

**RHETORICAL SYSTEMS LIMITED**  
**REPORT AND FINANCIAL STATEMENTS**  
**YEAR ENDED 31 DECEMBER 2002**

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205735



**RHETORICAL SYSTEMS LIMITED**  
**REPORT AND FINANCIAL STATEMENTS**  
**YEAR ENDED 31 DECEMBER 2002**

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**RHETORICAL SYSTEMS LIMITED**  
**OFFICERS AND PROFESSIONAL ADVISERS**

<b>DIRECTORS :</b>	MFJ Moens PA Taylor AL Robison JR Oberlander
<b>SECRETARY:</b>	AL Robison
<b>REGISTERED OFFICE :</b>	Saltire Court 20 Castle Terrace Edinburgh EH1 2ET
<b>AUDITORS :</b>	LWC Audit Limited 18 Greenside Lane Edinburgh EH1 3AH
<b>BANKERS :</b>	Bank of Scotland The Mound Edinburgh EH1 1YZ
<b>SOLICITORS :</b>	Shepherd & Wedderburn WS Saltire Court 20 Castle Terrace Edinburgh EH1 2ET
<b>COMPANY NUMBER :</b>	SC 205735

**RHETORICAL SYSTEMS LIMITED**  
**DIRECTORS' REPORT**  
**YEAR ENDED 31 DECEMBER 2002**

The directors present their report and the audited financial statements for the year ended 31 December 2002.

**1 ACTIVITIES**

The principal activities of the company are the research, development and sale of text to speech software and the provision of related consultancy services.

**2 RESULTS, DIVIDENDS AND FUTURE PROSPECTS**

The results for the year are disclosed on page 5. No dividend is proposed and the loss of £1,013,000 (2001 loss (as restated): £1,400,000) has been transferred to reserves.

The directors are satisfied with the development of the company and will continue to pursue appropriate business opportunities. Further details of activities during the year and future prospects are included within the Directors' Report of the ultimate parent undertaking, Rhetorical Group plc.

**3 DIRECTORS**

The present membership of the board is set out on page 1.

The interest of the directors who served during the period in the shares of the company were as follows:-

	Ordinary Shares Of £0.01 each 31 December 2002	Ordinary Shares Of £0.01 each 31 December 2001
MFJ Moens	-	-
PA Taylor	-	-
JR Oberlander	-	-
AL Robison	-	-
MS Durrant (resigned 1 May 2002)	-	-

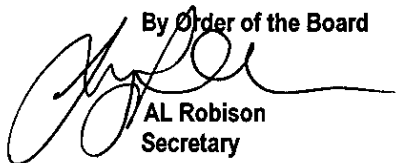
The company is a wholly owned subsidiary of Rhetorical Group plc. The interests of the directors in the shares of Rhetorical Group plc are disclosed in the accounts of that company.

**4 AUDITORS**

As part of a re-organisation of their business, on 31 December 2002, Lyon Windram Crolla resigned as auditors of the company. LWC Audit Limited was appointed by the directors with effect from 1 January 2003 to fill the resulting vacancy.

LWC Audit Limited will be proposed for reappointment in accordance with Section 385 of the Companies Act 1985.

24 March 2003

By Order of the Board  
  
AL Robison  
Secretary

**RHETORICAL SYSTEMS LIMITED**  
**STATEMENT OF DIRECTORS' RESPONSIBILITIES**

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing those financial statements, the directors are required to:-

- Select suitable accounting policies and then apply them consistently;
- Make judgements and estimates that are reasonable and prudent;
- Prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and to enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.



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## AUDITORS' REPORT TO THE SHAREHOLDERS

OF

### RHETORICAL SYSTEMS LIMITED

We have audited the financial statements of Rhetorical Systems Limited for the year ended 31 December 2002 on pages 5 to 15. These Financial Statements have been prepared under the historic cost convention and the accounting policies set out on pages 8 and 9.

This report is made solely to the company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

#### Respective responsibilities of directors and auditors

As described on page 3 the company's directors are responsible for the preparation of financial statements which are in accordance with applicable law and United Kingdom Accounting Standards.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Report of the Directors is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions with the company is not disclosed.

We read the Report of the Directors and consider the implications for our report if we become aware of any apparent misstatement within it.

#### Basis of opinion

We conducted our audit in accordance with United Kingdom Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

#### Opinion

In our opinion the financial statements give a true and fair view of the state of the company's affairs as at 31 December 2002 and of its loss for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

24 March 2003

*LWC Audit Limited*

LWC Audit Limited  
Registered Auditors  
Edinburgh

Directors:  
John McLeod, Aidan McLaughlin.

Registered office: 18 Greenside Lane, Edinburgh EH1 3AH  
Company Number: SC234008

**RHETORICAL SYSTEMS LIMITED**  
**PROFIT AND LOSS ACCOUNT**  
**YEAR ENDED 31 DECEMBER 2002**

	Note	£ '000	2001 (as restated) £ '000
<b>TURNOVER</b>	<b>4</b>	1,244	865
Cost of sales		93	731
<b>GROSS PROFIT</b>		1,151	134
Administrative expenses		2,689	1,760
Other operating income		405	92
<b>OPERATING LOSS</b>	<b>5</b>	(1,133)	(1,534)
Interest receivable and similar income		139	82
<b>LOSS ON ORDINARY ACTIVITIES BEFORE TAXATION</b>		(994)	(1,452)
Tax (charge)/credit on ordinary activities	<b>7</b>	(19)	52
<b>LOSS ON ORDINARY ACTIVITIES AFTER TAXATION</b>	<b>15</b>	(1,013)	(1,400)
		=====	=====

Turnover and operating loss for the year derive wholly from continuing operations.

**RHETORICAL SYSTEMS LIMITED**  
**STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES**  
**YEAR ENDED 31 DECEMBER 2002**

	£ '000	2001 (as restated) £ '000
<b>Loss for the financial year</b>	(1,013) -----	(1,400) -----
Total recognised gains and losses relating to the financial year	(1,013)	(1,400) =====
Prior year adjustment (note 3)	(562) -----	
<b>Total gains and losses recognised since last annual report.</b>	<b>(1,575)</b> =====	



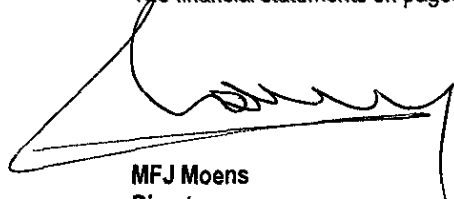
# RHETORICAL SYSTEMS LIMITED

## BALANCE SHEET

AT 31 DECEMBER 2002

	Note	£ '000	£ '000	2001 (as restated) £ '000
<b>FIXED ASSETS</b>				
Intangible assets	8		45	60
Tangible assets	9		368	423
			413	483
<b>CURRENT ASSETS</b>				
Debtors	11	1,015		439
Cash at bank and in hand		2,201		4,354
		3,216		4,793
<b>CREDITORS: Amounts falling due within one year</b>	12	6,106		6,726
<b>NET CURRENT LIABILITIES</b>			(2,890)	(1,933)
			(2,477)	(1,450)
<b>CREDITORS : Amounts falling due after one year</b>	13		(11)	(25)
			(2,488)	(1,475)
<b>CAPITAL AND RESERVES</b>				
Called up share capital	14		1	1
Share premium account	15		199	199
Profit and loss account	15		(2,688)	(1,675)
<b>EQUITY SHAREHOLDERS' FUNDS</b>	16		(2,488)	(1,475)

The financial statements on pages 5 to 15 were approved by the Board of Directors on 24 March 2003 and signed on its behalf by:

  
MFJ Moens  
Director

**RHETORICAL SYSTEMS LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**YEAR ENDED 31 DECEMBER 2002**

**1 ACCOUNTING POLICIES**

**a) Accounting Convention**

The financial statements have been prepared in accordance with applicable accounting standards and under the historical cost convention.

**b) Going Concern**

The company's accounts are prepared on the going concern basis which assumes that continued financial support will be available from the ultimate parent company, Rhetorical Group plc. At the date of approval of the accounts, the directors of Rhetorical Group plc have indicated their continued support.

**c) Turnover**

Turnover derives from the principal activities of the company and is stated net of Value Added Tax.

Perpetual software licenses supplied are included in turnover when software has been delivered against a binding obligation on the customer. All associated support revenues are recognised over the contract period.

In respect of funded development projects, turnover is recognised over the life of the project. Profit is recognised from the point at which the directors are satisfied as to the overall profitability of the project with reference to the achievement of applicable milestones included within the contract.

**d) Depreciation**

Depreciation is provided on all tangible fixed assets at rates calculated to write off the cost over the estimated lives of the assets.

The rates of depreciation are as follows:-

Leasehold Property	10% per annum straight line
Office Equipment	25% per annum straight line
Computer Equipment	33.3% per annum straight line

**e) Deferred Taxation**

Deferred taxation is provided at the anticipated tax rates on differences arising from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in the financial statements.

**RHETORICAL SYSTEMS LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**YEAR ENDED 31 DECEMBER 2002**

**1 ACCOUNTING POLICIES – Continued**

**f) Research & Development**

Research and development costs are written off in the year in which they are incurred.

The directors consider it appropriate to change the company's accounting policy in respect of expenditure incurred on the development of the company's products prior to June 2001. This change is designed to bring the company's accounting policies into line with wider industry practice. This change in accounting policy has required a prior year adjustment, as detailed in note 3. The company's previous accounting policy was to write off development expenditure as incurred except where the expenditure was in connection with a separately identifiable project on which revenue would be earned in future accounting periods. In such cases, the expenditure was capitalised and amortised against future revenue streams, having regard to the ultimate commercial viability of the product.

**g) Intangible Assets**

Intangible assets are capitalised and amortised in equal instalments over the directors' estimate of their useful economic life.

The database licence is amortised over five years.

**h) Hire Purchase and Finance Leases**

Assets obtained under finance leases and hire purchase contracts are capitalised at their fair value on acquisition and depreciated over their estimated useful lives. The finance charges are allocated over the period of the lease in proportion to the capital element outstanding.

Operating lease rentals are charged to income in equal annual amounts over the lease term.

**i) Pension Costs**

The company operates a defined contribution pension scheme. The assets of the scheme are held separately from those of the company in an independently administered fund. Contributions are charged to the profit and loss accounts as they become payable in accordance with the rule of the scheme.

**j) Foreign Currencies**

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies are translated at the rate of exchange ruling at the balance sheet date.

All differences are taken to the profit and loss account

**k) Grants**

Government grants in respect of revenue expenditure are recognised in the profit and loss account in line with the recognition of the related expenditure.

**RHETORICAL SYSTEMS LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**YEAR ENDED 31 DECEMBER 2002**

**2 GOING CONCERN**

The accounts have been prepared on a going concern basis which assumes that continued financial support will be made available by the parent company, Rhetorical Group plc.

At the date of approval of these accounts, the directors of Rhetorical Group plc have confirmed that continued support will be made available in accordance with the group business plan.

**3 PRIOR YEAR ADJUSTMENT**

As described in note 1, the company has changed its accounting policy in respect of development expenditure. Such expenditure is now charged to the profit and loss account as incurred. Had the previous accounting policy been applied in the current year, the amortisation charge to the profit and loss account would have been £180,000. The effect of the change in policy on the previous year's results is to increase the loss by £407,000, including a reduction in the amortisation charge for that period of £32,000, and to reduce brought forward profit and loss reserves brought forward at 1 January 2000, by £155,000.

**4 TURNOVER**

Turnover is stated net of value added tax and arises wholly from the principal activities of the company within the United Kingdom.

**5 OPERATING LOSS**

	£ '000	2001 (as restated) £ '000
<b>Operating Loss is stated after charging (crediting):</b>		
Depreciation on owned assets	149	75
Depreciation on fixed assets held under hire purchase	11	4
Amortisation of intangible assets	15	15
Auditors' remuneration	5	4
Payments under operating leases – rent	147	137
Research and development	1,342	1,239
Grants received	(302)	(92)
	=====	=====

**6 STAFF COSTS**

The average number of persons employed by the company, including directors, during the period was as follows:-

	No.	2001 No.
Management and administration	6	8
Production	30	27
Sales	9	3
	-----	-----
	45	38
	-----	-----

**RHETORICAL SYSTEMS LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**YEAR ENDED 31 DECEMBER 2002**

**6 STAFF COSTS (Continued)**

The aggregate payroll costs of these persons were as follows:-

	£ '000	2001 £ '000
Wages and salaries	1,695	1,248
Redundancy payments	15	-
Social Security	160	100
Other pension costs	82	44
	<u>1,952</u>	<u>1,392</u>
	=====	=====
 Directors' emoluments	 £ '000	 £ '000
Fees	-	47
Other emoluments	255	216
Pension contributions	14	10
	<u>269</u>	<u>273</u>
	=====	=====

Three directors (2001: 3) accrued benefits under the group defined contribution pension scheme.

The emoluments of the highest paid director (excluding pension contributions) were £83,000 (2001: £76,000).

During the prior year, AL Robison and MS Durrant were granted options to subscribe for shares in the ultimate parent company.

	Date Granted	Number	Exercise Price	Expiry Date
AL Robison	25 May 2001	100,000	58p	25 May 2011
	20 December 2001	50,000	67p	20 December 2011
MS Durrant	25 May 2001	100,000	58p	25 May 2011

The options are exercisable 33% two years after the date granted, 34% three years after the date granted and the remainder four years after the date granted.

Options granted to MS Durrant lapsed during the year and ended on his resignation from the company.

**7 TAX ON LOSS ON ORDINARY ACTIVITIES**

	£ '000	£ '000
Research and development tax credit	-	52
Overprovision for research and development tax credit in prior years	(19)	-
	<u>=====</u>	<u>=====</u>

The company has corporation tax losses of approximately £1,676,000 available to carry forward against future trading profits.

**RHETORICAL SYSTEMS LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**YEAR ENDED 31 DECEMBER 2002**

**8 INTANGIBLE FIXED ASSETS**

	<b>Database Licence £ '000</b>
<b>Cost</b>	
At 1 January 2002 (as restated)	75
Additions	-
	-----
At 31 December 2002	75
	-----
<b>Amortisation</b>	
At 1 January 2002 (as restated)	15
Charge for the year	15
	-----
At 31 December 2002	30
	-----
<b>Net Book Value</b>	
At 31 December 2002	45
	=====
At 31 December 2001 (as restated)	60
	=====

**9 TANGIBLE FIXED ASSETS**

	<b>Leasehold Property £ '000</b>	<b>Computer Equipment £ '000</b>	<b>Office Equipment £ '000</b>	<b>Total £ '000</b>
<b>Cost</b>				
At 1 January 2002	131	300	102	533
Additions	8	84	13	105
	-----	-----	-----	-----
At 31 December 2002	139	384	115	638
	-----	-----	-----	-----
<b>Depreciation</b>				
At 1 January 2002	3	97	10	110
Charge for the year	14	118	28	160
	-----	-----	-----	-----
At 31 December 2002	17	215	38	270
	-----	-----	-----	-----
<b>Net Book Value</b>				
At 31 December 2002	122	169	77	368
	=====	=====	=====	=====
At 31 December 2001	128	203	92	423
	=====	=====	=====	=====

The net book value of tangible fixed assets includes £30,000 (2001: £41,000) in respect of assets held under hire purchase and finance lease agreements.

**RHETORICAL SYSTEMS LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**YEAR ENDED 31 DECEMBER 2002**

**10 INVESTMENTS**

Rhetorical Systems Limited holds the entire issued share capital of Rhetorical Trustees Limited. Rhetorical Trustees Limited holds shares in Rhetorical Group plc in trust for the benefit of the employees of Rhetorical Systems Limited. The investment of £1 in Rhetorical Trustees Limited, a company registered in Scotland, is held at no value in the accounts.

**11 DEBTORS**

	£ '000	2001 £ '000
Trade debtors	253	39
Sundry debtors	197	237
Corporation tax recoverable	-	52
Amounts due by related parties	454	-
Prepayments and accrued income	111	111
	-----	-----
	1,015	439
	=====	=====

Included within sundry debtors is a rental deposit of £195,000 (2001: £195,000) which is recoverable after more than one year.

**12 CREDITORS: Amounts falling due within one year**

	£ '000	£ '000
Trade creditors	22	112
Accruals and deferred income	155	423
Other taxes and social security costs	61	37
Amounts due to related parties	5,852	5,908
Other creditors	1	231
Hire purchase and finance lease	15	15
	-----	-----
	6,106	6,726
	=====	=====

**13 CREDITORS : Amounts falling due after one year**

	£ '000	£ '000
Hire purchase and finance lease	11	25
	=====	=====

*Hire purchase and finance lease creditors are secured against the related assets and are wholly repayable within five years.*

**14 CALLED UP SHARE CAPITAL**

	£ '000	£ '000
<b>Authorised</b>		
102,000 Ordinary shares of £0.01 each	1	1
	=====	=====
<b>Allotted called up and fully paid</b>		
102,000 Ordinary shares of £0.01 each	1	1
	=====	=====

**RHETORICAL SYSTEMS LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**YEAR ENDED 31 DECEMBER 2002**

**15 RESERVES**

	<b>Share Premium Account</b>	<b>Profit &amp; Loss Account</b>	<b>Total</b>
	<b>£ '000</b>	<b>£ '000</b>	<b>£ '000</b>
At 1 January 2002 (as originally stated)	199	(1,113)	(914)
Prior year adjustment	-	(562)	(562)
	-----	-----	-----
At 1 January 2002 (as restated)	199	(1,675)	(1,476)
Movement in the year	-	(1,013)	(1,013)
	-----	-----	-----
At 31 December 2002	199	(2,688)	(2,489)
	=====	=====	=====

**16 RECONCILIATION OF MOVEMENTS IN  
SHAREHOLDERS' FUNDS**

	<b>2001 (as restated) £ '000</b>
Loss for the financial period	(993)
Opening shareholders' funds (as restated)	(482)
	-----
Closing shareholders' funds	(1,475)
	=====

The opening deficit on shareholders' funds at 31 December 2001 as previously reported amounted to £913,000 before the prior year adjustment of £562,000

**17 OPERATING LEASE COMMITMENTS**

At 31 December 2002, the company was committed, under a non-cancellable operating lease expiring after more than five years, to lease property at a current annual rental of £165,000.

**18 RELATED PARTY TRANSACTIONS**

In preparing these accounts, the company has taken advantage of exemption contained within Financial Reporting Standard 8 (Related Party Transactions) from the requirement to disclose transactions with other group companies.

**19 ULTIMATE CONTROLLING PARTY**

The ultimate controlling party is Rhetorical Group plc, which holds 100% of the ordinary shares.



**RHETORICAL SYSTEMS LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**YEAR ENDED 31 DECEMBER 2002**

**20 RHETORICAL GROUP EMPLOYEE BENEFIT TRUST**

The Rhetorical Group Employee Benefit Trust is the holder of 1,164,667 ordinary shares of £0.05 in Rhetorical Group plc (2001 : 1,194,000)

On 30 November 2000, 12,000 ordinary shares of £0.01 in Rhetorical Systems Limited were gifted to the Trust by JR Oberlander, a director of Rhetorical Systems Limited. Through the acquisition of Rhetorical Systems Limited by Rhetorical Group plc and subsequent sub-division of the issued share capital of Rhetorical Group plc (as described in note 13) this holding became 1,200,000 ordinary shares of £0.05 in Rhetorical Group plc.

As the transfer to the Trust was a gift there are no entries in the consolidated profit and loss account or the balance sheet in this respect.

*The market value of the shareholding, on the basis of the issue price of shares at 2 November 2001 is £780,192.*

Options are granted to employees under the terms of both an EMI and unapproved scheme at £nil cost, based on individual performance and basic salary. Options are due to be exercised between 2002 and 2012.

At 31 December 2001, 1,146,000 shares were under option to employees of Rhetorical Systems Limited and 40,000 shares are under option to another party. During the year 29,333 options were exercised, 100,000 lapsed and 183,333 were awarded to employees.

**RHETORICAL SYSTEMS LIMITED**  
**DETAILED PROFIT AND LOSS ACCOUNT**  
**YEAR ENDED 31 DECEMBER 2002**

		2001 (as restated) £ '000
	£ '000	£ '000
<b>TURNOVER</b>	1,244	865
<b>COST OF SALES</b>		-----
Direct staff costs	109	560
Other direct costs	126	135
Release of provisions	(231)	-
Depreciation	89	36
	-----	-----
	93	731
<b>GROSS PROFIT</b>	1,151	134
<b>ADMINISTRATIVE EXPENSES</b>		
Wages and salaries	1,852	920
Management charges	-	63
Recruitment	45	28
Recordings	54	60
Premises costs	202	195
Telephone	37	20
Depreciation	71	42
Amortisation	15	15
Travel and subsistence	136	70
Professional fees	71	135
Marketing	86	113
Other costs	100	96
Bad debts	7	-
Bank charges	1	2
Foreign currency charges	12	1
	-----	-----
	(1,538)	(1,760)
Grants received	302	92
<b>OPERATING LOSS</b>	(1,236)	(1,534)
<b>OTHER INCOME</b>		
Interest received	139	82
Rental income	7	-
Other income	96	-
	-----	-----
<b>LOSS ON ORDINARY ACTIVITIES BEFORE TAXATION</b>	(994)	(1,452)
	=====	=====