First-quarter report 2004

Q1/04

SOFTWARE AG
THE XML COMPANY

Key figures
IFRS, unaudited

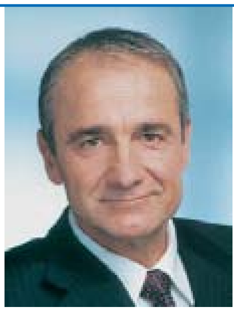
€ millions (unless stated)	**March 31, 2004**	**March 31, 2003**	**Change in %**
Revenue	**95.7**	**103.1**	**– 7 %**
Products	67.4	69.2	– 3 %
of which licensing	23.3	21.9	6 %
of which maintenance	44.1	47.3	– 7 %
Professional services	28.0	33.6	– 17 %
Other	0.3	0.3	0 %
EBIT	**15.1**	**8.0***	**–**
as % of revenue	16 %	8 %	
Income before taxes	**15.8**	**– 23.1**	**–**
as % of revenue	17 %	– 22 %	
Income after taxes	**9.8**	**– 14.8**	**–**
as % of revenue	10 %	– 14 %	
Earnings per share (€)	**0.36**	**– 0.54**	**–**

€ millions (unless stated)	**March 31, 2004**	**Dec 31, 2003**	**Change in %**
Total assets	**523.5**	**509.1**	**3 %**
Cash and cash equivalents	**83.1**	**74.2**	**12 %**
Shareholders' equity	**286.8**	**269.2**	**7 %**
as % of total assets	55 %	53 %	
Employees	**2,512**	**2,885****	**– 13 %**
of which in Germany	898	1,119**	– 20 %

*pre restructuring expensive **as of March 31, 2003

Profile

Software AG is an international provider of systems software and XML integration and data-management services. We offer integration solutions based on XML (eXtensible markup language), a key technology for the smooth exchange of data and documents, and a powerful means of introducing state-of-the-art applications into existing IT architectures. We are the European No. 1 and one of the world leaders in this area.



Karl-Heinz Streibich
Chief Executive Officer

Firm foundations for the future

Software AG hit the ground running in the first quarter of 2004. With lower costs and higher efficiency leading to a marked improvement in earnings, we reaped the rewards of the effective reorganizational activities carried out in the previous months.

The first three months of the year were not only successful in terms of overall business development: We also made tangible progress in the implementation of our new strategy.

The XML Integration business line now has a clearly structured portfolio, comprising Enterprise Integration Services, Enterprise Information Services and Legacy Integration. These are designed to help customers increase integration of existing IT systems.

The business line Enterprise Transaction Systems Modernization now provides defined product packages aimed at increasing the value of customers' existing investments in Adabas/Natural. Software AG specialists are currently building new ETS Advantage Services to complement our product packages, creating total solutions.

The new organizational structure defined last year is now in place, with a dedicated team of software architects for each business line. Drawn directly from the Research and Development unit, team members will interface closely between R&D and the sales organization, ensuring effective knowledge transfer. Teams will provide feedback to the sales force on their experience with customers, and, via the two business lines, will influence future research and development. In this way, we are fostering a sustainable, market-driven approach to the development of new products and solutions.

The new structure will accelerate Software AG's transformation into a learning organization.
We have further strengthened our international orientation by appointing Joe Gentry, from the US, and Jonathan Airey, from the UK, to lead the ETS Modernization and XMLi business lines respectively. These moves reflect our determination to maximize intra-Group, cross-border collaboration.

The international nature of the Group creates added value for all Software AG companies. By establishing effective links between countries, we create a global pool of resources which benefits our technologies, solutions, and customer relationships. And intensified marketing efforts, allied with the creation of a focused corporate identity, are supporting the shift to a team-oriented, learning organization.

Karl-Heinz Streibich
Chief Executive Officer

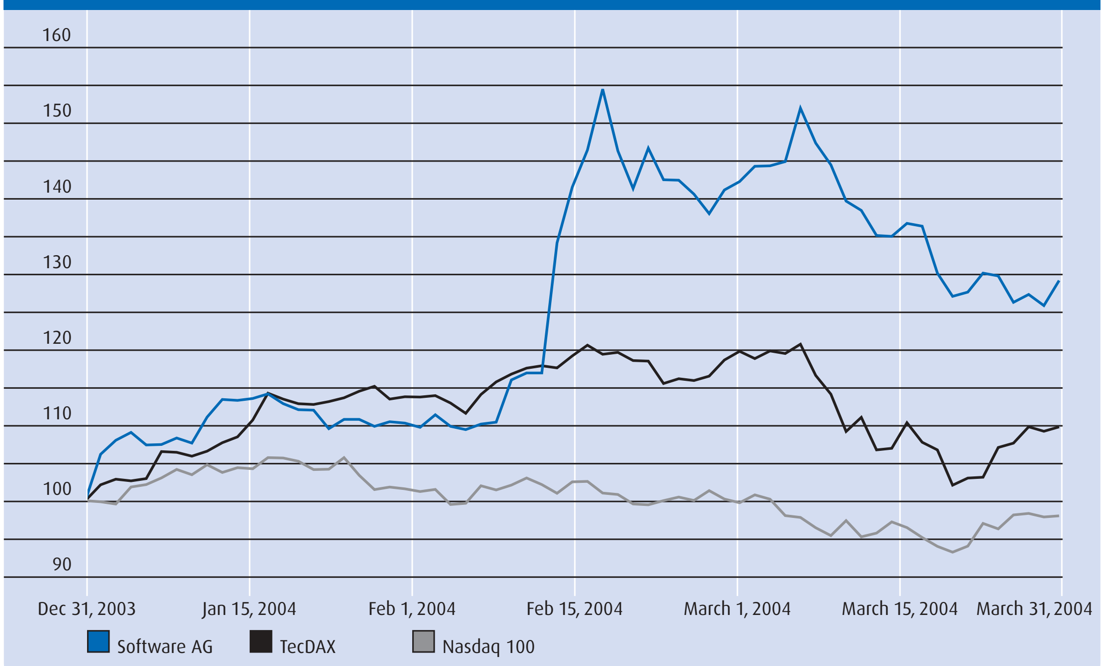
Leading indices outperformed

The notable upswing in the value of Software AG shares during fiscal 2003 continued into the first quarter of 2004. The price rose from €16.30 at December 31, 2003 to €21.04 at March 31, 2004.

As a result, Software AG stock outperformed both the TecDAX and the Nasdaq 100 by a clear margin. The TecDAX rose by 9.8 percent and the Nasdaq 100 fell by 2.0 percent, while the price of Software AG shares rose 29.1 percent.

This reflects growing investor confidence in Software AG. As a result of the strategic focus on Enterprise Transaction Systems (ETS) and XML Integration announced in early December 2003, we succeeded in convincing not only our customers, but also financial analysts and investors of the positive outlook for the Company and for Software AG shares. Financial results for the fourth quarter of 2003 and the first three months of 2004 significantly exceeded market expectations. The program of cost savings initiated in 2003 has significantly raised profitability, leading to improved ratings. Forecast earnings per share for 2004 have been revised upward to between €2.50 to €2.60. This includes approximately €0.88 in proceeds from the sale of holdings.

Comparison of share development with leading indices



Improved ratings from financial analysts

During the first quarter of 2004, investor relations concentrated on communicating the benefits of the new business strategy. At two investor conferences, and by means of a large number of face-to-face meetings with analysts and investors, we provided information on the new strategy and on Software AG's potential. Press and analyst earnings conferences for year-end 2003 and first-quarter 2004 were broadcast live via the Internet, and the presentations are available as downloads. We also organized a special event at Company headquarters for financial analysts, who are important opinion leaders with influence over both private and institutional investors. These activities contributed to improved ratings from financial analysts: The number of sell recommendations fell from seven to two, and the number of hold recommendations from six to four. At the same time, buy recommendations increased from seven to twelve. The average share-price target was increased several times during the course of the first three month, reaching €29 after first-quarter results were published on April 27, 2004.

Software AG shares

	March 31, 2004	March 31, 2003
XETRA closing price (in €)	21.04	11.55
Number of shares	27,266,752	27,266,752
Market capitalization (in € millions)	574	315
52-week high/low	25.16/9.81	

Frankfurt (Prime Standard/TecDAX), ISIN DE 0003304002, ticker symbol SOW

Positive start to the year – annual targets within reach

Business development in the first quarter was strongly influenced by the positive impact of restructuring. Operating profit (EBIT) rose by 89 percent to €15.1 million; pre-tax profit rose to €15.8 million; net profit improved to €9.8 million.

Consolidated revenues for the first quarter totaled €95.7 million, €103.1 million in the same period of 2003. More than 28 percent of revenues were posted in US dollars. As a result, the weak dollar had a significant impact on reported figures. Adjusted for currency translation effects, quarterly revenues were 2 percent lower than in 2003.

Product sales remain stable

Product revenue, compromising of both license and maintenance services, remained the main source of revenue. Product revenues totaled €67.4 million (€69.2 million in Q1 2003). Adjusted for currency translation effects, this represents an increase of 3 percent.

Licensing revenues developed particularly positively. Adjusted for currency translation effects, sales increased by 11 percent to €23.3 million. This growth was primarily attributable to the Enterprise Transaction Systems (ETS) Business Line, which contributed more than 76 percent of all licensing revenues.

ETS revenues exceed forecasts

The business line ETS Modernization generated licensing sales of €17.8 million, an increase of 31 percent. This reflects both the slightly improved willingness of customers to invest in IT, but also the impact of our intensified marketing efforts. The new strategic focus takes into account the importance of ETS products. Moreover, this clear long-term commitment provided a boost to the morale of the ETS sales force.

Nevertheless, customers remain cautious with regard to investment in new technologies. XML Business Integration license sales fell to €3.8 million (€6.1 million in Q1 2003) in the first quarter. However, the launch of our new XML Integration Packages in the second quarter is expected to lead to improvement over the remainder of the year.

Breakdown of revenues by segment

€ millions	Q1 2004	Q1 2003	Change in % (adj. for currency translation)
Products	67.4	69.2	3
of which maintenance	44.1	47.3	0
of which licensing	23.3	21.9	11
Project services	28.0	33.6	– 15
Other	0.3	0.3	0
Total	95.7	103.1	– 2

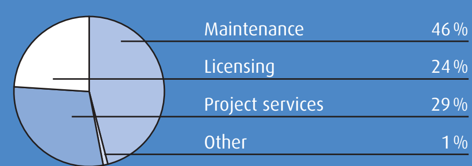
Fall in revenues from professional services

Before currency translation effects, revenues from maintenance services remained unchanged year-on-year, contributing €44.1 million to product sales. Project services contributed revenues of €28.0 million, with market oversupply playing a significant role in this lower figure. In addition, Software AG has deliberately focused professional services on high-margin areas since 2003. The fall in revenues for this segment is a direct result of the reduction in the consultant headcount. IT consultant utilization was unchanged in comparison to 2003.

Increased revenues from licensing in the regions

Three of Software AG's regional subsidiaries posted increased revenues from licensing. In northern Europe, Asia/Pacific, and South Africa, license sales from new software increased by almost a third to €7.4 million. In Central and Eastern Europe, the increase was 21 percent. In Southern and Western Europe, revenues from licensing rose 19 percent to €5.3 million. In the Americas, the weak dollar led to a drop in revenues from licensing to €5.2 million in comparison to €7.4 million over the same period of 2003.

Breakdown of revenues by segment



Profitability

89 percent increase in operating profit

Lower costs as a result of restructuring helped to lift profitability. Strict cost management reduced other operating costs by €10.6 million.

As a result, earnings figures, reported for the first time in accordance with International Financing Reporting Standards (IFRS), improved significantly. Earnings before interest and tax (EBIT) rose to €15.1 million, an increase of 89 percent. This is equivalent to an EBIT margin of 16 percent

Pre-tax profit rose to €15.8 million, in comparison to a loss of –€23.1 million in the same period of 2003 (largely a result of restructuring costs of €31.8 million). Net income for the quarter totaled €9.8 million, contrasting with a loss of –€14.8 million in the first quarter of fiscal 2003. This represents earnings per share of €0.36 (–€0.54 in Q1 2003). Fluctuations in currency rates have less impact on profitability than on revenues, since a significant proportion of costs are also posted in US dollars, and hedging is employed to shield forecast earnings from the potentially negative impact of significant changes in exchange rates.

Further increase in equity-to-assets ratio

Software AG has further improved its financial footing. Shareholders' equity increased to €286.8 million from €242.3 million in the first quarter of 2003. As a result, the equity-to-assets ratio improved further, reaching 54.8 percent.

Cash and cash equivalents increased from €80.9 million in the first quarter of 2003 to €83.1 million. Assets rose to €256.6 million, primarily as a result of improved valuations for financial assets. Despite an increase in restructuring payments of €6.4 million, cash flow from operating activities totaled €10.7 million in comparison to €12.0 million in the first quarter of 2003.

As a result of the adoption of International Financial Reporting Standards (IFRS), goodwill was frozen at €176.5 million on January 1, 2003 (the date of the changeover from HGB to IFRS). Therefore goodwill rose by €22.0 million on December 31, 2003 (i.e. the amount amortized one year previously).

Progress on the strategic front

On track to becoming a global networked company

Software AG is a global player, with a presence in 59 countries. Global reach offers enormous opportunities, which we intend to leverage by becoming a global networked company. This entails closer cooperation and greater knowledge transfer between all units and functions, with the goal of establishing a learning organization driven by the needs of our customers.

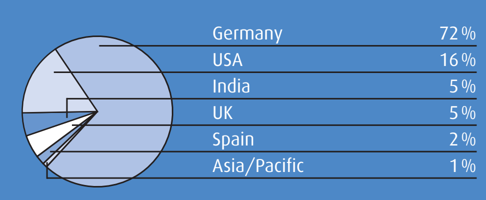
Global Networked Company

Synergy through a worldwide R&D organization

The implementation of an international research and development network is in progress. R&D centers in the US, the UK, Germany, and Spain are engaged in the optimization of the core products of both business lines, ETS and XMLi. Software AG India is responsible for some XML Business Line development. This new arrangement results in lower costs; a greater synergy and a greater focus on market requirements.

R&D activities were reorganized in order to concentrate more fully on the Company's core competencies. Software AG now channels its R&D effort more directly into products and solutions with market potential. Technology architects act as interfaces between market requirements and Software AG's R&D units. These architects understand customer requirements, product features and various best-practice projects. They help us to integrate and combine skills and resources throughout the enterprise in order to better meet customer requirements.

R&D employees by location



Customer-driven sales activities

In line with our new strategic focus, we strengthened marketing and sales efforts in the first quarter. The Customer First Program, originally developed in the US, will be implemented throughout the Group. The aim is to create a "customer-first" culture in all areas of Software AG. In other words, we wish to ensure that the Company is focused on the customer and customers' requirements and not just on the sales front but in all aspects and activities of Software AG.

Quality of customer relationships improves

The Company also succeeded in broadening and deepening relations with key decision makers at customer organizations. According to market analysts, top managers are responsible for the allocation of more than 90 percent of IT budgets. As a result, maintaining good relations with key executives is vital to the generation of new business. We have intensified efforts to involve Software AG in the earliest possible phase of the sales cycle, helping us to gain access to high-value contracts.

Against the background of our renewed focus on market requirements, we have established a customer knowledge-management system. Designed to capture and collect knowledge relating to the market, customers and solutions, it aggregates information throughout the enterprise, and makes it available worldwide, and in real time. We are confident that this will provide further impetus for the Company.

Staffing

Employee numbers realigned

On March 31, 2004, Software AG employed 2,512 people, 373 less than on March 31, 2003. Headcount fell primarily in Germany, particularly at headquarters. 64 percent of the Software AG workforce is based outside Germany.

Significant increase in forecast earnings

During the first three months of the year, we laid solid foundations for a successful fiscal 2004, with strong operating earnings and buoyant license sales. During the coming three quarters, we will continue to focus on stabilizing revenues and streamlining costs.

We believe our decision to concentrate on two core business lines will generate sufficient revenues to offset the withdrawal from non-strategic areas. XML license sales are expected to pick up in the second half of the year, particularly as a result of the launch of our XML Integration Packages in the second quarter. Moreover, the Project Services division is expected to benefit from increasing revenues from integration work.

At the same time, we will continue to reduce operating costs, partly as a result of the ongoing consolidation of R&D activities. Improvements in operating margin, additional cost savings, and healthy cash flows will further strengthen Software AG's finances. Against this background, we expect full-year operating profit to exceed the 2003 figure by around 25 percent.

Consolidated income statement for the three months ended March 31, 2004 (January1 to March 31, 2004)

IFRS, unaudited

€ thousands		March 31, 2004	March 31, 2003
Revenues			
Products		67,389	69,212
of which licensing	23,252		21,865
of which maintenance	44,137		47,347
Professional services		27,999	33,576
Other		331	352
Total revenues		**95,719**	**103,140**
Total costs of sales		– 33,305	– 39,434
Gross profit		**62,414**	**63,706**
Research and development		– 15,031	– 16,233
Sales, marketing and distribution		– 20,586	– 25,973
Administrative costs		– 11,106	– 15,084
Total operating expenses		**– 46,723**	**– 57,290**
Other income/expenses		– 561	– 30,172*
Interest income/expenses		**651**	**704**
Pre-tax profit		**15,781**	**– 23,052**
Taxes		**– 6,024**	**8,281**
Consolidated net income		**9,757**	**– 14,771**
Earnings per share in € (basic = diluted)		0.36	– 0.54

* Including restructuring expenses incurred in the first quarter of 2003 to the amount of €31,780 thousand.

Consolidated balance sheets as of March 31, 2004

IFRS, unaudited

€ thousands	March 31, 2004	March 31, 2003	Dec 31, 2003
Assets			
A. Cash and cash equivalents			
1. Cash in hand and bank balances	53,355	51,730	53,083
2. Securities	29,743	29,154	21,076
	83,098	80,884	74,159
B. Current assets			
1. Inventories	235	417	387
2. Trade receivables	122,241	118,736	124,578
3. Other receivables and other assets	6,818	14,501	7,701
	129,294	133,654	132,666
C. Fixed assets			
1. Intangible assets	1,421	1,380	1,491
2. Goodwill	176,472	176,591	176,472
3. Property, plant and equipment	46,613	52,367	47,880
4. Financial assets	32,062	15,735	25,028
	256,568	246,073	250,871
D. Deferred taxes	44,837	49,087	44,959
E. Deferred expenses	9,726	10,203	6,476
Total assets	523,523	519,901	509,131
Equity and liabilities			
A. Current liabilities			
1. Current financial liabilities	4,536	5,017	6,546
2. Trade payables	19,942	20,245	26,770
3. Other current liabilities	22,091	31,570	25,294
4. Current provisions	63,714	73,935	77,791
	110,283	130,767	136,401
B. Non-current liabilities			
1. Non-current financial liabilities	4,600	8,140	4,356
2. Trade payables	27	0	22
3. Other non-current liabilities	3,785	3,665	3,641
4. Provisions for pensions	19,753	19,027	19,666
5. Non-current provisions	5,116	3,455	5,596
	33,281	34,287	33,281
C. Deferred taxes	12,761	16,270	12,798
D. Deferred income	80,260	96,290	57,330
E. Minority interest	126	0	126
F. Equity			
1. Share capital	81,800	81,800	81,800
2. Capital reserves	132	132	132
3. Retained earnings	156,454	149,358	149,358
4. Consolidated net income	9,757	– 14,771	7,096
5. Currency translation differences	– 25,827	– 8,379	– 32,340
6. Other comprehensive income	64,496	34,147	63,149
	286,812	242,287	269,195
Total equity and liabilities	523,523	519,901	509,131

Cash flow statements for the three months ended March 31, 2004 (January 1 to March 31, 2004) IFRS, unaudited		
€ thousands	**Q1 2004**	**Q1 2003**
Consolidated net loss	9,757	– 14,771
Depreciation	2,250	3,080
Interest result	– 651	– 704
Income taxes	5,523	– 8,867
Cash generated from operations	16,879	– 21,262
Income from sale of assets	2	11
Changes in inventories, receivables and other current assets	690	1,659
Changes in payables and other liabilities	– 3,431	39,770
Income taxes paid	– 3,998	– 8,837
Interest paid	– 200	– 383
Interest received	803	1,016
Net cash used in/provided by operating activities	**10,745**	**11,974**
Cash received from the sale of property, plant and equipment/intangible assets	22	292
Investments in property, plant and equipment/intangible assets	– 737	– 1,870
Cash received from the sale of financial assets	35	4
Investments in financial assets	– 557	– 465
Net cash used in/provided by investing activities	**– 1,237**	**– 2,039**
Repayment of loans from acquisitions and other financial liabilities	– 727	– 3,645
Net cash used in/provided by financing activities	**– 727**	**– 3,645**
Change in cash funds from cash-relevant transactions	**8,781**	**6,290**
Currency translation adjustments	**158**	**– 828**
Net change in cash and cash equivalents	**8,939**	**5,462**
Cash and cash equivalents at beginning of period	74,159	75,423
Cash and cash equivalents at end of period	**83,098**	**80,885**

Segment report for the three months ended March 31, 2004 (January 1 to March 31, 2004)

IFRS, unaudited

€ thousands	Americas	Southern and Western Europe	Northern Europe, Asia/Pacific, South Africa	Central and Eastern Europe	Total	Central functions, R&D and Consolidation	Total Group
Licenses	5,165	5,323	7,409	5,355	23,252	0	23,252
Maintenance	18,926	6,489	8,853	9,884	44,151	– 14	44,137
Services	3,183	16,410	2,024	6,387	28,004	– 5	27,999
Other	99	49	35	22	205	126	331
Total revenues	**27,374**	**28,270**	**18,321**	**21,648**	**95,612**	**107**	**95,719**
EBITA	7,481	2,670	4,972	3,860	18,984	– 3,854	15,130
Amortization							0
Interest result							651
Restructuring expense							0
Profit before tax							15,781
Taxes							– 6,024
Net income							9,757
Proportion of total revenues	28.6 %	29.6 %	19.2 %	22.6 %	100.0 %		
Product revenues	24,091	11,811	16,262	15,238	67,403		
Proportion of total product revenues	35.7 %	17.5 %	24.1 %	22.6 %	100.0 %		

Segment report for the three months ended March 31, 2003 (January 1 to March 31, 2003)

IFRS, unaudited

€ thousands	Americas	Southern and Western Europe	Northern Europe, Asia/Pacific, South Africa	Central and Eastern Europe	Total	Central functions, R&D and Consolidation	Total Group
Licenses	7,387	4,488	5,574	4,417	21,866	– 1	21,865
Maintenance	21,343	6,702	9,440	10,215	47,700	– 353	47,347
Services	4,647	17,994	1,835	9,194	33,669	– 93	33,576
Other	1	21	31	53	107	245	352
Total revenues	**33,378**	**29,205**	**16,880**	**23,880**	**103,342**	**– 202**	**103,140**
EBITA	7,792	3,123	3,820	1,673	16,408	– 8,384	8,024
Amortization							0
Interest result							704
Restructuring expense							– 31,780
Profit before tax							– 23,052
Taxes							8,281
Net income							– 14,771
Proportion of total revenues	32.3 %	28.3 %	16.3 %	23.1 %	100.0 %		
Product revenues	28,730	11,189	15,014	14,632	69,566		
Proportion of total product revenues	41.3 %	16.1 %	21.6 %	21.0 %	100.0 %		

Development of shareholders' equity for the three months ended March 31, 2004 (January 1 to March 31, 2004)

IFRS, unaudited

€ thousands	Shares		Capital reserves	Retained earnings	Consolidated income	Currency translation differences	Other comprehensive income	Total
	Number	Share capital						
At January 1, 2004	27,266,752	81,800	132	156,454	0	– 32,340	63,149	**269,195**
Consolidated income for the period					9,757			9,757
Currency translation differences						6,513		6,513
Fair market valuation of financial assets Currency translation							1,347	1,347
At March 31, 2004	27,266,752	81,800	132	156,454	9,757	– 25,827	64,496	**286,812**

Development of shareholders' equity for the three months ended March 31, 2003 (January 1 to March 31, 2003)

IFRS, unaudited

€ thousands	Shares		Capital reserves	Retained earnings	Consolidated income	Currency translation differences	Other comprehensive income	Total
	Number	Share capital						
At January 1, 2003	27,266,752	81,800	132	149,358	0	0	27,639	**258,929**
Consolidated income for the period					– 14,771			– 14,771
Currency translation differences						– 8,379		– 8,379
Fair market valuation of financial assets Currency translation							6,508	6,508
At March 31, 2003	27,266,752	81,800	132	149,358	– 14,771	– 8,379	34,147	**242,287**

Accounting principles

Basis

The consolidated financial statements of Software AG to March 31, 2004, were for the first time prepared in accordance with the International Accounting Standards Board's (IASB) International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS). Software AG complied with the IAS and IFRS, and IFRIC (International Financial Reporting Interpretations Committee, formerly SIC) interpretations applicable on December 31, 2003.

Figures in the consolidated financial statements are, unless otherwise stated, quoted in thousands of euros (€ thousands).

Principals of consolidation

The consolidated financial statements include Software AG and companies under its control. Control is generally taken to be proven where the Group holds, directly or indirectly, the majority of voting rights for authorized capital in a company, and/or can determine the fiscal or business policy of the company.

The financial statements of consolidated companies are compiled according to consistent accounting and valuation principles.

Subsidiaries established by Software AG are consolidated on the date they are formed. However, first-time consolidation occurred after the date of foundation for Softinterest Holding AG and its subsidiaries – which were consolidated for the first time in 1994 – as well as for the Asian subsidiaries, for SQL and for SAG-IRL.

The first-time consolidation of all companies was undertaken using the book value method. Subsequent consolidation is derived from the figures employed for first-time consolidation.

Debit balances arising from capital consolidation and relating solely to goodwill from acquisitions before January 31 were netted against capital reserves, pursuant to Section 309, Subsection 1, of the German Commercial Code (HGB). Goodwill from acquisitions after January 31 was capitalized and will be amortized over ten years. In accordance with the option granted by IFRS 1.14, the Company has not applied IAS 22 retrospectively, but has continued to use the figures for mergers and acquisitions posted according to HGB.

Revenue, expenses and income, receivables, liabilities, and provisions arising between consolidated companies have been eliminated. Intercompany earnings from services provided within the Group were also eliminated where these were not realized from services to third parties.

Consolidated companies

There were no changes to the scope of consolidation in comparison with December 31, 2003.

Estimates and assumptions

In a few instances, estimates and assumptions were made which could impact the statement and amount of figures posted for balance-sheet assets, debt, income, expenses and contingent liabilities. True values may deviate from these estimates and assumptions.

Currency translation

The financial statements of foreign subsidiaries are translated using functional currencies: As these companies have organizational, financial, and commercial independence, the respective local currency is identical to the functional currency. Assets and liabilities are translated according to the price on the balance-sheet date, and expenses and income according to monthly averages. Currency translation differences are posted as such under equity, but not recognized in net profit or loss for the period.

In the individual financial statements for consolidated companies, foreign-currency items are translated on the balance-sheet date, and included in net profit or loss for the period. Translation differences from long-term intercompany cash items are excepted from this rule. These are posted as other comprehensive income under equity, but not recognized in net profit or loss for the period.

Cash on hand and bank balances

This item includes cash and short-term investments, plus short-term cash equivalents.

Cash equivalents are short-term, highly liquid financial investments which can be converted to cash at any time, and which are only subject to immaterial fluctuations in value.

Securities and financial assets

Financial assets are initially valued at the cost of acquisition, including transaction costs. The subsequent valuation depends on their classification.

Financial assets which are available for sale are valued according to their price on the balance-sheet date (i.e. the fair market value). Price gains or losses are posted as other comprehensive income under equity, but not recognized in net profit or loss for the period.

Software AG uses hedging instruments to protect against the risks posed by worldwide currency fluctuations. Company policy is to hedge against currency risks in their totality, and not take specific action for each individual transaction. Open positions in futures transactions are valued at the fair market price, and listed on the balance sheet under securities held for trading purposes. Price gains or losses are included in the net income figure for the relevant year.

Financial assets are recorded at their individual fair market values where this is possible to calculate and the assets have not been held until maturity. Loans and receivables included under this item which are not held for trading purposes, and assets with no publicly available price on an active market, where it is not possible to reliably calculate a fair market price, are valued at the adjusted cost of acquisition. All values are subject to regular, objective impairment testing, and value impairment, where it has occurred, is reflected in earnings for the period.

Inventories

Inventories are recorded at the lower of cost of acquisition/manufacture or net realizable value. Net realizable value is the estimated amount that would be raised from a sale during normal operations, less the estimated costs arising until manufacture is complete, and less sales costs.

Trade receivables

Trade receivables are posted at the fair value applicable when revenues are realized or services provided, and valued at the net book value, less any necessary value adjustments.

This item also includes unbilled services from projects for which a fixed price has been agreed, but for which the percentage of completion method is applied.

Other current assets

Other current assets are valued at cost of acquisition, which corresponds to fair market value.

Intangible assets
Concessions, industrial and similar rights and assets, and licenses to such rights are capitalized at cost of acquisition and amortized over their useful economic lives according to the straight-line method. These assets are regularly subject to impairment testing.

Goodwill
Debit balances arising from capital consolidation as defined by HGB are calculated according to book value, with no disclosure of hidden reserves. Before January 31, 2001, balances were offset against capital reserves, pursuant to Section 309, Subsection 1 of HGB. After this date, goodwill was capitalized and amortized over ten years according to the straight-line method. The term over which goodwill is amortized is established at the time of the acquisition, based on the useful economic life of the goodwill. Software AG makes use of IFRS 1.13, which allows the Company to retain HGB valuations of goodwill arising before the transition to IFRS accounting on January 1, 2003. In accordance with IFRS 3, the historical HGB valuation of goodwill was posted at €176,591 thousand on this date. IFRS 3 requires that goodwill is no longer amortized, but subject to regular impairment testing and examination of its future useful economic life. The residual book value is written down to its fair value where the value has been impaired.

Property, plant and equipment
Property, plant and equipment are stated at cost of acquisition or manufacture less accumulated depreciation and impairment costs. Where items are sold or scrapped, the relevant cost of acquisition and accumulated write-downs are eliminated – any realized income/loss from the disposal of the asset is shown on the income statement.

Tangible assets acquired for €410 or less are fully written down in the year they are first posted.

Cost of acquisition/manufacture comprises purchase price, including any customer payments and non-refundable income tax, and costs that are directly attributable to preparing the asset for its intended use. Expenditure such as maintenance incurred once the asset is in use is posted in the period during which it is incurred. Subsequent expenditure is only booked under assets where this improves the condition of the asset beyond its originally assessed standard of performance. Financing costs are not included under cost of acquisition/manufacture.

Property, plant and equipment are depreciated over their useful economic lives according to the straight-line method:

Buildings	50 years
Improvements to property	8 – 10 years
Office and plant equipment	3 – 13 years
Computer and equipment	1 – 4 years

Useful economic lives and methods of depreciation are periodically examined to ensure that theoretical values correspond with actual expected values.

Assets under construction are allocated to unfinished property, plant and equipment, and stated at cost of acquisition/manufacture. Depreciation only takes place once manufacture is complete and the asset is in use.

Impairment of the value of intangible assets and property, plant and equipment
Where there is evidence that the value of intangible assets, property, plant and equipment has been impaired, these are immediately written down to their recoverable values, i.e. the higher of net realizable value and value in use. Value in use is the cash value of forecast future cash flows from the continued use of an asset and from disposal at the end of its useful economic life.

Leasing

Fixed assets include assets provided under leasing contracts. Software AG leases property, plant, and equipment. According to IAS 17, leasing contracts are classified as capital leases (where the leased asset is allocated to the lessee) or operating leases (where the leased asset is allocated to the lessor).

Capital leases: Leased items are posted on the balance sheet under both assets and leasing liabilities (at the same amount). The fair market value of the leased item at the beginning of the contract is used, or, where less, the cash value of the total minimum leasing payments. Calculation of this cash value is based on the interest rate of the overall lease agreement, where this figure can be practically identified. Otherwise, the lessee's threshold borrowing interest rate is used. Capital leases are amortized over their scheduled useful economic lives according to the straight-line method. Future lease installments are posted as financial liabilities.

Operating leases: Operating lease payments are expensed throughout the life of the leasing agreement.

Deferred taxes

Tax assets and liabilities are deferred according to the balance-sheet liability method for temporary differences between figures stated for tax purposes and those on the consolidated balance sheets. Taxes are also deferred on loss carryforwards.

Deferred taxes are calculated according to the tax rate expected to apply in the year in which they will be realized. Dividends are only included once the annual shareholders' meeting has voted on the use of earnings.

Deferred tax assets and liabilities are not discounted.

The book values of deferred taxes are regularly examined and, where necessary, adjusted.

Prepaid expenses

This item includes prepayments made by Software AG within the scope of license and rental agreements. Amounts are reversed and booked as expense in the accounting period when the service is delivered to Software AG.

Liabilities

Short-term liabilities are stated at their repayment or fulfillment value.

Long-term liabilities are stated at adjusted cost of acquisition, calculated according to the effective interest method, i.e. by discounting expected future repayments.

Provisions

Provisions are formed where the Company has a de jure or de facto obligation to a third party arising from an event in the past, where it is likely that the Company will have to settle this obligation, and a reliable estimate can be made of the value of the liability. Estimates are subject to regular scrutiny and adjustment.

Where the interest effect is material, the valuation of a provision is the present value of the expenditures expected to be required to settle the obligation.

Provisions for pensions

Software AG operates both defined-benefit and defined-contribution pension plans. The actuarial calculation of provisions for pensions follows the projected unit credit method described in IAS 19, whereby expected future increases in pensions and salaries are also included.

For the defined-contribution plan, Software AG has no obligations beyond its undertaking to pay all contributions to earmarked funds.

Deferred income

Deferred income includes prepayments from customers for maintenance services. Amounts are reversed and posted as revenue in the period Software AG delivers the service.

Other comprehensive income

Other comprehensive income comprises differences arising from the translation of the financial statements of commercially independent non-German subsidiaries, and effects from the valuation of financial instruments. Also included are translation differences from cash positions that are primarily part of a net investment in a commercially independent non-German subsidiary. Figures are quoted after tax.

Equity

Development of shareholders equity is shown on page 13.

In addition, contingent capital at March 31, 2004, comprised the following amounts:

1.) Up to €3,357 thousand in up to 1,118,962 no-par value shares, reserved to cover subscription rights granted under the first share-option plan (Management Incentive Plan I, MIP I) for Executive Board members and senior executives of the Software AG Group. The terms and conditions of this plan, as well as the numbers of shares allocated/exercised, are given under 8 e).
2.) Up to €3,000 thousand in up to 1,000,000 no-par value shares, reserved to cover subscription rights granted under the second share-option plan (Management Incentive Plan II, MIP II) for Executive Board members and senior executives of the Software AG Group. The terms and conditions of this plan, as well as the numbers of shares allocated/exercised, are given under 8 e).
3.) Up to €13,515 thousand in up to 4,505,000 no-par value shares, reserved to grant option rights to holders of warrants from cum-warrant bonds, and to grant conversion options to holders of convertible bonds in accordance with the bonds' terms. The Executive Board is authorized to issue such bonds, with a term of up to 10 years, once or more than once in the period to April 27, 2006, up to a total nominal value of €500,000 thousand. The Executive Board did not make use of this authorization in the first quarter of fiscal 2004.

At the balance-sheet date, the Executive Board is further authorized, with the consent of the Supervisory Board, to increase the Company's subscribed capital by up to €37,989 thousand once or more than once in the period to April 27, 2006, by issuing up to 12,663,036 registered shares against cash and/or non-cash contributions (authorized capital). With the exception of the cases detailed below, shareholders will be granted pre-emptive subscription rights:

- The Executive Board is authorized to deviate from shareholders' pre-emptive subscription rights with respect to fractional amounts.
- The Executive Board is further authorized, with the consent of the Supervisory Board, to deviate from shareholders' pre-emptive subscription rights with respect to capital increases against non-cash contributions effected for the purpose of acquiring participations, holdings, companies or business units.
- The Executive Board is also authorized, with the consent of the Supervisory Board, to deviate from shareholders' pre-emptive subscription rights provided that the capital increase against cash effected on the basis of this authorization does not exceed 10 percent of the subscribed capital at the time this authorization is first exercised, and provided that the issue price is not significantly lower than the market value.

- Finally, the Executive Board is authorized, with the consent of the Supervisory Board, to deviate from shareholders' pre-emptive subscription rights with respect to a nominal amount not exceeding €6,503 thousand in order to offer new shares to employees of Software AG and its affiliated companies (in accordance with sections 15 ff. of the German Stock Corporation Act) under an employee share option plan. The new shares can also be transferred to a bank on condition that sale is restricted to entitled persons in accordance with the Company's instructions.

Revenues

Software AG primarily generates revenues from software licenses (for unlimited periods of usage), maintenance, and other services. Incoming monies from software licenses are only posted as revenues once a contract has been signed with the customer, all possible rights of return have expired, the software has been supplied, and a price has been agreed or can be established, and there is sufficient probability that payment will be made.

Maintenance revenues are prorated over the period of service provision.

Revenues from contract work invoiced according to man-hours are recognized once the services have been provided by Software AG.

Pursuant to IAS 11 and IAS 18, revenues from fixed-price service contracts are recognized according to the percentage of completion method where the revenues can be reliably measured, there is sufficient probability that Software AG will receive the economic benefits of the transaction, and that all related costs expected until completion of the service can be reliably measured.

Revenues figures are net of all discounts and rebates.

Costs of manufacture

Costs of manufacture include all production-related costs on the basis of normal utilization levels. They include individual unit costs that can be directly allocated to projects, plus fixed and variable overheads. Borrowing costs are not capitalized in costs of acquisition/manufacture. No unscheduled write-downs on inventories were required during the reporting period.

Research and development costs

Research and development costs are expensed in the income statement as they are incurred.

The creation of and subsequent improvements to software involve closely linked, highly interwoven research and development phases. Accordingly, it is not possible to strictly separate expenses incurred for research from those incurred for development, and the criteria for separately reporting development costs laid out in IAS 38, Section 41, in conjunction with 42, cannot be met.

Sales, marketing and distribution

These include personnel and materials costs, write-downs, and advertising expenses.

Administrative costs

These include personnel and materials costs, and write-downs.

Earnings per share

Earnings per share are calculated by dividing net income allocable to shareholders for the period by the weighted number of shares outstanding during the period. Software AG only has common stock.

Notes on the first-time application of IAS/IFRS

Accounting and valuation

Pursuant to IFRS 1, International Accounting Standards (IAS)/International Financial Reporting Standards (IFRS) are applied retrospectively upon their initial adoption. Figures from previous periods are adjusted accordingly to allow effective comparison.

New standards published as part of the International Accounting Standards Board Improvement Project in December 2003, whose application is not compulsory until January 1, 2005, have not been employed for these financial statements.

Of the new standards published during the previous quarter, whose application is not compulsory until January 1, 2005, or later, Software AG chose to apply the provisions of IFRS 3 relating to the impairment testing of goodwill to these financial statements.

Application of IAS/IFRS involves the following material deviations from the accounting and valuation principles set out in German law:

- Goodwill is no longer amortized, but subject to regular impairment testing
- Securities available for sale are valued at their fair market value, even where this exceeds the cost of acquisition. Gains and losses are included in other comprehensive income under equity, but are not recognized in net profit or loss.
- Derivative instruments are valued at their fair market value, even where this exceeds the cost of acquisition. Both gains and losses are recognized in net profit or loss for the period.
- Revenues are recognized according to the percentage-of-completion method.
- Property is depreciated according to its useful economic life, and not according to tax scales.
- Finance leases, according to the more restrictive IFRS provisions, are posted as assets and leasing liabilities.
- Provisions are only formed where obligations to third parties exist, and the probability that these obligations will be fulfilled is at least 50 percent. Medium and long-term provisions are stated at cash values. Provisions are not formed for failure to perform maintenance or for other expenses.
- Provisions for pensions are formed according to the projected unit credit method.
- Deferred taxes are calculated according to the balance-sheet liability method. Deferred taxes on loss carryforwards are formed where the Company expects to be able to make use of these loss carryforwards.
- Cash positions in foreign currencies are valued at the balance-sheet-date rate and recognized in net profit or loss for the period. However, translation differences from long-term intra-Group cash positions are posted in other comprehensive income under equity, but are not recognized in net profit or loss for the period.

Balance-sheet reconciliation on January 1, 2003 (HGB to IFRS)

€ thousands	Note	HGB Jan 1, 2003	Income Statement related changes	Reclassifications	IFRS Jan 1, 2003
Assets					
A. Cash and cash equivalents					
Cash in hand and bank balances		75,423	0	0	75,423
Securities		0	0	0	0
		75,423	**0**	**0**	**75,423**
B. Current assets					
Inventories	(1)	4,628	0	– 3,873	755
Trade receivables	(1)	122,160	616	3,873	126,649
Other receivables and other assets	(2)	10,395	1,048	0	11,443
		137,183	**1,664**	**0**	**138,847**
C. Fixed assets					
Intangible assets		1,551	0	0	1,551
Goodwill		176,591	0	0	176,591
Property, plant and equipment	(3)	37,000	15,776	0	52,776
Financial assets	(4)	5,937	9,909	0	15,846
		221,079	**25,685**	**0**	**246,764**
D. Deferred taxes	(5)	**188**	**38,060**	**0**	**38,248**
E. Deferred expenses		**6,947**	**0**	**0**	**6,947**
Total assets		**440,820**	**65,409**	**0**	**506,229**
Equity and liabilities					
A. Current liabilities					
Current financial liabilities	(6)	3,395	3,016	0	6,411
Trade payables	(7)	13,992	0	8,474	22,466
Other current liabilities	(7)	18,046	0	12,934	30,980
Current provisions	(8)	97,950	– 16,110	– 28,413	53,427
		133,383	**– 13,094**	**– 7,005**	**113,284**
B. Non-current liabilities					
Non-current financial liabilities	(6)	0	8,395	0	8,395
Trade payables		0	0	0	0
Other non-current liabilities	(7)	448	0	3,393	3,841
Provisions for pensions	(9)	8,781	10,653	0	19,434
Non-current provisions	(7)	0	0	3,612	3,612
		9,229	**19,048**	**7,005**	**35,282**
C. Deferred taxes	(5)	**2,012**	**14,994**	**0**	**17,006**
D. Deferred income		**81,728**	**0**	**0**	**81,728**
E. Equity					
Share capital		81,800	0	0	81,800
Capital reserves		132	0	0	132
Retained earnings		132,959	34,552	– 18,153	149,358
Consolidated income		0	0	0	0
Currency translation differences		– 423	0	423	0
Other comprehensive income	(10)	0	9,909	17,730	27,639
		214,468	**44,461**	**0**	**258,929**
Total equity and liabilities		**440,820**	**65,409**	**0**	**506,229**

Notes on the balance-sheet reconciliation from HGB to IFRS (January 1, 2003):

(1) Work in progress as defined by HGB was recognized and invoiced according to the percentage of completion method (including margin).

(2) Derivative instruments are valued at fair market value, even where this exceeds the cost of acquisition.

(3) Depreciation of property was adjusted to take account of expected useful economic lives. Assets from capital leases were capitalized.

(4) This change is a result of the fair-market valuation of securities. The change is included in other comprehensive income under equity, but not recognized in net profit or loss for the period.

(5) Deferred tax assets are primarily formed for loss carryforwards and provisions. Deferred tax liabilities are primarily formed for deferred expense and property, plant and equipment.

(6) Long and short-term financial liabilities include capitalized liabilities from capital leases.

(7) Certain provisions under HGB were reclassified as short or long-term liabilities to comply with IFRS.

(8) The adjustment of provisions (recognized in net profit or loss) primarily comprises dissolved provisions for expenses (maintenance, guarantees) and provisions where the probability of the obligation having to be settled is less than 50 percent (legal costs, contingent losses, general risks). Reclassifications comprise provisions which, according to IFRS, are to be posted as liabilities. See also note (7).

(9) The increase in pension provisions is primarily a result of the requirement under IFRS to include indirect pension obligations at SAG UK. These were not previously included, in accordance with the option granted by Article 28 of the Introductory Act to the German Commercial Code (EGHGB).

(10) Other comprehensive income includes unrealized gains from the fair-market valuation of securities and differences from the translation of long-term intra-Group cash positions in foreign currencies (i.e. not in euros).

Reconciliation of equity on January 1, 2003 (HGB to IFRS)

€ thousands	Note	
Equity in accordance with HGB as at Jan 1, 2003		**214,468**
Revenue recognized according to percentage of completion	(1)	616
Depreciation of buildings	(3)	8,884
Finance leases	(3), (6)	– 4,519
Market value of securities and financial derivatives	(2), (4)	10,957
Deferred tax assets	(5)	38,060
Adjustments to other provisions	(8)	16,110
Adjustments to pension provisions	(9)	– 10,653
Deferred tax liabilities	(5)	– 14,994
Equity in accordance with IFRS as at Jan 1, 2003		**258,929**

Balance-sheet reconciliation on March 31, 2003 (HGB to IFRS)

€ thousands	Note	HGB March 1, 2003	Income Statement related changes	Reclassifications	IFRS March 1, 2003
Assets					
A. Cash and cash equivalents					
Cash in hand and bank balances		51,730	0	0	51,730
Securities		29,154	0	0	29,154
		80,884	**0**	**0**	**80,884**
B. Current assets					
Inventories	(1)	5,681	0	– 5,264	417
Trade receivables	(1)	111,607	1,865	5,264	118,736
Other receivables and other assets	(4)	13,657	844	0	14,501
		130,945	**2,709**	**0**	**133,654**
C. Fixed assets					
Intangible assets		1,380	0	0	1,380
Goodwill	(2)	171,128	5,463	0	176,591
Property, plant and equipment	(3)	36,749	15,618	0	52,367
Financial assets	(4)	6,398	9,337	0	15,735
		215,655	**30,418**	**0**	**246,073**
D. Deferred assets	(5)	**30,339**	**18,748**	**0**	**49,087**
E. Deferred expenses		**10,203**	**0**	**0**	**10,203**
Total assets		**468,026**	**51,875**	**0**	**519,901**
Equity and liabilities					
A. Current liabilities					
Current financial liabilities	(6)	2,001	3,016	0	5,017
Trade payables	(7)	11,497	6	8,742	20,245
Other current liabilities	(7)	16,180	0	15,390	31,570
Current provisions	(8)	112,584	– 7,669	– 30,980	73,935
		142,262	**– 4,647**	**– 6,848**	**130,767**
B. Non-current liabilities					
Non-current financial liabilities	(6)	0	8,140	0	8,140
Trade payables		0	0	0	0
Other non-current liabilities	(7)	272	0	3,393	3,665
Provisions for pensions	(9)	8,374	10,653	0	19,027
Non-current provisions	(7)	0	0	3,455	3,455
		8,646	**18,793**	**6,848**	**34,287**
C. Deferred taxes	(5)	**3,963**	**12,307**	**0**	**16,270**
D. Deferred income		**96,290**	**0**	**0**	**96,290**
E. Equity					
Share capital		81,800	0	0	81,800
Capital reserves		132	0	0	132
Retained earnings		146,017	21,494	– 18,153	149,358
Consolidated income		– 9,694	– 5,409	332	– 14,771
Currency translation differences	(10)	– 1,390	0	– 6,989	– 8,379
Other comprehensive income	(11)	0	9,337	24,810	34,147
		216,865	**25,422**	**0**	**242,287**
Total equity and liabilities		**468,026**	**51,875**	**0**	**519,901**

Notes on the balance-sheet reconciliation from HGB to IFRS (March 31, 2003):

(1) Work in progress as defined by HGB was recognized and invoiced according to the percentage of completion method (including margin).

(2) Scheduled amortization of goodwill pursuant to HGB was reversed as, according to IFRS 1, where IFRS 3 is voluntarily applied to 2004, it should also be applied to 2003. Accordingly, 2003 goodwill was not amortized according to the straight-line method.

(3) Depreciation of property was adjusted to take account of expected useful economic lives. Assets from capital leases were capitalized.

(4) This change is a result of the fair-market valuation of securities. The change is included in other comprehensive income under equity, but not recognized in net profit or loss for the period. Derivative instruments are valued at fair market value, even where this exceeds the cost of acquisition.

(5) Deferred tax assets are primarily formed for loss carryforwards and provisions. Deferred tax liabilities are primarily formed for deferred expense and property, plant and equipment.

(6) Long and short-term financial liabilities include capitalized liabilities from capital leases.

(7) Certain provisions under HGB were reclassified as short or long-term liabilities to comply with IFRS.

(8) The adjustment of provisions (recognized in net profit or loss) primarily comprises dissolved provisions for expenses (maintenance, guarantees) and provisions where the probability of the obligation having to be settled is less than 50 percent (legal costs, contingent losses, general risks). Reclassifications comprise provisions which, according to IFRS, are to be posted as liabilities. See also note (7).

(9) The increase in pension provisions is primarily a result of the requirement under IFRS to include indirect pension obligations at SAG UK. These were not previously included, in accordance with the option granted by Article 28 of the Introductory Act to the German Commercial Code (EGHGB).

(10) The change in currency translation differences arose primarily from the fact that, as permitted by IFRS 1.22, the HGB figure was reset to zero for the IFRS statements on January 1, 2003. From this date, only IFRS currency translation adjustments were recorded.

(11) Other comprehensive income includes unrealized gains from the fair-market valuation of securities and differences from the translation of long-term intra-Group cash positions in foreign currencies (i.e. not in euros).

Reconciliation of equity on March 31, 2003 (HGB to IFRS)

€ thousands	Note	
Equity in accordance with HGB at March 31, 2003		**216,865**
Revenue recognized according to percentage of completion	(1)	1,865
Adjustment to goodwill amortization	(2)	5,463
Depreciation of buildings	(3)	8,893
Finance leases	(3), (6)	– 4,431
Fair-market valuation of securities and financial derivatives	(4)	10,181
Deferred tax assets	(5)	18,748
Adjustments to other provisions	(8)	7,669
Adjustments to pension provisions	(9)	– 10,653
Deferred tax liabilities	(5)	– 12,307
Other		– 6
Equity in accordance with IFRS at March 31, 2003		**242,287**

Reconciliation of net income on March 31, 2003 (HGB to IFRS)

€ thousands	Note	
Net loss in accordance with HGB at March 31, 2003		**– 9,694**
Revenue recognized according to percentage of completion	(1)	1,249
Adjustment to goodwill amortization	(2)	5,463
Depreciation of buildings	(3)	9
Finance leases	(3), (6)	88
Fair-market valuation of securities and financial derivatives	(4)	– 204
Deferred tax assets	(5)	– 6,254
Adjustments to other provisions	(8)	– 8,441
Adjustments to pension provisions	(9)	0
Deferred tax liabilities	(5)	2,687
Other		326
Net loss in accordance with IFRS at March 31, 2003		**– 14,771**

Seasonal effects

The following table shows a breakdown of revenues and pre-tax profits (adjusted for restructuring costs) over the four quarters of 2003:

€ thousands	Q1 2003	Q2 2003	Q3 2003	Q4 2003	2003
Revenues	103,140	103,136	98,680	115,086	420,042
% of revenues at year-end	24.6 %	24.5 %	23.5 %	27.4 %	100.0 %
Pre-tax profit	8,728	18,241	16,426	18,420	61,815
% of net income at year-end	14.1 %	29.5 %	26.6 %	29.8 %	100.0 %

Revenues developed similarly to previous years – largely in line with the sales cycle. Software AG expects a similar pattern for fiscal 2004.

Contingent liabilities

At March 31, 2004, no provisions had been formed for the following contingent liabilities (stated at face values), for which it was deemed improbable that the Company would have to fulfill obligations:

€ thousands	
Bank guarantees	5,509
Other	810
	6,319

Share-option plans

The Software AG Group runs various share-option plans for Executive Board members, senior executives, and other employees which are not expensed in the consolidated financial statements.

First share-option plan:

At March 31, 2004, Executive Board members held 145,846 subscription rights to shares in the Company, and senior executives 69,069 – unchanged over March 31, 2003. These could not be exercised before March 31, 2004. Options have a term of seven years from the date on which they are granted, and may only be exercised, after an initial blocking period of 24 months as of the Software AG IPO, quarterly, after the publication of quarterly, biannual, and annual earnings figures.

The subscription price per share is the issue price less a 20 percent mark-down, but no less than €28.12 (DM 55.00). As Company stock was floated at €30, this minimum applied.

Holders of subscription rights must fulfill the following three conditions before they may exercise their conversion rights:

- Consolidated earnings from ordinary activities (according to HGB) must have increased by 30 percent between 1997 and 1999.
  This condition was fulfilled between 1997 and 1999.
- Consolidated earnings from ordinary activities (according to HGB) must total at least 10 percent of revenues for the fiscal year prior to conversion.
- The share price must exceed the minimum conversion price.

Second share-option plan:
At March 31, 2004, Executive Board members held 232,250 subscription rights to shares in the Company, and senior executives 309,350. These rights could not be exercised before March 31, 2004. In the relevant period, 41,125 new options from this plan were issued to Executive Board members, and 15,175 to senior executives during the first quarter. However, these rights could not be exercised.

The subscription price is the average XETRA closing price over the previous five trading days on the Frankfurt Stock Exchange before the date of conversion.

Holders of subscription rights must fulfill the following two conditions before they may exercise their conversion rights:

- Consolidated revenues must have increased for the fiscal year prior to conversion by at least 10 percent in comparison to the previous year.
- Consolidated earnings from ordinary activities (according to HGB) must total at least 10 percent of revenues for the year prior to conversion.

The terms, blocking period, and conversion dates correspond to those of the first share-option plan.

Other financial obligations

Software AG has entered into rental and leasing contracts for buildings, real estate, IT and PBX systems, and vehicles. Obligations from these contracts (where the contracts are still within their minimum durations) until the end of fiscal 2004 total €13,482 thousand. Obligations until the end of fiscal 2008 total €29,919 thousand. The leasing contracts are operating leases as defined by IAS 17.

Employees

The Software AG workforce averaged 2,519 during the first quarter of 2004, and totaled 2,512 on March 31, 2004.

Executive Board and Supervisory Board

The composition of the Executive Board and Supervisory Board at March 31, 2003, was unchanged in comparison to December 31, 2003.

Events subsequent to the balance-sheet date

Sale of SAP SI stake boosts earnings per share
In April 2004, Software AG signed a contract to transfer its 1,272,100-strong stockholding in SAP Systems Integration AG (SAP SI) to SAP AG, Walldorf, in return for a payment of €20.40 per share. The sale will generate €26.0 million for Software AG, which will further strengthen liquidity. As a result of this transaction, an extraordinary profit of €24 million will be posted for the second quarter. This €0.88 per share profit is expected to lift full-year EPS to between €2.50 to €2.60.

By resolution of the annual shareholders' meeting on April 30, 2004, Dr. Andreas Bereczky, Director of Production at German public-service TV broadcaster ZDF, Mainz, was elected to succeed Dr. Peter Lex on the Software AG Supervisory Board.

Financial Calendar 2004

July 29	Q2 earnings figures
September 30	HVB German Investment Conference, Munich, Germany
October 28	Q3 earnings figures
November 23/24	German Equity Forum, Deutsche Börse AG, Frankfurt, Germany

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