repay loans or other liabilities.

Please see the schedule of equity.

(16) Short-term Reserves

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

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

(17) Liabilities

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

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

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

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

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

H. Other Information

(18) Reporting on Financial Instruments

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

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

For details see figures at C. 2.

(19) Cash Flow Statement

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

Interest income €15K (previous year: €12K)

Interest expenses €44K (previous year: €498K)

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

(20) Participating Interests

I. Allied Companies (§ 271 Section 2 HGB)

	Name	Domicile	Participation	Equity	Result
			%	€ K	€ K
1.	*aap* Biomaterials GmbH & Co. KG*	Dieburg	100	-1,152	180
2.	*aap* Biomaterials Verwaltungs-GmbH**	Dieburg	100	38	2
3.	OSARTIS GmbH & Co. KG	Elsenfeld	100	-1,129	924
4.	OSARTIS Verwaltungs GmbH	Elsenfeld	100	26	1

	Name	Domicile	Participation	Equity	Result
			%	€ K	€ K
5.	ADC Advanced Dental Care GmbH & Co. KG	Elsenfeld	54	-8	6
6.	ADC Advanced Dental Care Verwaltungs GmbH	Elsenfeld	51	16	0

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

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

II. Participation Interests

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

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

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

(21) Other Financial Commitments

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

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

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

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

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

(22) Related Enterprises and Persons

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

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

Transactions are undertaken on market terms and conditions.

In accordance with a resolution adopted by the annual meeting of shareholders on June 10, 2005, Mr. Uwe Ahrens waived the loan he made to the company in 2000 totaling €736K in return for 449,713 new shares. No interest was incurred in the year under review (previous year: €34K).

(23) Management Board, Supervisory Board

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

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

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

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

Management remuneration totaled:

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

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

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

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

Members of the company's Supervisory Board are:

Herr Jürgen W. Krebs, business management specialist,
Kilchberg near Zurich, Switzerland (Chairman)

Herr Rubino Di Girolamo, business management specialist,
Oberägeri near Zug, Switzerland (Deputy Chairman)

Herr Prof. Dr. Dr. med. Reinhard Schnettler, university professor,
Giessen

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

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

Herr Jürgen Krebs	€12,500
Herr Rubino di Girolamo	€9,375
Prof. Dr. Dr. Reinhard Schnettler	€6,250

No payments were made and €2K was offset.

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

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

Supervisory Board and Management Board members held the following shares:

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

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

(24) Auditor's Fees

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

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

(25) Statement on the German Corporate Governance Code

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

(26) Publication

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

Berlin, March 28, 2006

The Management Board

Oliver Bielenstein

Bruke Seyoum Alemu

Auditor's Certification

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

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

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

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

Our audit led to no objections.

In our opinion, based on what we learnt in the course of the audit, the consolidated financial statements comply with IFRS as applied in the EU and with the additional commercial law provisions of § 315 a Section 1 of the German Commercial Code and convey, with due regard to these regulations, a picture of the Group's assets, financial and earnings position that is in accordance with the actual

circumstances. The report on the situation of the Company and the Group tallies with the consolidated financial statements, conveys an accurate idea of the company's situation and accurately describes the risks of future development.

Berlin, March 30 2006

Dr. Röver & Partner KG
Wirtschaftsprüfungsgesellschaft
Steuerberatungsgesellschaft

Helmut Schuhmann
Auditor

Bettina Grothe
Auditor