Developing
Pharmaceutical
Success....

ANNUAL REPORT **2005**

DEVELOPMENT OF IMPORTANT KEY FIGURES

in KEUR	2005	2004
Net sales	2,068	3,023
Result from operating activities	- 6,337	- 5,458
Period result	- 6,277	- 5,821
Earnings per share (EUR)	- 0.77	- 0.89
Shares in circulation (annual average; in thousands)	8,188	6,574
Equity	9,159	- 49
Equity ratio	81.5%	- 0.7%
Balance sheet total	11,244	6,730
Cash flows from operating and investing activities	- 5,833	- 4,474
Cash flows from financing activities	10,653	3,352
Net change in cash and cash equivalents	4,820	- 1,122
Cash and cash equivalents	6,878	2,058
Number of employees (annual average)	48	57

GENERAL INFORMATION

Management Board Dr Ulrich Dauer, CEO
Dr Gerhard Keilhauer, CDO
Dipl.-Kfm. Enno Spillner, CFO (since 16 September 2005)
Dr Daniel Vitt, CSO
Dr Stefan Busemann, CFO (until 2 August 2005)

Principal Office 4SC AG
Am Klopferspitz 19a
82152 Martinsried
Deutschland

MILESTONES 2005

February Commencement of the comprehensive research collaboration with the Japanese pharmaceutical group Sanwa Kagaku Kenkyusho (SKK). 4SC AG develops new drug candidates for two target proteins defined by SKK.

March Successful conclusion of the clinical phase 1 studies of the most advanced product candidate SC12267. This is a protein inhibitor for the treatment of rheumatoid arthritis that could potentially also be used against multiple sclerosis.

April Expansion of the research collaboration with Schwarz Pharma AG. The objective is the identification of an early development candidate for the prevention or treatment of an illness from the indication area of urology.

May Support from the Federal Ministry of Education and Research: the further research work on the latest project of 4SC AG, an ion channel blocker for the treatment of multiple sclerosis, is being supported with a total of EUR 1.2 million.

July The KfW Mittelstandsbank and Bayern Kapital participate in the second closing of the fourth round of financing.

November Successful conclusion of the pre-listing share capital increase with an overall volume of EUR 10.16 million.

December Listing of 4SC AG: since 15 December 2005, the company's shares have been traded on the German Stock Exchange in the Prime Standard.

CONTENTS OVERVIEW

DEAR SHAREHOLDERS

This is the first annual report of 4SC AG as a public company and I am pleased at this time to be able to report to you on a successful 2005 fiscal year. We succeeded, not least, in completing two capital increases and placing the shares of 4SC AG in the Prime Standard of the Frankfurt Stock Exchange at the end of the year. With the funds that have been raised and the sales revenues from our collaborative business, we have created the conditions for consistently expediting the development of the value of our therapeutic projects for the treatment of patients who suffer from cancer and chronic inflammatory diseases.

Our pipeline

We have been able to achieve substantial progress in our clinical project for the treatment of patients with autoimmune diseases such as rheumatoid arthritis and multiple sclerosis. In two comprehensive phase I trials, we determined a safe and well-tolerated dose of our drug candidate SC12267, which forms the basis for our further development strategy. 4SC AG is now concentrating on the impending phase IIa trial in patients who suffer from rheumatoid arthritis. In addition to the safety and tolerability of the drug candidate, the goal of this study is to show its convincing efficacy. This would satisfy an important prerequisite to the promise of an innovative treatment option that is well tolerated and efficacious for the patient, something that is so urgently needed in this indication area.

In initial animal studies, we have already successfully tested an innovative new class of drug candidates for the treatment of other diseases, such as chronic intestinal inflammations, rheumatoid arthritis or chronic inflammations of the respiratory passages. Their effect on the NFκB mechanism, which is so important to the activation of the immuno-response, gives us the chance to put into clinical development the first small molecular and orally available drug with dual effect as a therapy and pain reliever – for example, for the treatment of patients with chronic intestinal inflammation.

With the proteasome blocker SC68896 and innovative blockers of protein kinases, 4SC AG is creating the basis for new and tolerable treatment options for patients who suffer from life-threatening cancerous diseases. Both projects are on the direct road toward clinical development. On the other hand, our newest project with an ion channel as the target protein is still in the research phase. This project will serve the development of innovative therapies for the treatment of patients who suffer from multiple sclerosis. The Federal Ministry of Education and Research (BMBF) has acknowledged this promising project since May of last year with subsidy funds in the total amount of approximately Euro 1.2 million.

All five of the stated projects serve a high medical need and address markets with enormous revenue potential. 4SC AG is thus making itself into an interesting partner of the pharmaceutical industry, which is urgently dependent upon licence partnerships to supplement their product pipelines.

Our partnerships

Our projects are, without exception, products of the innovative power of our employees in conjunction with our company's comprehensive technology portfolio. The innovative power of 4SC AG is unique in the German biotechnology sector and is appreciated by our partners accordingly.

During the 2005 fiscal year, we were able to get two trendsetting research partnerships underway. For the first time, we have been able to gain an important Japanese pharmaceutical company as a partner, Sanwa Kagaku Kenkyusho. The partnership arrangement, which is designed to cover multiple years, already bore fruit at the beginning of this year with the achievement of a critical research milestone. In addition, we succeeded in expanding our partnership with Schwarz Pharma, which has been in existence since 2004, concluding a cooperation agreement designed to cover multiple years.

Dr Ulrich Dauer, CEO

Our listing on the stock exchange

With the pre-listing share capital increase of Euro 10.16 million and the listing of 4SC AG in the Prime Standard of the Frankfurt Stock Exchange in mid-December, we reached another important milestone in the development of our company. The public listing is an opportunity for our shareholders to participate in our company's growth potential in the stock exchange environment. The public listing also gives our company a higher level of recognition in the international life science sector and additional flexibility in the pursuit of company goals through the possible use of the share as a strategic currency.

We owe the successful public listing to the committed work of our employees, the consistent support of our existing shareholders and, above all, the trust of the new shareholders that we were able to gain within the framework of the pre-listing capital increase. In addition, a critical role in the preparation and implementation of the listing was played by our new CFO Enno Spillner, who has expanded our management team since September 2005 and brought with him his many years of experience with investments in the biotechnology sector, along with his great personal commitment.

Our next goals

The further expansion of our pipeline projects is at the forefront of our research and development activities. Our most advanced drug candidate SC12267 for the treatment of rheumatoid arthritis will also play a key role in the future.
Our preclinical projects are being systematically prepared for clinical development. In this context we supplemented our development team at the beginning of the year to include two additional employees with industrial experience. We are convinced that we will be able to show additional successes in the development of our pipeline projects within the foreseeable future. We are thereby creating a solid base for substantial licence partnerships with international pharmaceutical companies.

As a public company, it is naturally also important to us to keep our shareholders informed and, in addition, increase investors' attention to 4SC AG and 4SC share on the capital markets. We will increasingly introduce our company at national and international investor conferences and, in addition to targeted IR measures, intensify the direct dialogue with investors.

At this time I would like to sincerely thank our shareholders for their trust in 4SC AG and their support. I would also particularly like to thank our employees, who have laid the foundation for the future success of the company through their tireless commitment. I am happy to be able to continue to work on our company's growth with this committed team.

Dr Ulrich Dauer
Chief Executive Officer

THE CORPORATION'S **EXECUTIVE BODIES**

MANAGEMENT BOARD

Dr Ulrich Dauer, CEO
Dr Ulrich Dauer is a founding member of 4SC AG and Management Board Spokesman. Prior to that he held a senior position at Tripos GmbH, Munich, a subsidiary of US company Tripos Inc. Tripos is among the leading providers of contract research, screening libraries, software and system integration in the bioscientific and pharmaceutical field. There he was responsible for key customers and the acquisition of new customers in Europe. Ulrich Dauer studied chemistry and earned his doctorate at the university of Würzburg.

Dr Daniel Vitt, CSO
Dr Daniel Vitt is likewise a founding member of 4SC AG; today he is the CSO (Chief Scientific Officer) and responsible for research and technology, as well as the collaborative business. In 1997, he developed the virtual high throughput screening technology of 4SC AG through a stipend from the Bavarian State Government. He thereby laid the foundation for the company's current technology platform. Daniel Vitt studied chemistry at the university of Siegen and the university of Würzburg, where he later earned his doctorate at the Institute of Organic Chemistry.

Enno Spillner, Dipl.-Kfm. (graduate business administrator), CFO
Enno Spillner has been CFO of 4SC AG since September 2005. Prior to that he ran the Finance & Controlling Department of Bio^{M} AG, Martinsried, for more than six years. In addition, he was responsible there for substantial parts of the equity investment business and looked after various portfolio firms as an investment manager. During that time he had various Advisory Board and Supervisory Board mandates. In 2001, he additionally took over the management of Bio^{M} Venture Capital Fonds as partner. Enno Spillner studied business administration at the university of Bamberg.

Dr Gerhard Keilhauer, CDO
Dr Gerhard Keilhauer has been CDO (Chief Development Officer) at 4SC AG since 2001. The doctor of neurobiology previously worked in leadership positions in the biopharmaceutical industry for fifteen years. From 1986 to 2001, he worked in various functions at Knoll AG, Ludwigshafen, including as Director Screening and Director Molecular Pharmacology. He gained additional experience as Director of Oncology at BASF Bioresearch Corp. in Cambridge, Massachusetts, USA. Gerhard Keilhauer studied biology and chemistry at the university of Heidelberg.

SUPERVISORY BOARD

Dr Jörg Neermann, Supervisory Board Chairman
Dr Jörg Neermann has been a member of the Supervisory Board since August 2000. The general manager of VCG Venture Capital Gesellschaft mbH (DVC), Munich, has many years of experience in the international VC business with an emphasis on life science. Jörg Neermann studied biotechnology and business science amongst others at MIT in Cambridge, USA, and Harvard Business School in Boston, USA.
Jörg Neermann is a member of the Supervisory Board or Monitoring Board of:

- Probiodrug AG, Halle/Saale (Vice Chairman)
- Epigenomics AG, Berlin (until 3/2005 – Chairman and Vice Chairman of the Supervisory Board)
- Develogen AG, Göttingen (until 8/2005)
- G2M Cancer Drugs AG, Frankfurt am Main (until 2/2005 Vice Chairman)
- Igeneon AG, Vienna, Austria (until 3/2005)
- Topotarget A/S, Copenhagen, Denmark
- Keyneurotek AG, Magdeburg (Vice Chairman)
- Avontec GmbH, Planegg (member of Advisory Board)
- EBCP European BioCapital Partners GmbH, Munich (managing partner)

SUPERVISORY BOARD

Dr Robert B. O'Connell, Supervisory Board Vice Chairman

Dr Robert B. O'Connell has been a member of the Supervisory Board since July 2001. The doctor of chemistry has comprehensive experience in the international chemistry and pharmaceutical industry; he founded his own consulting company in 1998, The Catalyst Agency Ltd., in Great Britain. Prior to that, he worked for two decades in various leadership positions for Merck KGaA in Darmstadt. Robert B. O'Connell is a member of the Supervisory Board of:

- Key Organics Ltd., Camelford, Great Britain
- Scottish Prudential Investment Association Ltd., Dorset, Great Britain
- Forelle Estates Holding Ltd., Dorset, Great Britain
- Global Environmental Management Ltd., Sevenoaks, Great Britain

Dr Brian Morgan, Member

Dr Brian Morgan has been a member of the Supervisory Board since August 2003. Today the doctor of biochemistry runs his own consulting company for companies in the area of inlicensing and outlicensing. Brian Morgan is also active as a non-executive director for numerous biotech companies in England, Israel and France. Prior to that, he worked in the pharmaceutical industry for 30 years, including at Beecham Pharmaceuticals plc, London, and SmithKline Beecham plc, London. Brian Morgan is a member of the Supervisory Board or Monitoring Board of:

- Protaffin AG, Graz, Austria
- Scottish Biomedical Ltd., Glasgow, Great Britain (Non-Executive Director)
- Belmont School (Feldmore) Educational Trust Ltd., Holmbury, Great Britain (Chairman of Board of Governors)

Dr Manfred Rüdiger, Member

Dr Manfred Rüdiger has been on the Supervisory Board since August 2005. He was the Chairman of the Management Board of Igeneon AG, Vienna, Austria, and Executive Vice President of Aphton Corp., Philadelphia, USA. Prior to the doctor of biochemistry's switch to business, he taught at the technical university of Braunschweig. Manfred Rüdiger was a member of the Supervisory Board of:

- G2M Cancer Drugs AG, Frankfurt am Main (until 2/2005)

Dr Clemens Doppler, Member

Dr Clemens Doppler has been a member of the Supervisory Board since August 2005. As Director of private equity firm 3i Group plc., London, Great Britain, he has ten years of experience in the pharmaceutical and biotechnology industry. Clemens Doppler studied biology with an emphasis in molecular and cellular biology and was employed on multiple occasions in various leadership positions with international biotech companies. Clemens Doppler is a member of the Supervisory Board or Monitoring Board of:

- Sensovation AG, Stockach (Vice Chairman)
- Micromet AG, Munich
- EMBL Technologie Fund, Heidelberg (member of Advisory Board)

Stefan Meissner, Member

Stefan Meissner has been on the Supervisory Board since September 2005. He has been the Executive Director of the Equity Capital Markets Department of WestLB since 1999. Since that time he has concentrated on capital market finance and the area of life science. Various professional stations, such as at DZ Bank, Frankfurt am Main, or Dresdner Bank, Frankfurt am Main, form the basis for Stefan Meissner's 15 years of experience in the capital market and investment banking.

Dr Ulrich Pidun, Supervisory Board Vice Chairman (until 12 Sept 2005)
Patrick Schwarz-Schütte, Member (until 16 Aug 2005)
Prof. Dr Erich Schlick, Member (until 16 Aug 2005)

4SC **SHARE**

The shares of 4SC AG have been listed since 15 December 2005, under the abbreviation VSC on the Regulated Market (Prime Standard) of the Frankfurt Stock Exchange. The going public was carried out by way of listing of the shares subsequent to a pre-listing capital increase, in which the company raised EUR 10.16 million from existing investors and new institutional investors.

The opening price was EUR 4.41, and thus 4% above the issue price of EUR 4.24 that the investors had previously paid within the framework of this private placement. The percentage of freely tradable shares is approximately 25%*, which largely corresponds to the 2.4 million shares issued with the private placement. This percentage could increase to about 57% in 12 months in the course of incrementally expiring lock-up periods.

Strict lock-ups agreed upon

The shares issued during the pre-listing capital increase of EUR 10.16 million were freely tradable immediately after listing. The shares of management and the investors that were issued in earlier financing rounds are subject to strict trading restrictions (lock-up periods): Management and the founders are first permitted to trade 20% of their shares after 12 months and 50% after 18 months, and they cannot freely dispose of all of their shares until after 24 months. Existing investors were able to trade 3% of their shares immediately after the listing; otherwise a similar graduated scale applies: 20% after six months, 50% after 12 months, and a holding period no longer exists after 18 months. The existing shareholders include venture capital providers 3i, DVC, Bio^{M}, BdW, Mulligan Biocapital, Bayern Kapital and KfW Mittelstandsbank. In total, 4SC AG has raised funds amounting to about EUR 44 million since the commencement of business activity in 1999.

Public listing increases visibility

The private placement and listing were led by Conrad Hinrich Donner Bank AG, Hamburg. The background for the relatively quiet public listing without any associated capital increase was the moderate capital needs of 4SC AG. The company's business model permits a continuous flow of promising drug candidates that are intended to be outlicensed at a relatively early point in time. This requires only moderate funding by industry comparison and enables early revenues. In this way, 4SC AG clearly differs from other biotech companies that develop their own products to a state of market readiness and have a correspondingly high need for financing. In addition, 4SC AG generates revenues through collaboration agreements with other biopharmaceutical companies. The EUR 10.16 million that was raised prior to

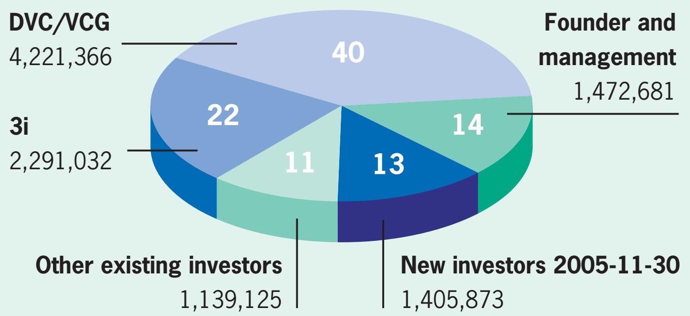
THE SHARE

WKN	575381
ISIN	DE0005753818
SE Code	VSC
Stock category	Bearer shares
Number of shares	10,530,077
Market segment	Prime Standard
Trading location	Xetra and all German stock exchanges
Designated sponsors	Close Brothers Seydler AG VEM Aktienbank AG
First day of trading	15 December 2005

* In accordance with the regulations of Deutsche Börse (Stock Exchange) in Frankfurt concerning the determination of the percentage of freely tradable shares, the free float of 4SC AG is only about 14%. Accordingly, all of a shareholder's shares that make up an aggregate of at least 5% of a corporation's capital stock allocable to a share category are deemed to be largely held.

SHAREHOLDERS' STRUCTURE

Share property (at the date of the listing)
Number of shares (totalling 10,530,077)



the listing, along with the expected sales arising from the collaborative business, will be used to advance the clinical development projects of 4SC AG according to plan and further expand the project pipeline over the next two years.

The central motivation for 4SC AG's public listing was to gain additional visibility. The company's recognition level in the international life science industry, and thus among potential research and development partners, increases substantially with the listing. This background also explains the choice of the Prime Standard, with its proven transparency duties and corresponding credibility. In addition, the tradable shares can be used as a kind of "currency" in research and licensing partnerships and potential acquisitions of companies. And finally, the listing also serves to motivate important employees, who are able to participate in the increase in the company's value as part of stock option programmes.

Pre-listing valuation confirmed by the market

The development of the price of 4SC shares since the new listing has confirmed the valuation proposed within the framework of the pre-listing capital increase. Between 15 December 2005, and 15 March 2006, the respective daily closing prices (Xetra) varied between EUR 4.24 and 4.70. The company's market capitalisation was thus about EUR 49.5 million on 15 March. Against the backdrop of the currently still low percentage of freely tradable shares, the trading volume during the past three months was 527,938 shares.

Close Brothers Seydler AG and VEM Aktienbank AG are acting as designated sponsors of 4SC AG. SES Research commenced reporting on 4SC stock and publishes regularly updated versions of its analyses. The company hopes to be able to gain additional analysts in the future for reporting on 4SC AG.

Continuous dialogue with the financial market

In addition to the duties associated with the listing in the Prime Standard, 4SC AG's management relies on rapid, comprehensive and reliable communications with all financial market participants. CFO Enno Spillner and Bettina von Klitzing, in her capacity as Investor Relations Manager, maintain a continuous dialogue with investors, analysts and media representatives. In this regard, they utilise all available information channels, such as the Internet and e-mail, telephone conferences and individual discussions, as well as presentations at industry trade shows and equity capital forums. The plan is to regularly inform existing investors and potential investors on 4SC AG's course of business and prospects as part of road shows.

Since the public listing, information concerning the stock, company presentations, financial reports and ad hoc anouncements, as well as a financial calendar and information concerning corporate governance, have been available at www.4sc.com.

CONTACT

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DRUG CANDIDATES FOR THE **PHARMACEUTICAL INDUSTRY**

The pharmaceutical industry is under pressure: it must get more and more products in an ever shorter period of time into its pipeline and onto the market, while, on the other hand, the patent protection of drugs successfully marketed in the past is threatening to expire. International pharmaceutical groups in particular are suffering increasingly from a lack of new products coming through in the pipeline and from productivity bottlenecks in their own research and development operations.

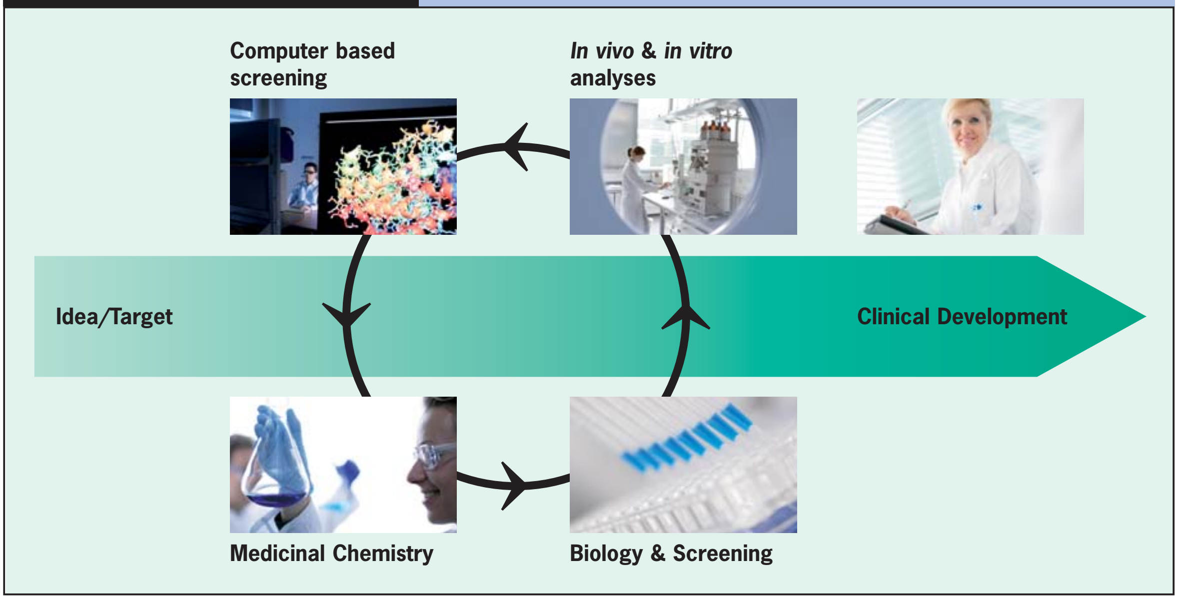
This represents an opportunity for comparatively small and flexible biotechnology companies, such as 4SC AG, who specialise in the discovery and development of innovative drug candidates. In practical terms, they function as the innovative driving force within the sector by pursuing their own projects right through to clinical development then licensing them out to the pharmaceutical industry.

In 1997, 4SC GmbH was founded based on the concept that the requirement for drug candidates could be satisfied particularly rapidly and efficiently through the use of computer simulation in conjunction with the traditional disciplines of chemistry and medicinal chemistry. Accordingly, the name 4SC stands for "fo(u)r smart chemistry", as the founding team consisted of four members. In 1999, after they had succeeded in convincing other colleagues and sources of venture capital, including DVC, Bio^{M}, Bayern Kapital and tbg to back their concept, 4SC GmbH started its business operations in Martinsried. Since then, over several rounds of financing the company has been able to raise a total of 44 million euro. Since 2000, the company has operated as a limited joint-stock company (AG).

The insufficient supply of the project pipeline of the pharmaceutical industry is an opportunity for innovative biotech companies

INTEGRATED TECHNOLOGY PLATFORM

Every drug candidate repeatedly undergoes an extensive optimisation process until it is ready for clinical testing.

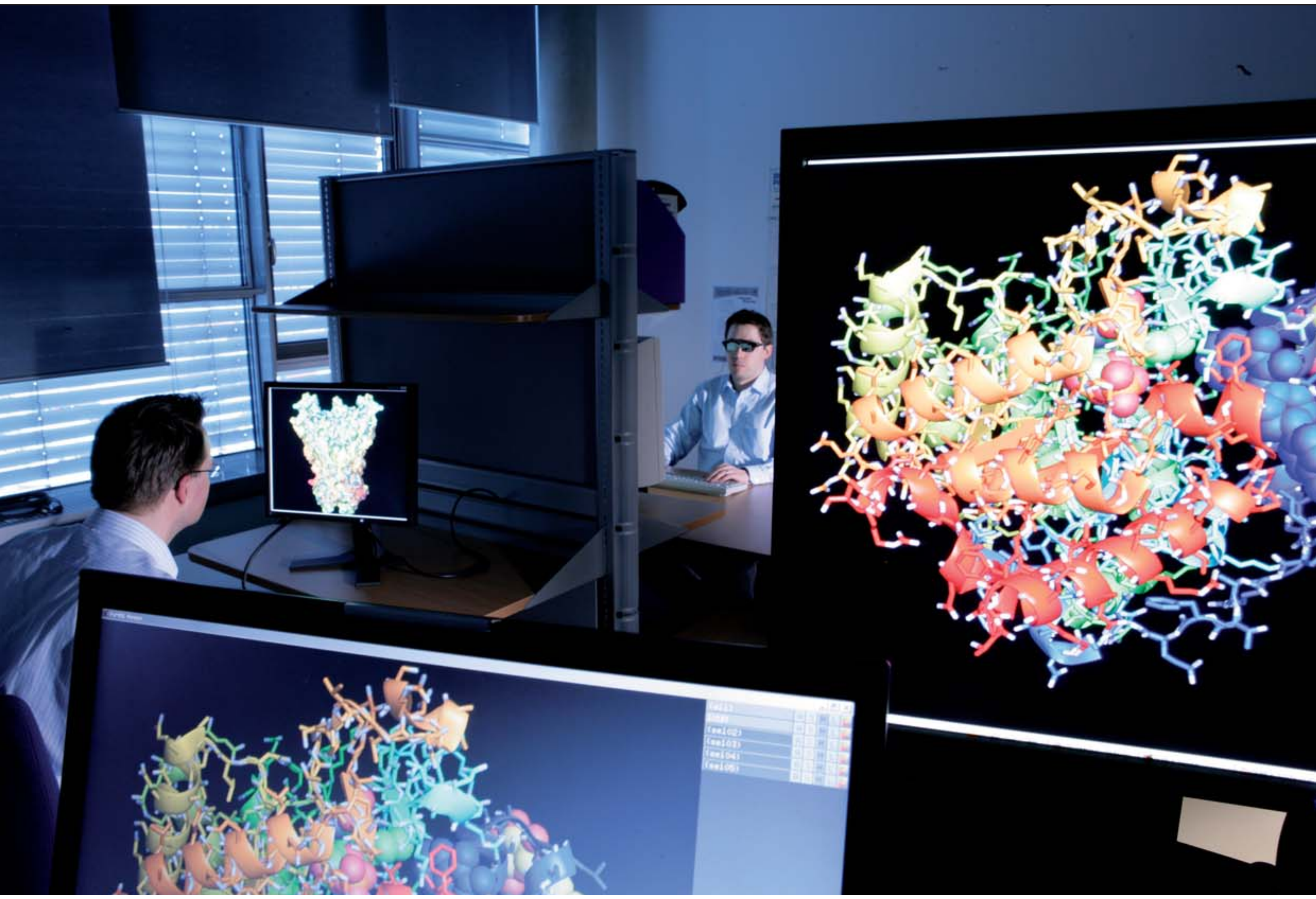


Computer simulation speeds up the development of active agents

In its product development, 4SC AG relies on the support of research processes from computer simulations and has developed the patented 4SCan® technology required for this purpose. Simulations of this kind, which have resulted in significant increases in productivity in almost all industries, still play a relatively minor role in pharmaceutical research.

However, the process is as simple as it is efficient: the principle of high throughput screening, as is applied in early phases of drug discovery to detect drug candidates in the laboratory, is for the most part transferred from the laboratory bench (*in vitro*) to the computer (*in silico*). The computer simulates the binding of drug candidates to a target molecule (the target) of relevance to a disease. A database of 6.2 million substances is screened to identify possible “hits”. In visual terms, this corresponds to searching for the right key to a lock. This process of virtual screening on the computer produces a preliminary selection and ranking list of a few hundred molecules, which bind to the target. Unlike the traditional *in vitro* screening processes, this requires only a very short time and minimal experimental effort.

4SC AG’s integrated technology platform consists of more than just *in silico* screening, however. The drug candidates preselected with the help of 4SCan® are then chemically synthesised and subjected to a wide range of biological tests (*in vitro* assays). Even at this early phase, the company is in a position to make predictions in terms of the suitability of these drug candidates for the subsequent pre-clinical phase. A series of computer programmes developed in-house are also used by means of which it is possible, for example, to predict the absorption or toxicity of active agents within the human body (ADMET analysis) and to filter out molecules with an undesirable profile. In an iterative process, all of the steps – computer-based screening, medicinal chemistry, biological tests and ADMET analysis – are run through a number of times, until a series of optimised drug candidates is in place for the purposes of pre-clinical and clinical development.



Virtual screening: the computer simulates the binding of a drug candidate to a disease-relevant target molecule

The figures speak for themselves: with the use of the 4SC AG integrated technology platform, the average hit rate for active agents in the early phase of biological activity tests is increased by a factor of 20-50. And the average time required for the process from the positively-tested drug candidate through to the lead structure for the drug is reduced by half. In this way, the development time needed from target through to the start of clinical development can be cut by two to two and a half years on average. This in turn means that within the context of the term of its patent, a drug can be marketed exclusively for longer – a fairly decisive argument in terms of pharmaceutical research.

All pharmaceutical disciplines under one roof

4SC AG's business model is primarily based on the use of its technology platform for the development of its own drug candidates from the target through to clinical development. Accordingly, the company's core competence lies in the seamless integration of the virtual high throughput screening process into all other phases of drug development. There is absolutely no break in the pharmaceutical value chain. Although the company currently has only 55 employees, it has integrated all of the necessary disciplines for drug discovery and development, from *in silico* through to *in vivo* within the company.

Apart from the core areas of medicinal chemistry and computer screening, the technological repertoire also includes the latest methods in molecular biology, protein biochemistry and cell biology, through to equipment with electrophysiological measuring devices for investigating ion flows within cells. This means that the company can process a large number of target classes. In addition, it also has its own animal facility for pre-clinical studies: in conjunction with sensitive bio-analytics, the behaviour of active agents in the living organism (*in vivo*) is investigated as early as possible. The portfolio of expertise is rounded off by a clinical team under the leadership of Dr Charlotte Herrlinger, who has managed more than 60 national and international clinical studies from phase I to phase IV for a number of pharmaceutical companies.

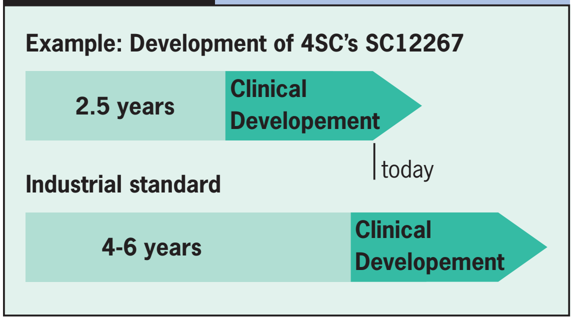
Last but not least, thanks to the efficiency of its technological platform, within two and a half years the company has been able to bring its project for combating rheumatoid arthritis through to clinical development. Considering that the standard time for the industry is four to five years, this represents a time saving of almost 50%. This also means that 4SC AG is the first German biotech company to carry through a project from its own research in the field of small molecules (orally available) all the way from the project concept to the clinical development stage.

Sights set on blockbuster markets

It is not by chance that 4SC AG's first clinical project for the treatment of people suffering from rheumatoid arthritis addresses a major market with blockbuster potential, as potential partners in the pharmaceuticals industry are primarily interested in products responding to a high medical need and promising corresponding levels of sales.

Against this background, in building up its pharmacological expertise the company has concentrated on the development of active agents combating inflammatory diseases and cancer. In both cases there is one common principle: uncontrolled cell growth as the basic cause of the disease. And in both cases, generally the corresponding products are compatible with the technology platform of 4SC AG and, in addition, that the expenditure involved for studies in phases I and II remains within acceptable limits. This is also an important criterion for a biotech company with a lean structure, which is pursuing a number of projects at the same time.

COMPARISON *Development times until the start of clinical studies*



Not putting all eggs in the same basket

Part of 4SC AG's business model is to avoid relying on only one single drug candidate. Instead, the risk is distributed over a number of projects which at a comparatively early stage in their development – generally speaking based on the "proof of concept" in phase IIa – are to be licensed out to pharmaceutical partners. Against this background, the company is already involved in discussions with the pharmaceutical industry in respect of several projects – thus exploiting a clear trend in the pharmaceutical sector.

Highly promising active agents are being bought in today at increasingly earlier stages and at increasingly higher prices. On the one hand, many new developments soon to be ready for the market have already been licensed out by biotech companies. On the other hand, pharmaceutical companies have an interest in taking over control of the development of highly promising active agents as early as possible. According to studies by pharmaceutical companies, the average value of deals with products in the pre-clinical stage or phase I has almost doubled within three years.

SUSTAINABLE
PROJECT PIPELINE

4SC PIPELINE

Five projects are already in different stages of development; each bar represents the current study phase. Behind them is the sales potential of a corresponding drug according to projections by 4SC AG.

INFLAMMATION

Indication	Drug Discovery	Preclinical	Phase I	Phase II	Peak Sales Potential (m/€)
Rheumatoid Arthritis	SC12267, DHODH				> 500
Inflammation	NFκB				> 500
Inflammation	Kv1.3				> 250

CANCER

Indication	Drug Discovery	Preclinical	Phase I/II	Phase II	Peak Sales Potential (m/€)
Cancer MM, SCLC	Proteasome				> 250
Cancer	Aurora/VEGF-R				> 600

Project to combat rheumatoid arthritis in phase II – SC12267, DHODH

4SC AG's most advanced drug candidate at present is the active agent SC12267, a protein inhibitor used to combat rheumatoid arthritis (RA), which also has the potential for the treatment of multiple sclerosis. In the successfully completed phase I, it has already been possible to identify a safe and well-tolerated dose for SC12267. The new active agent is responding to an acute medical need: 1-2 per cent of the population is affected by RA. This is a painful joint inflammation, which can lead to complete destruction of the joints. The total market for RA is in the region of 6-7 billion euro per annum, with the sales potential for SC12267 alone being estimated at over 500 million euro per annum.

The project's chances of success are high as SC12267 is aimed at the suppression of a target, which has already been clinically validated – the so-called DHODH protein – which has been largely elucidated in terms of its effective mechanism. The Aventis drug Arava® is already available on the market, targeting the same protein. However, because of its chemical structure and despite its high anti-rheumatic activity, its application is limited due to side-effects, including stomach and intestinal complaints, and in some cases severe liver damage. As a consequence of this unfavourable side effect profile a significant number of patients discontinue their

OPPORTUNITIES

"Inhibition of DHODH is known to be effective for the control of rheumatic inflammation in RA. The use of the only available DHODH inhibitor is frequently limited by its safety profile. Therefore, developing alternative compounds with the same target but improved safety is certainly worthwhile."

PROF. DR MED. BERNHARD MANGER
UNIVERSITY ERLANGEN-NUREMBERG

Medicinal chemistry: the drug candidates that are pre-selected with the help of the computer are then chemically synthesised and tested

treatment with Arava®. 4SC AG has developed drug candidates from a new type of chemical substance class and has set themselves the target of developing a new drug, which is at least as efficacious but is much better tolerated.

At present, the extensive preparatory work for the launch of clinical phase IIa is under way. This second phase of clinical studies to determine a safe and efficacious dose is expected to start in the autumn of 2006 with 120 patients and a 3-month dosing regime. It is due to end in mid-2007.

FURTHER PROJECTS APPROACHING THE **CLINICAL TRIAL** STAGE

NFκB

4SC AG has identified a new class of drug candidates with an inhibiting effect on NFκB, a central mechanism in inflammatory processes. These substances are able to regulate the activation of human immune cells. The possible areas of treatment in which they might be used include diseases with high medical need, such as chronic intestinal inflammation (Morbus Crohn, Colitis Ulcerosa), rheumatoid arthritis or chronic inflammation of the respiratory tract. In the medium term, application in the field of cancer therapy or for the treatment of viral infection diseases is conceivable.

In initial studies carried out in a special animal model for autoimmune diseases, one of 4SC's NFκB inhibitors has already displayed highly promising activity. The company's NFκB inhibitors have the opportunity of being the first to appear on the market as an orally-available, small-molecular weight combination of an analgesic and therapeutic substance for inflammatory intestinal diseases. As a result of the wide range of possible applications, a peak sales potential of 500 million euro is expected.

Proteasome

The development of a proteasome inhibitor under the designation SC68896 is also showing great potential. It is currently at the pre-clinical development stage. Through the targeted blocking of this enzyme, it is possible to specifically kill off rapidly growing cancer cells. Unlike the only appoved drug presently available in this sector (Velcade®), the inhibitor developed by 4SC AG is not chemically reactive and therefore, in spite of being highly efficacious, carries a significantly reduced risk of side-effects. Studies carried out up to now have shown that SC68896 is better tolerated by tumour-bearing mice than, for example Velcade®, by a factor of over one hundred. Possible areas of application are bone marrow malignancies, small-cell lung cancer and brain tumours. The estimated peak sales potential is between 250 and 500 million euro.

Aurora/VEGF-R

With its 4iP programme for the development of new types of inhibitors of what are termed protein kinases, 4SC AG has pressed forward into the high-growth market for innovative cancer therapies. Kinases are special enzymes, which produce uncontrolled growth in cancer cells. In recent times, kinase inhibitors have been among the global blockbusters with sales in the region of several billion USD per annum. In conjunction with the company ProQinase GmbH (Freiburg) which specialises in this field, 4SC AG has been pursuing what is termed a “multiple-target” approach: attacking the cancer cells on two fronts, in which cell division (proliferation) and the supply of nutrients through the creation of blood vessels (angiogenesis) are both prevented. The most highly promising active agent at present within this project is an inhibitor for the kinase pair Aurora and VEGF-R. In the light of the positive response from a number of pharmaceutical companies, it would appear that partial licensing out might even be possible before the start of clinical studies. The overall market for therapies combating solid tumours in 2004 amounted to more than 40 billion USD and is growing at an annual rate of 11-16 percent. According to independent estimates, the market potential for innovative Aurora/VEGF-R inhibitors stands at well over 600 million euro a year.

Kv1.3

The latest project in the 4SC AG pipeline is an ion channel blocker, in this case for the “Kv1.3” potassium channel. Even if the substance is still at the discovery stage, highly promising prospects can already be identified in the field of multiple sclerosis (MS) therapy. The Federal Ministry of Education and Research (BMBF) has also recognised this and since 2005 has allocated some 1.2 million euro to fund development in this area. As none of the current methods of treating MS is satisfactory, substances for oral administration such as the ion channel blocker will satisfy an enormous medical need if they are successful.

Dr Charlotte Herrlinger and her team coordinate the pan-European patient recruitment for clinical studies

Pre-clinical studies measure, amongst others, the concentration of an active agent in the blood

RESEARCH COLLABORATIONS WITH **MAJOR PHARMACEUTICAL** COMPANIES

Although 4SC AG focuses on the use of its technology platform for the development of its own products, the company also offers its expertise within the context of research collaborations with the pharmaceutical industry. This offers a number of advantages: high-profile partners provide additional validation of the integrated technology platform and through this cooperation the company gains in experience in terms of how pharmaceutical partners think and work. In addition initial revenue has been generated in this way.

Collaboration partners such as Schwarz Pharma, Sanofi-Aventis or the Japanese pharmaceuticals manufacturer Sanwa Kagaku Kenkyusho provide 4SC AG with target structures within the context of their own projects, on the basis of which the company can develop the projects with its own resources – ideally, right through to initial clinical studies. So it is not so much about making exclusive use of the proprietary 4SCan® method but about exploiting the integrated research and development capacity of the company as a whole. In return, apart from having its costs directly refunded, 4SC AG also receives success-related milestone payments and potential royalties on sales. Overall, in recent years the company has entered into research collaborations involving more than 27 million euro in milestone potential, as well as potential participation in sales from a total of six different licensing agreements each involving a participation in sales of up to three percent.

For their part, the pharmaceutical companies benefit from the efficient structures and rapid processes in place at 4SC AG, as well as from the flexible opportunities for using the technology platform. In this way they can react more rapidly to current developments and carry out any necessary strategic realignments in a relatively cost effective way, without having to build up their internal capacities. Here, too, flexibility is the crucial keyword.

Broad range of potential for growth and added value

As the company's projects deal exclusively with possible blockbuster markets, it has a broad range of potential for added value in the form of potential sales growth from a series of milestone payments and initial royalties.

By 2007, 4SC AG intends to have up to four projects running at the clinical development stage. As well as the project combating rheumatoid arthritis in phase IIa, there should be two or three others in phase I or phase I/II. In addition, one or two projects are due to be added to the pipeline.

As a basic principle, thanks to its integrated technology platform 4SC AG has a number of options open to it, such as adding projects to the pipeline and the development of selected projects through to phases II and III and therefore closer to the market. In any case, the integrated technology platform and the expertise of the workforce will ensure a sustainable project pipeline. This means that 4SC AG will have no shortage of innovative product candidates in future.

MANAGEMENT REPORT

1. PRESENTATION OF THE COURSE OF BUSINESS

1.1 Development of the overall economy

1.1.1 Economic development

The world economy grew substantially in 2005, although the expansion pace slowed at the end of the year, which was in turn mainly triggered by the declining growth in the USA and euro zone. In the major industrialised nations, the average economic growth for 2005 was 2.5%, according to information from the Deutsche Bundesbank. The slight increase in intra-year inflation, which was caused primarily by the sharp increase in the price of crude oil products, as well as other industrial raw materials, had calmed by the end of the year. This occurred, thanks not least to several small interest rate increases by the U.S. Treasury and, after a long pause, the first small interest rate increase by a quarter percent by the European Central Bank ECB in December 2005. In the opinion of the Deutsche Bundesbank, the industrial economy in Germany showed movement in a clearly positive direction at the end of the year. For the year 2005 as a whole, the current calculations of the Federal Office of Statistics reveal a rise in the German gross domestic product (GDP) of only 0.9% in real terms. In particular, the still weak domestic demand and the declining foreign trade impetus were probably the key factors for this 2005 result.

1.1.2 Development of the stock exchange segments

The worldwide stock exchange indices developed very positively for the most part. Some of the most important indices rose substantially; for example, the S&P 500 rose by 2.9%, the Nikkei 225 rose by 40.6% and the DAX rose by 26.9%. The stock indices that are relevant to the biotechnology market, particularly the NASDAQ Biotechnology Index (+2.6%), the Amex Biotechnology Index (+25.1%) and the Prime IG Biotechnology Performance-Index (+19.1%), likewise developed positively in 2005.

1.2 Developments in the biotechnology industry

Worldwide, the pharmaceutical and biotechnology industry remains on the rise, and the demand for more efficacious and better tolerable active agents in a wide range of indications is unbroken. However, this is not taking place without significant setbacks, of which Biogen Idec, (USA) and Elan Pharma, (Ireland), with the suspension of Tysabri®, is probably the most prominent example. With Vioxx®, also Merck & Co., (USA) still faces an immense wave of complaints that will inflict lasting damage on the company. Such events affect entire segments in this industry negatively, such as when other companies with very similar technological approaches or targets develop their products. It must be assumed that the regulatory authorities will respond to such incidents with more elaborate and time-consuming reviews.

The development of the biotechnology industry in Europe and Germany exhibited a split picture in 2005. On the one hand, many predominantly privately financed companies were not successful in advancing development to the extent that they had planned. This, in turn, was often associated with reticence on the part of providers of venture capital. The latter themselves continued to have substantial difficulties in procuring funds on a large scale. Some, primarily early-stage, biotechnology firms had to accept additional cuts or even declare insolvency, which contributed to further consolidation of the industry.

On the other hand, there was also a great deal of positive news in Germany concerning successful, in some cases extremely large, financing rounds (elbion and Wilex, for example), mergers (Trigen/ProCorde and Curacyte/IBFB, for example) and acquisitions by pharmaceutical companies and biotech firms (GlycArt/Roche and Morphosys/Biogenesis, for example). Overall, the market began moving in a positive direction once again in 2005, but continued to behave very selectively and remained under consolidation pressure. With Arpida, Paion, Intercell, Speedel, Jerini and Biofrontera,

4SC-Team in Martinsried/Munich

biotech companies successfully showed in 2005 that public listings and new alternative financing channels were once again feasible.
On the product development and cooperation side as well, many companies were able to report positive news (e.g. Basilea, GPC, Idea, Morphosys, MediGene, Paion, Wilex, among others). This further corroborated the impression of stabilisation of biotechnology as an independent industry and the successful formation of the necessary critical mass within the industry.

1.3 Business conditions and general conditions
4SC AG has specialised in the research and development of innovative therapies for chronic inflammatory diseases and cancer. For this purpose, the company has established a strong pipeline of in-house therapeutic projects that are planned to be developed up to early clinical phases. The goal is to realise the commercial potential of these projects by means of license contracts with the pharmaceutical industry. The company intends to generate lasting company growth through sales revenues from license fees, milestone payments and royalties that are being sought. This is the purpose of the “Drug Discovery & Development” segment. The therapeutic focus of 4SC AG is in the area of cancerous and inflammatory diseases, because these indications, which have heretofore had unsatisfactory treatment options, promise significant market potential with simultaneously moderate development costs and development times in early clinical development.

In the reporting year 2005, the company goals concentrated, firstly, on the preliminary regulatory work relating to the performance of the clinical phase IIa for the DHODH Project and the further development of the existing proteasome and NFκB projects in the preclinical phase. In addition, the progress in the Aurora/VEGF-R kinase project in cooperation with ProQinase GmbH, Freiburg, and in the Kv1.3 project were important for the further development of 4SC AG's project pipeline.

In the "Collaborative Business" segment, 4SC AG makes its technology platform available to partners and customers from the pharmaceutical and biotechnology industry as a service package within the framework of cooperation agreements. As a result of this, it is possible to earn sales revenues that support the self-financing of 4SC AG.

1.4 Development with respect to sales revenue and orders

Net sales in the reporting year totalled KEUR 2,068 and ended up KEUR 955 or 31.6% less than in the previous year (KEUR 3,023). In this regard, KEUR 1,936, i.e., 93.6% of the net sales, was attributable to the "Collaborative Business" segment (2004: KEUR 1,356), which was thus successfully increased by 42.8%. In addition to the cooperation contracts that were concluded or continued in 2005 in the "Collaborative Business" segment, 4SC AG was able, at the end of December 2005, after successfully reaching an important milestone, to extend the cooperation with Sanwa Kagaku Kenkyusho Co., Ltd., Nagoya (Japan), which had started in January 2005. However, this activity no longer affected liquidity in the financial year 2005.

In the "Drug Discovery & Development" segment, net sales amounted to KEUR 132 (2004: KEUR 1,667). This decline by KEUR 1,535 or 92.1% was expected, because 4SC AG did not license any projects to external partners during the financial year 2005, but instead concentrated on the independent further development of the project pipeline.

1.5 Procurement

4SC AG's procurement and logistics processes, as well as its inventory warehousing, continue to be organised and handled through a central purchasing department. The processes are standardised and established. Importance was placed, in particular, on a high level of integration of purchasing processes up to the individual workplace. The close collaboration between purchasing and bookkeeping also guarantees a smooth flow from the order and request to the payment of the invoice.

Reaction carousel for parallel synthesis

4SC AG places importance on not being dependent upon individual suppliers. In principle, purchasing sources are selected according to price, availability and qualitative aspects. In this regard, it was also possible to further improve delivery terms and conditions in the reporting year by means of successful negotiations with suppliers and active involvement in a regional purchasing association.

1.6 Investments and fixed assets

The company continues to profit from its substantial fixed asset investments from 2002. During the reporting year, therefore, new investments in fixed assets totalled only KEUR 76 (2004: KEUR 50). This primarily involves replacement investments for technical laboratory equipment and IT hardware. In addition, the company invested KEUR 33 in the acquisition of new software (2004: KEUR 0). Accordingly, the book values for fixed assets and intangible assets were reduced, declining by KEUR 714 from KEUR 4,068 in the previous year to KEUR 3,354 in the reporting year. Scheduled depreciation on fixed assets and intangible assets totalled KEUR 819 in the reporting year (2004: KEUR 958).
4SC AG continues to hold an equity interest of 48.8% in quattro research GmbH, Martinsried, as a financial asset.

1.7 Goodwill

As was already the case in previous years, capitalised goodwill is recognised on the balance sheet resulting from the fusion of 4SC GmbH with 4SC AG in the year 2000. This goodwill totals KEUR 1,786 (2004: KEUR 1,786) and has been valued in accordance with the provisions of IFRS 3 since the reporting year. Accordingly, no scheduled depreciation is taken in accordance with IFRS 3 and IAS 36; instead at least one annual impairment test is undertaken for capitalised goodwill. The impairment test conducted at the end of the reporting year revealed no necessity to correct the valuation as of 31 December 2005.

1.8 Financial measures

During the reporting year, various financing measures took place that, in the aggregate, contributed to the strong improvement of the corporation's financial situation. This applies, above all, to the last pre-listing financing round with the ensuing listing. Since 15 December 2005, 4SC AG has been listed in the Prime Standard of the regulated market of the German Stock Exchange. Overall, the corporation's share capital rose in multiple steps from KEUR 6,956 at the beginning of the reporting year to KEUR 10,530 at the end of the reporting year.

From the capital increase of 29 December 2004, funds totalling KEUR 1,123 flowed to 4SC AG during the reporting year in two tranches. Within the framework of the capital increase of 6 June 2005, Technologie Beteiligungsfonds Bayern III GmbH & Co. KG, Munich, and KfW A.d.ö.R., Frankfurt a. M., were successfully gained as new shareholders. As a result, 4SC AG attracted an additional KEUR 1,660 in cash. A capital increase in exchange for cash and in-kind contributions was adopted at the extraordinary shareholders' meeting of 28 September 2005. Within the framework of this capital increase, a total of 1,179,245 shares were issued at a price of EUR 4.24 per share. Exclusively existing investors subscribed for these new shares. Since 353,773 of these shares were subscribed to in exchange for in-kind contribution, KEUR 3,500 in cash flowed to 4SC AG. A second capital increase in exchange for cash contributions, likewise adopted by the extraordinary shareholders' meeting of 28 September 2005, was successfully completed on 30 November 2005. Through the issuance of 1,217,193 shares to predominantly new investors, again at a price of 4.24 EUR per share, 4SC AG raised KEUR 5,161 in funds.

Overall, funds in the amount of KEUR 11,444 flowed to 4SC AG during the reporting year from the aforementioned capital increases. As a result of the cash flow from operating activities and investing activities in the amount of KEUR - 5,833 (2004: KEUR - 4,474) and as a result of the redemption of the liabilities due to silent partners and convertible bonds, the balance of cash and cash equivalents (current asset securities) rose only by KEUR 4,820 to KEUR 6,878 (2004: KEUR 2,058) at the end of the reporting year.

1.9 Personnel and social security

On average, during the reporting year, 48 employees were employed at 4SC AG. This means a decline of nine employees compared to the 57 employees of the previous year. The background for this was natural employee fluctuation, which also gave 4SC AG the opportunity to further optimise several internal processes. The main portion of the personnel decline did not take effect until the second half of the year. Since, moreover, no provision had been created for the Management Board bonus for the previous year that was disbursed in the reporting year, and because a severance payment had to be made, the personnel costs rose slightly compared to the previous year to KEUR 3,569 (2004: KEUR 3,495). The provision for the Management Board bonus was not created, since during the compilation of the 2004 annual financial statement the prerequisite for the creation of a corresponding reserve did not exist.

Out of the 48 employees, 37 worked in research, nine in administration and two in the area of information technology. No new central positions were created during the overall reporting period. Only some of the departures were replaced during the reporting year; otherwise, they were mainly replaced at the beginning of 2006. Management Board member, Dr Stefan Busemann (CFO), left the company at the beginning of August 2005. This position was taken over by Enno Spillner, Dipl.-Kfm (graduate business administrator), in mid-September 2005.

In light of the advancing development of the company and its projects, various new positions are planned, which are intended to be filled in the course of 2006.
Since the company is of the opinion that it can only succeed with the help of the commitment and know-how of all employees, 4SC AG has continued to maintain the already existing employee option programmes and has issued stock options to employees and management. These option programmes have been part of the corporate culture since 2001 and are used as an instrument for strengthening employee loyalty.

1.10 Work safety and environmental protection
During the reporting year 2005, 4SC AG took all necessary measures to avoid or minimise environmental pollution. 4SC AG has two safety officers for the Biology and Chemistry departments and a safety head who, together with a work safety specialist, regulates the company's internal and external affairs in this area. Technical safety service is performed by Gesellschaft für Laborsicherheit (Laboratory Safety Corporation), Karlsfeld. No critical incidents from this area are known of for the reporting period.
In accordance with the applicable hazardous substance regulations, all chemicals are documented in a hazardous substance register and the laboratory employees are instructed on the handling of hazardous substances, in order to enable the greatest possible degree of safety for the employees and minimise the burden on the environment.
In order to save resources and reduce risks in the laboratory operation, the inventory quantities of hazardous substances and the use thereof are kept as low as possible. All safety facilities were controlled in accordance with the applicable regulations during the year 2005 and repaired when necessary. In addition, the requested risk evaluation was created and the resulting measures were implemented pursuant to prioritisation during the reporting year.
The existing laboratories of safety levels 1 and 2 and the radionuclide laboratory are approved by the relevant authorities and are under their constant supervision. A radiation protection officer and two deputies were appointed to guarantee the safe operation of the radionuclide laboratory. No events that would have necessitated a report or the intervention of the authorities occurred during the reporting period. The operation in the animal testing laboratory is subject to monitoring by an outside animal protection officer, who consults 4SC AG on questions of animal experimentation and animal protection. All animal experimentation work took place exclusively within the framework of the governmentally approved testing projects.

1.11 Research and development
1.11.1 Technology
Also in the financial year 2005, 4SC AG was able to further expand its technological leadership position in the area of computer-supported active agent development. With the newly developed dynamic docking technology, 4SC AG is now in a position to also use *in silico* screening processes for "fine tuning" in the area of lead optimisation. In contrast to established processes, the new method uses a dynamic protein geometry for the calculation of the interaction between the target and new drug candidates. An additional success was achieved in the area of simulation of substance properties: 4SCan/ADMET supports scientists in the selection and synthesis of substances with improved solubility, increased oral bioavailability and reduced side-effects. The new methods have already been successfully used for in-house research and development projects and pharmaceutical cooperation projects of 4SC AG.

1.11.2 Project pipeline
The further development of drug candidate, SC12267, was at the forefront of research activities during the reporting year. The necessary preliminary regulatory work for the start of a clinical phase II study concerning the treatment of rheumatoid arthritis got under way. The further development of the three pre-clinical projects also proceeded positively in the direction of possible clinical development. In addition, 4SC AG, flanked by a subsidy programme of the BMBF (Federal Ministry of Education and Research), started a new project concerning the identification of ion channel blockers. The goal of this new innovative project is the identification of new medications for the treatment of multiple sclerosis.

A glance at the stock of chemical substances

Inhibitors of dihydroorotate dehydrogenase (DHODH) for the treatment of autoimmune diseases (rheumatoid arthritis, RA; multiple sclerosis, MS)

In this project, the objective is the identification of chemically innovative substances that have an improved side-effect profile and possess the same mechanism of action as the product Arava® by Sanofi-Aventis, which is already on the market. In particular, the liver toxicity of the marketed product, as well as its side-effects in the intestinal tract (diarrhoea), should absolutely be avoided in order to guarantee significantly better tolerability and thus the long-term compliance of the product. In addition to the development substance SC12267, 4SC AG has a broad pool of potential proprietary backup substances that are at various stages of pre-clinical development.

Now that the clinical phase I studies have been able to show with healthy subjects that the substance SC12267 has good tolerability and pharmacokinetics superior to the Arava® benchmark, 4SC AG prepared the initial application on patients during the reporting period. For this purpose, the strategy and the design for the clinical proof of concept phase IIa study in the indication of rheumatoid arthritis were discussed and defined in multiple expert rounds. It is planned that patients with early active rheumatoid arthritis will be treated with two doses of the test substance per day over a period of three months. It is intended that this provide proof of clinical efficacy with respect to this disease. This study will be double-blind and placebo-controlled.

Kinase inhibitors (cancer)

Kinases play a particularly important biological role in the treatment of cancer, because these proteins are important to the transmission of cellular signals. The goal heretofore in the development of new kinase inhibitors was to block a specific kinase that was linked to a specific tumour disease and thereby achieve a therapeutic effect. As a result of this selectivity, however, medications such as Gleevec® (Roche) or Gefinitib® (Astra Zeneca) have only a limited therapeutic potential and also contain the risk of the emergence of resistances. In 2003, 4SC AG, working jointly with Freiburg-based ProQinase GmbH, started an extensive project to identify multi-specific kinase inhibitors. The plan is to attack the tumour simultaneously from multiple sides. Several important research milestones were reached during the reporting period. For example, inhibitors of Aurora B Kinase, which inhibit cell division ("proliferation") even at low nanomolar concentrations, were successfully found. At the same time, an additional group of kinases (VEGF-R Kinases), which is responsible for the formation of new blood vessels ("angiogenesis') in tumours, is blocked by these active substance molecules. These active substances should thus be in a position to simultaneously inhibit two important mechanisms of cancer development, the tumour's growth and its supply of oxygen and nutrients. The next goals will lie in the selection and development of the most appropriate representatives of these substance classes with an eye toward further pre-clinical and clinical development.

Biological test series of 4SC's drug candidates

Proteasome (cancer)

In 1998, the substance Velcade® (Millennium) was approved in the USA as a third-line therapy for the treatment of recurrent (returns after complete healing) multiple myeloma. Velcade® generated sales revenues of nearly USD 300 million in a short period of time and is today the method of choice for the second and third-line therapy of this cancerous disease. According to current studies, the clinical potential of this kind of proteasome inhibitor is still much greater, but is dampened by the toxicity of Velcade®.
SC68896 is an innovative small molecular inhibitor of proteasome that 4SC AG has developed in recent months. Unlike Velcade®, however, SC68896 contains no chemically reactive groups and therefore leads to the expectation of substantially improved tolerability. Due to the strong in vitro activity on tumour cells, the high degree of tolerability and the good pharmacokinetic properties, the substance SC68896 and some similar compounds are now being studied in suitable pre-clinical models. It is intended that the cancerous diseases that best respond to these substances be identified in this way. The start of formal development, followed by one or more clinical phase I/II studies, is planned for 2006, depending on two pre-clinical milestones.

NFκB (inflammation and cancer)

The so-called NFκB mechanism plays a key position in the emergence of chronic inflammations and autoimmune diseases. This mechanism is also believed to play a further role in the area of tumour formation and, in particular, the development of resistances to cancer medications. The development of medications that regulate the NFκB mechanism is therefore a highly promising approach for the treatment of diseases such as rheumatoid arthritis, inflammatory intestinal diseases and psoriasis.
4SC AG has identified a new class of drug candidates that have an inhibiting effect on the NFκB mechanism. These substances are able to regulate the activation of human immune cells. In initial studies on a DTH animal model, a model for autoimmune diseases, it was successfully shown that one of the NFκB inhibitors exhibits promising activity. The properties of this entire series of NFκB inhibitors have been successfully optimised with respect to oral bioavailability, cellular activity and solubility. The selection of a promising clinical development candidate that exhibits the defined substance profile is planned for the financial year 2006, depending on additional scientific results.

Kv1.3 (multiple sclerosis)

Within the framework of a grant from the Federal Ministry of Education and Research (BMBF), a new project was started during the summer of the reporting year to identify new medications for the treatment of multiple sclerosis (MS). The Kv1.3 channel exists primarily in immune cells, which are, in an outbreak of MS, of central importance to the advancement of this disease. A blockade of the ion stream through the channel prevents the increase of this immune cell subtype and should therefore have positive effects on the course of illness. The new MS medications that are currently being pushed onto the market are primarily proteins (particularly antibodies) and are therefore highly expensive. They are not orally available and often lead to a drastic worsening of the clinical picture after discontinuation of the medication. It is expected that a specific, orally available, chemical-organic active agent can be positioned outstandingly in MS therapy. Based on the already existing know-how concerning the processing of ion channels, 4SC AG has been able to identify molecules that block both the Kv1.3 channel and the increase of immune cells in the low micromolar area.

In addition to the aforementioned projects that are currently being actively expedited at 4SC AG, substances arising from other projects that are currently not further chemically-synthetically processed continue to be characterised for commercial applicability in collaborations.

Quorum Sensing Blocker (QSB, bacterial infections)

4SC AG is a pioneer in the area of quorum sensing blockers In this innovative approach, the cell-cell communication of gram-negative bacteria is inhibited without exercising a toxic effect on the bacteria. As a result, the virulence of these bacteria (formation of biofilm, release of virulence factors, such as toxins and enzymes) is suppressed. Compounds synthesised and characterised at 4SC AG that exhibit a high specific activity are currently being evaluated primarily in collaboration with leading industry representatives for use in medical technology and for skin care products.

BK ion channel
(erectile dysfunction, incontinence, asthma)

For priority reasons, the identified modulators of the BKca ion channel were not further developed during the reporting year. Since no internal resources are being invested in this project, the potential of these active agents will be evaluated in collaboration with academic clinical research institutions and possibly, industrial collaboration partners.

Malaria

The European Union is subsidising the development of new therapies for the treatment of malaria. Since December 2005, 4SC AG has been part of a consortium of over 20 research institutions and pharmaceutical companies devoting themselves to the development of new therapies for this illness. The anti-malaria substances discovered by 4SC AG in earlier work are being examined in this context for their mechanism of action and their suitability for application in higher organisms. If this work is successful, licensing out to a suitable development partner is planned.

1.12 Measures for the protection of intellectual property

At the end of the reporting period, 4SC AG expanded its patent portfolio to 77 active applications, which belong to 17 patent families. One patent, whose subject matter is new active substances, was issued in the USA during the financial year 2005, and seven additional new applications were filed. All seven patent applications filed during the reporting year relate to the protection of new substances ("composition of matter") and their use as medications. In addition, 4SC maintains two other patents jointly with business partners, but the patents are licensed out to these partners.

Some of the word and picture marks for the protection of the company logo and company name were issued during the financial year 2005. The 4SC picture and word marks were issued in Germany; the 4SC word mark, in Europe, with an initial term through 2021. The word mark "4SCan" was issued in Europe with a restriction in the area of image reproduction for diagnostic purposes/physiotherapy and chemical products for diagnostic purposes.

2. PRESENTATION OF THE SITUATION

2.1 Net assets position

Non-current assets declined during the reporting year from KEUR 4,282 to KEUR 3,516 compared to the previous year. This decline is primarily attributable to the planned depreciation on software and the IT and laboratory equipment. At KEUR 819 (2004: KEUR 958), planned depreciation was substantially above the investments that were made in the amount of KEUR 109 (2004: KEUR 50). A second reason for the reduction of non-current assets in the reporting year is the decline in the long-term portion of the receivables from associated companies. Receivables from associated companies fell from KEUR 214 in the previous year to KEUR 162 in the reporting year. This account receivable is a purchase price claim against quattro research GmbH, Martinsried, concerning a software package that was sold and is being repaid for over a period of eight years in accordance with the contractual payment plan.

The non-current assets consist predominantly of goodwill in the amount of KEUR 1,786 (2004: KEUR 1,786), which results from the fusion of 4SC GmbH with 4SC AG in the year 2000, and fixed assets (primarily laboratory and IT equipment, installations) in the amount of KEUR 1,503 (2004: KEUR 2,171).

Current assets increased in the reporting year, from KEUR 2,448 in the previous year to KEUR 7,728. This increase results primarily from the financing activities during the reporting year and the increase associated therewith in cash and cash equivalents from a total of KEUR 2,058 to KEUR 6,878. Prepaid expenses and deferred income rose from KEUR 84 to KEUR 236, and other current assets rose from KEUR 238 to KEUR 374.

The trade receivables increased from KEUR 49 to KEUR 205 based on the closing date. In addition, the short-term portion of the purchase price claim against quattro research GmbH, Martinsried, in the amount of KEUR 21 (2004: KEUR 4) is stated within the current assets.

The equity of 4SC AG increased from KEUR - 49 in the previous year to KEUR 9,159 in reporting year. The reason for this is the various financing measures that were associated with an increase of subscribed capital by KEUR 3,574 to KEUR 10,530 and the allocation of KEUR 11,870 into additional paid-in capital. As a result of these financing measures, a total of KEUR 11,444 in funds flowed to 4SC AG.

The liabilities due to silent partners were reduced from KEUR 2,905 to KEUR 0 in the reporting year. In this regard, KEUR 690 in liabilities was converted into a loan, which is due on 31 December 2008, and has an interest rate of 5.0% p.a. At the same time, the provision obligations for end remuneration claims of the silent partners fell from KEUR 571 in the previous year to KEUR 0 in the reporting year. The repayment of the remaining end remuneration claim is converted into an interest-free long-term loan. The redemption of this loan is deferred to 31 December 2008.

All convertible bonds still in existence on last year's balance sheet closing date were converted into shares during the reporting year (KEUR 2,500) or repaid (KEUR 21).

The provisions totalled KEUR 785 on the balance sheet closing date (2004: KEUR 142) and were in large part obligations resulting from the listing on the Frankfurt Stock Exchange that took place in December.

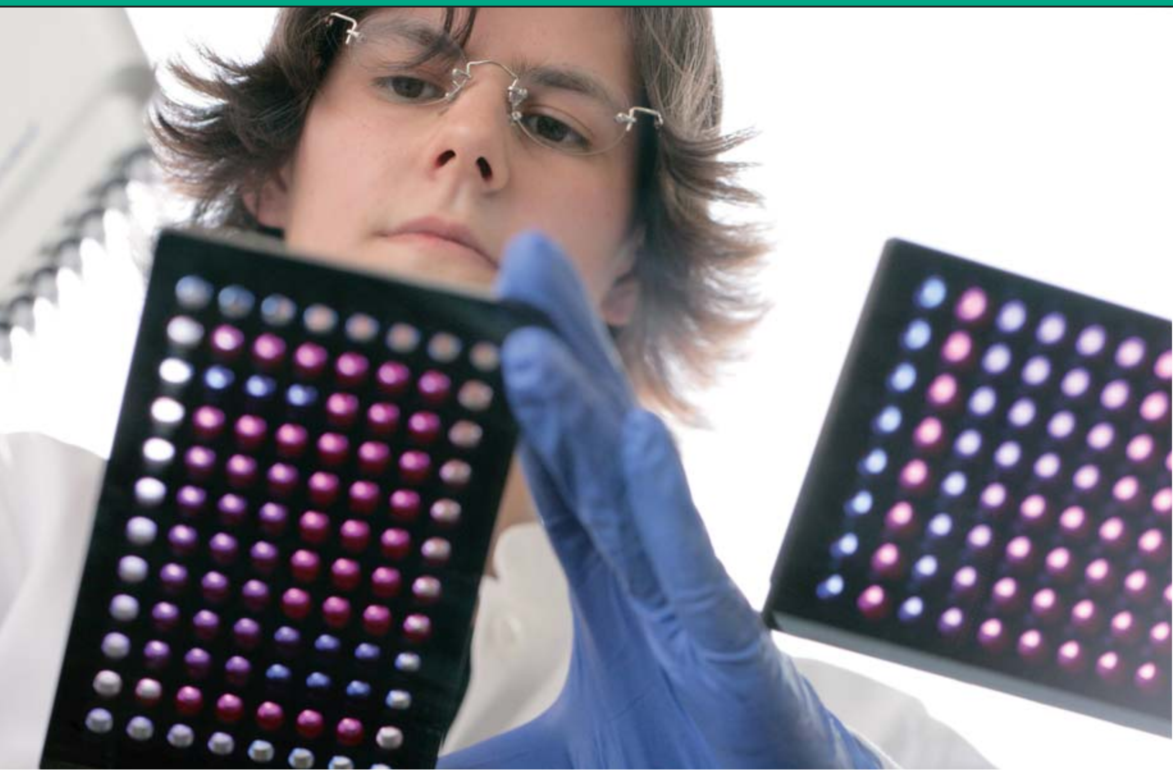
The trade payables increased as of closing date, from KEUR 122 in the previous year to KEUR 271 in the reporting year.

2.2 Financial position

The cash flow from operating activities totalled KEUR - 5,725 in the reporting year (2004: KEUR - 4,403). This increase in the outflow of funds compared to the previous year results primarily from the worsening of the period result, which was KEUR - 6,277 in the reporting year (2004: KEUR - 5,821).

The outflow of funds from investing activities increased in the reporting year by KEUR 37 to KEUR - 108 (2004: KEUR -71), because the payments for investments in fixed assets and intangible assets increased to KEUR 109 (2004: KEUR 50).

The cash flow from financing activities totalled KEUR 10,653 in the reporting year (2004: KEUR 3,352). An additional to-



A chemical compound is examined for its cellular effect

tal of KEUR 1,123 in funds flowed to 4SC AG during the reporting year from the capital increases of 29 December 2004, in two tranches. Within the framework of the capital increase of 6 June 2005, an additional KEUR 1,660 in funds was acquired from new shareholders. In connection with the extraordinary shareholders' meeting on 28 September 2005, a capital increase in exchange for cash and in-kind contributions was adopted, which led to an inflow of funds in the amount of KEUR 3,500. A second capital increase in exchange for cash contributions, which was likewise adopted at the extraordinary shareholders' meeting of 28 September 2005, was successfully concluded on 30 November 2005, and resulted in an additional increase in liquid assets of KEUR 5,161. In total, KEUR 11,444 flowed to 4SC AG as a result of these financing measures during the reporting year. In total, the balance of cash and cash equivalents increased compared to the previous year by KEUR 4,820 to KEUR 6,878 (2004: KEUR 2,058) as of the end of the reporting year.

2.3 Earnings position

Net sales totalled KEUR 2,068 in the reporting period. That is a decline of KEUR 955 or 31.6% compared to the KEUR 3,023 listed in the previous year. The background for this decline is the drop in net sales from KEUR 1,667 to KEUR 132 in the "Drug Discovery & Development" segment. This decline by KEUR 1,535 was expected, since 4SC AG did not license out any projects to outside partners in the financial year 2005, but instead concentrated on the independent further development of the project pipeline.

On the other hand, net sales in the "Collaborative Business" segment increased by 42.8% to KEUR 1,936 (2004: KEUR 1,356) as a result of the consistent expansion of this business segment. Overall, 93.6% of the net sales of 4SC AG were attributable to the "Collaborative Business" segment. The other operating income in the amount of KEUR 32 (2004: KEUR 272) result primarily from the subleasing of office space, as well as the release of provisions during the reporting year.

The result of operating activities of 4SC AG totals KEUR - 6,337 in the reporting year, which is thus a reduction of KEUR 879 compared to the previous year (2004: KEUR - 5,458). This decline results from the lower net sales and the one-time expenditures in the amount of KEUR 1,079 arising from the commencement of 4SC AG's listing on the Frankfurt Stock Exchange. Accordingly, the administrative costs increased to KEUR 2,998 (2004: KEUR 1,803). The decline of distribution costs to KEUR 433 (2004: KEUR 625) results from the lower number of employees in the Business Development Department. Since extensive third-party services were purchased for the phase I development of the DHODH Project in the previous year, the research and development costs declined from KEUR 5,402 in the previous year to KEUR 4,259 in the reporting year.
The financial result amounts to KEUR 60 (2004: KEUR - 363). The finance income in the amount of KEUR 267 (2004: KEUR 35) includes the earnings from the application of the Effective Interest Method for long term loans in the amount of KEUR 173 (2004: KEUR 0), earnings from the release of the provision for remuneration claims of silent partners in the amount of KEUR 49 (2004: interest expense in the amount of KEUR 159), interest earnings in the amount of KEUR 37 (2004: KEUR 24), which resulted predominantly from the bank accounts that bore interest close to that of the money market.
The finance expenses in the amount of KEUR 207 (2004: KEUR 395) include primarily the interest payments to the silent partners in the amount of KEUR 169 (2004: KEUR 185) and the interest expenses for convertible bondholders in the amount of KEUR 36 (2004: KEUR 25).

The net period result for the reporting year is KEUR - 6,277 (2004: KEUR - 5,821). The undiluted and diluted result per share is EUR - 0.77 (2004: EUR - 0.89).

The overall situation of 4SC AG has improved substantially compared to the previous year as a result of the financing measures described above and the successful listing on the Frankfurt Stock Exchange and gives the corporation a higher degree of flexibility for further development.

Working in the synthesis laboratory

3. RISK REPORT

3.1 Risk management system and internal control system

As a young and not yet profitable enterprise, 4SC AG is operating in an environment that, in addition to conventional business risks, is confronted with additional risks, particularly in the areas of research and development, intellectual property, cooperation and financing. A comprehensive risk management system has been established in order to identify impending risks in a timely manner and avoid negative effects on 4SC AG.

The risk management system of 4SC AG has been implemented since 2002 and has been continuously optimised and maintained since that time. The system is an integral component of the corporate management and monitoring measures. In accordance with a defined risk management process, the risk managers in the various departments constantly identify, analyse and evaluate risks on a quantitative basis with respect to their appearance, the amount of damage they could potentially cause, the likelihood of occurrence and planned countermeasures. These risks are recorded in an IT-supported risk management and controlling system and reported to the Management Board by the company's risk management officer on a quarterly basis. This risk report provides management with diverse steering information at the project and company level and is thus simultaneously used for controlling the internal research and development projects. At the same time, the risk management system shows existing residual risks. As a result, management can make targeted decisions concerning how to deal with such residual risks.

In addition to the risk management system, 4SC AG has introduced an extensive internal control system, which is likewise constantly optimised. Important components of the internal control system are emergency plans, the second set of eyes principle and signature provisions that contribute to the monitoring and reduction of existing residual risks.

The substantial individual risks listed below are interrelated in some cases and can influence one another positively or negatively.

3.2 Handling of financial instruments

4SC AG constantly monitors its trade receivables, in order to keep the risk of bad debts as low as possible. The funds of 4SC AG are invested exclusively in money market funds and highly-rated bonds within the framework of a conservative investment policy.

3.3 Achieving profitability

As an enterprise that remains focused on research and development, 4SC AG must earn substantial milestone payments, license revenues and revenue participation from license contracts with pharmaceutical and biotech companies in order to reach the profits zone. To date, 4SC AG has earned only a small amount of revenue from milestone payments, license revenues and sales participation from the granting of license rights to third parties; this revenue does not yet enable the self-financing or profitability of the company. In light of this background and taking into account the additional in-house research and development expenditures, the corporation will continue to post a negative operating result for the time being. In order to earn the necessary sales revenues, 4SC AG is dependent upon the conclusion of additional contracts with the pharmaceutical industry and major biotechnology companies; the plan is for these contracts to lead to the desired profitability on a medium-range basis. For this purpose, a regular exchange takes place with a number of pharmaceutical and biotechnology companies.

3.4 Additional financing

During the reporting year 2005, various corporate actions were carried out that ensure the financing of the corporation for the time being and lay a good foundation for achievement of the desired company and development goals. Nevertheless, additional financing measures by means of the procurement of equity and third-party capital will be necessary in order to realise the further goals and growth plans of the corporation and avoid a potential cutting of equity capital in half or illiquidity, possibly in the course of day-to-day business activities. It is not guaranteed that 4SC AG will be able to obtain the financing in a timely manner, in the necessary amount or under favourable terms and conditions.

3.5 Service collaborations

4SC AG currently generates a substantial portion of its sales revenues in the "Collaborative Business" segment with Schwarz Pharma AG, Monheim, and Sanwa Kagaku Kenkyusho Co. Ltd., Nagoya (Japan). Termination of the contracts by one of the partners would have a substantially negative effect on the development of sales revenues, and thus on the future financial and earnings situation. In light of this background, 4SC AG is endeavouring to distribute its sales revenues over multiple cooperation partners and is pursuing an active acquisition policy. Termination of the aforementioned contracts is not foreseeable at this time.

3.6 Industrial proprietary rights for the protection of the active substance candidates

A substantial component for the protection of the company's own technologies and developments, as well as its market potential, consists of the generation of proprietary rights, along with comprehensive patent and licensing strategies. Even if patents have been issued or are issued in the future, the possibility cannot be ruled out that third parties will dispute the validity of the patents in whole or in part or dispute the patent application itself. The mere assertion by third parties that patents or patent applications belonging to 4SC AG might be contestable could have a negative effect on sales revenues, and thus on the financial and earnings situation. Thus far, 4SC AG has not been hit by patent disputes. Nevertheless, the possibility cannot be ruled out that 4SC AG will have to license patents from third parties, in order to be able to further develop and market its own projects or that it will find itself in patent disputes with third parties. It may become necessary to file a complaint, either for the purpose of defending the company's own intellectual property or proceeding against patents and patent applications of third parties that might hinder 4SC AG's further development. Such proceedings are generally protracted and cost-intensive. In order to avoid such conflicts, 4SC AG engages in careful observation of competitors' patents, as well as an application strategy whose goal is the formulation of clear claims and the prompt filing of applications for proprietary rights.

3.7 Risks of product development

As a product-oriented biotechnology company, 4SC AG is subject to the typical development risks, which are particularly pronounced in this industry as a result of the long development times of an active substance. Currently, one product candidate is in the clinical phase; three projects are in the pre-clinical phase, and another is in the research phase. Risks exist that it will not be possible to develop individual or all medication candidates successfully from the standpoint of their effectiveness, side-effects or production or that the necessary approvals will not be issued by the government agencies or will only be issued on a delayed basis.

Currently, SC12267, a potential medication for the treatment of chronic inflammatory diseases such as rheumatoid arthritis, is the most advanced drug candidate. SC12267 has already successfully completed two clinical phase I studies, and the results have led to the identification of a well tolerated daily dose. 4SC AG is currently preparing a clinical phase IIa study to examine the efficacy of SC12267 in patients with rheumatoid arthritis.

4SC AG cannot rule out the possibility that SC12267 might not show sufficiently strong activity in patients or that unexpected safety-relevant side-effects will occur during the first-time use of the substance in patients. The side effects could either be completely new or they can be unexpectedly strongly pronounced. Depending on the seriousness and frequency of the safety-relevant results, such results could lead to a significant delay or even discontinuation of the study. In addition, the possibility exists that it will not be possible to market products and product candidates in an economical manner or that products and product candidates will not be sufficiently competitive.

4SC AG's strategy is to reduce these risks as much as possible by means of a project pipeline of research and development projects that is designed as broadly and risk-balanced as possible. For this reason, all of 4SC AG's projects are regularly and systematically evaluated and are valued within the overall portfolio. In this way, targeted steering measures are carried out to reduce the intrinsic project risk in all individual research and development projects.

3.8 Partners for clinical studies

4SC AG relies on contractual partners, so-called Contract Manufacturing Organisations (CMOs), in the delivery of the pharmaceutical active agent for its drug candidates and in the manufacture of clinical and commercial quantities. If 4SC AG loses one of these partners or if the partner does not deliver active substances in satisfactory quality, sufficient quantity, at acceptable prices or in a timely manner, the clinical development and marketing of its active agent candidates could be substantially delayed. In order to minimise this risk, 4SC AG devotes special attention to the selection and regular evaluation of appropriate CMO's.

3.9 Collaborations on marketing

It is part of 4SC AG's current strategy to cooperate with experienced partners for the foreseeable future in the form of cooperation and license agreements concerning the advanced clinical development and marketing of 4SC AG's existing and future drug candidates. If 4SC AG is not successful in concluding such cooperation or license agreements at terms and conditions that are economically acceptable to the company, or is unable to do so at all, the development and marketing of its existing or future drug candidates could be delayed and its development and marketing costs could increase – or, depending on the situation, 4SC AG could be forced to accept unfavourable economic terms and conditions.

In addition, it is possible that 4SC AG will not receive any milestone payments or license fees in the future if a cooperation partner or license partner does not succeed in developing or marketing one of the active substance candidates of 4SC AG.

If one of these risks comes to pass, this would impair 4SC AG's ability to develop and market one or more of its drug candidates and negatively affect the financial and earnings situation.

For this reason, the company presents its current projects on the market at an extremely early stage and evaluates all potential cooperation partners. Numerous discussions with a wide range of pharmaceutical companies documents the existence of interest in 4SC AG's drug candidates. This also increases the chances of the conclusion of contracts at attractive terms and conditions.

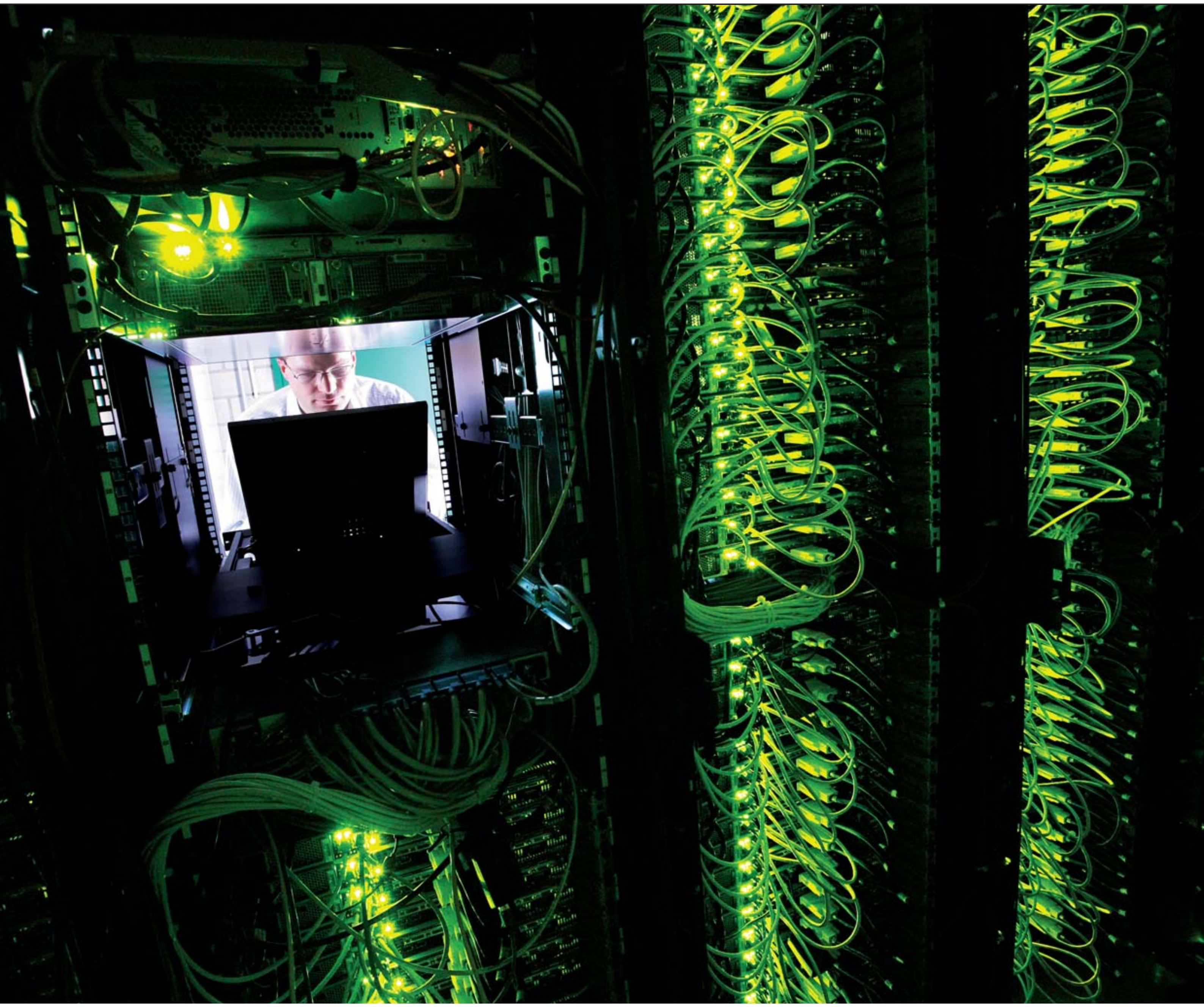
3.10 Key personnel and holders of know-how

The success of 4SC AG depends primarily on its managers and its scientific and technical specialists. Many of these employees have considerable experience with the company and would be difficult to replace. In addition, the competition for specialists is intense in the biotechnology industry, although 4SC AG has always succeeded thus far in filling the relevant positions with suitable employees at reasonable terms and conditions. If 4SC AG loses managers or scientific or technical specialists in key positions or is unsuccessful in the future in acquiring highly qualified personnel, this could have a negative effect on its competitiveness. In addition to competitive salaries, 4SC AG tries to additionally strengthen the employees' loyalty to the company, for example, through employee stock option programmes, as well as active personnel work and leadership work. For this purpose, defined leadership structures and extensive leadership instruments are implemented within the company; they are actively used and continuously developed.

3.11 Industry-specific risks

The industry in which 4SC AG is active is characterised by short technology cycles and high innovative strength. Different technologies could come onto the market, by means of which new drug candidates could be developed more cost effectively and/or rapidly.

The business activity of 4SC AG is subject to extensive legal regulation and controls. The ability to develop and market new drug candidates can be impaired on a lasting basis by administrative, statutory or political processes, over which 4SC AG has only limited influence. However, no such restrictions are foreseeable at this time.



In the server basement, 770 processors ensure the necessary speed for the virtual high throughput screening

4. EVENTS AFTER THE END OF THE FINANCIAL YEAR

In January 2006, an important milestone was reached in the collaboration with Japanese pharmaceutical company, Sanwa Kagaku Kenkyusho Co., Ltd., Nagoya (Japan). As a result, it was possible to post corresponding incoming payments at the end of January 2006. Within the framework of this collaboration, 4SC AG is employing its integrated technology platform with the goal of developing drug candidates for targets provided by Sanwa. 4SC AG will earn additional sales revenues from this in the year 2006 and receive payments that become due when further defined milestones are reached. In addition, 4SC AG will receive revenue participation in the event of subsequent successful marketing of the active agents.

5. OUTLOOK OF FURTHER BUSINESS DEVELOPMENT

5.1 Outlook for the overall economy

In principle, the International Monetary Fund (IMF) sees a positive outlook for 2006 with slightly above-average growth compared to the long-term trend, along with continued moderate inflation. However, the IMF makes a strong distinction between the individual economic regions. Whereas the USA should lose some dynamic strength with respect to economic growth, but nevertheless have stable development at the forecasted growth rate of 3.3%, Europe, with a forecast of 1.8% for 2006, will continue to be unable to keep up with the growth rate of 4.25% forecasted for the world economy. This is attributed, above all, to the lack of industrial demand and the lack of structural reforms. For Germany, institutions such as ifo-Konjunkturtest, GfK-Konsumklima and ZEW have been speaking of a brightening of the business climate relatively consistently since mid-2005.

5.2 Outlook for the biotechnology industry

Corporate news in the first two months of 2006, particularly in the German biotechnology sector, appears to confirm the positive trend started in the reporting year 2005. It is likewise pleasing for the biotechnology industry that the medium-size and large pharmaceutical companies, which frequently lack a supply of innovative drug candidates, are looking to biotechnology companies increasingly earlier. This development, combined with a further maturing product portfolio and increasing market proximity of the biotechnology industry, will lead to further attractive collaborations and license agreements between the pharmaceutical and biotechnology industries and further increase the value of biotechnology products. On the capital side as well, various studies assume that the issuing activity will have a stimulating effects internationally and that biotechnology companies will be increasingly able to cover their needs with funding on the capital market.

Overall, the outlook for the industry is once again optimistic. However, the market environment continues to be a major challenge, which will make its presence felt, in particular, through a high degree of selectivity in the financial area and in pharmaceutical collaborations. In addition, the positive picture should not be allowed to hide the continuing consolidation pressure and the risks inherent in biotechnology (failure of development candidates, for example).

In Germany, in particular, individual pieces of long-awaited corporate news will have a signal effect for the entire industry. This is true, for example, of the further development of the leading product candidates of GPC Biotech and MediGene.

Management Board of 4SC AG (from left to right: Dr Daniel Vitt, Dr Ulrich Dauer, Enno Spillner and Dr Gerhard Keilhauer)

5.3 Company outlook

5.3.1 Research, development and collaborations

In the "Drug Discovery & Development" segment, the plan for 2006, with respect to the leading project from the Development segment (DHODH), is to meet all formal prerequisites for entering into a clinical phase IIa and start the clinical phase IIa. In addition, 4SC AG plans to advance one to two additional in-house product candidates from the research and pre-clinical phase toward phase I.

At the same time, the process for identifying licensees and cooperation partners for the in-house projects will be expedited intensively. The company is in regular discussions with various potential collaboration partners in this regard. In the future, it is intended that the "Drug Discovery & Development" segment make a growing contribution to the self-financing of 4SC AG and, on the median-range basis, generate the predominant portion of the company's revenues.

The plan is to further develop the "Collaborative Business" segment with existing and new customers in the financial year 2006. Currently this segment relies primarily on the two collaboration partners Schwarz Pharma AG, Monheim, and Sanwa Kagaku Kenkyusho Co., Ltd., Nagoya (Japan). It is intended that this customer base shall be broadened in 2006, for which purpose 4SC AG is already in negotiations with various industrial partners. Overall, it is intended that this segment continues to finance itself from its own sales revenues.

Arising from the collaboration with Sanwa Kagaku Kenkyusho Co., Ltd., Nagoya (Japan), described in section 4, 4SC AG intends to earn further sales revenues and possibly receive payments that become due when additional defined milestones are reached.

5.3.2 Employees

4SC AG is well equipped for its current tasks from a personnel standpoint and will be able to realise further developmental steps on this basis. In addition to some replacement hiring, additional experts are being recruited for individual, newly created positions. Overall, moderate personnel growth is planned.

5.3.3 Financial goals

4SC AG is still in the development phase. This means, firstly, increasing development costs with the advancement of the project pipeline in the clinical phases, but, secondly, increasing out-licensing and sales revenue potential as well. For the financial year 2006, the company expects an overall negative net period result, as in the previous year, but, as a result of sales revenues in the "Collaborative Business" segment and the potential first license revenues from the "Drug Discovery & Development" segment, the negative net period result will probably be less than in the reporting year. The challenge with respect to financial planning will be predicting when and in what amount out-licensing will take place.
Based on funds raised within the financial year 2005 as well as planned revenues, the further financing of the company is secured for the next two years. Further measures, which go beyond those mentioned above, will be contemplated openly and taken, if considered attractive or necessary.

All in all 4SC AG considers itself well positioned for achieving its strategic and commercial goals, since the company, according to the management board's view, can be significantly further developed through the closing of revenue relevant service, collaboration and out-licensing contracts over the forthcoming 24 months.

Martinsried, 17 March 2006

Dr Ulrich Dauer, CEO

Dr Gerhard Keilhauer, CDO

Dipl.-Kfm. Enno Spillner, CFO

Dr Daniel Vitt, CSO

FINANCIAL STATEMENTS (IFRS)

INCOME STATEMENT

for the financial year from 1 January to 31 December 2005

in KEUR	2005	2004	Notes
Net sales	2,068	3,023	4.1
Cost of sales	- 600	- 340	4.3
Gross profit	**1,468**	**2,683**	
Distribution costs	- 433	- 625	4.4
Research and development costs	- 4,259	- 5,402	4.5
Administrative costs	- 2,998	- 1,803	4.6
Other operating income	32	272	4.7
Other operating expenses	- 147	- 226	4.8
Impairment of goodwill	0	- 357	4.10
Result from operating activities	**- 6,337**	**- 5,458**	
Financial result			4.11
Loss from an associate accounted for according to the equity method	0	- 3	
Finance income	267	35	
Finance expenses	- 207	- 395	
Financial result	**60**	**- 363**	
Period result	**- 6,277**	**- 5,821**	
Earnings per share (undiluted and diluted, EUR)	- 0.77	- 0.89	6.

BALANCE SHEET – ASSETS

for the financial year ended 31 December 2005

in KEUR	2005-12-31	2004-12-31	Notes
ASSETS			
Non-current assets			
Intangible assets	1,851	1,897	7.1
Fixed assets	1,503	2,171	7.2
Receivables from associated companies	162	214	7.3
Total non-current assets	**3,516**	**4,282**	
Current assets			
Inventories	14	15	7.5
Trade receivables	205	49	7.6
Receivables from an associate	21	4	7.3
Cash	368	2,058	7.7
Current asset securities	6,510	0	7.8
Other current assets	374	238	7.9
Prepaid expenses and accrued income	236	84	7.10
Total non-current assets	**7,728**	**2,448**	
TOTAL ASSETS	**11,244**	**6,730**	

BALANCE SHEET – EQUITY AND LIABILITIES

for the financial year ended 31 December 2005

in KEUR	2005-12-31	2004-12-31	Notes
EQUITY AND LIABILITIES			
Equity			7.11
Subscribed capital	10,530	6,956	
Additional paid-in capital	13,303	1,392	
Retained earnings	67	67	
Loss carryforward	- 8,464	- 2,643	
Period result	- 6,277	- 5,821	
Total equity	**9,159**	**- 49**	
Non-current liabilities			
End remuneration claims of silent partners	0	571	7.12
Long-term loans	747	0	7.13
Convertible bonds	0	17	7.14
Liabilities due to silent partners	0	2,905	7.15
Total non-current liabilities	**747**	**3,493**	
Current liabilities			
Provisions	785	142	7.16
Financial leasing obligations	0	41	7.17
Convertible bonds	0	2,504	7.14
Trade payables	271	122	7.19
Accounts payable to associated companies	29	29	7.20
Down payments received	0	225	7.21
Other current liabilities	253	223	7.22
Total current liabilities	**1,338**	**3,286**	
TOTAL EQUITY AND LIABILITIES	**11,244**	**6,730**	

CASH FLOW STATEMENT

for the financial year from 1 January to 31 December 2005

in KEUR	2005	2004	Notes
Cash flows from operating activities:			8.1
Period result before taxes	- 6,277	- 5,821	
Corrections for:			
Scheduled depreciation on fixed assets and intangible assets and impairment of goodwill	819	1,315	
Loss/Gain from the retirement of fixed assets	0	1	
Non-cash affecting expenses and income	344	- 90	
Financial result	- 60	363	
Non-cash affecting change of end remuneration claims	- 279	159	
Repayment of end remuneration claims	- 292	0	
Interest received	37	24	
Interest paid	- 206	- 212	
Decrease/Increase of trade receivables	- 156	229	
Decrease/Increase of accounts receivable from associated companies	35	- 218	
Decrease of inventories	1	3	
Decrease/Increase of other current assets	- 136	34	
Decrease/Increase of prepaid expenses and accrued income	- 152	41	
Decrease/Increase of trade payables	149	- 160	
Increase of accounts payable to associated companies	0	29	
Decrease of down payments received	- 225	- 9	
Increase/Decrease of provisions	643	- 77	
Increase/Decrease of other current liabilities	30	- 14	
Cash flows from operating activities:	**- 5,725**	**- 4,403**	
Cash flows from investing activities:			8.2
Purchase of intangible assets	- 33	0	
Purchase of fixed assets	- 76	- 50	
Proceeds from sale of fixed assets	2	2	
Acquisition of an associate	0	- 12	
Interest paid for financial leasing	- 1	- 11	
Cash flows from investing activities:	**- 108**	**- 71**	

in KEUR	2005	2004	Notes
Cash flows from financing activities:			8.3
Payments to subscribed capital	2,434	410	
Payments to additional paid-in capital	9,010	665	
Payments from issuance and redemption of convertible bonds	- 21	2,478	
Financial leasing obligations	- 41	- 201	
Repayment of liabilities due to silent partners	- 729	0	
Cash flows from financing activities:	**10,653**	**3,352**	
Net change in cash and cash equivalents	**4,820**	**- 1,122**	
+ Cash and cash equivalents at the beginning of the period	2,058	3,180	
= Cash and cash equivalents at the end of the period	**6,878**	**2,058**	

The cash flow statement was prepared in accordance with the provisions of IAS 7.
The cash and cash equivalents break down as follows:

in KEUR	2005-12-31	2004-12-31	Notes
Cash	368	2,058	7.7
Current asset securities	6,510	0	7.8
	6,878	**2,058**	

STATEMENT OF CHANGES IN EQUITY

for the financial year from 1 January to 31 December 2005

in KEUR	Subscribed capital	Additional paid-in capital shares	Additional paid-in capital WSV[1]	Additional paid-in capital ESOP[2]	Retained earnings	Loss carryforward	Total
Balance on 2004-01-01	**12,808**	**15,278**	**16**	**14**	**67**	**- 23,688**	**4,495**
Issued options (ESOP 2003)				56			56
Issuance of options (ESOP 2004)				5			5
Issued convertible bonds to the Supervisory Board				3			3
Redemption of convertible bonds to the Supervisory Board			- 4				- 4
Capital increase of 29 December 2004	552	665					1,217
Capital reduction of 29 December 2004	- 6,404	- 14,641				21,045	0
Period result 2004						- 5,821	- 5,821
Balance on 2004-12-31	**6,956**	**1,302**	**12**	**78**	**67**	**- 8,464**	**- 49**
Payments into additional paid-in capital due to capital increase of 29 December 2004		229					229
Issued options (ESOP 2003)				23			23
Issued options (ESOP 2004)				14			14
Issued convertible bonds to the Supervisory Board				2			2
Payments into additional paid-in capital due to capital increase of 29 December 2004 (2nd tranche)		894					894
Capital increase of 6 June 2005	392	1,268					1,660
Exercise of convertible bonds	786	1,714					2,500
Redemption of convertible bonds to the Supervisory Board			-1				- 1
Issuance of options (ESOP 2005)				3			3
Capital increase of 28 September 2005	2,396	7,765					10,161
Period result 2005						- 6,277	- 6,277
Balance on 2005-12-31	**10,530**	**13,172**	**11**	**120**	**67**	**- 14,741**	**9,159**

1: WSV = convertible bond; 2: ESOP = option programme for employees and Management Board

Additional explanations concerning the components of and changes in equity can be found in “7.11 Equity”.

NOTES TO THE FINANCIAL STATEMENTS 2005

for the financial year from 1 January to 31 December 2005

1. Business activity

4SC AG, headquartered at Am Klopferspitz 19a, 82152 Martinsried, is registered in the Commercial Register of the Munich Municipal Court under HRB no. 132917. A Commercial Register excerpt of 11 January 2006, with the most recent entry dated 13 December 2005, which documents the resolutions of the extraordinary shareholders' meeting of 28 September 2005, has been received. The pre-listing capital increases of 28 September 2005, and 30 November 2005, are documented in this Commercial Register excerpt. These capital increases are also fully reflected in these financial statements.

The version of the articles of incorporation dated 30 November 2005, is in effect.

The shares of 4SC AG are listed under the stock exchange abbreviation VSC, securities identification number 575381 and ISIN DE0005753818, on the Regulated Market (Prime Standard) of the Frankfurt Stock Exchange.

The purpose of the enterprise is the identification, research and optimisation of active agents and the development, use and marketing of chemical, biotechnological and computer processes.

The company is authorised to engage in all transactions that are expedient to and foster the achievement of the corporate purpose. For this purpose it is also permitted to found, acquire, obtain equity interests in and assume the management of other enterprises domestically and abroad, lease companies or business operations, conclude intercompany agreements, particularly profit transfer and control contracts, and establish branch offices and field offices domestically and abroad.

The financial year is the calendar year.

2. Basis of preparation and significant accounting and valuation policies

2.1 Basis of preparation

The present financial statements were created in their entirety in accordance with the accounting specifications of the International Financial Reporting Standards (IFRS) and according to the requirements of the International Accounting Standards Board (IASB). The recommendations of the Standing Interpretations Committee (SIC) and the International Financial Reporting Interpretations Committee (IFRIC) have been taken into account. All the IFRS adopted by the European Commission have been taken into consideration. As a basic principle, new standards adopted by the IASB are applied from the financial year from which their use is mandatory. Since the financial year 2003, and as exceptions to this basic principle, the IFRS 1 and 2, IAS 8, 10 and 33 as well as IAS 32 and 39 are being used on a voluntary basis even before they come into force. The voluntary adoption of these provisions did not have any material impact on the asset, financial and profit situation of 4SC AG.

Newly adopted standards and interpretations that have not been used in the financial year 2005 will either never be applied by 4SC AG or will not have any material impact on the asset, financial and profit situation of the company. These standards and interpretations concern IFRS 4 (Insurance Contracts), IFRS 5 (Non-current Assets Held for Sale and Discontinued Operations), IFRS 6 (Exploration for and Evaluation of Mineral Resources), IFRS 7 (Financial Instruments: Disclosures), IFRIC 1 (Changes in Existing Decommissioning, Restoration and Similar Liabilities), IFRIC 2 (Members' Shares in Co-operative Entities and Similar Instruments), IFRIC 3 (Emission Rights), IFRIC 4 (Determining whether an Arrangement contains a Lease), IFRIC 5 (Rights to Interests Arising From Decommissioning, Restoration and Environmental Rehabilitation Funds) and IFRIC 6 (Liabilities arising from Participating in a Specific Market – Waste Electric and Electronical Equipment).

During the preparation of the financial statements, the management had to make a few estimates and assumptions that influence the disclosed value of the assets and liabilities and the disclosure of uncertain assets and eventual liabilities as per the balance sheet date and of the expenditure and revenue within the reporting period. The actual value may deviate from these estimates.
The management makes these arbitrary decisions, in particular in the estimate of the recoverability of losses carried forward by estimating their ability to be allocated to future profits, in the depreciation of receivables by having to evaluate the potential to collect a receivable and in the assessment of the impairment of the goodwill. For the purpose of the last-mentioned required estimate of the value in use, 4SC AG has to estimate the anticipated future cash flows from the cash-generating unit and select the appropriate discount rate. Furthermore, the management has to assess whether it exerts a dominating influence on quattro research GmbH, Martinsried, and thus whether a consolidation obligation exists in accordance with IAS 27. The management has concluded that the requirements for an effective control of quattro research GmbH, Martinsried, do not exist.
In the management's view, the requirements for a consolidation of quattro research GmbH as a special purpose entity in accordance with SIC-12 do not exist either.

4SC AG classifies assets and liabilities as current if their realisation or amortisation is expected within the next twelve months from the balance sheet date, if these are primarily kept for trading purposes or if they are cash and cash equivalents.

In accordance with the accounting option according to IAS 1.88, 4SC AG has drawn up its income statement according to the cost-of-sales method.

The principle of the going concern in accordance with IAS 1.23 has been taken into consideration.

Expenditure and revenue positions are shown separately and only balanced to the extent permitted in accordance with IAS 1.32 et sqq.

The present financial statements represent the individual statements of the Germany based 4SC AG and, in addition to 4SC AG, also take into consideration the associated company quattro research AG, Martinsried.

The currency of presentation is the euro; the degree of precision used in the presentation is thousand euros (KEUR). Initially all positions of a foreign currency transaction are converted in the functional currency with the exchange rate between the functional currency and the foreign currency valid on the respective day of the business transaction (IAS 21.21). For each balance sheet date, monetary positions in a foreign currency are converted according to IAS 21.23 using the exchange rate on the respective date. Non-monetary positions that are evaluated in a foreign currency do not exist at 4SC AG.

The annual statement was approved by the Management Board on 27 March 2006 for publication.

2.2 Significant accounting and valuation policies

The following accounting and valuation policies were material in the drawing up of the annual statement.
Except for one change, the accounting and valuation policies used correspond to those of the annual statement as per 31 December 2004. This change refers to the goodwill, which is included in the balance sheet with effect from this reporting year in accordance with the specifications of IFRS 3 and thus is no longer amortised from this reporting year onwards. The effects of this change are explained below under 'Goodwill' and under Point "7.1 Intangible assets".

Intangible assets

Intangible assets acquired are recognised at their acquisition costs when accounted for the first time. After they have been accounted for the first time, intangible assets are recognised with their acquisition costs less all regular cumulated linear depreciation. The estimated useful life of the assets is based on the scheduled depreciation of the asset. The assumed useful life is between three and five years depending on the asset. An intangible asset is either derecognised when it is disposed of or when no further commercial use is to be expected from using it further or selling it. The profits or losses resulting from the derecognition of the asset are determined as the difference between the net sales proceeds and the book value, and recognised and recorded as income or expenses in the income statement in the period in which the position is derecognised. Research costs are recorded as expenditure in the period in which they are incurred. An intangible asset that is generated from the development within the framework of an individual project is only then capitalised when the technical feasibility of the completion of the intangible asset and the intention to complete, use or sell these can be proven. The criteria for a capitalisation of development costs in accordance with IAS 38.57 are not fulfilled.

Goodwill

The goodwill shown in the balance sheet results from the fusion of 4SC GmbH into 4SC AG in 2000. In the capitalisation of goodwill, the company has made use of a de facto accounting option with regards to the method used. The goodwill was capitalised at acquisition costs and linearly amortised as planned over a useful life of ten years up to and including the financial year 2004. For the financial year starting 1 January 2005, the regulation of IFRS 3 will be adopted for the first time. The transitional regulation used is IFRS 3.79. Accordingly, from the financial year 2005 onwards the planned amortisation of the goodwill will be stopped, the book value of the associated cumulated amortisations will be offset with an appropriate reduction of the goodwill and the goodwill checked at least once a year for impairment in accordance with IAS 36. Impairment on the goodwill is recognised if the carrying amount is less than the book value of the asset value. The carrying amount of an asset is the higher amount of the current market value minus divestiture costs and value in use. As the goodwill does not generate any independent cash flows, the carrying value is determined for the cash-generating unit, which the goodwill belongs to or to which it can best be allocated. For this impairment test, 4SC AG allocates the goodwill to the project DHODH as the cash-generating unit. For the impairment test, the value in use of the DHODH project is compared with the book value of the goodwill. To determine the value in use, a risk-adjusted cash flow forecast is calculated for the period of further development up until the expiry of the project patents in 2020. The cash flows determined are discounted with a risk-adjusted rate of interest that is customary in the market. Important factors in the determination of the creation of the cash flow forecast are the discounting rate, the market entry probability and the market share.
The discontinuation of the planned amortisation gives rise to an improvement of the period result from the financial year 2005 – before taking into account contingent amortisation due to an impairment test – by KEUR 357.

Fixed assets

The fixed assets are recognised at acquisition costs and reduced by planned linear depreciation. The sums of cash and cash equivalents used to procure the asset are calculated as the acquisition costs. The planned depreciation is based on the estimated useful life of the assets. The assumed useful life is between three and fourteen years depending on the investment. The book values of the fixed assets are checked for impairment as soon as there are indications that the book value of an asset exceeds its carrying value. A fixed asset is either derecognised when it is disposed of or when no further commercial use is to be expected from using it further or selling it. The profits or losses resulting from the derecognition of the asset are determined as the difference between the net sales proceeds and the book value and recognised and recorded as income or revenue in the income statement in the period in which the position is derecognised. The residual values of the assets, useful life and depreciation methods are checked at the end of each financial year and adapted where necessary. The development of the fixed assets and the intangible assets is shown in the asset schedule under point "7.2 Fixed assets" in accordance with IAS 16.73.

Borrowing Costs

In accordance with IAS 23.4, costs of borrowing are not included in the acquisition costs. Instead, they are recognised as expenditure in accordance with the benchmark method of IAS 23.7.

Receivables from associated companies

The capitalisation of receivables from associated companies is done at acquisition costs that correspond to the value at the effective date of the given return service. The receivables from associated companies are returned in accordance with a defined amortisation plan and reduced by the sum of the payment received. The payments resulting from the amortisation plan are shown separately in the balance sheet as current- or non-current positions. As interest is paid on the receivables at usual market conditions, the effective interest method is not applied.

Financial assets

At the beginning of January 2004, the spin-off of an independent company, quattro research GmbH, was completed. 4SC AG holds a shareholding of 48.8% in this company. 4SC AG provides just one of three members of the Advisory Board of quattro research GmbH and thus has no dominating influence on the business policy of this company. Consequently, the share in the company as an associated company is entered in the balance sheet according to the specifications of IAS 28 and using the equity method. According to the equity method, shares in an associated company are recorded in the balance sheet at acquisition costs plus changes to the share of 4SC AG in the net assets of the associated company that occur after the acquisition. The goodwill connected with an associated company is included in the book value of the share and is not subject to amortization. When using the equity method, 4SC AG ascertains whether it is necessary to take into account additional impairment loss with regards to the net investment of 4SC AG in the associated company. The income statement includes the share of 4SC AG in the profit of the associated company. Changes that are recognised directly in the equity capital are also recognised by 4SC AG to the sum of their share directly in the equity capital and – where necessary – included in the statement of changes in equity. The effective date of the balance sheet and the accounting and valuation methods for similar business transactions and events of the associated company and 4SC AG comply with one another.

Inventories

The stock of raw, auxiliary and operating materials is valued at the lower value of acquisition or manufacturing costs and net sales proceeds in accordance with IAS 2.9. The FIFO method in accordance with IAS 2.27 is used as an allocation procedure.

Trade receivables

Trade receivables are accounted for at the original invoice amount minus a value adjustment for doubtful receivables. Value adjustments for doubtful receivables are based on the assessment of the management regarding the potential to collect certain customer receivables and on the age structure of the receivables from goods and services. Receivables are derecognised as soon as they are considered irretrievable.

Cash and cash equivalents

The liquid funds include the cash assets, bank deposits and short-term deposits.

Current asset securities

The current assets securities are classified "at fair value through profit or loss" in accordance with IAS 39.9. They serve as the interest-bearing investment of liquid reserves available at short notice.

In accordance with IAS 39.43, the securities are calculated at the acquisition costs and the transaction costs, and are valued as per the effective date of the balance sheet with the carrying amount that corresponds to the value on the stock market. Changes in value of the carrying amount are recognised as income or expenditure and shown in the income statement. Acquisitions and sales are entered in the balance sheet at the price on the day of trading.

The current asset securities are extremely liquid financial investments that can be converted into cash at any time and are only subject to minor fluctuations in value. They thus fulfil the requirement to be used as cash equivalents in the cash flow statement.

End remuneration claims of silent partners and liabilities due to silent partners

The liabilities due to silent partners from the prior year and the resulting end remuneration claims have been valued at acquisition costs using the effective interest method.

Long-term loans

The long-term loans are recognised at the carrying amount that results from the discounting of the repayment obligations with a risk-adjusted rate of interest that is equivalent to the loan duration and corresponds to the usual market conditions. After initial recognition, the long-term loans are valued at amortised costs using the effective interest method.

Convertible bonds

The valuation and disclosure of convertible bonds from the prior year is done in accordance with IAS 32 and IAS 39, i.e. with a division into equity and debt capital.

Provisions

Provisions are recognised in accordance with IAS 37.14 when there is a current legal or de facto obligation from an event in the past, the outflow of resources is probable and a reliable estimate of the total sum of the obligation is possible. The costs of forming the provision are shown in the income statement.

Finance lease

In the prior year, the 4SC AG lease items were classified as finance leases in accordance with IAS 17.4, since the opportunities and risks from the underlying contracts were largely transferred to the 4SC AG.
The lease items are recognised in the balance sheet as assets in the amount of the lease item's attributed present value at the beginning of the leasing relationship. This asset will be amortised over the estimated useful life. A liability from finance leasing is recognised in the same amount as the asset. This liability is amortised over the period of the leasing contract.
The lease payments made will be divided up between the financing costs and the amortised portion of the residual debt. The financing costs will thereby be distributed over the period of the leasing relationship, so that a constant interest rate will exist over the period of the remaining residual debt.

Trade payables

The trade payables are short-term debts in accordance with IAS 1.60 and will be recognised accordingly with the repayment amount. Trade payables will be derecognised when the underlying liability for this debt is fulfilled or has expired. Foreign currency debts will be recognised based on the period end exchange rate.

Down payments received

Down payments received in advance from customers are to be accounted for separately as debts for future commitment to the provision of a scientific service and are to be recognised with the value of the service to be provided. These prepayments will be released immediately in accordance with the contractual service progress and derecognised after complete service delivery.

Revenue recognition

In conjunction with the company's discovery and cooperation agreements, the 4SC generates revenues from upfront payments, milestone payments, royalties and license fees.
Revenues from discovery and cooperation agreements will be included as discovery payments, which were made within the framework of the respective cooperation agreements. These amounts will be calculated, in general, in accordance with the nature of their services on the basis of lump sum payments per included scientist ("FTE"). The number of the FTEs will be agreed upon in advance in the cooperation agreements. Incoming payments will be treated as prepayments received before the fulfilment of the service and released as earnings at the end of every period according to the actual service progress made according to project management.
Upfront payments accrue at the beginning of a cooperation. This is a prepayment upon closing of a contract, without having already performed a specific service. Revenues from upfront payments will be recognised as revenue accrual items and realised as earnings divided over the term of the contract.
Milestone payments are pursuant to the achievement of previously defined contractual goals. The achievement of milestones is dependent on the basic prerequisites so that the resulting revenues cannot be recognised as such after the milestone has been completely achieved and the business partners have confirmed the achievement of the contractual content.

Royalties are revenues, which result from the sale of products or product prospects arising from research work within the framework of the cooperation agreements. They will be recognised as sales at the point in time from which the cooperation partner generates external revenues that lead to the accrual of royalties.
Licenses will be assigned for a contractually defined period during which the revenues will be treated accordingly as license fees and recognised as sales.
The services performed in the "Collaborative Business" segment will be periodically realised as revenue based on services rendered. Licensing in the segment "Drug Discovery & Development" will be defined as starting at the time of the transfer of the user rights to the licensee and recognised as revenue over the term of the license.
IAS 11 is not applicable given that during the performance of services, they are not dealing with a long-term, customer specific product based on IAS 11.3 and IAS 11.5.

Cost of sales
All personnel, material and other costs, which are directly attributable to sales, will be accounted for as cost of sales.

Distribution, research and development and administrative costs
The following costs from the respective functional areas will be included as distribution costs, research and development costs and administrative costs:

- Direct personnel and material costs
- Depreciations
- Other direct costs
- Prorated overhead

Public grants
In accordance with IAS 20.12, the public sector grants will be recognised as revenues in the period in which the expense that should be compensated by the grant occurs. Since this grant is a reimbursement of research expenses, these will be netted with the research and development costs from the relevant period and illustrated separately in the notes.

3. Segment report

The following segment reporting has been prepared in accordance with the principles of IAS 14.

The primary segment report format is the business segments in which 4SC AG is active. According to IAS 14.26, the secondary report format is geographical segments.

4SC AG is active in the two business segments of “Drug Discovery & Development” and “Collaborative Business”. In the “Drug Discovery & Development” segment, 4SC AG is the holder of proprietary and patent rights and decides on the progress of projects. In contrast, the cooperation partner in the “Collaborative Business” segment is the holder of proprietary and patent rights and decides on project progress.

Segment report according to business segments:

in KEUR	Drug Discovery & Development		Collaborative Business		Not assigned		Consolidated	
	2005	**2004**	**2005**	**2004**	**2005**	**2004**	**2005**	**2004**
Net sales	132	1,667	1,936	1,356	0	0	2,068	3,023
Personnell expenses	- 1,633	- 1,808	- 543	- 448	- 1,393	- 1,239	- 3,569	- 3,495
Depreciation	- 497	- 663	- 211	- 115	- 111	- 537	- 819	- 1,315
Other income and expenses	- 1,430	- 2,220	- 612	- 406	- 1,975	- 1,045	- 4,017	- 3,671
Segment result/Result from operating activities	**- 3,428**	**- 3,024**	**570**	**387**	**- 3,479**	**- 2,821**	**- 6,337**	**- 5,458**
Financial result							60	- 363
Period result							**- 6,277**	**- 5,821**
Segment assets	1,091	1,702	584	346	9,569	4,682	11,244	6,730
Segment liabilities	0	35	0	229	2,085	6,515	2,085	6,779
Investments	31	17	31	2	47	31	109	50

In particular, the administrative costs are not assigned. Only net sales with external customers will be realised and shown.

Net sales according to location of customers:

in KEUR	Germany		Japan		EU		USA		Switzerland		Consolidated	
	2005	**2004**	**2005**	**2004**	**2005**	**2004**	**2005**	**2004**	**2005**	**2004**	**2005**	**2004**
Net sales	1,371	847	450	0	245	509	2	0	0	1,667	2,068	3,023

Germany is the geographical location of the overall segment assets and the segment investments.

4. Notes to the income statement

4.1 Net sales

in KEUR	2005	2004	Change
Drug Discovery & Development	132	1,667	- 92.1%
Collaborative Business	1,936	1,356	42.8%
	2,068	**3,023**	**- 31.6%**

The reason for the decline in net sales is the decreased net sales in the “Drug Discovery & Development” segment, which could not be offset by the increased net sales in the “Collaborative Business” segment.
In the “Drug Discovery & Development” segment, the net sales in the reporting year total KEUR 132 (2004: KEUR 1,667). That is a decline of KEUR 1,535 or 92.1% compared to the previous year. The reason for this decline is the fact that no significant licensing revenues were earned in the reporting year as expected. In the previous year, in contrast, revenue in the amount of KEUR 1,667 was realised from an option agreement for the DHODH Project by a Swiss biopharmaceutical company.
In the “Collaborative Business” segment, the net sales in the reporting year total KEUR 1,936 (2004: KEUR 1,356). This is an increase of KEUR 580 or 42.8%. The reason for this increase is the fact that two long-term collaborations involving major volumes were completed during the reporting year, which generated a total of 75% of the net sales. The net sales consist in substantial part of FTE payments and result-dependent milestone payments. The increase of net sales thus reflects the strategic focus of the “Collaborative Business” segment to increase the value-creation share of 4SC AG in collaborations with biotech and pharmaceutical companies.

4.2 Personnel costs

in KEUR	2005	2004	Change
Wages and salaries	3,019	2,891	4.4%
Social security charges	510	543	- 6.1%
ESOP[1]	40	61	- 34.4%
	3,569	**3,495**	**2.1%**
Employees (incl. Management Board)	52	61	- 14.8%

1: ESOP = Employee stock option programme for employees and Management Board

In spite of the declining average number of employees, the personnel costs grew in comparison to the prior year, due to the fact that on the one hand, severance payments totalling KEUR 80 were paid out in the reporting year and on the other hand, no provision was built in the annual financial statements 2004 for the management bonuses totalling KEUR 62, since during the compilation of the annual financial statements 2004 the prerequisite for the creation of a corresponding reserve did not exist.
The employee and management salary waiver contributions to direct insurance were paid in this reporting year. These contributions are to be classified as defined contribution plans and will be recognised and valuated in accordance with IAS 19.44. The total amount of the expenditure to the defined contribution plan equals KEUR 63 in the reporting year (2004: KEUR 56). Out of the total sum, KEUR 13 (2004: KEUR 12) is attributable to members of the Management Board.

In addition, the options issued to the employees and Management Board members during the reporting year in accordance with the provisions of IFRS 2 were recognised as personnel costs. The total amount of the personnel costs resulting from the option issuance is KEUR 40 (2004: KEUR 61). Of that amount, KEUR 8 (2004: KEUR 5) is attributable to members of the Management Board.
The personnel costs are recognised in the income statement under the “Costs of sales,” “Distribution costs,” “Research and development costs” and “Administrative costs” items according to their functional affiliation.

4.3 Cost of sales

in KEUR	2005	2004	Change
Personnel	367	268	36.9%
Material	179	72	148.6%
Miscellaneous	54	0	n/a
	600	**340**	**76.5%**

The rise in the cost of sales is attributable in substantial part to the increased net sales in the “Collaborative Business” segment.

4.4 Distribution costs

in KEUR	2005	2004	Change
Personnel	301	442	- 31.9%
Rent and ancillary rent costs	43	41	4.9%
Travel and meetings	40	41	- 2.4%
Legal consulting and miscellaneous consulting	19	53	- 64.2%
Miscellaneous	30	48	- 37.5%
	433	**625**	**- 30.7%**

The decline in distribution costs is attributable in substantial part to the lower number of employees in the “Business Development” department.

4.5 Research and development costs

in KEUR	2005	2004	Change
Personnel	1,808	1,988	- 9.1%
Third-party services	820	1,335	- 38.6%
Depreciation	707	778	- 9.1%
Rent and ancillary rent costs	639	629	1.6%
Patents	200	178	12.4%
Material	180	235	- 23.4%
Software licenses	122	150	- 18.7%
Miscellaneous	109	178	- 38.8%
Public grants (EU and BMBF)	- 326	- 69	372.5%
	4,259	**5,402**	**- 21.2%**

The decline in research and development costs is attributable in substantial part to the extensive third-party services for the clinical phase I development of the DHODH project, which were performed in the previous year. Thus, research and development costs were reduced by approximately KEUR 650. In addition, it was possible to collect substantially more public grants than in the previous year as a result of the beginning of subsidisation within the "BioChance" programme of the BMBF (Federal Ministry of Education and Research). Thus, research and development costs were reduced by further KEUR 214.

4.6 Administrative costs

in KEUR	2005	2004	Change
Personnel	1,092	797	37.0%
Public listing	1,079	0	n/a
Rent and ancillary rent costs	255	260	- 1.9%
Legal consulting and miscellaneous consulting	262	261	0.4%
Depreciation	109	174	- 37.4%
Insurance and contributions	53	69	- 23.2%
Travel and meetings	27	60	- 55.0%
Miscellaneous	121	182	- 33.5%
	2,998	**1,803**	**66.3%**

The rise in administrative costs is attributable in substantial part to the implementation of the listing on the Frankfurt Stock Exchange in December 2005. This resulted in the incurrence of costs in the amount of KEUR 1,079 in the reporting year.

4.7 Other operating income

in KEUR	2005	2004	Change
Sublease quattro research GmbH	16	15	6.7%
Release of provisions	11	36	- 69.4%
Sale of software quattro research GmbH	0	211	- 100.0%
Miscellaneous	5	10	- 50.0%
	32	**272**	**- 88.2%**

The decline in other operating income is attributable in substantial part to the fact that a software package was sold to quattro research GmbH, Martinsried in the amount of KEUR 211 in the previous year.

4.8 Other operating expenses

in KEUR	2005	2004	Change
Impairment of trade receivables	84	168	- 50.0%
Supervisory Board	40	37	8.1%
Monetary transactions	19	8	137.5%
Miscellaneous	4	13	- 69.2%
	147	**226**	**- 35.0%**

The decline in other operating expenses compared to the previous year results in substantial part from the lower impairments of trade receivables in the amount of KEUR 84 (2004: KEUR 168).

4.9 Planned depreciation

in KEUR	2005	2004	Change
Planned depreciation	**819**	**958**	**- 14.5%**

The decline in planned depreciation is attributable in substantial part to the fact that only a small quantity of replacement investments were made during the reporting year and, at the same time, fixed assets reached the end of their useful lives.
The planned depreciation is recognised in the income statement under the “Distribution costs”, “Research and development costs”, and “Administrative costs” items.

4.10 Impairment of goodwill

in KEUR	2005	2004	Change
Impairment	**0**	**357**	**- 100.0%**

The decline in impairment of goodwill is explained by the first-time adoption of IFRS 3. In this regard, see the explanations to section “7.1 intangible assets”

4.11 Financial result

in KEUR	2005	2004	Change
Loss from an associate accounted for according to the equity method	0	- 3	- 100.0%
Finance income	267	35	662.9%
Finance expenses	- 207	- 395	- 47.6%
	60	**- 363**	**- 116.5%**

The loss from an associate accounted for according to the equity method amounted to KEUR 0 (2004: KEUR 3). Compare to the commentary in “7.4 Financial Assets”.

The finance income include the income from the application of the Effective Interest Method for long-term loans in the amount of KEUR 173 (2004: KEUR 0), earnings from the release of the provision for end remuneration claims of silent partners in the amount of KEUR 49 (2004: interest expense in the amount of KEUR 159), interest earnings in the amount of KEUR 37 (2004: KEUR 24), which resulted predominantly from the bank accounts that bore interest close to that of the money market, as well as earnings from the valuation of current asset securities and options in the amount of KEUR 8 (2004: KEUR - 13).

The finance expenses include primarily the interest payments to the silent partners in the amount of KEUR 169 (2004: KEUR 185) and the interest expenses for holders of convertible bonds in the amount of KEUR 36 (2004: KEUR 25).

5. Income tax and deferred taxes

Thus far the company has not incurred any expenses arising from income taxes.

The company is still in an early phase of its corporate development and has accumulated losses since the commencement of its business. The company expects that it will accumulate additional losses in the coming years as a result of its activities and only earn profits on a medium-range to long-range basis.

Deferred tax claims have not been listed on the balance sheet to date, because the company has a history of losses, and deferred tax claims arising from unused tax benefits could only be listed on the balance sheet to the extent that the company has adequate taxable temporary differences or to the extent that substantial evidence exists that adequate profit will be available in the future, against which the unused tax losses can be used (IAS 12.34).

The value of unused tax losses for which no deferred tax claim is recognised in the balance sheet, but which must be disclosed in accordance with IAS 12.81(e), is as follows on the balance sheet closing date:

in KEUR	**2005-12-31**
Taxable losses carried forward on 2005-12-31	34,204
Effective tax rate	34.15%
Value of taxable losses carried forward	11,681

The calculation is based on the assumption that the effective tax rates as of 1 January 2006 will be valid in the future for the realisation of the value of the taxable losses carried forward.

The amount of the taxable losses carried forward is conditional on an audit by the tax authorities. The losses carried forward can be carried forward indefinitely and can be used to offset future profits, whereby the restrictions for the use of losses carried forward are to be observed. A portion of the losses carried forward was used for the offset of the deferred tax liabilties mentioned below.

From the point of view of the 4SC AG, it is assumed that the currently existing losses carried forward will no longer be available in the future for an offsetting with future profits, since the company has been supplied to a large extent with new working capital due to numerous capital increases.

The determination of the effective tax rate is based on the following assumptions: taxes in Germany from income and from earnings are made up of corporate income tax, excise tax and the solidarity tax. The corporate income tax in Germany equals a uniform 25% for distributed and retained profits. For the calculation of the deferred taxes, an effective tax rate of 21.11% was used for the corporate income tax and of 13.04% was used for the excise tax. The corporate income tax rate was based on the uniform tax rate of 25%, the solidarity tax of 5.5% and the allowed deduction of the excise tax for a collection rate of 300%.

The development of the unbalanced deferred tax liabilities is shown in the following overview:

in KEUR	2005	2004
Fixed assets	34	89
Current assets securities	3	0
End remuneration claims of silent partners	0	42
Long-term loans	59	0
Convertible bonds	0	1
Liabilities due to silent partners	0	5
Provisions and other current liabilities	3	0
Losses carried forward	- 99	- 137
	0	**0**

The deferred tax liabilities in the fixed assets are a result of the financing lease relationship due to the capitalisation of the assets. The deferred tax liabilties in the end remuneration claims of silent partners and the long-term loans are a result of the different interest rates used in the calculation of the present value of the respective balance sheet approach.

The reconciliation between the profits tax yield and the product from the balance sheet period results and the applicable interest rate for the 4SC AG is made up as follows:

in KEUR	2005	2004
Period result before taxes	- 6,277	- 5,821
Profit tax yield at a tax rate of 34.15%	- 2,144	- 1,988
Less the tax effect on deferred differences and losses carried forward for which no deferred taxes were included in the past periods	2,101	1,855
Non-deductible expenses	5	6
Impairment of goodwill	0	122
Permanent differences	23	17
Other differences	15	- 12
Profit tax yield accounted for in the income statement	**0**	**0**

6. Earnings per share

The undiluted earnings per share is calculated in accordance with IAS 33.9 et sqq from the division of the period results to which the shareholders are entitled (numerator) by the weighted average number of the shares which were in circulation in the reporting period (denominator). This is based on a share count of 8,187,743 for the reporting year and a share count of 6,574,037 for the prior year. The share count for 2004 was adjusted in accordance with IAS 33.26 et sqq due to the convertible bonds exercised in 2005. The original, average count for the prior year was 6,407,150.

Since, as a result of the loss situation at 4SC AG, the convertible bonds and options that have been issued will not have a diluting effect, the diluted earnings per share correspond to the undiluted earnings per share.

in EUR	2005	2004
Earnings per share (undiluted and diluted)	**- 0.77**	**- 0.89**

7. Notes to the balance sheet

7.1 Intangible assets

The development of the intangible assets within the meaning of IAS 38.118 is presented in the asset schedule in "7.2 Fixed assets".

The additions in the reporting year are largely attributable to biology crystallisation software (KEUR 26) and spam filter software (KEUR 4).

The retirements relate to software that is no longer used.

The assumed useful lives are between three and five years.

Intangible assets with assumed unlimited useful lives and self-created intangible assets do not exist.

The elective right to revalue the intangible assets in accordance with IFRS 1.17. in the course of the conversion to IFRS in the year 2003 was not exercised.

The scheduled depreciation is listed on the income statement under the "Distribution costs," "Research and development costs" and "Administrative costs" items.

There is no restricted ownership right, and no collateral has been given that would have to be stated in accordance with IAS 38.122 (d).

Goodwill

in KEUR	2005-12-31	2004-12-31	Change
Goodwill	**1,786**	**1,786**	**0.0%**

The goodwill of 4SC AG results from the fusion of 4SC GmbH with 4SC AG in the year 2000. At that time a fair value of KEUR 3.572 was determined. Through the financial year 2004, the goodwill had been amortised in accordance with IAS 22.44.

The provisions of IFRS 3 and IAS 36 have been applicable since the reporting year. In accordance with IFRS 3.55 and IAS 36.88 et sqq., therefore, no planned amortisation is taken on the goodwill; instead, at least one annual impairment test is undertaken for capitalised goodwill.

The impairment test conducted at the end of the reporting year revealed no necessity to correct the valuation of 31 December 2005. For this impairment test, the value in use of the DHODH project was compared with the carrying value of the goodwill. The value in use was calculated based primarily on the cause variable discounting rate, likelihood of market entry and market share.

7.2 Fixed assets

The fixed assets include the office equipment, laboratory equipment, miscellaneous tools and equipment, the IT equipment (hardware) and lessee installations.
Changes in fixed assets in accordance with IAS 16.73 are presented in the asset schedule.

in KEUR	Useful life up to – years	Acquisition costs				Depreciation				Book values	
		Status on 2005-01-01	Additions 2005	Retirement 2005	Status on 2005-12-31	Status on 2005-01-01	Additions 2005	Retirement 2005	Status on 2005-12-31	Status on 2005-12-31	Status on 2004-12-31
Intangible assets											
Software	3 - 5	476	33	39	470	365	79	39	405	65	111
Goodwill	n/a	3,572	0	0	3,572	1,786	0	0	1,786	1,786	1,786
Intangible assets		**4,048**	**33**	**39**	**4,042**	**2,151**	**79**	**39**	**2,191**	**1,851**	**1,897**
Fixed assets											
Office equipment	8 - 14	131	1	0	132	35	11	0	46	86	96
Laboratory equipment	4 - 13	2,152	38	2	2,188	1,402	398	2	1,798	390	750
Low-value assets	n/a	2	5	2	5	2	5	2	5	0	0
Installations in third-party real property	5 - 14	946	0	0	946	186	76	0	262	684	760
Miscellaneous BGA	5 - 13	116	2	0	118	39	13	0	52	66	77
IT equipment	3 - 7	1,468	30	69	1,429	980	237	65	1,152	277	488
Fixed assets		**4,815**	**76**	**73**	**4,818**	**2,644**	**740**	**69**	**3,315**	**1,503**	**2,171**
Total capital assets		**8,863**	**109**	**112**	**8,860**	**4,795**	**819**	**108**	**5,506**	**3,354**	**4,068**

The changes in fixed assets during the previous year are presented in the following asset schedule:

in KEUR	Useful life up to – years	Status on 2004-01-01	Additions 2004	Retirement 2004	Status on 2004-12-31	Status on 2004-01-01	Additions 2004	Retirement 2004	Status on 2004-12-31	Status on 2004-12-31	Status on 2003-12-31
		Acquisition costs				**Depreciation**				**Book values**	
Intangible assets											
Software	3 - 5	476	0	0	476	246	119	0	365	111	230
Goodwill	10	3,572	0	0	3,572	1,429	357	0	1,786	1,786	2,143
Intangible assets		**4,048**	**0**	**0**	**4,048**	**1,675**	**476**	**0**	**2,151**	**1,897**	**2,373**
Fixed assets											
Office equipment	8 - 14	127	4	0	131	24	11	0	35	96	103
Laboratory equipment	5 - 13	1,419	0	1	1,418	664	272	1	935	483	755
Laboratory equipment (finance lease)	4 - 6	721	13	0	734	311	156	0	467	267	410
Low-value assets	n/a	13	2	13	2	13	2	13	2	0	0
Installations in third-party real property	5 - 14	946	0	0	946	110	76	0	186	760	836
Miscellaneous BGA	5 - 13	116	0	0	116	25	14	0	39	77	91
IT equipment	3 - 7	1,502	31	72	1,461	740	307	70	977	484	762
IT equipment (finance lease)	7	7	0	0	7	2	1	0	3	4	5
Fixed assets		**4,851**	**50**	**86**	**4,815**	**1,889**	**839**	**84**	**2,644**	**2,171**	**2,962**
Total capital assets		**8,899**	**50**	**86**	**8,863**	**3,564**	**1,315**	**84**	**4,795**	**4,068**	**5,335**

The additions in the reporting year are in substantial part replacement investment for workstation computers and notebooks (KEUR 20), a microtiter plates reading device (KEUR 18) and a Raid system (KEUR 6). Overall, replacement investments were made, in substantial part, since the company is currently adequately equipped.
The retirements mainly include sales of no longer needed IT equipment. The loss arising from the retirements is KEUR 0 (2004: KEUR 1).
The planned depreciation is listed on the income statement under the “Distribution costs,” “Research and development costs” and “Administrative costs” items.
There is no restricted ownership right, and no collateral has been given that would have to be stated in accordance with IAS 16.74.
The statements concerning the fixed assets that were classified in the previous year as financial leasing in accordance with IAS 17.4 are located in “7.17 Financial leasing obligations”.

7.3 Receivables from associated companies

The outstanding purchase price of KEUR 183 (2004: KEUR 215) for a software package sold to the quattro research GmbH, Martinsried will be accounted for. The receivable is interest bearing at 6.0% p.a. The repayment of the purchase price will take place based on a repayment plan through the year 2011. Since the repayment will occur at several yearly rates, the current and non-current portion of the receivable will be accounted for separately. At the end of the reporting year, the long-term portion of the receivable amounts KEUR 162 (2004: KEUR 214).

7.4 Financial assets

The participation at quattro research GmbH, Martinsried is shown as financial asset.
In the reporting year, quattro research GmbH, Martinsried earned a period result of KEUR 11 (2004: KEUR -7) with net sales of KEUR 367 (2004: KEUR 311). The debts of quattro research GmbH total KEUR 222 (2004: KEUR 240) with a balance sheet total of KEUR 251 (2004: KEUR 258).
The carrying value in the balance sheet was not corrected to reflect the share of the period result attributable to 4SC AG in the amount of KEUR 5, since interim profits within the meaning of IAS 28.22 exist in the amount of KEUR 99, which result from the financial year 2004 and have to be offset. These interim profits result from the sale of a software package to quattro research GmbH in the financial year 2004 and are calculated in accordance with IAS 28.22. According to this, profits arising from "downstream" transactions with an associated company can only be entered in the amount of the portion that is attributable to third parties. Since the third-party share in quattro research GmbH totals 51.2%, it is only permissible to have a result-effective listing in the amount of this portion of the sales proceeds of KEUR 220. Since complete interim profit elimination would have led to a negative carrying, residual interim profits arising from this transaction in the amount of KEUR 99 were carried forward to the reporting year. After offset against the prorated period result of quattro research GmbH in the amount of KEUR 5, still to be offset interim profits of KEUR 94 remain at the end of the reporting year.
Overall, the facts described above result in a carrying value in quattro research GmbH in the amount of KEUR 0 (2004: KEUR 0) as non-current asset.

7.5 Inventories

in KEUR	2005-12-31	2004-12-31	Change
Consumable materials	11	13	- 15.4%
Solvents	3	2	50.0%
	14	**15**	**- 6.7%**

7.6 Trade receivables

in KEUR	2005-12-31	2004-12-31	Change
Domestic	153	19	705.3%
Third countries	52	0	n/a
EU	0	30	- 100.0%
	205	**49**	**318.4%**

An impairment in the amount of KEUR 84 (2004: KEUR 168) was undertaken on trade receivables in accordance with IAS 39.63 et seq.
The payment for the residual trade receivables was received in a timely manner in January and February 2006.

7.7 Cash and cash equivalents

in KEUR	2005-12-31	2004-12-31	Change
Bank balances	366	2,058	- 82.2%
Cash	2	0	n/a
	368	**2,058**	**- 82.1%**

The bank balances are invested at near money market interest rates.
Cash assets have declined substantially on the previous year, since a large part of the cash inflows from the listing on the stock exchange in December 2005 was invested as current asset securities in December 2005.
The "Cash and cash equivalents" balance sheet item, together with the "Current asset securities" balance sheet item, makes up the liquid funds in the capital flow statement.

7.8 Current asset securities

in KEUR	2004-12-31	Purchase 2005	Sale 2005	Revenue 2005	2005-12-31
Current asset securities	0	6,502	0	8	6,510

The current asset securities are classified in accordance with IAS 39.9 "at fair value through profit or loss". They are used for the interest-bearing investment of liquidity reserves available at short notice. In the reporting year it was possible to earn net revenue of KEUR 8 (2004: KEUR 7).
The cash and cash equivalents that were received by the listing on the stock exchange in December 2005 were predominantly invested in current asset securities. On the balance sheet date, the entire portfolio of current asset securities is invested in "Activest" money market funds.
Therewith, the current asset securities accounted for in the balance sheet are not subject to any significant interest changes, default or solvency risks. Further information concerning 4SC AG's exposure to risks resulting from financial instruments, objectives and risk management methods and to the processes, which were implemented by the management for risk control, are found in the management report under point "3.2 Handling of financial instruments" as well as under point "3.1 Risk management system and internal control system".
The "Current asset securities" balance sheet item, together with the "Cash and cash equivalents" balance sheet item, makes up the liquid funds in the capital flow statement.

7.9 Other current assets

in KEUR	2005-12-31	2004-12-31	Change
Rent security deposit IZB West	157	0	n/a
Tax refund claims	108	87	24.1%
BMBF grants	102	0	n/a
Accounts receivable from shareholders	0	142	- 100.0%
Others	7	9	- 22.2%
	374	**238**	**57.1%**

The receipt of payment, which was accounted for as an outstanding receivable on the BMBF stated appropriations statement for the fourth quarter 2005, took place in February 2006. The receipt of payment for corporate income and sales tax refund claims arising during the reporting year for 2004 and 2005 in the amount of KEUR 94 took place on the due date in February 2006.

7.10 Prepaid expenses and accrued income

The prepaid expenses and accrued income in the amount of KEUR 236 (2004: KEUR 84) consist in substantial part of prepaid invoices for third-party scientific services, maintenance contracts, training and licenses.

7.11 Equity

7.11.1 Share capital and shares

The share capital of 4SC AG currently totals EUR 10,530,077. It is divided into 10,530,077 common bearer shares without par value (no-par shares). Each share represents a pro rata amount of the share capital of 4SC AG in the amount of EUR 1.00 and grants one vote in the shareholders' meeting. The current share capital is fully paid-up.
The form of the share documents and the profit-sharing and renewal certificates is determined by the Management Board with the consent of the Supervisory Board. The company can consolidate individual shares wholly or in part in share documents that evidence multiple shares (global shares, global certificates). The shareholder's right to the documentation of his share or the individual documentation of shares is barred under § 6 paragraph 3 of the articles of incorporation. The shares of 4SC AG are documented in two global documents without profit-sharing certificates, which have been deposited with Clearstream Banking AG, Frankfurt am Main, in its capacity as the collective security deposit bank.

During the reporting year, the share capital developed as described below as a result of capital increases.

At the beginning of the reporting year the company's share capital totalled EUR 6,955,969.

On 6 June 2005, the Management Board, acting with the consent of the Supervisory Board, adopted a capital increase, in exchange for a cash contribution, of EUR 391,510 to EUR 7,347,479 from the then-existing Approved Capital 2004/I. The 391,510 new registered no-par shares were issued to shareholders Technologie Beteiligungsfonds Bayern III GmbH & Co. KG, Munich, and KfW A.d.ö.R., Frankfurt am Main, at an issue price of EUR 4.24 per share. This capital increase was recorded in the Commercial Register on 30 June 2005. The new shares are endowed with profit-sharing rights effective 1 January 2005.

In July 2005, 786,160 registered no-par shares were issued as a result of the conversion of all of the convertible bonds issued by 4SC AG arising from Conditional Capital V, which was created for that purpose at that time, such that the share capital increased to EUR 8,133,639 as a result. The conversion price, and thus the issue amount, of the new shares was EUR 3.18 per share. The change of capital stock number was recorded in the Commercial Register on 15 November 2005. The new shares are endowed with profit-sharing rights effective 1 January 2005.

The shareholders' meeting of 28 September 2005, adopted a capital increase of EUR 1,179,245 to EUR 9,312,884 in exchange for a cash and in-kind contribution. The new bearer no-par shares are endowed with profit-sharing rights effective 1 January 2005. The new no-par shares arising from the capital increase in exchange for cash and in-kind contribution were issued at an issue amount of EUR 4.24 each. 117,925 of the new bearer no-par shares were subscribed to an exchange for a cash contribution by DVCG Deutsche Venture Capital Gesellschaft mbH & Co. Fonds II KG, Munich; an additional 707,547 shares were subscribed to in exchange for a cash contribution by VCG Venture Capital Gesellschaft mbH & Co. Fonds III KG, Munich, and an additional 353,773 shares were subscribed to in exchange for an in-kind contribution by tbg Technologie-Beteiligungs-Gesellschaft mbH, Bonn. tbg Technologie-Beteiligungs-Gesellschaft mbH, Bonn, paid the issue amount for the 353,773 new bearer shares by means of in-kind contribution by assigning to 4SC AG the claims for

(a) repayment of the capital contribution in the amount of EUR 153,387.56 arising from the silent participation granted to the company by means of the contract concerning the establishment of a silent partnership dated 24/30 March 1999,
(b) repayment of the capital contribution in the amount of EUR 766,937.82 arising from the silent participation granted to the company by means of the contract concerning the establishment of a silent partnership dated 15/22 September 1999,
(c) repayment of the capital contribution in the amount of EUR 579,000.00 arising from the silent participation granted to the company by means of the contract concerning the establishment of a silent partnership dated 26 January/6 February 2001, and
(d) repayment of a partial sum in the amount of EUR 672.14 of the capital contribution in the amount of EUR 500,000.00 arising from the silent participation granted to the company by means of the contract concerning the establishment of a silent partnership dated 26 January/6 February 2001.

The residual amount of the latter contribution of EUR 500,000.00 arising from the silent participation granted to 4SC AG in the amount of EUR 499,327.86 by means of the contract concerning the establishment of a silent partnership dated 26 January / 6 February 2001 was repaid to tbg.
The capital increase in exchange for cash and in-kind contribution dated 28 September 2005 was recorded in the Commercial Register on 15 November 2005.

The shareholders' meeting of 28 September 2005, also adopted an additional capital increase ("capital increase in exchange for cash contributions") of up to EUR 3,537,736. Since investors had subscribed to 1,217,193 new bearer no-par shares by the end of 30 November 2005, the share capital of 4SC AG was increased by means of this capital contribution by EUR 1,217,193 from 9,312,884 to EUR 10,530,077. The new no-par shares arising from this capital increase in exchange for cash contributions were issued at an amount of EUR 4.24 per new share certificate. The new no-par shares are endowed with profit-sharing rights effective 1 January 2005.

The capital increase in exchange for cash contribution dated 28 September 2005 was recorded in the Commercial Register on 13 December 2005.

The shareholders' meeting of 28 September 2005 also resolved to convert the heretofore registered shares of 4SC AG into bearer shares. In addition, it was resolved that the division of shares that had existed up to that point in time, namely, into common shares and Series A to Series E preferred shares has to be cancelled and that all existing shares are to be converted into common shares. Differences existed between the common shares and the various series of preferred shares primarily with respect to participation in the liquidation proceeds of 4SC AG. In addition, all of the various series of preferred shares would have been redeemed at prices that were agreed upon in advance and which varied between the individual series, if all of the shareholders of a series of preferred shares had so demanded on specific dates, determined in advance, after 15 August 2007.
The corresponding amendments of the articles of incorporation were recorded in the Commercial Register of 4SC AG on 15 November 2005, such that only one uniform category of bearer shares (common shares) now exists, and differences no longer exist with respect to voting rights, profit participation rights, redeemability of the shares or participation in the liquidation proceeds.

7.11.2 Conditional capital

The company's shareholders' meetings resolved on 1 March 2001, and 28 July 2004, to conditionally increase the company's capital stock as follows:

Conditional capital	**Amount (KEUR)**	**Shareholders' meeting resolution on**	**Purpose**
I	288	2001-03-01	Grant of options to members of the Management Board and employees of the company with a term of up to seven years
III	213	2004-07-28	Grant of options to members of the Management Board and employees of the company with a term of up to seven years

Additional conditional capital that existed in the interim has since been cancelled. Conditional Capital II does currently not exist.

7.11.3 Approved capital

At the shareholders' meeting of 28 September 2005, the Management Board was authorised to increase the share capital of 4SC AG, with the consent of the Supervisory Board, on a one-time basis or on multiple occasions by 27 September 2010, by a total of up to EUR 4,656,442 in exchange for cash contribution and/or in-kind contributions by means of the one-time or multiple issuance of a total of up to 4,656,442 new bearer no-par shares (Approved Capital I from the year 2005). It is intended that the new shares arising from a cash capital increase be subscribed to by credit institutions or companies within the meaning of § 186 para. 5 sentence 1 AktG (Stock Corporation Act) with the obligation to offer them to the shareholders for subscription. However, the Management Board is authorised to exclude fractional shares from the shareholders' subscription rights, with the consent of the Supervisory Board.
The Management Board was also authorised to exclude the shareholders' subscription right, with the consent of the

Supervisory Board, in order to issue a total of up to 931,288 new bearer shares in exchange for cash contribution at an issue amount that does not fall substantially below the stock exchange price of the shares of 4SC AG at the time of the setting of the issue amount. The Management Board was further authorised to exclude the shareholders' subscription right, with the consent of the Supervisory Board, in order to issue a total of up to 2,328,221 new no-par shares in exchange for in-kind contributions for the purpose of the acquisition (including indirect acquisition) of companies, parts of companies, equity interests in other companies or assets of other companies in exchange for the transfer of shares of 4SC AG. The Management Board was authorised to define, with the consent of the Supervisory Board, the additional details of implementation of capital increases from Approved Capital I. The Supervisory Board was authorised to adjust the version of the articles of incorporation of 4SC AG according to the scope of the capital increase(s) from Approved Capital I following complete or partial implementation of the increase from Approved Capital I and after the expiration of the authorisation period.

7.11.4 Additional paid-in capital

The additional paid-in capital consists of three components. Firstly, it consists of premiums that were deposited by shareholders at the time of implementation of capital increases within the framework of financing rounds.
The second component is the equity capital shares in connection with the issuance of convertible bonds (see "7.14 Convertible bonds").
In addition, the amount of the options issued to employees and the Management Board during the reporting year and during previous years in accordance with the provisions of IFRS 2 are shown in the additional paid-in capital.
The determination is explained in "9. Stock option programme".

7.11.5 Appropriation of results

The balance sheet loss in the amount of KEUR 14,741 was carried forward to the new statement.

7.11.6 Transaction costs for the issuance of equity

Based on IAS 32.35 transaction costs from an equity transaction, reduced by all income tax benefits associated with it, are to be accounted for as a deduction from equity.
Since the 4SC AG undertook a pre-market increase in share capital, the material costs of the listing do not have a direct connection to the equity transaction. Only immaterial costs occurred in direct association with this transaction. A deduction from the equity was therefore not made.

7.12 End remuneration claims of silent partners

In the reporting year, all silent partners were – as described in "7.15 Liabilities due to silent partners" – either repaid, converted into a long-term loan or contributed to 4SC AG within the framework of an in-kind contribution.
Thus, all end remuneration claims of silent partners have also become due early. This end remuneration consists, in principle, of two components. Firstly, it consists of a fixed percentage rate of the participation amount that falls due without regard to the time of termination. Secondly, the silent partners are permitted to request a second defined percentage rate of the participation amount for each year after the end of the fifth full year of participation. In partial deviation from these principles, agreements were concluded in the course of the reporting year with both tbg Technologie-Beteiligungs-Gesellschaft mbH der Deutschen Ausgleichsbank (tbg) and Technologie Beteiligungsfonds Bayern GmbH & Co. KG (Technofonds Bayern), the content of which was the repayment or deferment of repayment of the individual end remunerations.

An agreement was concluded with tbg concerning the repayment of KEUR 200. Thus, a provision in the amount of KEUR 119 was released.
An agreement was concluded with Technofonds Bayern concerning the repayment of KEUR 92 and the conversion of KEUR 230 to an interest-free deferred loan until 31 December 2008. This agreement led to an allocation of KEUR 70 to the provision.
On a net basis, it was possible to realise revenue in the amount of KEUR 49 from releases of and allocations to the silent partners' end remuneration claims; this revenue is listed in the financial result.
The development of the end remuneration claims during the reporting year can be seen in the following overview:

in KEUR	2004-12-31	Allo-cation	Release	Repay-ment	Conversion to loan	2005-12-31
Technofonds Bayern	44	12	0	- 16	- 40	0
Technofonds Bayern	208	58	0	- 76	- 190	0
tbg	31	0	- 12	- 19	0	0
tbg	147	0	- 55	- 92	0	0
tbg	70	0	- 26	- 44	0	0
tbg	71	0	- 26	- 45	0	0
	571	**70**	**- 119**	**- 292**	**- 230**	**0**

7.13 Long-term loans

During the reporting year, silent participations of Technologie Beteiligungsfonds Bayern GmbH & Co. KG (Technofonds Bayern) in the amount of KEUR 690 were converted into a long-term loan. This loan quarterly bears interest at a rate of 5.0% p.a. and is due for repayment on 31 December 2008, although 4SC AG has the right to make early repayment. Since this interest calculation is not usual in the market, the repayment amount was discounted with a standard interest rate of 11.0% p.a. and the present value resulting from that was assessed.
The end remuneration claims from the Technofonds Bayern for KEUR 230 was converted to a non-interest bearing deferred loan as of 31 December 2008. Since the non-interest bearing calculation is also not usual inh the market, the repayment amount was calculated with a standard interest rate of 11.0% p.a. and the present value resulting from that was assessed.

7.14 Convertible bonds

in KEUR	2004-12-31	Conversion	Repayment	2005-12-31
Convertible bonds	**2,521**	**2,500**	**21**	**0**

The shareholders' meeting of 4SC AG of 9 September 2004 authorised the Management Board to issue convertible bonds with nominal value of up to EUR 2,500,000 and a term extending until 30 June 2005. The management board has fully availed itself of this authorisation.
These convertible bonds were fully converted into shares during the reporting year.
The interest expense arising from convertible bonds, whose interest rate was 4.0% p.a., totalled KEUR 35 in the reporting year (2004: KEUR 20).

Within the equity interest plan “Beteiligungsplan der 4SC AG 2001“ a total of 54,600 convertible bonds with a nominal value of EUR 1.00 each were issued to a total six (in some cases former) Supervisory Board members. During the 2004 fiscal year, the convertible bonds of three (former) Supervisory Board members were cancelled. The remaining convertible bonds were redeemed during the reporting year.

7.15 Liabilities due to silent partners

4SC AG had concluded a total of four silent partnerships with tbg Technologie-Beteiligungs-Gesellschaft mbH der Deutschen Ausgleichsbank (tbg) and a total of two silent partnerships with Technologie Beteiligungsfonds Bayern GmbH & Co. KG (Technofonds Bayern). All of the silent partnerships were, in the course of the reporting year, either repaid, converted into long-term loans or contributed to 4SC AG within the framework of an in-kind contribution.
An agreement was concluded with tbg concerning the contribution of KEUR 1,500 to 4SC AG as an in-kind contribution and the repayment of the remaining KEUR 729.
An agreement was concluded with Technofonds Bayern concerning the conversion of KEUR 690 into a loan, which has an interest rate of 5.0% p.a. and is due on 31 December 2008, and the repayment of the remaining KEUR 230.
The following provides an overview of the development of the liabilities due to silent partners:

in KEUR	2004-12-31	Repay-ment	Contribution as in-kind contribution	Conversion to loan	Expense release	2005-12-31
Technofonds Bayern	153	- 153	0	0	0	0
Technofonds Bayern	764	- 77	0	- 690	3	0
tbg	153	0	- 153	0	0	0
tbg	763	0	- 767	0	4	0
tbg	575	0	- 579	0	4	0
tbg	497	- 499	- 1	0	3	0
	2,905	**- 729**	**- 1,500**	**- 690**	**14**	**0**

7.16 Provisions

The development of the provisions in the reporting year is shown by the following overview:

in KEUR	2004-12-31	Consumption	Release	Allocation	2005-12-31
Public listing commission	0	0	0	397	397
Bonus to the Management Board	0	0	0	97	97
Outstanding invoices	31	19	0	66	78
Final statement and audit costs	33	33	0	70	70
Renovation IZB West	0	0	0	53	53
Supervisory Board remuneration	38	29	9	37	37
Employee bonus	0	0	0	26	26
Professional association dues	26	20	6	19	19
Ancillary cost statement	5	0	5	0	0
Miscellaneous	9	9	0	8	8
	142	**110**	**20**	**773**	**785**

7.17 Financial leasing obligations

4SC AG entered into various lease contracts for laboratory and IT equipment in previous fiscal years. The terms of the lease contracts were between 36 and 48 months. The lease objects of 4SC AG were classified as financial leasing in accordance with IAS 17.4. During the reporting year, all financing obligations expired, and 4SC AG has not entered into any new finance lease relationships. The laboratory equipment was acquired due to the exercise of a purchase option after the expiration of the lease contract.
The gross book value, depreciation and net book value on the balance sheet date are presented in the asset schedule. The asset schedule is located in ”7.2 Fixed assets”.

The development of the financing obligations in the reporting year is as follows:

	Acquisition month	Acquisition costs in KEUR	Overall-term in months	Residual term on 05-12-31 in months	04-12-31	Repayment 2005	05-12-31
QLCU mass spectrometer	05/2002	314	36	0	39	39	0
Copier Mita	02/2002	7	48	0	2	2	0
		321			**41**	**41**	**0**

7.18 Other financial obligations

Financial obligations exist from the rental agreement for the operational and office areas for 4SC AG for the year following the balance sheet date. The term of this contract runs through 31 March 2007. In addition, there are financial obligations from usage and scientific service contracts.

The payments to be made in the future from these contracts are as follows:

in KEUR	2006	2007	2008	Total
	1,227	219	13	**1,459**

The expenses included in the income statement for the reporting year from the rental agreement total KEUR 787 (2004: KEUR 838). The decline is the result of the ancillary rent cost calculation for 2004, from which a reimbursement of KEUR 76 was received.

In addition, financial obligations exist from an operating lease relationship, which is accounted for according to IAS 17.33. With application of this regulation, the leasing payments will included on a straight line basis over the period of the leasing relationship as an expense in the income statement.
The operating leasing relationship has to do with a copier for which a minimum lease payment of KEUR 2 in 2006 and KEUR 5 for 2007 through 2009 is to be made.

7.19 Trade payables

in KEUR	2005-12-31	2004-12-31	Change
Domestic	242	94	157.4%
EU	20	27	- 25.9%
Third countries	9	1	800.0%
	271	**122**	**122.1%**

The trade payables increased as of closing date.

7.20 Accounts payable to associated companies

Two contracts concerning the development, support and maintenance of software as well as the support and maintenance of the IT infrastructure and the databases for 4SC AG were concluded with quattro research GmbH. The debt in the amount of KEUR 29 (2004: KEUR 29) from the annual account for quattro research GmbH, Martinsried, were accounted for.

7.21 Down payments received

in KEUR	2005-12-31	2004-12-31	Change
Down payments received	**0**	**225**	**- 100.0%**

In the previous year down payments received from a collaboration partner were shown.

7.22 Other current liabilities

in KEUR	2005-12-31	2004-12-31	Change
Taxes	145	70	107.1%
Social security charges	48	56	- 14.3%
Holiday	48	50	- 4.0%
Miscellaneous	12	47	- 74.5%
	253	**223**	**13.5%**

8. Notes to the cash flow statement

8.1 Cash flows from operating activities

The outflow of funds arising from operating activity totalled KEUR 5,725 in the reporting year (2004: KEUR 4,403), which corresponds to an increase of 30.0% compared to the financial year 2004. This increase is explained in substantial part by the reduced pre-tax period result, which declined by 7,8% to KEUR - 6,277 in the reporting year. In addition, the changes in the end remuneration claims of silent partners, of which KEUR 292 was paid back in the reporting year, have an impact here. Detailed explanations in this regard can be found in "7.12 End remuneration claims of silent partners".

8.2 Cash flows from investing activities

The outflow of funds arising from operating activity totalled KEUR 108 in the reporting year (2004: KEUR 71), which corresponds to an increase of 52.1% compared to the financial year 2004. The investments in the reporting year involve, in substantial part, biology crystallisation software (KEUR 26), replacement procurements for workstation computers and notebooks (KEUR 20), a microtiter plate reading device (KEUR 18) and a Raid system (KEUR 6). Overall, replacement investments were made, in substantial part, because the company is currently adequately equipped.

8.3 Cash flows from financing activities

The inflow of funds arising from financing activity totalled KEUR 10.653 in the reporting year (2004: KEUR 3,352), which corresponds to an increase of 217.8% compared to the financial year 2004. This inflow originates in the amount of KEUR 8,661 from the deposits by the shareholders that were made within the framework of the pre-listing capital increases adopted at the special shareholders' meeting of 28 September 2005. Within the framework of these capital increases, silent participations in the amount of KEUR 1,500 were contributed to 4SC AG as an in-kind contribution, as a result of which the total volume of these capital increases amounts to KEUR 10,161. KEUR 1,660 flowed to 4SC AG in the reporting year from the capital increase of 6 June 2005, and KEUR 1,123 flowed to 4SC AG from the capital increase of 29 December 2004. In addition, silent participations in the amount of KEUR 729 were repaid during the reporting year. The exercise of convertible bonds in the amount of KEUR 2,500 did not involve any cash inflows. Likewise, the conversion of silent participations in the amount of KEUR 690 into a long-term loan did not result in any cash inflows. The remaining convertible bonds to various (in some cases former) Supervisory Board members in the amount of KEUR 21 were redeemed.

9. Stock option programme

Conditional capital in the amount of KEUR 213 was created within the framework of the shareholders' meeting of 28 July 2004 ("Conditional Capital III"). This conditional capital increase serves exclusively to grant options to members of the Management Board and employees of the company. These stock options are issued in multiple tranches. An initial tranche was issued on 30 September 2004.

The options that were issued between 2001 and 2003 originate from the conditional capital created within the framework of the shareholders' meeting of 1 March 2001 ("Conditional Capital I").

The following table gives an overview of the tranches issued to date, as well as the option conditions:

Title (K/KEUR)	Expenditure	Exercising price[1]	issued	outstanding 2005-01-01	forfeited 2005	exercised 2005	outstanding 2005-12-31	exerciseable 2005-12-31	Present value	cum. PE[2]	PE 2005[3]
ESOP 2001/1	01-03-31	9.60	74	63	4	0	59	44	n/a	0	0
ESOP 2001/2	01-10-10	9.60	110	110	20	0	90	68	n/a	0	0
ESOP 2002	02-06-30	12.00	120	95	20	0	75	38	n/a	0	0
ESOP 2003	03-09-30	5.08	318	308	75	0	233	0	0.74	144	23
ESOP 2004	04-09-30	4.24	122	122	27	0	95	0	0.72	53	14
ESOP 2005	05-09-30	4.24	93	0	2	0	91	0	0.71	49	3
Total			**837**	**698**	**148**	**0**	**643**	**150**		**246**	**40**

1: As a result of the capital reductions in December 2004, the subscription ratio is 2:1
2: cum. PE = cumulative personnel expense through the end of the vesting period
3: PE 2005 = Personnel expense for 2005

It is common to all tranches that the settlement of exercised options will only take place in shares and that the options given out will have a term of seven years. The first half of the option rights may be exercised three years after the issuance at the earliest. An additional 25% may be exercised a year later and the remaining 25% a year after that. The options may only be exercised if the value of the shares has increased by a minimum of 20% above the issuance value at the time that they are exercised. The weighted average maturity of all exercised options totals 4.5 years. The weighted average exercise price of all options issued totals EUR 5.78. Thereby, the fluctuation margin of the exercising price from EUR 4.24 to EUR 10 is sufficient. For the determination of the present value of the options, assumptions must be met. The 4SC AG uses the “Black – Scholes Model” for valuation of options. For the new options issued in the reporting year, a no risk interest rate of 2.75%, which was used for federal bonds with comparable maturities, was chosen. 32.1% was used for the volatility, the same as was used for the “NASDAQ Biotechnology Index”, since the 4SC AG has only been listed on the stock exchange since December 15, 2005. The market price for the options issued for the end of the 2004 fiscal year arose from the shareholder value for 4SC AG, which was closest to the time of the option issuance. The annual closing price of EUR 4.35, as determined by the Frankfurt Stock Exchange, was used for the options issued in the reporting year. There are no expected dividend payments.

For the options, which were exercised before 7 November 2002, no determination was made of the present value, since these options were not subject to the application of IFRS 2. Correspondingly, no personnel expenses were calculated for these options.

10. Related party disclosures

The overall remuneration of management in the reporting year totals KEUR 688 (2004: KEUR 441). KEUR 13 of this overall sum (2004: KEUR 12) is attributable to contribution-oriented retirement and disability benefit plans in accordance with IAS 19.7. The prorated personnel costs arising from options included within overall remuneration are KEUR 8 in the reporting year (2004: KEUR 5). 14,800 options were newly issued to members of the Management Board in the reporting year. These options have a value of KEUR 11, calculated in accordance with IFRS 2.

Individualised according to individual Management Board members, the overall remuneration for the reporting year and the share property as of the balance sheet date breaks down as follows:

Remuneration 2005 in KEUR/quantity	Fixed	Bonus	Severance	Options acc. IFRS 2	Total
Dr Ulrich Dauer	112	56	0	2	170
Dr Gerhard Keilhauer	133	27	0	2	162
Dipl.-Kfm. Enno Spillner	35	8	0	0	43
Dr Daniel Vitt	103	68	0	2	173
Dr Stefan Busemann	58	0	80	2	140
	441	**159**	**80**	**8**	**688**

Share property 2005-12-31 in KEUR/quantity	Shares	Options total	Options of 2005	Options exercised in 2005
Dr Ulrich Dauer	399,792	32,400	4,800	0
Dr Gerhard Keilhauer	9,025	94,200	4,800	0
Dipl.-Kfm. Enno Spillner	6,666	400	400	0
Dr Daniel Vitt	393,503	32,400	4,800	0
Dr Stefan Busemann	296,691	27,600	0	0
	1,105,677	**187,000**	**14,800**	**0**

The overall remuneration of the Supervisory Board in the reporting year totals KEUR 37 (2004: KEUR 39). Individualised according to individual Supervisory Board members, the overall remuneration for the reporting year breaks down as follows:

in KEUR	Remuneration 2005
Current members:	
Dr Jörg Neermann	10
Dr Robert O'Connell	6
Dr Brian Morgan	5
Dr Manfred Rüdiger	2
Dr Clemens Doppler	2
Stefan Meißner	1
In 2005 resigned members:	
Dr Ulrich Pidun	5
Patrick Schwarz-Schütte	3
Prof. Dr Erich Schlick	3
	37

During the reporting year in some cases, former members of the Supervisory Board received repayment of the remaining outstanding convertible bonds, in the amount of KEUR 21.

The consultant contracts concluded in previous years between 4SC AG and Supervisory Board members Dr Robert O'Connell, The Catalyst Agency Ltd., Dorset (Great Britain), and Dr Brian Morgan, Morgan Consulting and Abinger Common (Great Britain), were cancelled during the reporting year. The two Supervisory Board members received a fee in the total amount of KEUR 32 (2004: KEUR 42) from these consultant contracts.

The relation to the associated company quattro research GmbH, Martinsried, is explained in "7.3 Receivables from associated companies", "7.4 Financial assets" and "7.20 Accounts payable to associated companies".

11. Events after the balance sheet date

In January 2006 an important milestone in the collaboration with Japanese pharmaceutical company Sanwa Kagaku Kenkyusho Co., Ltd., Nagoya, Japan, (SKK), was reached. As a result, it was possible to post corresponding incoming payments at the end of January 2006.

AUDITORS' REPORT
TO 4SC AG

We have audited the attached financial statements of 4SC AG, Martinsried, as of December 31, 2005 comprising the balance sheet, the income statement, the notes to the financial statements, cash flow statement, segment reporting and the statement of changes in shareholders' equity. The financial statements are the responsibility of Company management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with the International Standards on Auditing (ISA). Those standards require that we plan and perform the audit such that it can be assessed with reasonable assurance whether the financial statements are free of material misstatement. The evidence supporting the disclosures and amounts in financial statements is examined primarily on a test basis. The audit includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audit provides a reasonable basis for our opinion.

In our opinion the financial statements give a true and fair view of the net assets and financial position of the Company as of December 31, 2005 and the results of operations and the cash flow for the past fiscal year in accordance with International Financial Reporting Standards.

Our audit, which also extends to the management report prepared by the Management Board for the fiscal year from January 1 to December 31, 2005 pursuant to Sec. 289 HGB, has not led to any reservations. In our opinion, the management report is consistent with the annual financial statements and as a whole provides a suitable view of the Company's position and suitably presents the opportunities and risks of future development.

The engagement, in the course of which we have performed the above-mentioned services for 4SC AG, Martinsried, is subject to the General Engagement Terms for "Wirtschaftsprüfer und Wirtschaftsprüfungsgesellschaften" (German Public Auditors and public Audit Firms) as of January 1, 2002 (Exhibit). By acknowledging and using the information contained in this auditor's report, the respective recipient acknowledges the agreements made therein (including the liability regulation in No. 9 of the General Engagement Terms) and accepts their application with respect to us.

We performed our work on the voluntary annual audit on behalf of the Supervisory Board of 4SC AG, Martinsried, and prepared this auditor's report exclusively for 4SC AG, Martinsried. Our auditor's report is not designed as a basis of decisions for third parties and is not to be used for any other purpose so that, in derogation of our "General Engagement Terms für Wirtschaftsprüfer and Wirtschaftprüfungsgesellschaften" promulgated by the Institut der Wirtschaftsprüfer as of January 1, 2002 which are applicable to both client and third parties, Ernst & Young AG Wirtschaftsprüfungsgesellschaft assumes no responsibility, liability or any other duties unless we entered into a written agreement to the contrary with the third party or such an exclusion of liability were invalid; we point out that we will not update the auditor's report to reflect events or circumstances which occur after the preparation of the auditor's report.

It is the responsibility of the reader to decide whether and to what extent the information contained in this auditor's report is useful or suitable for their purposes and to extend, verify or update the information by examinations of its own.

If the audited financial statements and/or management report are to be distributed or published and if these vary from the audited version or if a foreign-language version is to be prepared, reference to our auditor's opinion or to our audit in any context requires our written approval. The same applies for the translation of our auditor's report into a foreign language or if excerpts or quotations from the financial statements are passed on to third parties with a reference to our auditor's report.

Munich, March 17, 2006

Ernst & Young AG
Wirtschaftsprüfungsgesellschaft

Napolitano	Dötsch
Wirtschaftsprüfer	Wirtschaftsprüferin
(German Public Auditor)	(German Public Auditor)

REPORT OF THE **SUPERVISORY BOARD**

In the financial year 2005 (2005-01-01 to 2005-12-31), the Supervisory Board of 4SC AG, consisting of its members Dr Jörg Neermann (Chairman), Dr Ulrich Pidun (until 2005-09-12, Vice Chairman), Dr Bob O'-Connell (Vice Chairman as of 2005-09-27), Dr Brian Morgan, Patrick Schwarz-Schütte (until 2005-08-16), Prof. Dr Erich Schlick (until 2005-08-16), Dr Manfred Rüdiger (since 2005-08-17), Dr Clemens Doppler (since 2005-08-17) and Stefan Meißner (since 2005-10-12), came together for four in-person meetings and three telephone conferences. The Supervisory Board was kept constantly informed about the development of the company's business and any important matters by the Management Board, both orally and in writing. The regular monitoring of management raised no cause for objection.

Securing the financing of the company was the major focus in the work of 4SC AG's Supervisory Board in 2005. In December 2004, within the framework of the first closing, stock series E was issued for a stock capital increase. In addition to the second closing of the fourth financing round, the Supervisory Board dealt primarily with the preparations for the public listing and the pre-listing financing coming along with it.

In addition to addressing these financial topics, an intensive exchange took place both within the Supervisory Board and between the Supervisory Board and the Management Board concerning the set-up and development of the product pipeline. The other focal points of the work were the overall development and positioning of the company, strategic planning and personnel development within the company's Management Board. The Supervisory Board was integrated in all significant and company-relevant decisions. It advised the Management Board and monitored the management. This was done by means of detailed discussion with the Management Board concerning the Management Board's oral and written reports at each Supervisory Board meeting. Following these discussions there was no reason for additional review by means of inspection of the company's records or the engagement of professional experts. Whenever necessary, short-notice decisions were also discussed in telephone conferences.

The Supervisory Board has also convinced itself of the company having a functioning risk management system. Decisions were made on transactions that require consent under the Management Board´s rules of internal procedure.

Meetings of the Supervisory Board

In the course of the financial year 2005, the Management Board reported to the Supervisory Board on the substantial business matters, strategy and planning, as well as business development and the company's financial situation, within four in-person meetings on 10 March 2005, 9 June 2005, 29 September 2005, and 21 November 2005, as well as three telephone conferences on 7 February 2005, 31 October 2005, and 15 December 2005.

The Chairman of the Supervisory Board was kept constantly informed about significant developments and impending company decisions. In parallel, an intensive topic-related exchange took place between the Management Board and individual Supervisory Board members.

Committees of the Supervisory Board

The following committees, each consisting of three Supervisory Board members, were newly elected by the Supervisory Board members on 21 November 2005:

1) Audit Committee:	Chairman:	Stefan Meißner
	Members:	Dr Jörg Neermann, Dr Clemens Doppler
2) Personnel Committee:	Chairman:	Dr Jörg Neermann
	Members:	Dr Robert O'Connell, Dr Brian Morgan
3) Business Development/	Chairman:	Dr Robert O'Connell
Investor Relations Committee:	Members:	Dr Manfred Rüdiger, Dr Brian Morgan

The Personnel Committee met during the in-person Supervisory Board meetings on four occasions during the reporting year: on 10 March 2005, 9 June 2005, 29 September 2005, and 21 November 2005; the Audit Committee held two telephone conferences on 19 January 2005, and 30 March 2005. The Business Development/Investor Relations Committee did not hold any meetings during the financial year 2005.

Changes within the Management Board

As of 2 August 2005, the appointment of Management Board member Dr Stefan Busemann, who had been responsible for financial matters up to that time, came to an end. Beyond it, Dr Busemann worked for 4SC AG as a consultant until 30 September 2005.

Following numerous personal conversations that Personnel Committee members Dr Robert O'Connell, Dr Brian Morgan and Dr Jörg Neermann conducted with Enno Spillner, Dipl.-Kfm. (graduate business administrator), Mr Spillner could be identified as the successor for Dr Busemann.

Enno Spillner took up his office as 4SC AG's CFO on 16 September 2005.

Changes in the Supervisory Board

Dr Clemens Doppler and Dr Manfred Rüdiger were elected to the company's Supervisory Board at the annual general meeting on 16 August 2005. Dr Doppler took over the office of Prof. Dr Erich Schlick, and Dr Rüdiger took over the office of Patrick Schwarz-Schütte. Mr. Schwarz-Schütte and Prof. Dr Schlick had resigned their mandates as of 16 August 2005.

Dr Doppler is a director of the internationally active private equity company 3i Group plc and has more than ten years of experience in the pharmaceutical and biotechnology industry.

In 2005, Dr Rüdiger was Executive Vice President, Chief Operating Officer and Member of the Board of Directors of Apthon Corp. in Philadelphia (USA), which is listed on the U.S. stock exchange.

Stefan Meißner was elected to the Supervisory Board at the extraordinary general meeting on 28 September 2005, and took up his office on 12 October 2005. He took over the office of Dr Ulrich Pidun, who resigned his mandate as of 12 September 2005. Stefan Meißner is Executive Director of the Equity Capital Market Department of WestLB in Düsseldorf and has more than 15 years of experience in the capital markets and investment banking.

Audit of the annual financial statements

Ernst & Young AG Wirtschaftsprüfungsgesellschaft, Munich branch office, Arnulfstr. 126, 80636 Munich, is the independent auditor; the firm was proposed by the Supervisory Board and was elected and engaged by the 2005 annual general meeting. The auditor audited the annual financial statements and management report of 4SC AG in accordance with German (HGB [Commercial Code]) and international (IFRS) principles. The auditor issued its audit certificate in unrestricted form.

The Management Board submitted the annual financial statements and management report to the Supervisory Board in a timely manner prior to the relevant meeting. The auditor's report was sent to the members of the Supervisory Board. The Audit Committee carefully reviewed these documents and discussed them in detail during a telephone conference with the auditors on 13 March 2006; the Supervisory Board also dealt with them thoroughly. The annual financial statements and the management report were discussed in detail at the Supervisory Board meeting on 21 March 2006.

The responsible auditor, Dr Elia Napolitano, answered all of the Supervisory Board's inquiries at the Supervisory Board meeting of 21 March 2006.

Based on its own review of the annual financial statements and management report and on the recommendation of the Audit Committee, the Supervisory Board followed the result of the audit of the financial statements in accordance with § 172 AktG [Stock Corporation Act]. Following its definitive review, the Supervisory Board approved the annual financial statements and management report without restriction or supplementation. The annual financial statements are therefore adopted.

Corporate Governance

Within the compliance declaration that was adopted on 21 March 2006, the Management Board and Supervisory Board declared that they were in compliance with the recommendations of the German Corporate Governance Code, in the version dated 2 June 2005, with the exceptions stated in the compliance declaration dated 21 March 2006.

For additional information, see pages 83 to 87 of the "Corporate Governance Report and Remuneration Report." The compliance declaration is also reproduced there.

On behalf of my Supervisory Board colleagues, I thank the Management Board and the employees for its committed work and performance in the fiscal year 2005, particularly the successful implementation of the listing at the stock exchange.

Martinsried, March 2006

Dr Jörg Neermann
Supervisory Board Chairman

CORPORATE GOVERNANCE REPORT AND REMUNERATION REPORT

Close cooperation between all of the company's executive bodies, transparent communications and a performance-oriented remuneration structure are indispensable for a young, fast-growing company like 4SC AG. Therefore, the company has for years adhered to a number of norms and provisions set forth by the German Corporate Governance Code in its current version dated 2 June 2005. The management of 4SC AG used the listing in December 2005 as an occasion to once again critically review compliance with the Corporate Governance Code and to make adjustments where necessary.

Consequently, 4SC AG is to a very large extent in compliance with the recommendations of the Code. The exceptions relate primarily to recommendations that are very specifically tailored to large corporate groups and therefore apply less to companies like 4SC AG.

Shareholders and shareholders' meeting

The shareholders' meeting is a central body of the company. The Management Board presents the annual financial statements to the general meeting. At the annual general meeting, decisions are made including the election of the auditor of the financial statements, the discharge of the management and Supervisory Board and the election of Supervisory Board members. It is a matter of course for 4SC AG to make it easier for all shareholders to personally exercise their rights. The company will therefore make representatives available for the general meeting on 28 June 2006, who will, bound by instructions, exercise the voting rights on behalf of shareholders and also be available during the general assembly.

Intensive dialogue between the Management Board and Supervisory Board

4SC AG's Management Board and Supervisory Board cooperate closely for the purpose of increasing the company's value on a sustainable basis. The Management Board regularly coordinates the company's strategic direction with the Supervisory Board and discusses the strategic implementation with the Supervisory Board as well. For this purpose the Management Board provides regular, prompt and comprehensive information to the Supervisory Board on all company-relevant issues of planning, business development, finance, risk situation and risk management.
The Management Board informs the chairman of the Supervisory Board of all projects or events with high importance or urgency, also in-between the official meetings.
Some important business transactions are subject to agreement by the Supervisory Board, as defined in the current by-laws of 4SC AG. The Supervisory Board may define additional cases which are subject to agreement.

The Management Board – the management team

The four-strong Management Board of 4SC AG conducts business on a solely responsible basis with the goal of increasing the company's value on a sustainable basis. The Management Board members complement one another extremely well in terms of their abilities and experience and run the company as a team.
The Management Board's remuneration consists of a fixed portion, a variable portion and stock options. 4SC AG's Management Board earned a total of KEUR 688 in the financial year 2005, 65% of which being attributable to fixed remuneration sums and 35% to variable remuneration sums. The variable remuneration is based on company goals such as growth and innovative product development, as well as individual targets. The Supervisory Board annually reviews the appropriateness of the Management Board remuneration and the level of fulfillment of the targets. The list concerning the individual remuneration of the individual Management Board members can be found on page 75 to 76 in the notes to the IFRS 2005 financial statements.

The company also uses an employee stock option program (ESOP), in which the Management Board and all of the employees participate, as a remuneration component with a long-term incentive effect. These stock options entitle the employees and the Management Board to subscribe to shares of the company.

4SC AG is convinced that such an ESOP is ideally tailored to the company. 4SC AG therefore purposely foregoes the limitation recommended by the Code for extraordinary unforeseen developments (sec. 4.2.3 of the Code). The company therefore also refrains from relating the ESOPs to comparative parameters (sec. 4.2.3 of the Code).

The currently valid stock option plan was resolved upon by the shareholders' general meeting of 4SC AG on 28 July 2004. A general description of the various currently active programs can be found on pages 74 to 75 of the notes to the IFRS 2005 financial statements.

As of 31 December 2005, the current 4SC Management Board members hold a total of 159,400 stock options and 808,986 shares. In sum, the current Management Board members, including two founders, hold 8.7% of the company's shares.
In previous financial years, no excess was agreed upon by the Management Board members for D&O liability insurance as this is not standard international practice. An excess in the amount of KEUR 10 was incorporated into the D&O insurance on 2006-01-01, in order to comply with the recommendations of the Corporate Governance Code.

Competent control and consulting by the Supervisory Board

The Supervisory Board of 4SC AG currently consists of six members elected by the shareholders' general meeting. Chairman of the board is Dr Jörg Neermann, vice-chairman is Dr Robert O'Connell, further members are Dr Clemens Doppler, Stefan Meißner, Dr Brian Morgan and Dr Manfred Rüdiger.

All members of 4SC AG's Supervisory Board have many years' experience in the areas of the pharmaceutical and biotechnology industry and/or excellent expertise in the financial area of exchange-listed companies. This ensures a competent control and consulting of the Management Board. All of the members of the Supervisory Board act independently and are not bound by business or personal relations with 4SC AG. During the period prior to the stock exchange listing, consulting contracts that existed with Supervisory Board members Dr Robert O'Connell and Dr Brian Morgan were dissolved, in order to guarantee their independence in accordance with the Corporate Governance Code.

The Supervisory Board formed three committees (Audit Committee, Personnel Committee and the Business Development/Investor Relations Committee); the committees report on their activities to the plenum board.

Remuneration of the Supervisory Board

The total remuneration of the Supervisory Board in the financial year 2005 amounted to KEUR 37. The base remuneration for each Supervisory Board member was KEUR 5 for a full financial year, with the chairman of the Supervisory Board receiving double the base remuneration and his deputy receiving 1.5 times the base remuneration. The company does not pay a separate fee for membership in committees (sec. 5.4.7 of the Code). Contrary to what is provided by the Code, 4SC AG foregoes result-oriented remuneration of the Supervisory Board members (sec. 5.4.7 of the Code).

In the financial year 2005, three Supervisory Board members resigned their mandate (Dr Ulrich Pidun, Prof. Dr Erich Schlick and Patrick Schwarz-Schütte).
Dr Manfred Rüdiger, Dr Clemens Doppler and Stefan Meißner are new members and have been in office since the second half of 2005.
The list concerning the individual remuneration of individual Supervisory Board members can be found on page 76 to 77 of the notes to the IFRS 2005 financial statements.

Transparent communications

In order to ensure that shareholders and investors receive immediate and consistent information, 4SC AG publishes all relevant information on its own website (www.4sc.com), in addition to the channels regulated by law. All reports appear within the set periods recommended by the Corporate Governance Codex and the stock exchange regulations. This ensures that information is provided rapidly and consistently to all shareholders.

Director dealings

In line with the Directors' Dealings one transaction has been reported to 4SC AG since the listing of the stock exchange on 15 December 2005. The chairman Dr Jörg Neermann bought 1,500 4SC-shares close to EUR 4.60 per share in Xetra-exchange with a deal volume of KEUR 6,9 (DGAP-Notification of 20 March 2006).

DECLARATION OF CONFORMITY BY THE **MANAGEMENT BOARD & SUPERVISORY BOARD**

4SC AG places great value on good corporate governance and believes that transparency and value-oriented company management should be a matter of course. The company therefore implements all aspects of the recommendations of the German Corporate Governance Code, with the few exceptions stated below, and incorporates them into its work on an everyday basis.

Declaration in accordance with § 161 Aktiengesetz (AktG) [Stock Corporation Act] concerning compliance with the German Corporate Governance Code, as amended on 2 June 2005, at 4SC AG

I. Retrospective declaration (15 December 2005 to 20 March 2006)

4SC AG has, save for the following exceptions, complied with the recommendations of the German Corporate Governance Code as of the date of the commencement of the public listing on 15 December 2005:

1) No excess was reflected in the D&O liability insurance for the Supervisory Board and Management Board, (sec. 3.8 para. 2 of the Code).
2) No statements have been made to date concerning the value of the stock options (sec. 4.2.3 of the Code).
3) The option program for the members of the Management Board had no limitation for extraordinary, unforeseen developments (sec. 4.2.3 of the Code). The lack of such a limitation was already taken into account in the assignment of options.
4) The stock option programs were based on binding shareholders' meeting resolutions. The exercise of these options required an increase in the stock price. However, it was not tied to any further comparative parameters (sec. 4.2.3 of the Code).
5) No success-oriented remuneration of the members of the Supervisory Board existed (sec. 5.4.7 of the Code).

II. Present and future-oriented declaration (effective of 21 March 2006)

The Management Board and Supervisory Board of 4SC AG hereby declare, in accordance with § 161 AktG (Stock Corporation Act), that 4SC AG is in compliance with the recommendations of the "German Corporate Governance Code" government commission (as amended on 2 June 2005), save for the exceptions stated below, as of 21 March 2006:

1) Sec. 3.8 para. 2 of the Code: Although it is not internationally customary to agree upon an excess within the meaning of sec. 3.8 para. 2 of the Code, the current D&O liability insurance provides for such an excess for executive body members, the amount of which totals KEUR 10 per event of loss. This is pointed out on a precautionary basis, because it is uncertain when an excess within the meaning of the Code is viewed as adequate.

2) Sec. 4.2.3 of the Code: The option program for the members of the Management Board does not provide for a limitation in case of extraordinary unforeseen developments.

3) Sec. 4.2.3 of the Code: The current stock option programs are based on binding shareholders' meeting resolutions. The exercise of these options requires an increase in the stock price. However, it is not tied to any further comparable parameters.

4) Sec. 5.4.7 of the Code: A success-oriented remuneration of the members of the Supervisory Board does not currently exist.

Munich, 21 March 2006

For the Management Board
Dr. Ulrich Dauer

For the Supervisory Board
Dr. Jörg Neermann

GLOSSARY

4SCan®	Computer-based, high throughput screening technology developed by 4SC AG
Absorption	Biological process by which materials are taken in through the skin or mucus membrane
ADMET analysis	Study of the absorption, distribution, metabolism, excretion and toxicology of an active agent
Assay	Standardised experiment to provide evidence of the biological or chemical activity of a substance through the application of a specific method
Licensing out	Granting a right of use to third parties in respect of one or a number of protected rights
Auto-immune illness	An illness, the cause of which is a defence reaction within the immune system against the body's own tissue
Backup substance	A follow-up drug candidate with a slightly altered effective profile
Bio-availability	Measurement of the quantity and speed with which an active agent becomes available at the desired location in the human body
DHODH	Dihydroorotate dehydrogenase; an enzyme with an important role to play in the construction of DNA in the cell
Double-blind study	A study in which neither doctor nor patient knows whether it is the active ingredient or a placebo being administered
Enzyme	A protein, which makes possible or accelerates chemical reactions in the cells by acting as a catalyst
Gram-negative	A class of bacteria with a relatively thin cell wall, which, however, cannot be penetrated by some antibiotics
High throughput screening	Technique for the rapid study of molecules in relation to their actual (*in vitro*) or predicted (*in silico*) biological activity
In silico	With the help of computers
In vitro	In the test-tube
In vivo	In the living organism
Inhibitor	A substance inhibiting a specific enzyme reaction
Ion channel	A protein which makes it possible for ions to flow through the cell membrane
Kinasis	A protein which controls cellular signal transfer
Lead structure	A possible preliminary stage for a potential drug candidate
Morbus Crohn	Autoimmune disease of the intestine resulting in chronic inflammation of the intestine
Multiple sclerosis (MS)	Auto-immune disease of the central nervous system which results in degeneration of the nerve sheath
Nanomolar	Extremely low concentration (approx. $6x10^{14}$ particles per litre)
NFκB	Abbreviation for "Nuclear Factor κB": a protein family, which controls various processes by activating specific genes, provoking an inflammatory reaction, for example

Pharmacokinetics	Distribution of active agents throughout the various tissues of the organism in terms of space and time
Phase I	Clinical trialling of an active agent on a small number of healthy participants carried out under strict control. Used to investigate compatibility, pharmacokinetics, form of administration and safe dosage of the active agent
Phase II	Clinical study of a small number of ill patients carried out under strict control to identify side effects and risks for an active agent appearing in the short-term. For determining the effectiveness of the active agent and any defence reactions in the immune system appearing in response to the agent
Phase III	A study carried out on a large number of ill patients (a few hundred to a few thousand) to establish the safety, efficiency and optimum dosage for an active agent, under real therapeutic conditions
Placebo	A medical preparation containing no active agent
Pre-clinical study	A laboratory experiment carried out with a new candidate drug on animals, organs or cell cultures, carried out to provide evidence that a clinical study is justified and that the candidate drug can be classified as safe
Prime Standard	Listing segment of the German Stock Exchange with clearly-defined transparency requirements
Proof of concept	A milestone at which the feasibility of a project in principle is proven
Proteasome	Multi-protein complex for the decomposition of used cellular products
Protein	A large, complex molecule composed of amino acids. Proteins are essential for the structure, regulation and function of all organisms. Typical proteins are enzymes and antibodies
Rheumatoid arthritis (RA)	Auto-immune disease of the connecting tissues, principally the joints
Screening library	Database of substances already analysed
Second closing	Conclusion of a round of financing
Target	Specific biological molecule, for example an enzyme or a receptor, which plays an important role in the origination or development of a disease. Active agents/drugs bind onto target molecules, thus triggering their therapeutic activity
TNF-α	Abbreviation of "Tumour Necrosis Factor α"; a protein which plays a crucial role in activation of the immune response
Toxicity	Undesirable side-effects of a substance, dependent on the dose
Virulence	Degree to which a causative organism can give rise to an illness

FINANCIAL CALENDAR

30 March 2006	*Annual Report 2005 Conference Call for Annual Press Briefing (in German)*
15 May 2006	*Three Months' Report 2006*
28 June 2006	*Annual General Shareholders' Meeting 2006*
14 August 2006	*Six Months' Report 2006*
13 November 2006	*Nine Months' Report 2006*
27-29 November 2006	*Analyst Meeting: Deutsches Eigenkapitalforum, Congress Center Messe Frankfurt*

IMPRINT

Editor	*4SC AG / Am Klopferspitz 19a / 82152 Martinsried / Germany*
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