INTERSHOP™

Annual Report
2005

Annual Report 2005

This annual report contains forward-looking statements regarding future events or the future financial and operational performance of Intershop. Actual events or results may differ materially from the results presented in these forward-looking statements or from the results expected according to these statements. Risks and uncertainties that could lead to such differences include Intershop's limited operating history, the limited predictability of revenues and expenses, and potential fluctuations in revenues and operating results, significant dependence on large individual customer orders, customer trends, the level of competition, seasonal fluctuations, risks relating to electronic security, possible state regulation, and the general economic situation.

Ralf Männlein,
Management board member
responsible for Sales and Marketing

Dr. Jürgen Schöttler,
Chief Executive Officer

Letter to the Stockholders

Dear stockholders, customers, partners, and employees,

Let me begin with some good news: the IT industry in general – and the e-commerce sector in particular – is picking up again. According to a study conducted by Forrester Research last year, online shopping revenues in European countries will quadruple to around EUR 167 billion within the next five years. The study also forecasts that Germany will overtake the United Kingdom as Europe's leading e-commerce country in 2008.

Intershop is also upbeat and confident about the future, and regards 2005 as a positive year overall. We still have a lot to do, but the Company recorded a number of successes in the past year that we can now build on: we reduced our net loss by 62% compared with 2004 and increased license revenues – an important source of income for us – by 50% year-on-year. We are now in a good starting position to meet the challenges that face both us and our competitors in the IT market.

Intershop can now look back on a total of 14 years' experience in e-commerce. Today we are a globally renowned company in our segment, with prominent customers, leading products, and highly acclaimed experts who are specialists in their fields. The name Intershop is directly linked with e-commerce and stands for an entire sector. Admittedly, achieving this was not always easy.

Intershop has come through the worst and is now looking forward. To underpin this, we organized an Intershop Open in November 2005 for the first time in four years. Those of you who have been associated with Intershop for years appreciate the importance of this event for our Company. The first two Intershop Opens were held in New York in 1999 and 2000 and were symbolic of the unbelievable development and hype phase of the new economy, with its supposedly never-ending period of growth. I don't need to tell you what then happened in 2001.

Intershop has overcome an extremely difficult phase in its history. We are therefore all the more delighted to be able to tell you in measured tones that Intershop is again confidently positioned and is presenting itself as what it is: The E-Commerce Company.

On behalf of all Intershop employees, we would like to thank you, our stockholders, customers, and partners for your support. Please continue to track our progress in future with the same intensity and curiosity. We continue to rely on your confidence in us and will keep you regularly informed of developments at Intershop in the future.

Sincerely,

Dr. Jürgen Schöttler
Chief Executive Officer

Group Management Report and Management Report of Intershop Communications AG

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Overall Economy and Industry

In fiscal year 2005, the business of the Intershop Communications AG Group ("Intershop," "the Company," or "the Intershop Group") and Intershop Communications AG (the "AG"), which acts as the holding entity for the Intershop Group, was dominated by the economic consolidation and stabilization of the IT customer market. The software industry is undoubtedly undergoing a period of rapid change. For many years, it symbolized prosperity and spoiled everyone with double-digit growth rates. This was followed by a long sobering-up period. Today, the entire industry has become more mature, with the earlier euphoria giving way to a realistic assessment of market potential.

Intershop also went through this period and became a symbol of the hype and the fall of the new economy. The market contracted in 2001 and 2002, consolidated in 2003 and 2004, and is now showing initial signs of recovery. More than ever, the IT sector is becoming a key strategic industry in which the e-commerce segment is in turn playing a major role. The use of e-commerce software has become a measure of the competitiveness of global companies. In future, online shopping will drastically change conventional trading structures.

As a provider of e-commerce standard software, Intershop is part of this key segment. Since its formation in 1992, the Company has focused on innovation in e-commerce – a tradition it has continued to date. The Company believes that this positioning will lead to renewed growth in the foreseeable future. Intershop is in a good starting position to meet the challenge of generating higher revenues and achieving a positive result. Although it did not reach this goal in full-year 2005, the Company took an initial key step in this direction by generating a positive result in the fourth quarter of 2005.

Intershop's current healthy position is reflected not least in the fact that various capitalization measures have substantially increased its liquidity. This has given the Company a more positive starting position, particularly in discussions with potential customers who require an economically stable partner. When making major IT investments, customers decide not only on the basis of the software provider's technological expertise: other criteria, such as a service provider's financial stability, also play a key role in the decision to award a project. Intershop has now overcome this obstacle, which definitely hampered new customer acquisition in recent years. This has opened up new opportunities for Intershop to make urgent investments in sales and marketing. The Company began doing this in 2005 – and recorded initial successes.

Intershop has significantly increased its sales force. The Jena-based Company now employs 43 people in sales and marketing. Intershop's direct sales activities are focused solely on the German and U.S. markets. Other key markets, such as the United Kingdom, Scandinavia, the Benelux countries, Italy, and Austria, are served by sales partners operating under the Intershop name. Intershop's management is working intensively to meet the above-mentioned challenges of generating higher revenues and in particular gaining new customers. The Company will recruit more sales staff to drive its business forward.

In addition, Intershop presented a completely new price model for its Enfinity Suite 6 standard software at CeBIT 2005, and successfully positioned its "E-Commerce Express" turnkey end-to-end solution for middle-market companies.

Intershop presented a new sales strategy at CeBIT 2005, launching three new price models for e-commerce solutions based on Enfinity Suite 6 that will boost new customer acquisition in future.

Intershop is responding to its customers' different business requirements by offering a total of three flexible price plans for its Enfinity Suite 6 standard software. The range of functions offered by Enfinity Suite 6 is identical for all price plans. Intershop's Express price plan is an attractive price model aimed at middle-market companies, and also offers large customers a cost-effective entry-level solution for the Company's powerful e-commerce software. The Standard price plan has been optimized for customers with high-end requirements. Finally, the On Demand price plan is a price model tailored to customers who prefer a pay-as-you-go option. License costs start at EUR 0, while variable costs are calculated according to a customer's transaction volume. A turnkey offering offers a cost-effective way for middle market companies to begin taking their business online. Intershop's end-to-end "E-Commerce Express" package includes all the functionality offered by the standardized Enfinity Suite 6. A combination of software, hardware, and services makes this fixed-price offering particularly attractive for middle market companies. The launch of this flexible price system enables Intershop to target completely new customer segments, as well as tap new markets and revenue potential.

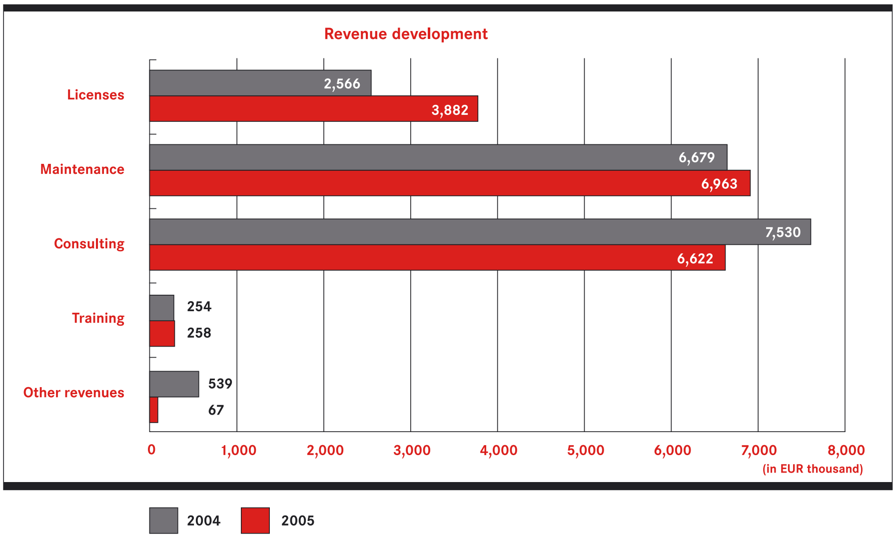
In the fourth quarter of 2005, Intershop launched Version 6.1 of its Enfinity Suite 6 standard software which features extended marketing and sales functionality in line with current developments in online shopping. Enfinity Suite 6.1 is an upgrade to the technology offered by Enfinity Suite 6 aimed at ensuring the continuing success of Intershop's flagship product. Since it was launched at CeBIT 2004, Intershop's latest software has been installed at a total of 44 customers, 19 of whom were new customers.

The market for Internet shopping has changed dramatically and rapidly in recent years, opening up completely new opportunities for both major global players and middle-market companies. Successful companies today regard the Internet as the driving force behind their business success. Their requirements for a complex e-commerce system are correspondingly high: more revenue in less time at lower cost. Our customers are the key focus of all our thoughts about the future of our industry – and they are the most important factor in our success. This is reflected particularly in the longstanding, close relationships we have with them. In the past year, Intershop also gained prominent new customers such as debitel, Elkjop, Lenscare, and Navteq for its Enfinity Suite 6, and generated license and service revenues from existing customers such as Otto and Deutsche Telekom.

In summer 2005, Intershop launched a nationwide advertising campaign in Germany's leading daily newspapers, business and specialist publications to give the Company a more positive image and to begin communications activities for the Intershop Open 2005. From November 8 to 9, 2005, the Company organized the third meeting of Intershop's global community – Intershop Open@home 2005 – in Jena in the German state of Thuringia. After a four-year break, this allowed Intershop to invite users and developers from all over the world to its headquarters in Jena, Intershop Tower. The Intershop Open meetings in 1999 and 2000 were held in New York. The 2005 event focused on the implementation of e-commerce strategies for the global business community. Especially in turbulent economic times, companies must leverage cost-cutting potential and revenue growth by exploiting the competitive advantages offered by enterprise-wide e-commerce. The event was attended by around 200 guests, including prominent e-commerce users, analysts, technology and sales partners, and a large number of representatives from leading business associations and the media from throughout Europe.

Revenue Development

In fiscal 2005, Intershop's total revenues increased slightly year-on-year from EUR 17.6 million in 2004 to EUR 17.8 million. However, license revenues which are an important source of income for the Company rose by 51% to EUR 3.9 million, and their share of total revenues climbed to 22% (previous year: 15%). Service, maintenance, and other revenues fell by 7% to EUR 13.9 million (previous year: EUR 15.0 million), and their share of total revenues dropped from 85% in 2004 to 78% in 2005. This is due to the decline in consulting revenues as a result of the reduction in the headcount, and to a slight decrease in average daily rates. Revenues from maintenance and training increased slightly.



Europe and North America remained Intershop's key revenue regions in fiscal year 2005. Once again, Europe was the Company's primary market in the year under review, with an 82% share of total revenues, compared with 80% in fiscal year 2004. Intershop generated revenues of EUR 3.1 million in North America in 2005, or 18% of the global total. Intershop's U.S. branch in San Francisco ensured that the Company continued to be represented in the strategically important U.S. software market in 2005.

The AG, which is responsible for the Group's business in Germany, generated revenues of EUR 15.1 million in the year under review, as against EUR 13.8 million in the previous year.

In Germany, Intershop has branch offices in Stuttgart and Hamburg.

Earnings Development

Intershop reduced its net loss by 62% in fiscal year 2005 to EUR 3.4 million or EUR 0.35 per share, compared with EUR 8.9 million or EUR 0.57 per share in 2004.

The restructuring measures implemented in recent years were more or less completed in 2005. The Group's structure was streamlined, and substantial cost savings were made. The class-action lawsuit pending in 2004 in the United States was settled in 2005.

The gross profit margin on total revenues increased from 49% in 2004 to 50% in 2005; this corresponds to EUR 8.6 million in 2004 and EUR 8.9 million in 2005. The gross profit margin on license revenues rose to 95% in 2005, compared with 89% in 2004, because licenses previously purchased from third parties were replaced by internal developments. The gross profit margin on service revenues (including services, maintenance, and other revenues) fell from 42% in 2004 to 37% in 2005, mainly due to the slight decline in average daily rates in the consulting business.

In the areas of research and development, sales and marketing as well as administration, costs alone were reduced by EUR 5.1 million or 29%. This is attributable to the areas of research and development as well as administration; in sales and marketing, the recruitment of new sales staff and higher advertising expenses led to a 16% increase in costs. In fiscal year 2004, general and administrative expenses included extraordinary expenses amounting to EUR 2.3 million relating to the settlement of the class-action lawsuit in the United States. Excluding these costs, this item fell by 35% due to the reduction in the workforce and efficiency gains.

Depreciation and amortization charges increased slightly in the year under review to EUR 0.6 million, compared with EUR 0.5 million in 2004. This relates to the deconsolidation of Intershop's subsidiary in the United Kingdom. Otherwise, most investments made in the year under review were replacements.

With the conclusion of the Company's restructuring, existing provisions for restructuring in the amount of EUR 0.8 million were reversed.

In 2005, the continued negative result from operating activities was reduced by 75% year-on-year. The net loss decreased from EUR 8.8 million in 2004 to EUR 2.2 million.

The interest expense included in the financial result increased by EUR 1.1 million from EUR 0.3 million in 2004 to EUR 1.4 million in 2005, due to the issue of the convertible bond in fiscal year 2005.

Research and Development

Research and development expenses declined by around one third to EUR 2.8 million in 2005, compared with EUR 4.1 million in 2004. This change is due in particular to a reduction in the workforce.

Intershop has its own development department. It developed the new Enfinity MultiSite product line in 2002, followed by a range of MultiSite-enabled solutions that added content management and procurement to the portfolio. Intershop consolidated its product line in fiscal year 2004 and presented Enfinity Suite 6 – an end-to-end application for multichannel e-commerce. In fiscal year 2005, Enfinity Suite 6 was enhanced and the new Enfinity Suite 6.1 version with extended marketing and sales functionality was launched.

Organization

There were no changes to the Management Board in fiscal year 2005.

Eckhard Pfeiffer, who had been Chairman of the Supervisory Board for many years, resigned from this position with immediate effect on August 25, 2005, and retired from the Supervisory Board with effect from September 30, 2005 for personal reasons. The existing Deputy Chairman of the Supervisory Board, Hans Gutsch, was appointed the new Chairman. Wolfgang Meyer – a member of the Management Board of Schott Lithotec AG and Chairman of the management of Schott Jenaer Glas GmbH, Jena – was appointed as the new third member of the Supervisory Board in addition to Hans Gutsch and Peter Mark Droste by the Gera Local Court on October 1, 2005.

Employees

Intershop's headcount remained unchanged year-on-year at 222 full-time equivalents as of December 31, 2005. However, the average number of employees fell to 219 full-time equivalents in 2005, compared with 244 in 2004.

The technical departments (research and development and service functions) employed 150 full-time equivalents as of December 31, 2005, or 67% of the entire workforce. The sales and marketing departments accounted for 43 full-time equivalents as of December 31, 2005, while 29 full-time equivalents were employed in general and administrative functions at this date.

93% of Intershop's global workforce was employed in Germany as of December 31, 2005 (207 full-time equivalents). The remaining 7% belong to the U.S. branch (15 full-time equivalents). As of December 31, 2004, 206 full-time equivalents were employed in Germany, 2 in the United Kingdom, and 14 in the United States.

Intershop Communications AG (single entity) had 207 staff as of December 31, 2005. The headcount increased by one employee as against December 31, 2004 (206).

Financial Position

In fiscal year 2005, Intershop implemented three financing measures that enabled it to strengthen its equity base and increase its liquidity.

In the first quarter of 2005, Intershop received gross cash amounting to EUR 11.3 million from the issue of a zero-coupon convertible bond. On November 24, 2004, Intershop announced its intention to issue a zero-coupon convertible bond with a total volume of up to EUR 20 million, as authorized by the resolution of the Annual Stockholders' Meeting on June 13, 2001, which created conditional capital of up to EUR 21,449,703 in order to grant conversion rights to the bondholders.
The zero-coupon convertible bond has a maturity date of December 14, 2008 and is composed of individual bonds with a nominal value of EUR 1.00 each. The principal features of the zero-coupon convertible bond are the repayment amount of EUR 1.46 per bond at maturity, if conversion has not taken place, corresponding to an effective interest rate of 10% p.a., and the right to convert the bond

into ordinary voting bearer shares of the Company during specified exercise periods. The conversion price on each occasion will be EUR 1.00, irrespective of any capital reductions. Automatic conversion will take place if the share price exceeds EUR 5.00 on ten consecutive trading days at any time after January 1, 2006. As collateral, Intershop has furnished a first-ranking lien on its worldwide copyright to the Enfinity Software.

Stockholders were granted an indirect right to subscribe for the bond at a ratio of 1.3 to 1 in the period from November 29 to December 14, 2004; they also received the right to subscribe for additional bonds. However, the minimum amount of EUR 5 million required for the issue of the convertible bond to proceed was not achieved during the subscription period. Additional bonds were then offered to investors in the form of a private placement. On January 26, 2005, Intershop announced that the convertible bond had been successfully placed. Convertible bonds with a value of EUR 11,331,000 were subscribed. The inflow of funds from the issue of the convertible bond strengthened the Company's liquidity.
In the first exercise period (November 1 to November 30, 2005), 4,886,402 convertible bonds were converted into shares of the Company; this corresponds to a proportion of 43.12%. The conversion enabled Intershop to increase its equity base.

In the third quarter of 2005, Intershop received gross cash amounting to around EUR 4.3 million from a cash capital increase. On September 28, 2005, Intershop announced that the Management Board and Supervisory Board had resolved to implement a cash capital increase from Authorized Capital I, while preserving stockholder subscription rights. Existing stockholders were able to subscribe for one new share at a price of EUR 1.00 per two existing Intershop ordinary bearer shares. To this end, Intershop issued 4,258,550 new shares from its authorized capital. The new shares were created on entry of the capital increase in the commercial register at the Gera Local Court on October 19, 2005 and were admitted to trading in the Prime Standard of the Frankfurt Stock Exchange on November 28, 2005. Intershop again strengthened its liquidity as a result of the inflow of funds from the cash capital increase.

In fiscal year 2005, the Company implemented a simplified capital reduction at a ratio of 3:1. The preparation of the 2004 single-entity financial statements of Intershop Communications AG in accordance with the Handelsgesetzbuch (HGB – German Commercial Code) revealed that half of the share capital of the German company Intershop Communications AG had been depleted. The depletion of more than half of the share capital was attributable to the losses incurred in fiscal year 2004 and the write-downs of the carrying amounts of investments at the 2004 balance sheet date. The Annual Stockholders' Meeting on April 26, 2005 resolved a simplified capital reduction at a ratio of 3:1 by merging three Intershop ordinary bearer shares into one Intershop ordinary bearer share in order to implement technical restructuring of the losses incurred. The reverse stock split was technically implemented on July 7, 2005 after the close of trading on the Frankfurt Stock Exchange. This meant that three old ordinary bearer shares were exchanged for one new ordinary bearer share, after 112 shares were retired without compensation. The new shares began trading on a consolidated basis on July 8, 2005. As a result of the capital reduction, the capital reserve and other reserve items were adjusted and the share capital reduced accordingly.

Net cash used in operating activities increased from EUR 5.4 million in 2004 to EUR 8.4 million in 2005. The 2005 figure includes around EUR 2.6 million that Intershop was required to pay to settle pending court proceedings (EUR 2.3 million of which relates to the settlement of the class-action lawsuit in the United States). Excluding this extraordinary expense, net cash used in operating activities would have risen slightly from EUR 5.4 million to EUR 5.8 million, which corresponds to an average utilization of funds of EUR 1.5 million per quarter.

Net cash provided by investing activities amounted to EUR 0.4 million, compared with net cash used in investing activities of EUR 0.8 million in 2004. This related primarily to the change in restricted cash.

Net cash provided by financing activities increased from EUR 5.2 million in the previous year to EUR 13.9 million due to the described financing measures.

Net Assets

Total assets increased by EUR 5.7 million or 33% year-on-year to EUR 23 million. On the assets side, this rise was largely due to cash and cash equivalents (+346%), while the liabilities side saw an increase in equity (+212%).

Noncurrent assets fell by 14% to EUR 9 million; this change was due to the reduction in property, plant, and equipment (EUR-0.4 million), other noncurrent assets (EUR-0.3 million), and restricted cash (EUR-0.8 million).

Current assets increased from EUR 6.8 million in 2004 to EUR 14 million. Trade receivables rose by 56 % due to growth in revenues in the fourth quarter of 2005 (EUR 5.3 million) compared with Q4 2004 (EUR 4.1 million). Other receivables and other assets increased from EUR 0.8 million to EUR 0,9 million.

Cash and cash equivalents included in noncurrent and current assets rose to EUR 13.5 million as of December 31, 2005, as against EUR 8.4 million as of December 31, 2004 – up around 61%. The amount of unrestricted cash included in cash and cash equivalents increased from EUR 1.6 million to EUR 7.3 million.

Equity rose from EUR 2.7 million in 2004 to EUR 8.3 million in 2005. The equity ratio increased to 36 % compared with 15% in the previous year. In addition to the reduction in the net loss for the year, this change is due to the capitalization measures implemented.

Noncurrent liabilities rose from EUR 0.4 million to EUR 5.8 million due to the recognition of the debt component of the convertible bond (EUR 5.6 million).

Current liabilities fell by 37% to EUR 9.0 million. Other current provisions decreased from EUR 4.0 million to EUR 0.8 million, primarily due to the conclusion of pending legal proceedings (including the settlement payment for the class-action lawsuit). Trade accounts payable increased from EUR 2.9 million in 2004 to EUR 3.8 million in 2005, while deferred revenue fell from EUR 4.5 million in 2004 to EUR 2.0 million.

Provisions for restructuring fell by 55% to EUR 0.8 million as the restructuring measures were more or less completed.

Group Risks and Risks Facing Intershop Communications AG

Intershop is exposed to a variety of risks that could endanger the Company's net assets, financial position, and results of operations as well as its continued existence as a going concern, including (but not limited to) the following:

Despite the successful placement of the convertible bond, which generated an inflow of liquidity of around EUR 11.3 million for the Company, and the implementation of a capital increase resulting in a further inflow of liquidity of around EUR 4.26 million in 2005, customers and partners continue to have certain reservations with regard to the Company's ability to survive in the long term. Such reservations could lead to reluctance on the part of Intershop's customers to place orders with the Company in the future as well, and could therefore impact Intershop's operations. However, the Company hopes that the measures it has taken to strengthen its liquidity for the long term and the results for the fourth quarter of 2005 published after the balance sheet date will have positive effects on the confidence of its customers and partners.

In past fiscal years, Intershop's business development has been dominated by the economic downturn, both globally and in particular in Germany, and the resulting reluctance of many companies to invest in IT, especially in Europe. This reluctance to invest could mean that Intershop is unable to generate revenues from corporate customers, that its operating result is significantly impacted in the future, and that a need for additional funding will arise.

The market for e-commerce applications is continuing to mature and is subject to ongoing changes. Future developments are therefore hard to predict – even for the short term – and forecasts are thus subject to a high degree of uncertainty. For planning purposes, Intershop uses analyses available from market research companies as well as its own findings, which are gathered on an ongoing basis from its many contacts with other market players. Nevertheless, there is a risk in principle that the Company may not identify market trends in good time and that management may not be able to correctly assess the demand for e-commerce solutions with regard to customer requirements.

In the past, Intershop's quarterly revenues included a certain number of large individual orders that accounted for a relatively high proportion of total quarterly revenues. Furthermore, the Company generated 20.3% and 12.8% of its total revenues in fiscal year 2005 from two individual customers. The Company's significant dependence on large individual orders or individual customers could continue to impact revenue forecasts in the future and could adversely affect Intershop's results of operations if the Company does not receive certain large individual orders during a quarter.

Operating results for future periods cannot be forecasted with complete certainty, even in times of economic stability. Intershop expects continued fluctuations in its quarterly results and in any forecasts about its financial results in future periods. These fluctuations, which could be significant in the future, could lead to substantial volatility in Intershop's share price and could impact the Company's ability to acquire funding.

Intershop is in direct competition with other providers of e-commerce technologies. Given the dynamic development of the e-commerce market, existing and new providers are expected to substantially improve their product range and their sales activities. If Intershop is unable to maintain or improve its competitiveness with regard to the profile and quality of its products and services or its sales methods, this could endanger its market position.

Intershop's success on the market is heavily dependent on the technical performance of its products. Software faults that lead to restrictions in the functionality and performance of existing and future products could considerably reduce the acceptance of Intershop's products.

The Company is a defendant in various legal proceedings arising from the normal course of business. A negative ruling in any such legal dispute, or in several or all such disputes, could have a material adverse effect on the Company's results of operations. The Company recognizes all legal costs associated with loss contingency as an expense as they are incurred.

Intershop has taken extensive measures to protect the brand names it uses as far as possible internationally. However, it is possible that conflicts with third parties will arise regarding the use of individual brands. In accordance with European practice, the programs and technologies developed by Intershop only have limited patent protection. Although Intershop takes great care in protecting its intellectual property, no assurance can be given that property rights will not be violated by third parties. It is also possible that third parties may sue Intershop for a violation of patents or other rights. Patent disputes are widespread in the software industry, particularly in the United States, and often entail significant costs for litigation or out-of-court settlements. Although Intershop is convinced that it has not violated any patents, it cannot be ruled out that Intershop's operating result will be adversely affected by such actions brought by third parties.

A customer's decision to acquire enterprise software is based partly on a provider's reputation and visibility, as well as on the performance of its products. Should Intershop fail to achieve the necessary visibility and the desired image with its target groups, this could have an adverse effect on the demand for its products.

Intershop's products are also sold and implemented via IT service providers. If Intershop is unable to train a sufficient number of these companies in the use of its own products and to gain them as partners, this could impact sales of its products.

The success of Intershop's business depends heavily on the performance of its executives and employees in key positions, particularly in the areas of product development and sales. If Intershop fails to retain existing employees and executives and to attract sufficient numbers of new personnel, this could have an adverse effect on the Company's operating result.

Licenses account for a substantial proportion of the Company's total revenues. Under IFRSs, the recognition of software license revenues requires among other things that a sales agreement has been signed, a license has been delivered, the license fee is fixed and determinable, and payment is probable. If an order entails services that are essential to the functionality of the software, revenue is recognized according to the percentage of completion of the project. Due to the uncertainty with regard to the length of sales and implementation cycles, which depends heavily on Intershop's customers, revenues may be subject to sharp fluctuations on a quarterly basis in particular. This applies all the more given that a small number of large orders often account for a substantial proportion of revenues. Since operating costs are largely dependent on the number of employees, and therefore can only be affected to a limited extent in the short term, fluctuations in revenues could lead to corresponding fluctuations in operating results.

In the software industry, a large proportion of license revenues is not recognized equally over a quarter, but frequently only towards the end of a quarter. This is because contracts are often not awarded until the last third of a quarter. As a result, uncertainty as to whether the forecast revenue target will be achieved usually persists until well into the quarter.

A certain proportion of Intershop's operating and financial results are reported in currencies that are not pegged to the euro at fixed exchange rates, and are therefore translated into euros for inclusion in the Company's consolidated financial statements. Since no measures have currently been taken to hedge currency risks, currency fluctuations could affect the results of Intershop's business activities and operations overall.

The financial statements of Intershop Communications Aktiengesellschaft show that as of December 31, 2005, the Company had investments in affiliated companies of EUR 8.9 million relating to its investment in Intershop Communications Inc. The carrying value of the investment was examined using discounted cash flow analysis performed by the Company itself. This carrying value represents a reduction compared with the value shown in the previous year's financial statements of EUR 1.8 million.

The measurement of the carrying value is based on a detailed forecast for 2006 through 2008, followed by a transition to a perpetual annuity. The reduction in the carrying amount of the investment is mainly due to the fact that the revenues generated in 2005 were lower than forecast, and as a result the revenue growth rates for future periods were also adjusted. Based on the sales forecast of Intershop Communications Inc., revenue is expected to grow by 50% in 2006, from the very low level achieved the previous year. Continuous revenue growth of only 5% per year is expected for 2007 and the subsequent years. Based on these assumptions the operating result of Intershop Communications Inc. will be EUR 0.85 million in 2006, and is expected to grow further over the period covered by the forecast. The continuous growth assumption is based on general analyst expectations with regard to investment activity in the area of information technology in the US market, as well as projects expected with existing and new customers. The present value is calculated by discounting free cash flows by 15%.

If the expectations described are not met, or if Intershop Communications Inc. cannot achieve the expected results for other reasons, a further write-down of the investments in affiliated companies would have to be charged in the financial statements of Intershop Communications Aktiengesellschaft.

Risk Management

Intershop's goal is to exploit business opportunities worldwide in order to increase enterprise value for its stockholders. In addition to these opportunities, however, Intershop is exposed to a number of risks that are inevitably associated with them. Risks to the Company's development cannot be ruled out completely due to the dynamic pace of market development and limited planning certainty with regard to the license business. Intershop aims to minimize the risks arising from its business activities by continuously enhancing its extensive risk management system.

At Intershop, various systems and procedures are used for the early identification, analysis, and documentation of risks for the Company. Intershop's risk management activities comprise a forward-looking product strategy that is geared to expected market developments and future needs, while focusing on product development and on the technological performance of the Company's products. In addition, Intershop continually endeavors to increase the Company's visibility among the relevant target groups, to gain new partners and form new alliances, to train third parties that market, sell, and implement Intershop's products, to recruit and retain executives and employees in key positions, and to provide the necessary organizational infrastructure.

The Company monitored market developments and its competitive environment on an ongoing basis in fiscal year 2005, using analyses and forecasts published by leading market research companies, among other things. Intershop has extensive project management and quality assurance systems in the area of product development, which is particularly dependent on risk identification.

Intershop uses financial accounting, controlling, and forecasting software by SAP and Hyperion as well as customer relationship management (CRM) software by Siebel Systems to globally capture and manage key corporate data. Quarterly financial statements ensured the timely recording of business developments. In addition to the annual budget planning, the Company used ongoing forecasts for short-term cost and revenue development. Ongoing accounting and controlling activities regularly provided information on deviations between actual and target figures in individual areas.

In addition, management regularly performed separate analyses of the Company's net assets, financial position, and results of operations. Frequent meetings at all levels of the Company have ensured an efficient exchange of information and rapid decision-making processes throughout the Company worldwide. The Management Board informed the Supervisory Board at least once a quarter, but usually more often, about important developments at the Company. The Supervisory Board's Audit Committee held regular meetings with the CFO and the head of accounting to discuss, analyze, and monitor financial issues relating to day-to-day business. On the basis of its internal risk management guidelines and internal controls on insider trading and the disclosure of information, the Company assumes that it fulfills both statutory and stock exchange requirements and that the principles of proper corporate governance as well as the guidelines contained in the German Corporate Governance Code have been materially implemented.

Events Subsequent to the Balance Sheet Date

As of January 1, 2006, the Company granted new options to employees under its stock option plans. 300,000 options were issued to the members of the Management Board under the 1999 Stock Option Plan, while 3,697,032 options were granted to employees under the 2001 Stock Option Plan. The issue of the options does not lead to any changes in earnings per share because the inclusion of the options would counter the dilutive effect.

On February 3, 2006, Intershop announced in the Frankfurter Allgemeine Zeitung that Heycom GmbH, Garbsen, informed the Company on January 27, 2006 that its share of Intershop's voting rights exceeded the 5% threshold on January 18, 2006 and amounts to 8.62%. Heycom GmbH also informed the Company on January 31, 2006 that its share of Intershop's voting rights fell below the 5% threshold on January 25, 2006 and now amounts to 1.11%.
On February 9, 2006, Intershop announced in the Frankfurter Allgemeine Zeitung that Mr. Sven Heyrowsky informed the Company on February 6, 2006 that his share of the Company's voting rights exceeded the 5% threshold on January 18, 2006 and amounts to 8.62%. Of this, 8.62% is attributable to Mr. Sven Heyrowsky in accordance with section 22(1) no. 1 of the Wertpapierhandelsgesetz (WpHG –

German Securities Trading Act). Mr. Sven Heyrowsky also informed Intershop on February 6, 2006 that his share of the Company's voting rights fell below the 5% threshold on January 25, 2006 and now amounts to 3.94%. Of this, 2.83% is attributable to Mr. Sven Heyrowsky in accordance with section 22(1) no. 1 of the WpHG.

In accordance with section 15a of the WpHG, the Company announced on February 22, 2006 that member of the Management Board Ralf Männlein purchased 50,000 Intershop convertible bonds with a total value of EUR 57,450 on February 21, 2006.

Outlook

Many experts believe that demand for e-commerce software products will increase further in 2006. The success and the pace of growth of e-commerce will continue this year, and online sales will in fact record disproportionately high growth compared with other sales channels. The Hauptverband des Deutschen Einzelhandels (HDE – the Central Association of German Retailers) forecasts online shopping revenues of EUR 16.3 billion for 2006, a year-on-year increase of around 13%. According to the HDE, multichannel providers – i.e., companies that combine online sales and fixed sales outlets – will profit from this trend in particular (source: www.hde.de).

A large number of Intershop customers are also gaining an edge on their competitors using multichannel sales. Multichannel strategies enable companies to access new groups of potential purchasers, and to target customers who do not want to rely on a single purchasing method. The exploitation of synergies between offline and online sales offers companies powerful instruments to increase revenues and cut costs. Companies must learn to play by different rules as a result of fiercer price wars and more intense competitive pressure. Professional multichannel sales will play an increasingly important role here in the future. This assumption is supported by the positive business development recorded by multichannel companies in Germany, 47% of which expect an increase in revenues in the short period up to the middle of 2006, according to the HDE. Successful multichannel retailers are able to efficiently manage several offline and online sales channels. Intershop has already recognized this trend and offers solutions that make it easier for these companies to execute their multichannel strategies in two respects: on the one hand, Intershop offers companies the opportunity to include any number of online channels within a system. Once implemented, these channels can be made available to other business units or partners, thus producing a network of decentralized sales channels. On the other hand, companies are integrating the IT systems belonging to their offline sales channels using comfortable interfaces. This ensures that critical data is made available beyond the limits of the sales channels.

It is not uncommon for Intershop's customers to generate annual online revenues in the triple-digit million range. Despite this and positive forecasts by experts, price pressure on e-commerce software products will continue. Competition in the e-commerce software provider segment is becoming fiercer. Both today and going forward, software manufacturers will have to face the challenges posed by completely new market conditions.

Business models in the online shopping sector are changing: they are becoming more diverse. E-commerce software companies are thus addressing new and different target groups, and are focusing increasingly on their customers' sales and marketing departments, rather than on IT managers. This means that in future it will not be sufficient to offer e-commerce software. As is known, e-commerce is a complex network of closely integrated processes, ranging from e-commerce software through electronic payment processes and fulfillment, to efficient online marketing and customer management.

Intershop is adapting to this trend and is presenting itself for the first time as a full-service e-commerce provider at CeBIT 2006. This enables the Company to offer customers its complete business model for successful online shopping. Intershop offers all aspects of e-commerce – webshop, marketing, and fulfillment – from a single source. Intershop manages its customers' entire online business on their behalf and works in partnership with them to achieve their ambitious business goals.

Thanks to this restructured offering and the Enfinity Suite 6 standard software, Intershop's Management Board believes that the Company is excellently positioned to meet market demands. The market for high-end e-commerce software continues to be dominated by development platforms and tools for programming business processes. Intershop offers its customers high-quality standard software and is making every effort to further extend its technology lead in the area of e-commerce software.

On the basis of the significant improvement in revenues as of the end of 2005 and assuming a slight increase in corporate IT expenditure in 2006, Intershop expects to generate a positive net result in fiscal year 2006.

Jena, March 23, 2006

The Management Board

Dr. Jürgen Schöttler   Ralf Männlein

Report of Independent Auditors Group

Auditor's Report

We have audited the consolidated financial statements prepared by the INTERSHOP Communications AG, Jena, comprising the balance sheet, the income statement, statement of changes in equity, cash flow statement and the notes to the consolidated financial statements, together with the group management report for the business year from January 1, 2005 to December 31, 2005. The preparation of the consolidated financial statements and the group management report in accordance with IFRSs, as adopted by the EU, and the additional requirements of German commercial law pursuant to § 315a Abs. 1 HGB are the responsibility of the parent company's management. Our responsibility is to express an opinion on the consolidated financial statements and on the group management report based on our audit.

We conducted our audit of the consolidated financial statements in accordance with § 317 HGB [Handelsgesetzbuch „German Commercial Code"] and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the consolidated financial statements in accordance with the applicable financial reporting framework and in the group management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Group and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the consolidated financial statements and the group management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the annual financial statements of those entities included in consolidation, the determination of entities to be included in consolidation, the accounting and consolidation principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements and group management report. We believe that our audit pro-vides a reasonable basis for our opinion.

Our audit has not led to any reservations.

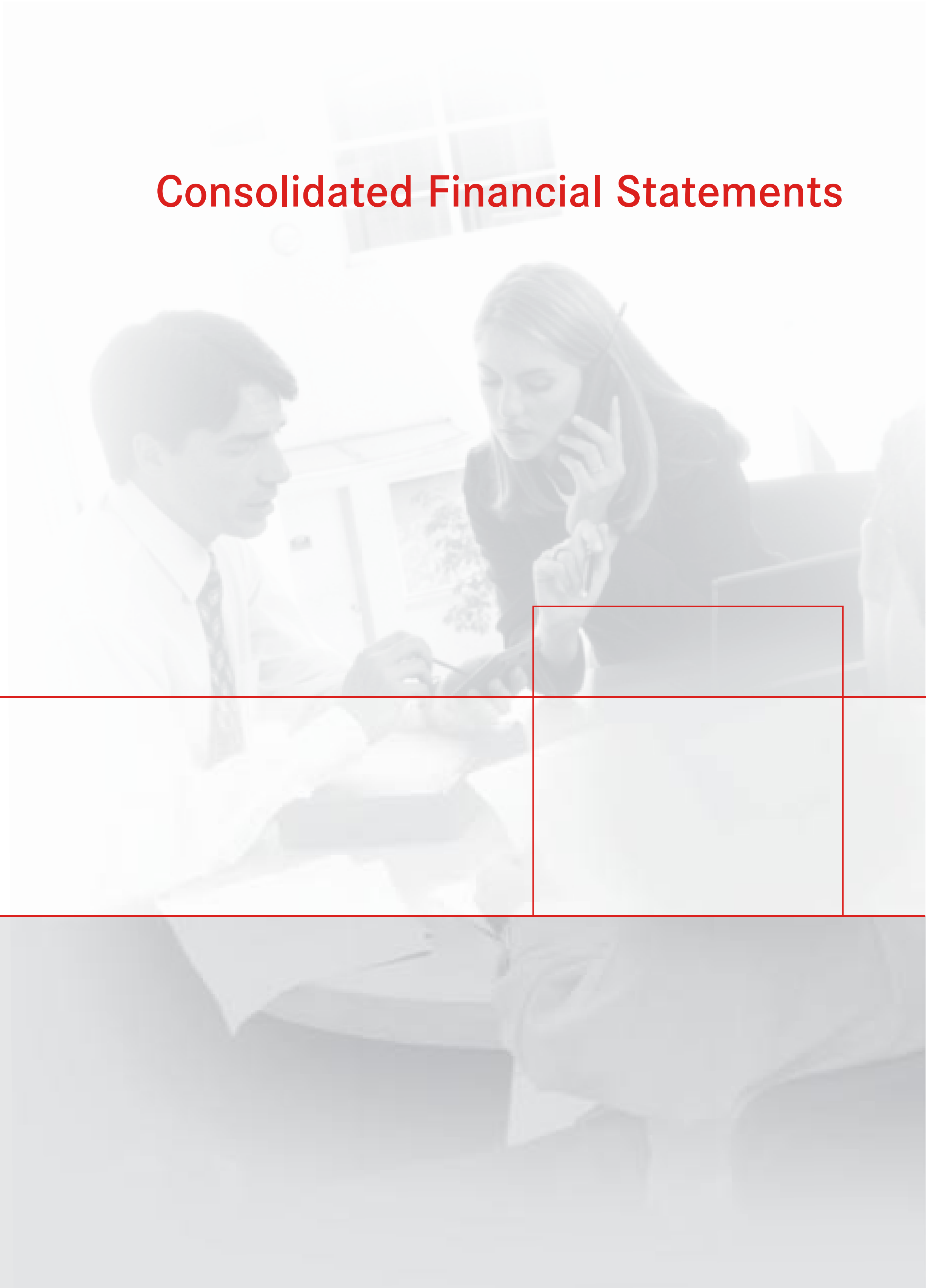
In our opinion, based on the findings of our audit, the consolidated financial statements comply with IF-RSs, as adopted by the EU, the additional requirements of German commercial law pur-suant to § 315a Abs. 1 HGB and give a true and fair view of the net assets, financial position and results of operations of the Group in accordance with these requirements. The group management report is consistent with the consolidated financial statements and as a whole provides a suitable view of the Group's position and suitably presents the opportunities and risks of future development.

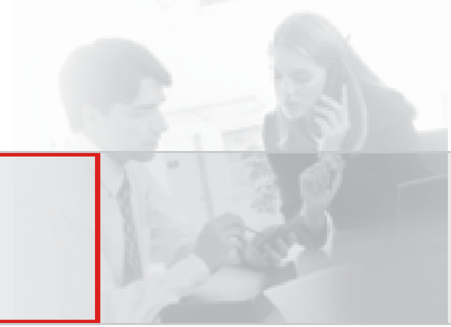
Leipzig, March 24, 2006

KPMG Deutsche Treuhand-Gesellschaft,
Aktiengesellschaft,
Wirtschaftsprüfungsgesellschaft

Dr. Georg Flascha	Maik Pülmanns
Wirtschaftsprüfer	*Wirtschaftsprüfer*

Consolidated Financial Statements





Consolidated Balance Sheet

December 31 (EUR thousand)	Note No.	2005	2004
ASSETS			
Non current assets			
Intangible assets	(1)	4,495	4,572
Property, plant and equipment	(2)	483	870
Financial investments	(3)	59	0
Other non current assets	(5)	105	432
Restricted cash	(6)	3,855	4,642
		8,997	**10,471**
Current assets			
Trade receivables	(4)	3,518	2,257
Other receivables and other assets	(5)	881	836
Restricted cash	(6)	2,355	2,112
Cash and cash equivalents	(6)	7,279	1,632
		14,033	**6,837**
TOTAL ASSETS		**23,030**	**17,308**
SHAREHOLDERS´ EQUITY AND LIABILITIES			
Shareholders´ equity	(7)		
Subscribed capital		17,662	25,551
Capital reserve	(7,1)	54	1,948
Other reserves	(7,2)	(9,444)	(24,843)
Treasury stock	(7,3)	0	(1)
		8,272	**2,655**
Non current liabilities			
Provisions for restructuring	(12)	17	186
Convertible bonds	(8)	5,600	0
Other non current liabilities		0	38
Deferred revenue	(11)	188	131
		5,805	**355**
Current liabilities			
Provisions for restructuring	(12)	790	1,591
Other current provisions	(13)	840	3,964
Trade accounts payable	(9)	3,817	2,929
Income tax liabilities	(24)	4	23
Other current liabilities	(10)	1,538	1,300
Deferred revenue	(11)	1,964	4,491
		8,953	**14,298**
TOTAL SHAREHOLDERS´ EQUITY AND LIABILITIES		**23,030**	**17,308**

Consolidated Income Statement

December 31 (EUR thousand)	Note No.	2005	2004
Revenues	**(14)**		
Licenses		3,882	2,566
Services, maintenance and other		13,910	15,002
		17,792	**17,568**
Cost of revenues	**(15)**		
Licenses		(199)	(288)
Services, maintenance and other		(8,772)	(8,673)
		(8,971)	**(8,961)**
Gross profit		**8,821**	**8,607**
Operating expenses, operating income			
Research and development	**(16)**	(2,774)	(4,179)
Sales and marketing	**(17)**	(5,842)	(5,034)
General and administrative	**(18)**	(4,049)	(8,545)
Restructuring costs	**(19)**	780	(406)
Other operating income	**(20)**	938	940
Other operating expenses	**(21)**	(53)	(150)
		(11,000)	**(17,374)**
Result from operating activities		**(2,179)**	**(8,767)**
Interest income	**(22)**	177	140
Interest expense	**(23)**	(1,365)	(271)
Financial result		**(1,188)**	**(131)**
Earnings before tax		**(3,367)**	**(8,898)**
Income taxes	**(24)**	**(3)**	**(23)**
Earnings after tax		**(3,370)**	**(8,921)**
Consolidated net loss		**(3,370)**	**(8,921)**
Earnings per share (EUR, basic)	**(25)**	(0,35)	(0,57)
Earnings per share (EUR, diluted)*	**(25)**	(0,35)	(0,57)
Weighted average shares outstanding (basic)		9,759	15,584
Weighted average shares outstanding (diluted)		19,167	15,584

** The diluted earnings per share were reduced to the lower undiluted earnings per share.*

Consolidated Statement of Cash Flows

	2005 EUR thousand	2004 EUR thousand
CASH FLOWS FROM OPERATING ACTIVITIES		
Earnings before tax	(3,367)	(8,898)
Adjustments to reconcile net loss to cash used in operating activities		
Financial result	1,188	131
Depreciation and amortization	618	456
Non cash effects from deconsolidation	(438)	(679)
Other non cash expenses	71	145
Allowances for doubtful accounts	(251)	(239)
(Gain) Loss on disposal of property and equipment	(36)	(26)
Changes in operating assets and liabilities		
Accounts receivable	(839)	1,266
Other assets	(60)	647
Liabilities and provisions	(2,975)	2,024
Deferred revenue	(2,450)	(308)
Net cash used in operating activities before income tax and interest	**(8,539)**	**(5,481)**
Interest received	164	131
Interest paid	(43)	(96)
Income taxes paid	(1)	0
Net cash used in operating activities	**(8,419)**	**(5,446)**
CASH FLOWS FROM INVESTING ACTIVITIES		
Restricted cash	544	(564)
Payments for investments in intangible assets	(9)	(72)
Proceeds on disposal of equipment	37	21
Purchases of property and equipment, net of capital leases	(207)	(233)
Net cash (used in) provided by investing activities	**365**	**(848)**
CASH FLOWS FROM FINANCING ACTIVITIES		
Purchase of common stock	0	(40)
Proceeds from re-issuance of treasury stock	0	35
Proceeds from placement of zero-coupon convertible bond	11,331	0
Expenses of placement of zero-coupon convertible bond	(1,353)	0
Cash received for unregistered stock	4,258	5,432
Expenses of cash received for unregistered stock	(385)	(206)
Net cash provided by financing activities	**13,851**	**5,221**
Effect of change in exchange rates on cash	(150)	94
Net change in cash and cash equivalents	**5,647**	**(979)**
Cash and cash equivalents, beginning of period	1,632	2,611
Cash and cash equivalents, end of period	**7,279**	**1,632**

Consolidated Statement of Shareholders´Equity

in EUR thousand	Common shares	Subscribed capital
Balance, January 1, 2004	**22,035,299**	**22,035**
Net loss		
Foreign currency translation adjustments		
Stock option expense		
Purchase of common stock		
Re-issuance of treasury stock		
Issue of new shares	3,516,113	3,516
Balance, December 31, 2004	**25,551,412**	**25,551**
Net loss		
Foreign currency translation adjustments		
Stock option expense		
Re-issuance of treasury stock		
Simplified withdrawal of shares	(112)	
Simplified capital decrease	(17,034,200)	(17,034)
Convertible bond	4,886,402	4,886
Issue of new shares	4,258,550	4,259
Balance, December 31, 2005	**17,662,052**	**17,662**

	Other reserves				
Capital reserve	**IFRS conversion reserve**	**Cumulative profit/loss**	**Cumulative currency differences**	**Treasury stock**	**Total shareholders´equity**
93	**(93)**	**(18,745)**	**3,048**	**0**	**6,338**
		(8,921)			(8,921)
			(129)		(129)
145					145
				(40)	(40)
		(3)		(39)	36
1,710					5,226
1,948	**(93)**	**(27,669)**	**2,919**	**(1)**	**2,655**
		(3,370)			(3,370)
			(663)		(663)
73					73
		3		1	4
					0
(3,419)		20,454			1
1,452		(640)			5,698
		(385)			3,874
54	**(93)**	**(11,607)**	**2,256**	**0**	**8,272**

Notes to the Consolidated Financial Statements

Notes to the Consolidated Financial Statements

General Disclosures

Basis of preparation

In fiscal year 2005, Intershop Communications AG prepared its consolidated financial statements for the first time in accordance with the International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board (IASB), and in accordance with the provisions required to be applied under section 315a(1) of the Handelsgesetzbuch (HGB – German Commercial Code).

The Company

Intershop Communications AG is an Aktiengesellschaft (German stock corporation) under German law. The Company's registered office is at Intershop Tower, Leutragraben 1 in 07740 Jena, Germany. The Company is listed on the German stock exchange in Frankfurt and is included in the Prime Standard.

Intershop Communications AG is entered in the commercial register of the Gera Local Court under number HRB 9419.

Intershop develops and sells software solutions for the management of e-commerce transactions.

Going concern

As of December 31, 2005, the Company had cash and cash equivalents (including restricted cash) of EUR 13.5 million, compared with EUR 8.4 million as of December 31, 2004. The Company has generated operating losses since it was established, and had an accumulated deficit of EUR 288.3 million as of December 31, 2005. In 2005, the Company's operating activities utilized cash of EUR 5.8 million. The Company anticipates that, taking into account the stabilization of its liquidity position, the reorganization of its cost structure and the expected results of operations, it will be able to continue as a going concern in 2006 without additional external financing.

Accounting principles (compliance statement)

The consolidated financial statements of Intershop Communications AG for 2005 were prepared in accordance with the International Financial Reporting Standards (IFRSs) valid at the balance sheet date and with the Interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC), as adopted by the EU.

The International Accounting Standards Board (IASB) has also issued the following Standards, Interpretations, and amendments to existing Standards whose application is not yet mandatory. The Company has decided not to adopt these Standards prior to their effective date:

- *IFRS 7, Financial Instruments: Disclosures*
  The IASB published IFRS 7 in August 2005. This Standard consolidates the disclosures on financial instruments that were previously contained in IAS 30, Disclosures in the Financial Statements of Banks and Similar Financial Institutions and IAS 32, Financial Instruments: Disclosure and Presentation. Individual disclosure requirements were amended or extended. IFRS 7 must be applied for fiscal years beginning on or after January 1, 2007.
  The Standard, which must be applied by all companies, will lead to extended disclosures on financial instruments by Intershop.

- *IFRIC 4, Determining whether an Arrangement contains a Lease*
  The IASB published IFRIC Interpretation 4 in December 2004. The subject of this Interpretation is the issue of how to determine whether an arrangement is or contains a lease, or when a reassessment of this is necessary. It also describes how lease payments can be separated from payments for any other elements in the arrangement.

This Interpretation must be applied for fiscal years beginning on or after January 1, 2006. The transitional provision offers the option to apply the Interpretation retrospectively, or to apply it to arrangements that exist at the beginning of the earliest period for which comparative information is presented in the financial statements.
Intershop does not expect the initial application in fiscal year 2006 to have any effects on the classification of individual leases as finance leases, or any consequences for the recognition of leased assets and corresponding liabilities.

- *IFRIC 8, Scope of IFRS 2*
  In January 2006, the IASB published IFRIC Interpretation 8 that addresses the scope of IFRS 2. IFRS 2, Share-based Payment must be applied to transactions in which a company receives goods or services as consideration for share-based payment. Under IFRIC 8, IFRS 2 must be applied even if the company cannot clearly identify the received goods or services.
  IFRIC 8 must be applied for fiscal years beginning on or after May 1, 2006.
  This Interpretation will not have any effects on Intershop's future consolidated financial statements because none of the companies included in the consolidated financial statements have performed the type of transactions specified in the Interpretation and will not do so in the foreseeable future.

- *Amendment to IAS 1, Presentation of Financial Statements – Capital Disclosures*
  In connection with the publication of IFRS 7, Financial Instruments: Disclosures, the IASB announced an amendment to IAS 1 in August 2005. Under this amendment, information must be published in the financial statements to enable users to evaluate a company's objectives, policies, and processes for managing capital.
  The amendment to IAS 1 must be applied for fiscal years beginning on or after January 1, 2007.
  The initial application of this amendment to IAS 1 by Intershop in fiscal year 2007 will lead to extended disclosures.

- *Amendment to IAS 39, Financial Instruments: Recognition and Measurement – the Fair Value Option*
  In June 2005, the IASB published an amendment to IAS 39 on the use of the fair value option. This amendment limits the classification of financial assets as "at fair value through profit or loss" as adopted by the EU and permits it for financial liabilities subject to certain requirements.
  The amendment to IAS 39 must be applied for fiscal years beginning on or after January 1, 2006.
  This amendment to IAS 39 is not expected to have any effect on Intershop's consolidated financial statements for fiscal year 2006.

Financial reporting for fiscal year 2005 has been prepared in accordance with the Standards and Interpretations required to be applied and gives a true and fair view of the net assets, financial position, and results of operations of the Intershop Group. The conversion to IFRSs has been implemented in accordance with IFRS 1, First-time Adoption of International Financial Reporting Standards.

Assets and liabilities are generally measured at historical cost. The stock option plans are measured at fair value. Convertible bonds are treated as compound financial instruments, consisting of a debt and an equity component. The debt component is carried at amortized cost using the effective interest rate method.

The consolidated financial statements have been prepared in euros. Unless stated otherwise, all amounts are given as thousands of euros (EUR thousand). Figures are rounded to the nearest thousand and totals may not sum due to rounding.

The fiscal year of Intershop Communications AG and its consolidated subsidiaries is the calendar year. The income statement has been prepared using the cost of sales method.

Estimates and assumptions

Preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and the accompanying notes. Estimates are based on past experience and other knowledge of transactions to be accounted for. Actual results may differ from these estimates. As a result, estimates and the assumptions on which they are based are regularly reviewed and assessed for their potential effects on the Company's financial reporting.

In particular, estimates are required to recognize and measure provisions for restructuring, legal costs and litigation risks, and guarantee provisions, as well as to assess the need for and measurement of impairment losses and valuation allowances.

Provisions for restructuring are recognized and measured on the basis of financial estimates and data available at the balance sheet date. Other provisions are recognized and measured on the basis of an estimate of the probability of a future outflow of economic benefits, as well as on the basis of historical data and the circumstances known at the balance sheet date. The actual obligation may differ from the amounts of the provisions.

Goodwill is tested for impairment using the test described in the section entitled "Impairment of assets."

Transition to IFRS reporting

In previous periods, the consolidated financial statements were prepared in accordance with United States Generally Accepted Accounting Principles ("U.S. GAAP"). The first-time adoption of IFRSs has resulted in the existing accounting policies and consolidation methods being adjusted to IFRSs.

The necessary disclosures relating to the transition from U.S. GAAP to IFRSs are presented in the reconciliation.

The effect of the transition from U.S. GAAP to IFRSs on the net assets, financial position, and results of operations is described in the reconciliation.

Basis of consolidation

In addition to the parent company, the basis of consolidation includes the following companies as of December 31, 2005:

- Intershop Communications, Inc., San Francisco, U.S.A.
- Intershop Communications Ventures GmbH, Jena, Germany
- Intershop Communications s. r. o., Prague, Czech Republic
- IS Nordic AB, Stockholm, Sweden
- Intershop Communications Australia Pty Ltd., Sydney, Australia

The following companies were deconsolidated in the course of 2005 and included in the consolidated financial statements until the date of deconsolidation:

- Intershop Communications Dubai LLC, Dubai, United Arab Emirates
- Intershop Communications K.K., Tokyo, Japan
- Intershop (UK) Ltd., London, United Kingdom

The following company was included in the consolidated financial statements for the first time in 2005:
- Intershop Communications s. r. o., Prague, Czech Republic

The following companies were deconsolidated in the course of 2004 and included in the consolidated financial statements up to the date of deconsolidation:
- Intershop Communications Hong Kong Co. Limited
- Intershop Communications Singapore Pte. Limited
- Intershop Communications Taiwan Co. Limited
- Intershop Communications Korea Co. Limited

Intershop Communications s. r. o., Prague, Czech Republic
The Company's subsidiary in Prague, Intershop Communications s.r.o., was formed in 2005 and entered in the local commercial register on September 7, 2005. The subsidiary was consolidated when the shares were acquired on August 16, 2005.
The cost of EUR 6,746 relates to the purchase price paid for the acquisition of the shelf company. The costs of EUR 2,030 directly attributable to the acquisition relate primarily to attorney fees. Cash of EUR 0 was used in connection with the acquisition, as the purchase price was paid from an existing bank deposit of EUR 6,746.
The company did not yet have any operating activities up to December 31, 2005.

IS Nordic AB, Stockholm, Sweden, and Intershop Communications Australia Pty Ltd., Sydney, Australia
The Company's subsidiary in Sweden, IS Nordic AB, and its subsidiary in Australia, Intershop Communications Australia Pty Ltd., have not had operating activities since fiscal year 2003.

Intershop Communications Dubai LLC, Dubai, United Arab Emirates
The Company's subsidiary in Dubai, Intershop Communications Dubai LLC, was liquidated and deconsolidated on March 13, 2005.

Intershop Communications K.K., Tokyo, Japan
The Company's subsidiary in Japan, Intershop Communications K.K., was liquidated and deconsolidated on May 13, 2005.

Intershop (UK) Ltd., London, United Kingdom
In December 2004, the Company took the decision to stop giving financial support to its subsidiary in the United Kingdom, Intershop (UK) Ltd. Its liquidation was resolved on January 14, 2005. The subsidiary was deconsolidated after the liquidation opening balance sheet was prepared as of September 30, 2005.

Intershop Communications Hong Kong Co. Limited
With effect from June 29, 2004, the Company disposed of its subsidiary Intershop Communications Hong Kong Co. Limited to the head of its operations in Asia, Mr. Felix Ko, by way of a management buyout. At this date, control over the operating activities passed to Mr. Felix Ko, with the result that Intershop Communications Hong Kong Co. Limited was deconsolidated as of this date. The shares in the company had not yet been transferred at the balance sheet date.

Intershop Communications Singapore Pte. Limited
With effect from June 29, 2004, the Company disposed of its subsidiary Intershop Communications Singapore Pte. Limited to the head of its operations in Asia, Mr. Felix Ko, by way of a management buyout. At this date, control over the operating activities passed to Mr. Felix Ko, with the result that Intershop Communications Singapore Pte. Limited was deconsolidated as of this date. The shares in the company had not yet been transferred at the balance sheet date.

Intershop Communications Taiwan Co. Limited
With effect from June 29, 2004, the Company disposed of its subsidiary Intershop Communications Taiwan Co. Limited to the head of its operations in Asia, Mr. Felix Ko, by way of a management buyout. At this date, control over the operating activities passed to Mr. Felix Ko, with the result that Intershop Communications Taiwan Co. Limited was deconsolidated as of this date. The shares in the company had not yet been transferred at the balance sheet date.

Intershop Communications Korea Co. Limited
With effect from June 29, 2004, the Company disposed of its subsidiary Intershop Communications Korea Co. Limited to the head of its operations in Asia, Mr. Felix Ko, by way of a management buyout. At this date, control over the operating activities passed to Mr. Felix Ko, with the result that Intershop Communications Korea Co. Limited was deconsolidated as of this date. The shares in the company had not yet been transferred at the balance sheet date.

The following list shows the subsidiaries of Intershop Communications AG and the Company's respective interest as of December 31, 2005:

	Interest in%	Currency	Nominal capital	Equity*	Net loss*
Intershop Communications, Inc,, San Francisco, USA	100	EUR	7,332,682	(114,150,230)	(4,941,495)
Intershop Communications Ventures GmbH, Jena	100	EUR	1,000,000	(2,076,289)	(102,733)
Intershop (UK) Ltd., London, United Kingdom	100	EUR	1,586	0	22,966,086
Intershop Communications S.a.r.l., Paris, France	100	EUR	300,000	0	0
IS Nordic AB, Stockholm, Sweden	100	EUR	11,437	39,318	10,737
Intershop Communications Hongkong Co. Ltd., Hong Kong, China	99,99	EUR	1,378	0	(742,881)
Intershop Communications Korea Co. Ltd., Seoul, Korea	99,98	EUR	50,940	0	347,100
Intershop Communications Taiwan, Taipeih, Taiwan	100	EUR	32,393	0	110,042
Intershop Communications Singapore Pte Ltd., Singapur	100	EUR	65,168	0	231,267
Intershop Communications Australia Pty Ltd., Sydney, Australia	100	EUR	238,278	(1,670,720)	(91,676)
Intershop Communications s.r.o., Prague, Czech Republic	100	EUR	6,746	(25,475)	(32,187)

** The above figures for equity and the net loss for the year are preliminary. The net profit figures for the year of the deconsolidated subsidiaries are primarily due to the derecognition of the liabilities to the parent company.*

Consolidation methods

The consolidated financial statements of Intershop Communications AG include the consolidated results of the Company and all its German and foreign subsidiaries over whose financial and operating policies Intershop Communications AG exercises direct or indirect control.

Subsidiaries

Acquisition accounting for companies acquired from third parties is performed at the date of acquisition using the purchase method in accordance with IFRS 3, Business Combinations. Under this method, the cost of the acquisition is compared with the Group's interest in the carrying amount of the equity of the company concerned. The difference between the cost of the acquisition and the Group's interest in the acquiree's equity is allocated to the acquirer's share of the fair value of the acquired assets, liabilities, and contingent liabilities of the acquiree at the time of acquisition. Any excess from acquisition accounting is recognized as purchased goodwill. Any negative difference is immediately recognized as an expense.

In subsequent periods, hidden reserves and liabilities realized at the time of initial consolidation are carried, written down, or reversed according to the treatment of the corresponding assets and liabilities. In subsequent periods, purchased goodwill is tested for impairment at least once a year, and if impaired, written down to the lower recoverable amount.

Foreign currency translation

Monetary items denominated in foreign currency in the local-currency single-entity financial statements of the consolidated companies are measured at the closing rate. Translation differences are recognized in income. Nonmonetary items denominated in foreign currency are measured at historical exchange rates.
The functional currency for it's the subsidiaries is the local currency of the country in which the subsidiary is based. The Company's functional currency is the euro. In accordance with IAS 21, The Effects of Changes in Foreign Exchange Rates, the financial statements of subsidiaries outside the euro zone are translated into euros using the modified closing rate method. Since from a financial, economic, and organizational perspective, the subsidiaries conduct their business independently, the functional currency is always the same as the company's local currency. Assets and liabilities are translated using the closing rate at the balance sheet date; income and expenses are translated at the average exchange rate for the year. The difference resulting from currency translation is taken directly to equity and reported separately in equity under other reserves (cumulative currency translation differences).

Transactions in foreign currencies are translated at the exchange rate prevailing at the date of each transaction. Differences in exchange rates between the date of a transaction denominated in a foreign currency and the date at which it is either settled or translated are recognized in the income statement and are shown in "other operating income" or "other operating expenses." Currency gains and losses were EUR 3,268 in 2004 and EUR-48,244 in 2005.

The following table shows the significant exchange rates used for foreign currency translation:

Country	Currency	Closing rate		Average rate for the year	
	1 Euro	**2004**	**2005**	**2004**	**2005**
United States	USD	1.36	1.18	1.24	1.25
United Kingdom	GBP	0.71	0.69	0.68	0.68
Czech Republic	CZK	30.51	29.00	31.95	29.96
Australia	AUD	1.75	1.62	1.69	1.64

Accounting Policies

The accounting policies are applied uniformly throughout the Intershop Group and to all periods reported in the consolidated financial statements.

Goodwill

In accordance with IFRS 3, goodwill resulting from consolidation is the excess of the cost of a business combination over the Group's interest in the fair value of the identifiable assets and liabilities of a subsidiary, associate, or joint venture at the date of acquisition.

Goodwill is recognized as an asset and tested for impairment at least once a year in accordance with IAS 36. Goodwill is tested for impairment on the basis of cash-generating units. An impairment loss is recognized if the recoverable amount of the cash-generating unit, which is the higher of net realizable value and value in use, is lower than its carrying amount.

Impairment losses are immediately recognized in the income statement and not reversed in subsequent periods.

At the balance sheet dates for 2004 and 2005, there were no impairment losses that had to be recognized.

Intangible assets

Purchased intangible assets are capitalized at cost. Intangible assets with finite useful lives are measured at cost less accumulated amortization and impairment losses. Intangible assets with indefinite useful lives, such as goodwill, are measured at cost less accumulated amortization and impairment losses (see Goodwill).

Software development costs

Development costs for newly developed products are capitalized at production cost in accordance with IAS 38 if a clear allocation of expenses is possible, and if both the technical feasibility and the marketability of the newly developed products is ensured. Capitalization of software development costs generally begins when the technological feasibility of the product is established; the Company defines this as the development of a prototype as well as the development of a beta version of the software. As the Company has consolidated its various product lines within the Enfinity Suite 6 for the first time and it was not possible to clearly allocate expenses to individual product lines in the past, software development costs will only be capitalized in the future if the production cost of the successor product can be clearly allocated.
Research costs may not be capitalized in accordance with IAS 38 and are therefore recognized directly as an expense in the income statement.

Property, plant, and equipment

Property, plant, and equipment is measured at cost less accumulated depreciation and impairment losses. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally ranging from three to five years. Leasehold improvements are depreciated on a straight-line basis over the shorter of the lease terms or their estimated useful lives. When items of property, plant, and equipment are decommissioned, sold, or abandoned, the gain or loss from the difference between the sale proceeds and the carrying amount is reported in "other operating income" or "other operating expenses."

Impairment of assets

For property, plant, and equipment and intangible assets with finite useful lives, an estimate is made at each balance sheet date to establish whether there are any indications that the assets in question may be impaired in accordance with IAS 36, Impairment of Assets.

If such indications exist, the recoverable amount of the asset is determined so that the impairment loss can be calculated. The recoverable amount is the higher of fair value less costs to sell and value in use. The fair value less costs to sell is defined as the amount that could be generated by the sale of an asset in an arm's length transaction between willing parties. The value in use is determined on the basis of discounted future cash flows using a market rate of interest before taxes that reflects the risks of the asset that are not yet included in the estimated future cash flows. If the recoverable amount of an asset is lower than its carrying amount, the asset must be written down to its recoverable amount. Impairment losses are recognized immediately in profit or loss. In 2005, the subsidiary in the United Kingdom recognized impairment losses in the amount of EUR 242 thousand, which were due to the adjustment of the subsidiary's balance sheet to its liquidation opening balance sheet.
No impairment losses were reported in 2004. In the case of reversals of impairment losses in a subsequent period, the carrying amount of the asset is adjusted to reflect the identified recoverable amount; however, the value of the asset may only be increased to the carrying amount that would have arisen if no impairment loss had previously been charged. Reversals of impairment losses must be recognized immediately in profit or loss. No such reversals were performed in 2004 and 2005.

The goodwill impairment test is to be performed on a cash generating unit. Goodwill includes software expertise. As it relates to software as a whole, no breakdown by different cash-generating units can be given. Goodwill is therefore tested for impairment at company level. As a first step, the fair value of the enterprise is compared with its carrying amount, whereby the fair value is derived from the Company's market capitalization. Only if the fair value is lower than the carrying amount is the need for goodwill to be written down determined in a second step. At the balance sheet dates for 2004 and 2005, there were no impairment losses requiring to be recognized. Impairment losses on goodwill are not reversed.

Leases

IAS 17 requires leases to be classified into financing leases and operating leases. Leases are classified as financing leases if the terms and conditions of the lease transfer substantially all risks and rewards incidental to ownership to the lessee. All other leases are classified as operating leases.

Financial instruments

Financial assets and financial liabilities, which include trade receivables and liabilities, cash and cash equivalents, restricted cash, and the convertible bond, are recognized in the balance sheet at the date when the Group becomes a party to the contractual provisions of the financial instrument.

Financial instruments are recognized at fair value on acquisition. Subsequent measurement depends on the classification of the financial instruments. Currently, Intershop's only financial instruments are trade receivables, which are recognized at amortized cost in accordance with IAS 39.

Trade receivables, other receivables and other assets

Trade receivables are recognized at the fair value of the recognized revenue or the consideration paid and are measured at amortized cost, net of any valuation allowances. Receivables from the sale of software licenses are recognized only when a contract has been signed with the customer, any right of return granted to the customer has expired, the software has been made available according to the contract, and it is more probable than not that the receivable will be collected.

Trade receivables are recognized at their principal amount, which equals fair value at the time of collection. Receivables with longer maturities (> 1 year) are discounted using market interest rates.

Other receivables and other assets are recognized at amortized cost. All identifiable risks of default are taken into account by deducting appropriate allowances.

The Company makes judgments as to its ability to collect outstanding receivables and recognizes allowances for the portion of receivables where collection becomes doubtful. Allowances are recognized based on a specific review of all significant outstanding invoices. For those invoices not specifically reviewed, allowances are recognized at differing rates, based on the age of the receivable. In determining these percentages, Intershop analyzes its historical collection experience and current economic trends. If the historical data the Company uses to calculate the allowances recognized for doubtful accounts does not reflect the future ability to collect outstanding receivables, additional allowances for doubtful accounts may be needed and the future results of operations could be materially affected.

Cash and cash equivalents

Cash and cash equivalents include cash on hand, checks, and unrestricted deposits with banks that have an original maturity of up to 90 days and are recognized at nominal value.

Restricted cash

Restricted cash is reported separately (see section entitled "Liquid Funds").

Stock option plans

Stock option plans allow employees to acquire shares in the Company. In accordance with IFRS 2, they are accounted for at the fair value of the options issued; they are recognized in employee-related expenses, with a corresponding increase in equity. See section entitled "Equity" for further details. Intershop has launched the following stock option plans (all information post 5:1 reverse stock split in 2002 and 3:1 reverse stock split in 2005; see section entitled "Equity"):

1997 Stock Option Plan

The Company had originally reserved 2,000,000 ordinary shares for issuance to employees, directors, and consultants under its 1997 Stock Option Plan (the 1997 Plan). The Supervisory Board may grant incentive or non-statutory stock options at prices not less than 100% or 85%, respectively, of the fair value as determined by the Supervisory Board at the grant date. Options vest ratably over periods determined by the Board, generally three years. The Management Board also has the authority to set exercise dates (no longer than ten years from the grant date), payment terms, and other provisions. The Company had the right of first refusal for all ordinary shares issued under the 1997 Plan should the holder intend to sell or otherwise transfer any of the shares. The Company's right of first refusal terminated at the effective date July 16, 1998, of the Company's initial public offering.

1999 Stock Option Plan

With effect from June 21, 1999, the Company adopted a new stock option plan (the 1999 Plan) for the issuance of shares to Management Board members, executives, and various employees. The options under the 1999 Plan vest ratably over a four-year period, beginning six months from the grant date; however, in accordance with the Aktiengesetz (German Stock Corporation Act), no options will be exercisable, even though a portion is vested, prior to the second anniversary of the grant date. The exercise price of the options is equal to 120% of the market price of the shares at the grant date, where the market price is determined to be the average closing price as quoted on the Prime Standard for the ten trading days prior to the grant date.

There are two pools of shares authorized under the 1999 Plan. There are 44,333 shares for grants of stock options to members of the Management Board and general managers of subsidiaries and 500,000 shares for grants of stock options to all other employees.

2001 Stock Option Plan

As of January 1, 2001, the Company adopted a new stock option plan (the 2001 Plan) for the issuance of shares to all employees. No options under this plan have been allocated to the Management Board. The options under the 2001 Plan vest ratably over a fifty-month period beginning from the grant date; however, in accordance with the Aktiengesetz, no options will be exercisable, even though a portion is vested, prior to the six months after the grant date. The exercise price of the options is the fair value at the grant date, defined as equivalent to the XETRA closing price on the Frankfurt Stock Exchange for voting shares of stock of the Company.

The Company has reserved 643,500 ordinary shares for issuance to employees under its 2001 Stock Option Plan.

Convertible bond

Convertible bonds are treated as compound financial instruments, consisting of a debt component and an equity component. The dept component is measured at the date of issue by discounting future payments using an appropriate standard market interest rate. The difference between the proceeds from the issue of the convertible bond and the fair value of the debt component represents the value of the embedded option to convert the liability into equity of the Group. The value of this option is included in the equity component. The issue costs are split between the equity and debt component of the convertible bond in relation to their relative carrying amounts at the date of issue. The portion allocated to equity is taken directly to equity. The interest expense for the debt component has been calculated using the standard market interest rate for comparable, nonconvertible debt instruments. The difference between the amount calculated in this way and the interest actually paid has been added to the carrying amount of the convertible bond. In subsequent periods, the debt component will be measured at amortized cost, using the effective interest rate method.

Other provisions and contingent liabilities

According to IAS 37, provisions are recognized for obligations to third parties if they have arisen from a past event, an outflow of resources is probable, and the amount can be reliably estimated. Provisions that do not lead to an outflow of resources in the subsequent year are recognized at the settlement value, discounted to the balance sheet date using market interest rates. The settlement value includes expected cost increases. Rights of recourse are not deducted from provisions.

Contingent liabilities are firstly possible obligations whose existence will be confirmed only by the occurrence or nonoccurrence of one or more uncertain future events not wholly within the control of the entity. Secondly, they are existing obligations where it is not probable that they will lead to an outflow of resources, or the outflow cannot be reliably quantified. According to IAS 37, contingent liabilities are not recognized in the balance sheet.

Trade accounts payable

Trade accounts payable do not bear interest and are recognized at their redemption amounts. Trade accounts payable are classified into current and noncurrent trade accounts payable. Trade accounts payable within one year are current liabilities, and trade accounts payable after one year are noncurrent liabilities.

Income and expense recognition

Intershop derives revenues from two primary sources: (1) software license revenues and (2) services revenues, which include maintenance, consulting, and education.

For software license arrangements that do not require significant modification or customization of the underlying software, the Company recognizes the services performed as revenue when: (1) it enters into a legally binding arrangement with a customer for the license of software; (2) it delivers the products or performs the services; (3) customer payment is deemed fixed or determinable and free of contingencies or significant uncertainties; and, (4) collection is probable. Substantially, all of the Company's license revenues are recognized in this manner.

Some of the Company's software arrangements additionally include implementation services sold separately under consulting engagement contracts. Revenues from these arrangements are generally accounted for separately from the license revenue. The more significant factors considered in determining whether the revenue should be accounted for separately include the nature of services (i.e., consideration of whether the services are essential to the functionality of the licensed product), degree of risk, availability of services from other vendors, timing of payments, and impact of milestones or acceptance criteria on the collectibility of the software license fee.

If an arrangement does not qualify for separate accounting of the license and service transactions, then license revenue is generally recognized together with the consulting services based on contract accounting using either the percentage-of-completion or completed-contract method as described below. Contract accounting is also applied to any arrangements: (1) that include milestones or customer-specific acceptance criteria, which may affect collection of the license fees; (2) where services include significant modification or customization of the software; (3) where significant consulting services are provided for in the contract without additional charges; or, (4) where the license payment is tied to the performance of consulting services.

Where several services are covered by a single agreement (so-called multi-component contracts) and contract accounting principles do not apply, the Company allocates total income to the individual elements of the transaction on the basis of their respective fair values. These fair values are determined using vendor-specific objective evidence ("VSOE"). Vendor-specific objective evidence of fair value for all elements of an arrangement is based upon the normal pricing and discounting practices for those products and services when sold separately. If the Company cannot objectively determine the fair value of any undelivered element included in bundled software and service arrangements, it defers revenue until all elements are delivered, services have been performed, or until fair value can objectively be determined. When VSOE of a license or other delivered element has not been established, the Company uses the residual method to record license revenue if VSOE of all undelivered elements is determinable. Under the residual method, VSOE of the undelivered elements is deferred and the remaining portion of the arrangement fee is allocated to the delivered elements and is recognized as revenue.

Intershop's license arrangements generally do not include acceptance provisions. However, if acceptance provisions exist within previously executed terms and conditions that are referenced in the current agreement, the Company then applies judgment in assessing the significance of the provision. If the Company determines that the likelihood of non-acceptance of these arrangements is remote, it then recognizes revenue once all of the criteria described above have been met. If such a determination cannot be made, revenue is recognized upon the earlier of receipt of written customer acceptance or expiration of the acceptance period.

Intershop assesses whether fees are fixed or determinable at the time of sale and recognizes revenue if all other revenue recognition requirements are met. The Company's standard payment terms are net 30 days; however, terms may vary based on the country in which the agreement is executed. Payments that extend beyond the country's standard payment terms are generally deemed not to be fixed or determinable, and thereby do not satisfy the required criteria for revenue recognition. Revenues for these agreements are deferred and recognized upon cash payment by the customer.

Revenue for consulting services is generally recognized as the services are performed. If there is a significant uncertainty about the project completion or receipt of payment for the consulting services, revenue is deferred until the uncertainty is sufficiently resolved.

The determination of the amount of revenues to be recognized is partly based upon the use of estimates. The Company estimates, for example, the percentage of completion on contracts with fixed or "not to exceed" fees on a monthly basis, utilizing hours incurred to date as a percentage of total estimated hours to complete the project. If Intershop does not have a sufficient basis to measure progress towards completion, revenue is recognized when the Company receives final acceptance from the customer. When total cost estimates exceed revenues, Intershop recognizes a provision for the estimated losses immediately, based upon an average fully burdened daily rate applicable to the consulting organization delivering the services.

The complexity of the estimation process and issues related to the assumptions, risks, and uncertainties inherent in the application of the percentage-of-completion method of accounting affect the amounts of revenues and related expenses reported in the Company's consolidated financial statements. A number of internal and external factors can affect Intershop's estimates, including costs for employees, utilization and efficiency variances, and specification and testing requirement changes.

Income taxes

In accordance with IAS 12, deferred tax assets and liabilities are recognized for all temporary differences between the tax base of an asset or liability and its carrying amount in the balance sheet, for tax credits, and for loss carryforwards. The Company uses the tax rate enacted as of the balance sheet date or future tax rates to calculate deferred tax assets and liabilities. The effect of changes in the tax rate on deferred taxes is recognized as of the effective date of the legal changes. Deferred tax assets are recognized only if it is probable that taxable profit will be available against which they can be utilized in the future.

Earnings per share

The basic net loss per share is determined in accordance with IAS 33, Earnings per Share for all periods presented. Basic net loss per share is computed using the weighted average number of outstanding shares of common shares.

The diluted net loss per share is computed using the weighted average number of ordinary shares outstanding and, in the case of dilution, the ordinary shares outstanding and the potential number of ordinary shares from options and warrants to purchase such shares using the treasury stock method. In the case of convertible securities the "if-converted method" is used. The options exercised that result in shares subject to repurchase have been excluded in computing the number of weighted average shares outstanding for basic earnings per share purposes. All potential ordinary shares have been excluded from the computation of the diluted net loss per share for 2004 and 2005 because the effect would be antidilutive.

Notes to the Individual Balance Sheet Items

(1) Intangible assets

EUR thousand	Software	Goodwill	Total
Costs of purchase			
Balance at January 1, 2004	**6,159**	**23,970**	**30,129**
Additions	75	0	75
Disposals	(64)	0	(64)
Additions to the basis of consolidation	0	0	0
Disposals to the basis of consolidation	0	0	0
Currency translation differences	0	0	0
Balance at December 31, 2004	**6,170**	**23,970**	**30,140**
Additions	9	0	9
Disposals	0	0	0
Additions to the basis of consolidation	0	0	0
Disposals to the basis of consolidation	0	0	0
Currency translation differences	180	0	180
Balance at December 31, 2005	**6,359**	**23,970**	**30,329**
Amortization, write-downs, and impairment losses			
Balance at January 1, 2004	**6,196**	**19,497**	**25,693**
Additions	73	0	73
Disposals	(153)	0	(153)
Additions to the basis of consolidation	0	0	0
Disposals to the basis of consolidation	0	0	0
Currency translation differences	0	0	0
Balance at December 31, 2004	**6,116**	**19,497**	**25,613**
Additions	41	0	41
Disposals	0	0	0
Additions to the basis of consolidation	0	0	0
Disposals to the basis of consolidation	0	0	0
Currency translation differences	180	0	180
Balance at December 31, 2005	**6,337**	**19,497**	**25,834**
Net carrying amount at December 31, 2004	**54**	**4,473**	**4,527**
Net carrying amount at December 31, 2005	**22**	**4,473**	**4,495**

(2) Property, plant, and equipment

EUR thousand	Computer equipment	Office and operating equipment	Leasehold improvements	Total
Costs of purchase				
Balance at January 1, 2004	**11,879**	**3,058**	**1,145**	**16,082**
Additions	193	5	34	232
Disposals	(1,455)	(192)	(48)	(1,695)
Disposals to the basis of consolidation	(504)	(117)	(378)	(999)
Currency translation differences	(109)	(7)	0	(116)
Balance at December 31, 2004	**10,004**	**2,747**	**753**	**13,504**
Additions	201	12	0	213
Disposals	(388)	(118)	0	(506)
Disposals to the basis of consolidation	(807)	(682)	(496)	(1,985)
Currency translation differences	63	14	6	83
Balance at December 31, 2005	**9,073**	**1,973**	**263**	**11,309**
Depreciation, write-downs, and impairment losses				
Balance at January 1, 2004	**11,513**	**2,620**	**694**	**14,827**
Additions	203	218	51	472
Disposals	(1,453)	(177)	(48)	(1,678)
Disposals to the basis of consolidation	(492)	(117)	(378)	(987)
Currency translation differences	0	0	0	0
Balance at December 31, 2004	**9,771**	**2,544**	**319**	**12,634**
Additions	179	141	263	583
Disposals	(388)	(117)	0	(505)
Disposals to the basis of consolidation	(807)	(654)	(496)	(1,957)
Currency translation differences	62	12	(3)	71
Balance at December 31, 2005	**8,817**	**1,926**	**83**	**10,826**
Net carrying amount at Dec. 31, 2004	**233**	**203**	**434**	**870**
Net carrying amount at Dec. 31, 2005	**256**	**47**	**180**	**483**

The “Disposals to the basis of consolidation” items show amounts incurred in connection with the deconsolidation of subsidiaries in the United Kingdom and Dubai.

(3) Financial investments

EUR thousand	Financial investments
Costs of purchase	
Balance at January 1, 2004	**0**
Additions	0
Disposals	0
Additions to the basis of consolidation	0
Disposals to the basis of consolidation	0
Currency translation differences	0
Balance at December 31, 2004	**0**
Additions	0
Disposals	0
Additions to the basis of consolidation	59
Currency translation differences	0
Balance at December 31, 2005	**59**
Impairment losses	
Balance at January 1, 2004	**0**
Additions	0
Disposals	0
Additions to the basis of consolidation	0
Disposals to the basis of consolidation	0
Currency translation differences	0
Balance at December 31, 2004	**0**
Additions	0
Disposals	0
Additions to the basis of consolidation	0
Currency translation differences	0
Balance at December 31, 2005	**0**
Net carrying amount at Dec. 31, 2004	**0**
Net carrying amount at Dec. 31, 2005	**59**

The financial investments relate to the deconsolidation of the subsidiary in the United Kingdom. This subsidiary is currently being liquidated. The value of EUR 59 thousand is the amount to which Intershop is entitled in accordance with the available liquidation opening balance sheet.

(4) Trade receivables

Trade receivables as of the balance sheet date include receivables from the sale of software licenses and the performance of services amounting to EUR 3,518 thousand (2004: EUR 2,257 thousand) and due within one year (current assets).

On average, settlement of receivables from the sale of licenses and the performance of services is due within 14 days of invoicing. Interest on receivables is not charged if they are settled within 30 days. Starting from the 30th day, the statutory rate of interest (8% above prime) is charged on outstanding amounts.

Allowances amounting to EUR 1,338 thousand have been recognized. This total includes allowances of EUR 1,056 thousand on trade receivables dating from 2001. The total allowance consists of specific and general bad-debt allowances. A specific allowance is recognized on all receivables that have been due for more than 90 days. For all other receivables, a general bad-debt allowance of 2% is recognized.

(5) Other receivables and other assets

Other receivables and other assets are composed of the following items:

in EUR thousand	December 31, 2005	December 31, 2004
Noncurrent assets		
Other noncurrent assets	**105**	432
Current assets		
Other receivables and other assets	**881**	836

Other noncurrent assets mainly comprise receivables from prepayments.

Other current receivables and current assets include the following items:

in EUR thousand	December 31, 2005	December 31, 2004
VAT and other tax receivables	71	174
Prepayments	210	67
Fixed-price projects	36	133
Receivables from employees and former employees	190	76
Other	374	386
	881	**836**

The fixed-price projects item amounting to EUR 36 thousand relates to an order with a total volume of EUR 40 thousand. All services were provided by the balance sheet date; however, final acceptance by the customer had not been performed as of the balance sheet date. As a result, EUR 36 thousand or 90 % of the order was recognized as revenue.

In the fiscal years ended December 31, 2005 and 2004, the Company charged write-downs on receivables from employees and former employees in the amount of EUR 527 thousand and EUR 640 thousand respectively.

(6) Cash and cash equivalents

Cash and cash equivalents include current and noncurrent restricted cash as well as current cash and cash equivalents.

in EUR thousand	December 31, 2005	December 31, 2004
Restricted cash – noncurrent	3,855	4,642
Restricted cash – current	2,355	2,112
	6,210	**6,754**
Cash and cash equivalents	7,279	1,632

A bank issued a guarantee to cover the lease payments on leased property in Jena, should the Company fail to fulfill its existing obligations under the lease. In this context, time deposits held by the Company were pledged (restricted cash). This rental guarantee provides for an annual reduction by way of a proportionate release of cash; however, this did not occur due to pending litigation (see section entitled “Litigation”). Current restricted cash includes the amounts for 2004 to 2006 that relate to the contractually agreed reduction. Noncurrent restricted cash includes the amounts from 2007 to the end of the lease period.

Restricted cash fell by EUR 0.5 million in fiscal year 2005, mainly due to the release of pledged cash and cash equivalents in connection with legal proceedings that were concluded in 2005.

Cash and cash equivalents include balances at various banks that are available at any time, as well as cash and checks.

(7) Equity

The development of Intershop Communications AG’s equity is shown in the statement of equity.

Subscribed capital

The subscribed capital amounts to EUR 17,662,052 and is divided into 17,662,052 no-par value bearer shares. The change of EUR 7,889,360 in the subscribed capital relates to a 3:1 share split, a cash capital increase from authorized capital, and a capital increase from conditional capital due to the exercise of conversion rights.

On April 4, 2005, Intershop announced in the Frankfurter Allgemeine Zeitung that Stephan Schambach informed the Company on March 30, 2005 that his share of the Company’s voting rights fell below 10 % as of January 25, 2005 and since then has amounted to 9.8%, i.e., more than 5% of the Company’s voting rights.
On July 22, 2005, Intershop announced in the Frankfurter Allgemeine Zeitung that Stephan Schambach informed the Company on July 20, 2005 that his share of the Company’s voting rights fell below 5% as of July 8, 2005 and amounts to 3.97%.

As of the balance sheet date, the Company was not informed of any equity interests of 5% or more than 5%.

Authorized capital

As of December 31, 2005, the Company had authorized capital of EUR 40,487,837. Under the Articles of Association of Intershop Communications AG, the Management Board is entitled, with the approval of the Supervisory Board, to increase the Company's share capital by issuing new ordinary shares as follows:

- By up to a total of EUR 30,835,337 against cash or noncash contributions up to December 11, 2007 (Authorized Capital I). When increasing the share capital, the Management Board is authorized to disapply the stockholders' subscription rights under certain conditions with the approval of the Supervisory Board. A cash capital increase including subscription rights was implemented in fiscal year 2005 from Authorized Capital I (see the section entitled "Capital increases in fiscal year 2005").
- By up to a total of EUR 9,652,500 against cash contributions while disapplying the stockholders' subscription rights on the basis of the resolution adopted by the Annual Stockholders' Meeting on June 6, 2002 (Authorized Capital II). The authorization of the Management Board applies until December 11, 2007. It was not exercised in fiscal year 2005.

Conditional capital

The Company's share capital was increased conditionally by up to EUR 25,418,317 in order to issue 25,418,317 shares. Due to capital reductions and the expiry of options, however, a maximum of 17,153,635 shares were issued from the conditional capital. The conditional capital is composed of the following:

- In order to grant employee stock options, EUR 8,165,000 (Conditional Capital I) is reserved for options in compliance with section 192(2) no. 3 of the Aktiengesetz (AktG – German Stock Corporation Act). Conditional Capital I is reserved for exercising the subscription rights under the 1999 stock option plan (see also the section entitled "1999 stock option plan"). Due to the 5:1 capital reduction resolved on October 30, 2002 that became legally effective on December 12, 2002, and the 3:1 capital reduction resolved on April 26, 2005 that became legally effective on June 28, 2005, the subscription rights arising from Conditional Capital I decreased at the same ratio, i.e., to 544,333 shares, in accordance with section 218 of the AktG.
- EUR 690,016 (Conditional Capital II) is reserved to implement the rights granted to all known holders of options to exchange shares in Intershop Communications, Inc., which was acquired by the Company in 1998. Due to the 5:1 capital reduction resolved on October 30, 2002 that became legally effective on December 12, 2002, and the 3:1 capital reduction resolved on April 26, 2005 that become legally effective on June 28, 2005, the subscription rights arising from Conditional Capital I decreased at the same ratio, i.e., to 46,001 shares, in accordance with section 218 of the AktG.
- Conditional Capital III was canceled by a resolution of the Annual Stockholders' Meeting dated July 7, 2004. The conditional capital increase was used to grant a right to convert Intershop Inc. shares into shares of the Company to Stephan Schambach and Burgess Jamieson; they exercised their conversion right in 2003.
- An amount totaling EUR 16,563,301 is available as Conditional Capital IV to issue 16,563,301 shares. A resolution of the Annual Stockholders' Meeting dated June 13, 2001 authorized the Management Board to grant, on one or several occasions up to May 31, 2006, bearer convertible bonds as well as bonds with warrants for a total of up to 21,449,703 no-par value bearer shares of the Company, under which the stockholders' subscription rights may be disapplied. 4,886,402 bonds from the convertible bond were converted in fiscal year 2005. Accordingly, Conditional Capital IV was reduced from EUR 21,449,703 to EUR 16,563,301 (see also the sections entitled "Capital increase 2004," "Capital increase 2005," and "Convertible bond").

Reverse stock split

A reverse stock split at a ratio of 5:1 was implemented in fiscal year 2002. On September 11, 2002, the Management Board of Intershop Communications AG announced that the Company's share capital has been depleted by 50% and convened a Special Stockholders' Meeting. This meeting on October 30, 2002 resolved a simplified capital reduction at a ratio of 5:1 to offset losses and other impairments. The capital reduction took effect on its entry in the commercial register on December 12, 2002 and was technically implemented at the close of trading on January 17, 2003. The Company's subscribed capital amounted to EUR 19,306,400 on December 31, 2002. The 5:1 reverse stock split of the Company's ordinary bearer shares admitted to trading was technically implemented on January 17, 2003 at the close of trading; the first trading date for the converted ordinary bearer shares was January 20, 2003.

A reverse stock split at a ratio of 3:1 was implemented in fiscal year 2005. The simplified capital reduction was resolved at the Annual Stockholders' Meeting on April 26, 2005 as a result of the depletion of half of the share capital that was established during the preparation of the 2004 single-entity financial statements of Intershop Communications AG. The reverse stock split was technically implemented on July 7, 2005 at the close of trading on the Frankfurt Stock Exchange. This meant that three existing ordinary bearer shares were exchanged for one new ordinary bearer share, as a result of which 112 shares were retired without compensation. The new shares began trading on a consolidated basis on July 8, 2005. Following the reverse stock split, the International Securities Identification Number (ISIN) of Intershop Communications AG's bearer shares changed from ISIN DE 0007472920 (equivalent to German Securities Identification Number – WKN 747292) to ISIN DE 000A0EPUH1 (equivalent to German Securities Identification Number – WKN A0EPUH). The ticker symbol of Intershop's shares in the Prime Standard was changed from ISH1 to ISH2.
As a result of the capital reduction, the capital reserve and other reserve items were adjusted and the share capital reduced accordingly.

Capital increases in fiscal year 2004

On March 5, 2004, Intershop announced that the Management Board and the Supervisory Board had resolved to implement a cash capital increase from authorized capital, while protecting the stockholders' subscription rights. Existing stockholders were able to subscribe for one new share per 11.5 existing Intershop ordinary bearer shares at a price of EUR 2.00. To this end, Intershop issued 1,916,113 new shares from authorized capital. The new shares were admitted to trading on April 6, 2004. As a result of the transaction, the Company received cash amounting to around EUR 3,832 thousand. The costs totaled EUR 74 thousand, while the proceeds from the issue were EUR 3,758 thousand.

On September 15, 2004, Intershop announced that the Management Board and the Supervisory Board had resolved to implement a cash capital increase from authorized capital while disapplying the stockholders' subscription rights. 1,600,000 shares were subscribed at a price EUR 1.00 per share, thus increasing the ordinary share capital to EUR 25,551,412. The new shares were admitted to trading on October 15, 2004. As a result of the transaction, Intershop received cash amounting to EUR 1,600 thousand; the costs totaled EUR 132 thousand. The Company thus generated proceeds from the issue of EUR 1,468 thousand.

Capital increases in fiscal year 2005

On September 28, 2005, Intershop announced that the Management Board and the Supervisory Board had resolved to implement a cash capital increase from Authorized Capital I, while protecting the stockholders' subscription rights. Existing stockholders were able to subscribe for one new share per two existing Intershop ordinary bearer shares at a price of EUR 1.00. To this end, Intershop issued 4,258,550 new shares from its authorized capital. The new shares took effect following the entry of the capital increase in the commercial register at the Gera Local Court on October 19, 2005, and were admitted to trading in the Prime Standard of the Frankfurt Stock Exchange on November 28, 2005. As a result of the transaction, Intershop received cash amounting to EUR 4,258 thousand; the costs totaled EUR 385 thousand. As a result of the transaction, the Company generated proceeds from the issue of EUR 3,873 thousand. The share capital increased from EUR 8,517,100 to EUR 12,775,650.

The first exercise period in which bonds arising from the zero-coupon convertible bond could be converted into shares of the Company was from November 1 to November 30, 2005. 4,886,402 bonds were converted. As a result of the exercise of the conversion option, the Company's share capital increased by EUR 4,886,402 from EUR 12,775,650 to EUR 17,662,052 due to the issue of 4,886,402 new shares from the Company's Contingent Capital IV (see the section on the convertible bond).

American Depositary Receipts (ADRs)

On January 14, 2004, Intershop announced that it would voluntarily delist from the Nasdaq National Market ("Nasdaq"), and gave notice to Citibank, N.A., the depositary for Intershop's ADRs (the "Depositary"), to terminate the ADR facility with effect from the close of trading on February 17, 2004. From this date, ADRs issued by Intershop were no longer tradable on Nasdaq. As of January 15, 2004, Intershop also terminated its F-6 registration statement with the U.S. Securities and Exchange Commission in respect of all 98,550,000 unissued ADRs in its ADR facility.

On January 27, 2004, Intershop announced that it had agreed with Citibank, N.A., to shorten the six-month period for holders of Intershop ADRs to surrender them in order to withdraw the underlying Intershop ordinary bearer shares ("surrender period"). In accordance with the termination provision, which was amended as of January 27, 2004, holders of Intershop ADRs were entitled to surrender their Intershop ADRs for withdrawal of the underlying Intershop ordinary bearer shares at any time up to February 27, 2004, i.e., ten days after conclusion of the surrender agreement on February 17, 2004 rather than six months as previously. Intershop ADR holders who chose not to surrender their Intershop ADRs for withdrawal of the underlying Intershop ordinary bearer shares received cash proceeds from the sale of such underlying Intershop ordinary bearer shares at the price obtained on the Frankfurt Stock Exchange. The Depositary then remitted the cash proceeds from the respective sale, net of any applicable fees, expenses, taxes, or charges levied by authorities, to the relevant Intershop ADR holders.

Intershop's issued and outstanding ADRs were deregistered with the SEC by submission of Form 15, with effect from June 26, 2004.

Stock option plans

Options issued under Intershop's stock option plans entitle employees to acquire shares of the Company (details on the stock option plans can be found in section under the heading "Stock option plans"). The lock-up period is six months for the 1997 and 2001 stock option plans, and two years for the 1999 stock option plan. Options expire if they are not exercised within 5 years (1999 and 2001 stock option plans) or 10 years (1997 stock option plan) from the grant date. If an employee leaves the Company, the options expire that are not exercisable up to the date on which the employee leaves; exercisable options may be exercised up to six months after the employee leaves the Company, but expire after this period. In addition, all options are withdrawn from employees if they leave the Company within the first six months of the grant date.

Option activity under the plans was as follows (thousands of euros, except per-share data).

Year ended December 31,	2005	2005	2004	2004
	Number of shares outstanding	Weighted average exercise price (EUR)	Number of shares outstanding	Weighted average exercise price (EUR)
Outstanding at beginning of period	523	120.60	685	109.50
Granted	46	2.25	7	6.03
Exercised	0	0	(3)	4.95
Forfeited	(116)	422.14	(165)	37.35
Outstanding at end of period	**453**	**18.38**	**523**	**120.60**
Exercisable options at end of period	297	24.48	324	185.43
Weighted average fair market valueof options granted during the year	46	16.23	7	3.78

The following table summarizes information with respect to the stock options outstanding on December 31, 2005:

Range of exercise Price	Number of options outstanding (EUR thousand)	Weighted average remaining contractual life (in years)	Weighted average exercise price (EUR)	Number exercisable on December 31, 2005 (EUR thousand)	Weighted average exercise price (EUR)
0.01 – 17.99	282	6.4	6.33	138	7.79
18.00 – 20.99	39	5.7	18.12	35	18.12
21.00 – 50.99	80	4.7	23.92	74	23.92
51.00 – 149.99	50	1.0	64.63	48	64.74
150.00 – 2,274.12	2	2.3	318.92	2	316.88
	453	**5.4**	**18.38**	**297**	**24.48**

The values of the options were calculated at the grant date using the Black-Scholes option pricing model on the basis of the following assumptions:

		Bandwidth from/to	
Expected term (in years)	in years	3.29	4.03
Risk-free interest rate (in%)	in%	3.00	3.85
Volatility (in%)	in%	79.00	109.78
Dividend yield	in%	0.00	0.00
Exercise price	in euros	3.00	7.65
Market price	in euros	2.79	7.65
Option value	in euros	1.73	4.62

Volatility was determined by calculating the average historical volatility of the Company's share price in the past 3 years.

In accordance with IFRS 2.53, only options that were granted after November 7, 2002 and were not exercisable before January 1, 2005 are recognized, as well as all options granted in 2004 and 2005.

In fiscal year 2005, the Company recognized expenses of EUR 73,485 relating to the stock option plans. These expenses amounted to EUR 144,648 in fiscal year 2004.

The 1997 Plan allows for the issuance of options that are immediately exercisable through execution of a restricted stock purchase agreement. Shares purchased subject to a restricted stock purchase agreement generally vest over three years. As of December 31, 2005, no shares of common stock issued and outstanding were unvested and subject to repurchase by the Company. All shares that were exercised early are held by a trustee on behalf of the employee. In the event that an employee leaves the Company with unvested shares, the Company repurchases the unvested shares from the employee at a price equal to the original issuance price and sells the shares in the open market, with the proceeds of the sale being contributed to the Company.

(7.1) Capital reserve

The capital reserve must be released due to the simplified capital reduction. The capital reserve only contains the expense from the stock options.

(7.2) Other reserves

Other reserves include the IFRS conversion reserve, reserves from cumulative gains/losses, and cumulative currency translation differences. The IFRS conversion reserve includes the expense from stock options that related to the first-time adoption of IFRSs. The reserve from cumulative currency translation differences shows the differences that result from the translation of the financial statements of subsidiaries into euros.

(7.3) Treasury stock

In 2004, the Company borrowed 20,000 own shares for a total price of EUR 40,000. 9,600 shares were issued at a price of EUR 1.65 under the employee stock option plan. The corresponding number of borrowed own shares were made available to cover this. In 2004, the Company returned 10,000 shares with a total value of EUR 20,000 to the lender. It held 400 treasury shares as of December 31, 2004. In 2005, the remaining 10,000 shares with a total value of EUR 20,000 were returned to the lender. 9,600 shares relate to old employee stock option plans whose shares are held in trust. 400 shares were taken from treasury shares. As a result, the Company did not hold any treasury shares as of the balance sheet date.

Financial liabilities

Financial liabilities relate exclusively to the liability from the convertible bond.

(8) Convertible bond liabilities

On November 24, 2004, Intershop announced its intention to issue a zero-coupon convertible bond with a total volume of up to EUR 20 million, as authorized by the resolution of the Annual Stockholders' Meeting on June 13, 2001, which created conditional capital of up to EUR 21,449,703 in order to allow the grant of conversion rights to holders of the bonds.
The zero-coupon convertible bond has a maturity date of December 14, 2008 and is composed of

individual bonds with a nominal value of EUR 1 each. The principal features of the zero-coupon convertible bond are the repayment amount of EUR 1.46 per bond at maturity, if conversion has not taken place, corresponding to an effective interest rate of 10% p.a., and the right to convert into bearer voting ordinary shares of the Company during specified exercise periods (starting in November 2005). The conversion price on each occasion will be EUR 1.00, irrespective of any capital reductions. Automatic conversion will take place if the share price exceeds EUR 5.00 on ten consecutive trading days at any time after January 1, 2006. As collateral, Intershop will furnish a first-ranking lien on its worldwide copyright to the Enfinity Software.
Stockholders were granted an indirect right to subscribe at a ratio of 1.3:1 in the period from November 29 to December 14, 2004; they also received the right to subscribe for additional bonds. However, the minimum amount of EUR 5 million required for the issue of the convertible bond to proceed was not achieved during the subscription period. Additional bonds were offered to investors in the form of a private placement. On January 26, 2005, Intershop announced that the convertible bond had been successfully placed. Bonds arising from the convertible bond with a value of EUR 11,331,000 were subscribed.

The income from the issue of the convertible bond was divided into a debt and an equity component. In the first conversion window (November 1 to November 30, 2005), 4,886,402 convertible bonds were converted into shares of the Company; this corresponds to a proportion of 43.12%. A standard market interest rate of 15% was used for the calculation. The interest rate used corresponds to a standard market rate for debt financing for four-year maturities and a credit rating that is comparable with that of Intershop.
The effective interest rate is 18.026% per year.

1.	Subscribed bonds	11,331
	Costs of placing the convertible bond	(1,353)
	Actual payment amount	**9,978**
2.	Actual payment amount	9,978
	Debt component before conversion	(8,526)
	Equity component	**1,452**
3.	Discounted payment amount	9,682
	Costs of placing the convertible bond	(1,353)
	Proportionate costs of placement for equity component	197
	Debt component before conversion	**8,526**
	plus interest on the convertible bond	1,322
	Amortized cost before conversion	**9,848**
4.	Amortized cost before conversion	9,848
	Converted portion relating to amortized cost (43.12%)	(4,246)
	Rounding difference for balancing	(2)
	Debt component after conversion	**5,600**
5.	Converted bonds	4,886
	Converted portion relating to amortized cost (43.12%)	(4,246)
	Change in equity component after conversion	**640**

The discounted payment amount is the present value of the actual payments to be made at the end of the term of the convertible bond, excluding conversion.
In accordance with IAS 32, interest on the convertible bond may not be reversed retrospectively. The recognized interest expense may not be offset retrospectively.

(9) Trade accounts payable

Trade accounts payable comprise unsettled liabilities relating to the delivery of goods and services. This item amounted to EUR 3,817 thousand in fiscal year 2005, compared with EUR 2,929 thousand in 2004.

(10) Other current liabilities

Other current liabilities comprise the following items:

in EUR thousand	**December 31, 2005**	**December 31, 2004**
Other liabilities relating to social security benefits	246	265
Liabilities to employees	627	554
Other VAT and wage tax liabilities	478	225
Liabilities to the Occupational Health and Safety Agency	71	84
Miscellaneous other liabilities	116	172
	1,538	**1,300**

Liabilities to employees mainly include liabilities from commissions and performance-related compensation.

(11) Deferred revenue

Deferred revenue relates to prepayments by customers, primarily in the form of revenue from maintenance agreements. Deferred revenue is reversed and revenue is recognized in the period in which the service was provided by Intershop.
In the case of current deferred revenue, reversal and recognition take place within a year.

(12) Provisions for restructuring

Provisions for restructuring developed as follows:

in EUR thousand	Noncurrent provisions	Current provisions	Total
Balance at January 1, 2005	**186**	**1,591**	**1,777**
Additions	0	0	0
Utilization	0	(247)	(247)
Reversal	0	(787)	(787)
Reclassification	(190)	190	0
Currency adjustments	21	43	64
Balance at December 31, 2005	**17**	**790**	**807**

For details on the recognition of the provisions for restructuring, see section entitled "Restructuring expenses."

(13) Other provisions

Other provisions are current provisions. The anticipated cash outflows are expected within a year.

The following table shows the development of other provisions:

in EUR thousand	Legal costs and litigation risks	Staff	Other	Total
Balance at January 1, 2005	**3,176**	**180**	**608**	**3,964**
Additions	192	210	347	749
Utilization	(2,678)	(189)	(342)	(3,209)
Reversal	(442)	0	(39)	(481)
Changes to the basis of consolidation	0	0	(231)	(231)
Currency adjustments	29	15	4	48
Balance at December 31, 2005	**277**	**216**	**347**	**840**

Provisions for legal costs and litigation risks as of January 1, 2005 include provisions for the cost of the settlement with the plaintiffs in the class-action lawsuit in the United States amounting to EUR 2.3 million. Please refer to section entitled "Litigation" for details of litigation risks.

Employee-related provisions mainly include provisions for vacation entitlements.

Miscellaneous other provisions relate primarily to provisions for the Annual Stockholders' Meeting and guarantee provisions. The "Changes to the basis of consolidation" item shows the amounts relating to the deconsolidation of the Company's subsidiaries in the United Kingdom and Dubai.

Notes to the Individual Income Statement Items

(14) Revenues

Revenues from services, maintenance, and other are composed of the following items:

in EUR thousand	2005	2004
Maintenance	6,963	6,679
Consulting	6,622	7,530
Training	258	254
Other revenues	67	539
	13,910	**15,002**

Other revenues primarily include income (in excess of the Company's own rental costs) from the subletting of office space. In fiscal year 2004, this mainly contains income from the office space sublet by the subsidiary in the United Kingdom, which includes the rents actually oncharged.

(15) Cost of revenues

The cost of revenues relating to licenses includes software license fees paid to third parties.

The cost of revenues relating to services, maintenance, and other are composed of the following items:

in EUR thousand	2005	2004
Maintenance	2,776	2,702
Consulting	5,678	5,641
Training	318	330
	8,772	**8,673**

(16) Research and development expenses

Research and development expenses comprise all expenses attributable to R&D activities; personnel expenses account for the majority of this item. The 33.6% fall in research and development expenses as against 2004 from EUR 4,179 thousand to EUR 2,774 thousand relates mainly to the reduction in the headcount.

(17) Sales and marketing expenses

Sales and marketing expenses primarily include personnel expenses for sales and marketing staff, sales commissions, advertising, and exhibition costs for CeBIT 2005 in Hanover. Sales and marketing expenses increased by 16.0% compared with 2004 to EUR 5,842 thousand, due to the recruitment of new sales staff and higher advertising expenses.

(18) General and administrative expenses

General and administrative expenses mainly include personnel and non-personnel expenses as well as depreciation and amortization that relates to administration. In fiscal year 2004, general and administrative expenses also included extraordinary expenses amounting to EUR 2.3 million relating to the settlement of the class-action lawsuit in the United States. General and administrative expenses fell by 52.6% as against 2004 from EUR 8,545 thousand to EUR 4,049 thousand. Apart from the extraordinary expenses in 2004 relating to the settlement of the class-action lawsuit in the United States, this is due to efficiency gains in operating areas, the fall in depreciation and amortization, and to the reduction in the workforce.

(19) Restructuring costs

In 2002, the Company adopted measures to reduce its workforce and to consolidate existing facilities, among other things. These measures were aimed at adapting the Company’s cost structure to reflect changing market conditions and accelerating its path to profitability. Among other things, in 2003 the Company transferred the majority of its European sales activities outside Germany to local distributors. In 2004, its sales activities in Asia were also transferred to local distributors.

The Company’s restructuring measures were almost fully completed in 2005.

The following table gives an overview of the restructuring expenses for fiscal year 2005 and provisions for restructuring as of December 31, 2005 (in EUR thousand):

	Employee-related charges	Facility-related charges	Total
Accrued restructuring costs as of January 1, 2004	224	2,433	2,657
Restructuring charges for the year	65	341	406
Cash payments	(84)	(1,158)	(1,242)
Currency adjustments	(10)	(34)	(44)
Accrued restructuring costs as of December 31, 2004	**195**	**1,582**	**1,777**
Restructuring charges for the year	(150)	(637)	(787)
Cash payments	(58)	(189)	(247)
Currency adjustments	13	51	64
Accrued restructuring costs as of December 31, 2005	**0**	**807**	**807**

Employee-related charges

The restructuring measures relating to the reduction of the workforce were concluded in the year under review. The provisions mainly comprise expected future payments relating to the termination of employment contracts, including severance payments, social security contributions, and legal costs.

Facility-related charges

In fiscal year 2005, the Intershop Group reversed EUR 637 thousand from the provision for restructuring in connection with the consolidation of facilities. In the previous years, the provision mainly included the expected future payments for existing lease commitments for property no longer in use, net of sublease income. The determination of facility-related charges is based on leases entered into that do not cover the charges on the one hand, and on assumptions with regard to the possibility of subletting and the expected period of time until the vacant space is sublet. This period varies between six and twelve months according to the space in question.

The sublease income was estimated on the basis of the contractual agreements in force as of the date the financial statements were prepared.

The landlord of the Group headquarters in Jena gave notice of termination of the lease on the building in November 2004. The reasons for termination were rent reductions and the set-off of contractual penalties that the Company claimed against the rent payable in 2003 and 2004. Intershop considers that the termination is unjustified because the Company was entitled to make deductions from the rent payable. Nonetheless, the Company has returned parts of the leased property which are no longer required and vacant to the landlord. The landlord then served notice to vacate the property in 2005, although it is currently no longer pursuing this action, and has applied to the court for the proceedings to be suspended. Nevertheless, the litigation regarding the rental payments is being continued. Regardless of the suspension of the termination proceedings, the Company cannot rule out a termination or variation of the lease in 2006, irrespective of its opinion that the notice to terminate has no legal justification. The Company believes that any payments due resulting from the termination or variation of the lease will not differ significantly from the amount of the liabilities already recognized. For this reason we have retained the basis of measurement described above. However, it reflects the fact that the landlord has entered into new leases with two tenants of returned parts of the leased property; as a result, the Company reversed the provisions attributable to these parts.

(20) Other operating income

Other operating income is composed of the following items:

in EUR thousand	2005	2004
Income from deconsolidation	438	707
Income from currency translation gains	5	38
Gain on disposal of noncurrent assets	38	36
Miscellaneous	457	159
	938	**940**

In fiscal year 2005, income from deconsolidation includes income generated by the deconsolidation of the subsidiaries in the United Kingdom, Dubai, and Japan. In fiscal year 2004, this item includes income recorded from the deconsolidation of the subsidiaries in Hong Kong, Singapore, Taiwan, and Korea (see section entitled "Basis of consolidation").

Miscellaneous other operating income mainly includes income relating to pending formerly legal proceedings.

(21) Other operating expenses

Other operating expenses relate to the following items:

in EUR thousand	2005	2004
Currency translation losses	53	35
Other taxes from previous years	0	115
	53	**150**

(22) Interest income

Interest income primarily includes interest on bank balances.

(23) Interest expense

Interest expense is composed of the following items:

in EUR thousand	2005	2004
Interest on the convertible bond	1,322	0
Other interest expense	43	271
	1,365	**271**

The interest on the convertible bond was determined using the effective interest rate method. The effective interest rate is 18.026%. (see the further details on the convertible bond in section entitled "Financial liabilities").

In 2004, other interest expenses included interest provisions for pending legal proceedings.

(24) Income taxes

The Company recognizes and measures income taxes using the balance sheet liability method in accordance with IAS 12. A corporate income tax rate of 25% (previous year: 25%) plus the solidarity surcharge of 5.5% (previous year: 5.5%), as well as an effective trade tax rate of 12.65% (previous year: 11.72%), were used to calculate the deferred taxes of the German companies as of December 31, 2005. The change in the effective trade tax rate is due to changes in the relevant trade tax multipliers.

The Group's income taxes are broken down as follows (in EUR thousand):

	Dec. 31, 2005	Dec. 31, 2004
Current taxes		
Abroad	3	0
Germany	0	23
Deferred taxes		
Abroad	0	0
Germany	0	0
Total	**3**	**23**

The Group tax rate of 39.03% applicable in fiscal year 2005 (previous year: 38.10%) was multiplied by IFRS earnings before taxes to calculate the expected tax income.

The tax rate reconciliation as of December 31, 2005, contains the following details (in thousands of euros):

Year ended December 31,	2005	2004
IFRS pretax income	(3,367)	(8,898)
Corporate tax rate	39.03%	38.10%
Expected income tax expense	(1,314)	(3,390)
Effects of prior years	(768)	29,413
Increase of valuation allowance	(6,702)	(22,509)
Foreign tax rate differentials and change in tax rates	2,566	1,246
Effects of currency translation adjustments	5,074	(3,329)
Effects of non-deductible expenses and changes of permanent differences	802	94
Effects of changes in basis of consolidation and others	345	(1,502)
Income taxes	3	23

The components of the deferred tax asset were as follows (in thousands of euros):

Year ended December 31,	2005	2004
Net operating loss carryforwards	192,309	185,112
Other	573	923
Deferred tax assets	**192,882**	**186,035**
Deferred tax liabilities	**425**	**280**
Valuation allowance	(192,457)	(185,755)
Net deferred tax assets	-	-

As of December 31, 2005, there are no other deferred tax assets arising from temporary differences in provisions and the convertible bond. Deferred tax liabilities result from the measurement of receivables and advance payments received.

A valuation allowance has been recorded for the entire deferred tax assets for all periods through December 31, 2005 as a result of uncertainties regarding the realization of the assets due to the limited operating history of the Company and its lack of profitability as of December 31, 2005.

For the year ended December 31, 2005, the Company had net loss carryforwards for tax reporting purposes in various tax jurisdictions as follows (in thousands of euros):

US Federal	112,425
US State	34,431
German corporate income tax	388,424
German municipal trade tax	380,701
Other	4,648

US federal and state net operating loss carryforwards expire in various periods through 2021. The German net operating loss carryforwards relate to corporate income tax and municipal trade tax and carry forward indefinitely. The US Tax Reform Act of 1986 and German tax laws contain provisions that may limit the net operating loss and tax credit carryforwards to be used in any given year upon the occurrence of certain events, including a significant change in ownership interest.

(25) Earnings per share

The calculation of basic and diluted earnings per share is based on the following data:

in EUR thousand	2005	2004
Basis for calculating basic earnings per share (consolidated net loss for the year)	(3,370)	(8,921)
Dilutive effect of potential ordinary shares: interest on the convertible bond	1,322	0
Basis for calculating diluted earnings per share	**(2,048)**	**(8,921)**

The number of shares is calculated as follows:

in EUR thousand	2005	2004
Weighted average number of ordinary shares used to calculate basic earnings per share	9,759	15,584
Dilutive effect of potential ordinary shares: convertible bond	9,408	0
Weighted average number of ordinary shares used to calculate diluted earnings per share	**19,167**	**15,584**

A reverse share split at a ratio of 3:1 was implemented in fiscal year 2005 (see section entitled "Equity"). In accordance with IAS 33.64, this was adjusted retrospectively when the number of shares was calculated in fiscal year 2004.

	2005	2004
Calculation of earnings per share (basic)		
Consolidated net loss for the year (in EUR thousand)	(3,370)	(8,921)
Weighted average number of shares (basic)	9,759	15,584
Earnings per share (basic) (in EUR)	**(0.35)**	**(0.57)**
Calculation of earnings per share (diluted)		
Basis for calculating diluted earnings per share	(2,048)	(8,921)
Weighted average number of shares (diluted)	19,167	15,584
Earnings per share (diluted) (in EUR)	(0.11)	(0.57)
Adjustment of earnings per share (diluted) (in EUR)	**(0.35)**	**(0.57)**

As the diluted earnings reduce the loss per share, an adjustment is made to the amount of basic earnings per share (antidilutive effect) in accordance with IAS 33 paragraph 43.

Notes to the Statement of Cash Flows

Cash comprises exclusively the cash and cash equivalents reported in the balance sheet. Restricted cash was not included.

In the statement of cash flows, cash flow are classified into net cash provided by/used in operating, investing, and financing activities.

Cash flows from operating activities are calculated on the basis of earnings before tax, adjusted for noncash income and expenses, and of the changes in operating assets and liabilities compared with last year's balance sheet.
Net cash used in operating activities increased from EUR 5,446 thousand in fiscal year 2004 to EUR 8,419 thousand in 2005. This is mainly due to negative changes in liabilities and provisions (EUR -2.975 thousand; 2004: EUR 2,024 thousand) and in deferred revenue (EUR -2,450 thousand; 2004: EUR -308 thousand). Net cash used in operating activities includes the payment relating to the settlement of the

class-action lawsuit in the United States (EUR 2.3 million). The financial result item which is adjusted for interest paid and received relates primarily to interest on the convertible bond.

Net cash provided by investing activities amounts to EUR 365 thousand and is largely due to the change in restricted cash.

Net cash provided by financing activities increased from EUR 5,221 thousand in the previous year to EUR 13,851 thousand. This positive figure relates to the issue of the convertible bond and the cash capital increase.

The changes in the balance sheet items used to determine the cash flow statement are not immediately evident from the balance sheet because effects from currency translation and from changes to the basis of consolidation do not impact cash and are eliminated.

Other Disclosures

Segment reporting

Segment reporting as of December 31, 2005

in EUR thousand	Germany	U.S.A.	Rest of the world	Consolidation	Group
Revenues from external customers					
Licenses	2,636	1,246	0	0	3,882
Consulting and training	6,346	534	0	0	6,880
Maintenance	5,583	1,337	43	0	6,963
Others	67	0	0	0	67
Total revenues from external customers	14,632	3,117	43	0	17,792
Intersegment revenues	57	0	0	(57)	0
Total revenues	14,689	3,117	43	(57)	17,792
Net profit/loss for the period	(27,739)	(4,941)	29,382	(72)	(3,370)
Net profit/loss for the period (adjusted)	(4,970)	1,398	222	(20)	(3,370)
Assets	22,301	662	67	0	23,030
Liabilities	13,736	1,021	11	(10)	14,758
Depreciation and amortization	362	14	242	0	618
Acquisitions of noncurrent assets	219	3	0	0	222
Noncash income	1,075	154	438	0	1,667
Noncash expenses	1,514	0	0	0	1,514

Segment reporting as of December 31, 2004

in EUR thousand	Germany	U.S.A	Rest of the world	Consolidation	Group
Revenues from external customers					
Licenses	1,830	646	90	0	2,566
Consulting and training	6,619	1,151	15	0	7,785
Maintenance	5,363	1,238	78	0	6,679
Others	206	0	332	0	538
Total revenues from external customers	14,018	3,035	515	0	17,568
Intersegment revenues	618	0	0	(618)	0
Total revenues	14,636	3,035	515	(618)	17,568
Net profit/loss for the period	(19,765)	(5,468)	16,332	(20)	(8,921)
Net profit/loss for the period (adjusted)	(8,287)	256	(869)	(21)	(8,921)
Assets	15,151	1,151	1,006	0	17,308
Liabilities	11,949	2,149	581	(26)	14,653
Depreciation and amortization	349	24	83	0	456
Acquisitions of noncurrent assets	292	13	0	0	305
Noncash income	0	0	679	0	679
Noncash expenses	2,962	0	0	0	2,962

The segment reporting is prepared in accordance with IAS 14 (Segment Reporting). Segmentation reflects the Intershop Group's internal management and reporting. The Company has two direct sales units: Germany and the United States.

The regions are broken down as follows:

Regions in 2005:
The "Germany" segment comprises the Germany sales unit including direct sales for Central Europe (Germany, Austria, Switzerland) as well as direct revenues from distributors in Denmark, Sweden, Norway, the Benelux countries, France, the United Kingdom, and Italy. The proportion of direct revenues from partners was less than 10% in 2005. The "U.S.A." segment comprises the U.S.A. sales unit including direct sales for North America. The "Rest of the world" segment includes the sales unit in Prague, the Czech Republic, which was established as a subsidiary in August 2005, as well as the subsidiaries in the United Kingdom, Japan, and Dubai that were deconsolidated in 2005. The "Consolidation" segment includes all transactions within the individual segments.

Regions in 2004:
The "Germany" segment comprises the Germany sales unit including direct sales for Central Europe (Germany, Austria, Switzerland). The proportion of direct revenues from distributors was less than 10% in 2004. The "U.S.A." segment comprises the U.S.A. sales unit including direct sales for North America. The "Rest of the world" segment includes the direct sales units in Northern Europe, the United Kingdom, Asia, and Australia. These were transferred to independent distributors in 2004. The "Consolidation" segment includes all transactions within the individual segments.

Notes to the content of the individual line items:

- Revenues from external customers represent revenues from the regions with third parties outside the Group.
- Intersegment revenues include revenues from intersegment relationships.
- The net profit/loss for the period (adjusted) is arrived at as follows: The net profit/loss for the period was adjusted for interest income and expense between group companies and income and expense from deconsolidation.
- The “net profit/loss for the period” segment variable is the consolidated net profit or loss as reported in the income statement.
- Segment assets are composed of noncurrent and current assets, while segment liabilities comprise noncurrent and current liabilities.
- Depreciation and amortization relates to segment assets allocated to the individual regions.
- Acquisitions of noncurrent assets relate to investments in tangible and intangible assets in the respective reporting period.
- Noncash income includes the reversal of provisions for restructuring and provisions for legal and litigation costs, as well as income from deconsolidation. Noncash expenses include interest on the convertible bond and provisions for legal and litigation costs.

The secondary segment reporting for 2004 and 2005 is as follows:

Segment reporting as of December 31, 2005

in EUR thousand		Licenses	Consulting/ training	Maintenance	Other	Total
Revenues						
	Germany	2,685	6,354	5,583	67	14,689
	U.S.A.	1,246	534	1,337	0	3,117
	Rest of the world	0	0	43	0	43
	Consolidation	(49)	(8)	0	0	(57)
	Total revenues	3,882	6,880	6,963	67	17,792
Assets		10,364	7,830	4,836	0	23,030
Acquisitions of noncurrent assets		112	77	33	0	222

Segment reporting as of December 31, 2004

in EUR thousand		Licenses	Consulting/ training	Maintenance	Other	Total
Revenues						
	Germany	2,007	7,060	5,363	206	14,636
	U.S.A.	646	1,151	1,238		3,035
	Rest of the world	90	15	78	332	515
	Consolidation	(177)	(441)	0	0	(618)
	Total revenues	2,566	7,785	6,679	538	17,568
Assets		8,135	5,365	3,808	0	17,308
Acquisitions of noncurrent assets		158	89	58	0	305

Operating leases

Certain facilities, office, and operating equipment are leased under operating leases. The minimum long-term lease payments reported in previous years' annual reports related mainly to the rental obligations for the headquarters building in Jena. In November 2004, the landlord terminated this long-term lease, due to run until 2013. The Company is of the opinion, however, that the termination is invalid. Nonetheless, the termination and notice to vacate served by the landlord give rise to a certain probability that the Company's occupation of its business premises will cease at the end of 2006. On the basis of this opinion, future minimum annual lease payments as of December 31, 2005 are as follows (in EUR thousand):

As of December 31	
2006	1,909
2007	161
2008	90
Total	**2,160**

In the event that the Company's opinion that the termination is legally invalid is upheld, future minimum annual lease payments as of December 31, 2005 are as follows (in EUR thousand):

As of December 31	
2006	2,418
2007	2,328
2008	2,257
2009	2,177
2010	2,177
Subsequent years	6,228
Total	**17,585**

Rent expense in 2004 and 2005 amounted to EUR 2.8 million and EUR 1.9 million, respectively.

Rent expense for 2004 and 2005 excludes any facility-related restructuring costs discussed in Note "Restructuring Costs". Rental income of EUR 0.5 million and EUR 1.9 million was received in 2005 and 2004 respectively and was offset against of rent expense, with the exception of EUR 0.03 million in 2005 and EUR 0.4 million in 2004.

Litigation

The Company is a defendant in various legal proceedings arising from the normal course of business. A negative ruling in any such legal dispute, or in several or all such disputes, could have a material adverse effect on the Company's results of operations. The Company recognizes all legal costs associated with loss contingency as an expense as they are incurred.

The Company is a defendant in a consolidated class-action lawsuit brought by shareholders in the United States. At the beginning of 2001, several securities class-action lawsuits were filed in the U.S. against Intershop Communications AG, Management Board members, several other executives, and the underwriting banks of the Company's IPO in September 2000. The plaintiffs alleged that the defendants made false statements about material points and omitted material facts when presenting the Company's business development, and sought an unspecified amount of damages. The Management Board is convinced that these allegations are unjustified and has vigorously defended itself against them. However, the Company decided to negotiate a settlement with the plaintiffs in respect of their claims. Such a settlement was concluded on January 26, 2005 and provides for a payment of USD 2 million plus an additional amount equal to 20% of the proceeds in excess of EUR 6 million that Intershop generates from the issue of the convertible bond of November 29, 2004. In addition, the plaintiffs will receive a further payment if Intershop is taken over within a year of the date of the settlement. After the plaintiffs agreed to the settlement, the competent court approved the settlement and finally dismissed the action by way of a decision dated December 5, 2005. To fulfill the settlement, the Company paid the administrator in the United States USD 2 million as well as EUR 797,884.78.

In Germany, the BaFin (Bundesanstalt für Finanzdienstleistungsaufsicht – German Federal Financial Supervisory Authority, formerly the Bundesaufsichtsamt für den Wertpapierhandel, BAWe – German Federal Supervisory Office for Securities Trading) announced in January 2001 that it had initiated an investigation regarding a possible breach of the obligation to disclose material information in connection with the presentation of Intershop Communications AG's preliminary results for 2000 on January 2, 2001. The BAFin handed this case over to the public prosecutor's office in Hamburg, which initiated an investigation in May 2001 into complaints about stock price manipulation. The Company is cooperating fully with these investigations and, to the best of the management's knowledge, has never previously been the subject of such an investigation. The Company is convinced that these allegations are unfounded. The proceedings initiated by the public prosecutor's office were discontinued by an order issued in March 2005; the proceedings instituted by the BaFin were discontinued in November 2005.

In 2002, another software company brought a claim for damages of around EUR 5 million for the alleged violation of a license agreement. An out-of-court settlement was initially agreed, but the software company declined to finally accept the terms of the settlement. In 2004, the Munich Regional Court dismissed its claim for payment. However, the court ordered Intershop to provide information on the delivery of software owned by the other software company. The Company has since provided this information. Intershop believes that the other software company has no further claims.

In 2004, a claim against the Company for approximately USD 750,000 was filed with a court in New York by a bank that advised the Company during its IPO in the United States in 2000. The claim relates to costs that the bank is alleged to have incurred in mounting a defense against the plaintiffs of the class-action lawsuit, in which a claim was also made against the bank. The Company is defending itself vigorously against the claims for payment and is of the opinion that a claim for reimbursement of costs is invalid for formal reasons, and that in any event the level of costs claimed is open to question.

The Company is involved in several legal disputes with the landlord of its headquarters in Jena with regard to claims under the lease. These comprise three claims brought by the landlord for payment of rent and ancillary costs, one claim against a bank of the Company for the release of portions of a rental guarantee, as well as a notice to vacate served by the landlord.
The background to all the actions is the reductions in rental payments and the offsetting of rental payments against contractual penalty claims by the Company since October 2003, which have been gradually increased; these actions are due to the improper construction and handover of rented space, defects in the rented property, and the improper invoicing of ancillary costs.
As a result of the reduced rent payments, the landlord has brought two claims in which it is seeking payment of a total of around EUR 1.44 million. After one of the claims was brought as a claim based solely on documentary evidence ("Urkundsklage"), the competent Regional Court ordered the Company to pay EUR 971,214 in 2004; the Company paid this amount plus interest. The Company was given leave to exercise its rights in the subsequent proceedings.
The landlord also brought an action for the payment of around EUR 220,000 in operating costs for 2002 and 2003. The Company refuses to make the corresponding payment, citing incorrect invoices and the billing of costs that were not contractually agreed.
In the action against the bank, the landlord asserted some of the claims that are already the subject of claims for payment brought against the Company itself. The action was brought as a claim based solely on documentary evidence ("Urkundsklage"); the Company has joined the dispute on the side of the bank. In a hearing on October 24, 2005, the competent court expressed its opinion that the key issue of fact, i.e., the proper construction and handover of space to the Company, had not been proven by the landlord in the summary proceedings. As a result, the landlord desisted from the summary proceedings and applied for the proceedings to be suspended. The bank and the Company consented to the suspension of the proceedings.
Finally, at the end of 2004 the landlord brought an action against the Company to vacate and surrender the entire rented property. The Company regards this action as unfounded because it believes that it is entitled to reduce the rent payments. However, the Company returned parts of the premises that it did not occupy with a total area of around 11,000 m² to the landlord in 2005, without recognizing any legal obligation. The landlord has informed the court that, until further notice, it no longer intends to pursue the action involving the notice to vacate; as a result, the court ordered the suspension of the proceedings by way of a decision dated October 18, 2005.
A hearing for the claims for payment brought by the landlord is scheduled for April 25, 2006. In several indicative rulings ("Hinweisbeschlüsse"), the court expressed its opinion that if the rented space in the entrance area of the building was not properly constructed and handed over, all of the landlord's claims for payment relating to the contractual penalty claims made by the Company would be invalid.
The Company believes that the claims for payment asserted are not valid and therefore the termination served is not effective.

In the year under review, the Company was also sued by an investment bank that has advised it in recent years in connection with corporate actions for payment of a consulting fee of EUR 593,807.01 plus

interest. The bank believes that it is entitled to this amount as a fee relating to the convertible bond successfully placed by the Company at the beginning of the year. The Company regards the claim as completely unfounded because it believes that the contract was terminated, and therefore the bank did not provide any services in 2004; finally, the fee claimed is a performance-related fee, and the bank did not provide any services whatsoever in connection with the issue of the convertible bond.
In addition to the litigation described in detail, the Company is a defendant in various other actions arising from the normal course of business. Although the outcome of these actions cannot be forecast with certainty, the Company believes that the outcome of the actions will not have any material effects on its net assets and results of operations.

Financial risk

Liquidity risk
The Company prepares a liquidity forecast based on a fixed planning horizon. This liquidity forecast plans the deployment of the financial resources available within the Company and thus attempts to ensure short- and medium-term liquidity. In the long term, a liquidity risk exists if the Company is unable to generate cash from its business operations in fiscal year 2006. In this case, the Company would be dependent on an additional cash injection from the capital markets.

Non-payment risks
The Company is exposed to a potential default risk mainly from its trade receivables. The Company performs ongoing creditworthiness checks on its customers. The default risk with regard to trade receivables is also mitigated by the fact that the Company has a broad customer base. In addition, the Company does not demand collateral for its receivables.

In 2005, customer A accounted for 20,3% of total revenues and 34,9% of trade receivables. Customer B accounted for 12,8% of total revenues in 2005 and 4,4% of trade receivables as of December 31, 2005. In 2004, customer A represented 16.2% of total revenues and 11.7% of trade receivables. Customer B accounted for 10.9% of total revenues in 2004 and 10.3% of trade receivables as of December 31, 2004.

Credit risk
A credit or interest rate risk could arise from a change in market interest rates for medium- or long-term liabilities. In terms of long-term liabilities, the Company only has to consider the 2004/2008 convertible bond that bears a fixed interest rate at maturity and is therefore not affected by market rate fluctuations.

Events Subsequent to the Balance Sheet Date

As of January 1, 2006, the Company granted new options to employees under its stock option plans. 300,000 options were issued to the members of the Management Board under the 1999 Stock Option Plan, while 3,697,032 options were granted to employees under the 2001 Stock Option Plan. The issue of the options does not lead to any changes in earnings per share because the inclusion of the options would counter the dilutive effect.

On February 3, 2006, Intershop announced in the Frankfurter Allgemeine Zeitung that Heycom GmbH, Garbsen, informed the Company on January 27, 2006 that its share of Intershop's voting rights exceeded the 5% threshold on January 18, 2006 and amounts to 8.62%. Heycom GmbH also informed the Company on January 31, 2006 that its share of Intershop's voting rights fell below the 5% threshold on January 25, 2006 and now amounts to 1.11%.

On February 9, 2006, Intershop announced in the Frankfurter Allgemeine Zeitung that Mr. Sven Heyrowsky informed the Company on February 6, 2006 that his share of the Company's voting rights exceeded the 5% threshold on January 18, 2006 and amounts to 8.62%. Of this, 8.62% is attributable to Mr. Sven Heyrowsky in accordance with section 22(1) no. 1 of the Wertpapierhandelsgesetz (WpHG – German Securities Trading Act). Mr. Sven Heyrowsky also informed Intershop on February 6, 2006 that his share of the Company's voting rights fell below the 5% threshold on January 25, 2006 and now amounts to 3.94%. Of this, 2.83% is attributable to Mr. Sven Heyrowsky in accordance with section 22(1) no. 1 of the WpHG.

In accordance with section 15a of the WpHG, the Company announced on February 22, 2006 that member of the Management Board Ralf Männlein purchased 50,000 Intershop convertible bonds with a total value of EUR 57,450 on February 21, 2006.

Related party disclosures

Related parties in accordance with IAS 24 are companies or persons that control or are controlled by the Intershop Group, provided that they are not already included in the consolidated financial statements. Control exists if a shareholder holds more than half of the voting rights of Intershop Communications AG or has the power to influence the operating policies of the Intershop Group's management by virtue of provisions of the Articles of Association or contractual agreements.
The Intershop Group did not have any relationships with unconsolidated subsidiaries, joint ventures, or associates as of the balance sheet date.

Members of Intershop Communications AG's Supervisory Board are also members of supervisory boards of other companies, with which the Intershop Group has no business relationships.

The compensation of the members of the Supervisory Board and the Management Board totaled EUR 782 thousand and exclusively comprises short-term benefits.

Disclosure requirements under German law

Management Board

- Dr. Jürgen Schöttler, Chairman of the Management Board, Chief Executive Officer, and Chief Financial Officer
- Ralf Männlein, Management Board member responsible for Sales and Marketing

Supervisory Board

- Hans W. Gutsch, Chairman
- Peter Mark Droste
- Wolfgang Meyer (appointed by the Gera Local Court on October 1, 2005)

Mr. Eckhard Pfeiffer resigned as Chairman as of the Supervisory Board on August 25, 2005 and retired from the Supervisory Board with effect from September 30, 2005.

Compensation of the members of the Management Board and the Supervisory Board

The compensation of the Management Board comprises fixed and variable components. The variable remuneration is determined by the Supervisory Board on the basis of an assessment of a member's personal performance, the business situation, and successes achieved. The Management Board also participates in the Company's stock option plan.
The compensation of the Management Board for fiscal year 2005 amounted to EUR 716,524; of this amount, a provision of EUR 309,052 was recognized for unpaid performance-related remuneration. No stock options were granted in 2005.

The Supervisory Board received the following compensation in 2005:

Name	Compensation in EUR thousand
Hans W. Gutsch (Chairman)	25
Peter Mark Droste	15
Wolfgang Meyer	4
Retired Supervisory Board members	21
Total Supervisory Board compensation	65

The compensation of the Supervisory Board consists solely of a fixed component payable at the end of the fiscal year.

Directors' holdings

As of December 31, 2005, the following members of the Company's executive bodies held Intershop Communications AG ordinary bearer shares or options to purchase such shares, as well as shares in the 2004/2008 zero-coupon convertible bond issued by the Company.

Name	Title, Function	Shares held *	Stock options held*, **	Convertible bonds
Hans W. Gutsch	Chairman of the Supervisory Board	155,018	–	–
Peter Mark Droste	Member of the Supervisory Board	100,000	–	–
Wolfgang Meyer	Member of the Supervisory Board	–	–	–
Dr. Jürgen Schöttler	Chairman of the Management Board	111,519	53,333	–
Ralf Männlein	Member of the Management Board	50,000	23,333	–

** All information post 5:1 reverse stock split in 2002 and the 3:1 reverse stock split in 2005.*
*** The stock options were granted at the conditions of the 1999 stock option plan. Details on the 1999 stock option plan can be found in section entitled "Stock option plans." Jürgen Schöttler's stock options have an average reverse stock split adjusted exercise price of EUR 12.48 per share, and Ralf Männlein's stock options have an exercise price of EUR 5.67 per share.*

Securities transactions subject to reporting requirements

In fiscal year 2005, the members of the Company's executive bodies made the following purchases and sales of Intershop ordinary bearer shares or shares in the 2004/2008 zero-coupon convertible bond issued by the Company.

Name	Date	Type of security	Type of transaction	Amount	Total value (EUR)
Supervisory Board:					
Eckhard Pfeiffer	January 25, 2005	Bond	Purchase	120,000	120,000
Hans W. Gutsch	January 25, 2005	Share	Sale	23,333*	52,990
	January 25, 2005	Bond	Purchase	152,990	152,990
	November 11, 2005	Bond	Conversion	152,990	152,990
Peter Mark Droste	January 26, 2005	Bond	Purchase	100,000	100,000
	November 11, 2005	Bond	Conversion	100,000	100,000
Management Board:					
Dr. Jürgen Schöttler	January 25, 2005	Share	Sale	5,027*	11,519
	January 25, 2005	Bond	Purchase	111,519	111,519
	November 11, 2005	Bond	Conversion	111,519	111,519
Ralf Männlein	January 26, 2005	Bond	Purchase	50,000	50,000
	November 11, 2005	Bond	Conversion	50,000	50,000

** reverse stock split adjusted.*

Employees

The Intershop Group had an average of 219 full-time employees in fiscal year 2005, of whom 217 were salaried employees and 2 were members of the executive bodies.

Employee-related expenses amounted to EUR 13,341 thousand in 2005 and EUR 14,478 thousand in 2004. The pension insurance contributions paid by the Company to statutory pension insurance funds totaled EUR 775 thousand in 2005 and EUR 839 thousand in 2004.

Auditors' fees

In fiscal year 2005, the Company incurred expenses of EUR 132 thousand (2004: EUR 124 thousand) for auditors' fees in respect of the audit of the annual and consolidated financial statements, as well as EUR 97 thousand (2004: EUR 7 thousand) for other assurance services and EUR 62 thousand (2004: EUR 0 thousand) for other services. There were no expenses for tax consulting services in 2005 and 2004. EUR 79 thousand (2004: EUR 0) of the other assurance services was appropriated to the capital reserve because these costs were incurred in connection with the placement of shares and the convertible bond on the stock exchange.

Declaration of Conformity

The Company has issued a declaration of conformity as required by section 161 of the Aktiengesetz by the annual deadline on February 8, 2006, and made this declaration permanently available to its stockholders. Further information is available in the "Corporate Governance Report".

Notes on the Effects of the Conversion from U.S. GAAP to IFRSs (Reconciliation)

Reconciliation of profits and losses for 2004

in EUR thousand	U.S. GAAP 2004	Reclassification not recognized in income	Transfer recognized in income	IFRS 2004
Revenues				
Licenses	2,566	0	0	2,566
Services, maintenance and other	15,002	0	0	15,002
	17,568	**0**	**0**	**17,568**
Cost of revenues				
Licenses	(288)	0	0	(288)
Services, maintenance and other	(8,630)	0	(43)	(8,673)
	(8,918)	**0**	**(43)**	**(8,961)**
Gross profit	**8,650**	**0**	**(43)**	**8,607**
Operating expenses, operating income				
Research and development	(4,149)	0	(30)	(4,179)
Sales and marketing	(5,007)	0	(27)	(5,034)
General and administrative	(8,501)	0	(44)	(8,545)
Restructuring costs	(406)	0	0	(406)
Other operating income	767	173	0	940
Other operating expenses	0	(150)	0	(150)
	(17,296)	**23**	**(101)**	**(17,374)**
Result from operating activities	**(8,646)**	**23**	**(144)**	**(8,767)**
Interest income	141	140	(1)	140
Interest expense	(271)	(271)	0	(271)
Financial result	**(130)**	**(131)**	**(1)**	**(131)**
Earnings after tax	**(8,776)**	**(108)**	**(145)**	**(8,898)**
Income taxes	**0**	**(23)**	**0**	**(23)**
Earnings after tax	**(8,776)**	**(131)**	**(145)**	**(8,921)**
Consolidated net loss	**(8,776)**	**(131)**	**(145)**	**(8,921)**

The transfers recognized in income relate exclusively to the employee-related expenses from stock option plans that must be recognized under IFRSs.

The reclassifications not recognized in income relate to other income that was reported as an aggregate amount under U.S. GAAP that is presented individually under IFRSs as other operating income, other operating expenses, and income taxes, as well as interest income and expenses recorded under the financial result.

Reconciliation of the balance sheet items to the opening balance sheet

Reconciliation of the consolidated balance sheet as of January 1, 2004:

in EUR thousand	U.S. GAAP **January 1, 2004**	**Reclassification not recognized in income**	**Transfer recognized in income**	IFRS **January 1, 2004**
ASSETS				
Non current assets				
Intangible assets	4,436	0	0	4,436
Property, plant and equipment	1,143	0	0	1,144
Financial investments	0	0	0	0
Other non current assets	557	(133)	0	423
Restricted cash	0	5,409	0	5,409
	6,136	**5,276**	**0**	**11,412**
Current assets				
Trade receivables	3,345	0	0	3,345
Other receivables and other assets	1,370	133	0	1,503
Restricted cash	6,190	(5,409)	0	781
Cash and cash equivalents	2,611	0	0	2,611
	13,516	**(5,276)**	**0**	**8,240**
TOTAL ASSETS	**19,652**	**0**	**0**	**19,652**
SHAREHOLDERS´ EQUITY AND LIABILITIES				
Shareholders´ equity				
Subscribed capital	22,035			22,035
Capital reserve	0	0	93	93
Other reserves	(15,697)	0	(93)	(15,790)
Treasury Stock	0	0	0	0
	6,338	**0**	**0**	**6,338**
Non-current liabilities				
Provision for restructuring	0	390	0	390
Convertible bonds	0	0	0	0
Other non current liabilities	0	23	0	23
Deferred revenue	23	654	0	677
	23	**1,067**	**0**	**1,090**
Current Liabilities				
Provision for restructuring	2,658	(390)	0	2,268
Other current provisions	2,059	(711)	0	1,348
Trade accounts payable	1,952	683	0	2,635
Income tax liabilities	0	0	0	0
Other current liabilities	1,565	5	0	1,570
Deferred revenue	5,057	(654)	0	4,403
	13,291	**(1,067)**	**0**	**12,224**
TOTAL SHAREHOLDERS´ EQUITY AND LIABILITIES	**19,652**	**0**	**0**	**19,652**

Under “Transfer recognized in income,” the capital reserve item includes the employee-related expenses that were incurred by the existing stock option plans from November 7, 2002 to December 31, 2003 and were not required to be reported under U.S. GAAP (IFRS 2). An IFRS conversion reserve was recognized under "Other reserves" as an offsetting item.

Under IFRSs, a distinction is made between noncurrent and current assets, and noncurrent and current liabilities. As a result, reclassifications directly in equity were required.
Under IFRSs, provisions and liabilities are also defined differently than under U.S. GAAP. Items from other provisions under U.S. GAAP are reported under liabilities under IFRSs. The reclassification was not recognized in income.

Reconciliation of the consolidated balance sheet as of December 31, 2004:

	U.S. GAAP			IFRS
in EUR thousand	**December 31, 2004**	**Reclassification not recognized in income**	**Transfer recognized in income**	**December 31, 2004**
ASSETS				
Non current assets				
Intangible assets	4,527	0	0	4,527
Property, plant and equipment	870	0	0	870
Financial investments	0	0	0	0
Other non current assets	458	(26)	0	432
Restricted cash	0	4,642	0	4,642
	5,855	**4,616**	**0**	**10,471**
Current assets				
Trade receivables	2,257	0	0	2,257
Other receivables and other assets	810	26	0	836
Restricted cash	6,754	(4,642)	0	2,112
Cash and cash equivalents	1,632	0	0	1,632
	11,453	**(4,616)**	**0**	**6,837**
TOTAL ASSETS	**17,308**	**0**	**0**	**17,308**

in EUR thousand	U.S.GAAP December 31, 2004	Reclassification not recognized in income	Transfer recognized in income	IFRS December 31, 2004
SHAREHOLDERS´ EQUITY AND LIABILITIES				
Shareholders´ equity				
Subscribed capital	25,551	0	0	25,551
Capital reserve	1,710	0	238	1,948
Other reserves	(24,605)	0	(238)	(24,843)
Treasury stock	(1)	0	0	-1
	2,655	**0**	**0**	**2,655**
Non-current liabilities				
Provision for restructuring	0	186	0	186
Convertible bonds	0	0	0	0
Other non current liabilities	0	38	0	38
Deferred revenue	10	121	0	131
	10	**345**	**0**	**355**
Current liabilities				
Provision for restructuring	1,778	(187)	0	1,591
Other current provisions	4,013	(49)	0	3,964
Trade accounts payable	2,893	36	0	2,929
Income tax liabilities	21	2	0	23
Other current liabilities	1,326	(26)	0	1,300
Deferred revenue	4,612	(121)	0	4,491
	14,643	**(345)**	**0**	**14,298**
TOTAL SHAREHOLDERS´ EQUITY AND LIABILITIES	**17,308**	**0**	**0**	**17,308**

Under "Transfer recognized in income," the capital reserve item includes the employee-related expenses that were incurred by the existing stock option plans from November 7, 2002 to December 31, 2003 and were not required to be reported under U.S. GAAP (IFRS 2), as well as the employee-related expenses for 2004. As offsetting items, the IFRS conversion reserve from 2003 in the amount of EUR 93 thousand was recognized under "Other reserves" and the employee-related expenses amounting to EUR 145 thousand for 2004 from the stock option plans were recorded under cumulative gains/losses.

Under IFRSs, a distinction is made between noncurrent and current assets, and noncurrent and current liabilities. As a result, reclassifications directly in equity were required.
Under IFRSs, provisions and liabilities are also defined differently than under U.S. GAAP. Items from other provisions under U.S. GAAP are reported under liabilities under IFRSs. The reclassification was not recognized in income.

Reconciliation of equity as of January 1, 2004

in EUR thousand	
Equity in accordance with U.S. GAAP as of January 1, 2004	**6,338**
Capital reserve	93
IFRS conversion reserve	(93)
Equity in accordance with IFRSs as of January 1, 2004	**6,338**

Reconciliation of equity as of December 31, 2004

in EUR thousand	
Equity in accordance with U.S. GAAP as of December 31, 2004	**2,655**
Capital reserve	238
IFRS conversion reserve	(93)
Cumulative gains/losses	(145)
Equity in accordance with IFRSs as of December 31, 2004	**2,655**

Reconciliation of cash flow

in EUR thousand	US-GAAP	Changes	IFRS
Net cash used in operating activities	**(5,446)**	**0**	**(5,446)**
Net cash used in provided by investing activities	**(848)**	**0**	**(848)**
Net cash provided by financing activities	**5,221**	**0**	**5,221**
Cash and cash equivalents, beginning of period	2,611	0	2,611
Cash and cash equivalents, end of period	**1,632**	**0**	**1,632**

Compared with U.S. GAAP, the only change in cash flow is that individual items within net cash used in operating activities have been combined. The additional employee-related expenses from the stock option plans in accordance with IFRSs were recorded under other noncash expenses.

Transition from U.S. GAAP to IFRSs

In making the transition from U.S. GAAP to IFRSs, Intershop applied IFRS 1, First-time adoption of International Financial Reporting Standards. IFRS 1 requires applying consistently and retrospectively through all fiscal years presented all IFRSs that are effective at the reporting date for the first full set of consolidated financial statements prepared under IFRSs. However, this standard includes exemptions and exceptions to this general requirement. The date of transition for Intershop is January 1, 2004. The company took advantage of the following exemptions:

Exemptions from the retrospective application of IFRS

a) Business combinations

Business combinations that occurred before January 1, 2004, are not restated retrospectively for compliance with IFRS 3. Thus, the carrying amounts as determined under U.S. GAAP of assets acquired and liabilities assumed as part of these past business combinations as well as the amounts of goodwill that arose from such transactions are considered their deemed cost under the IFRSs at the date of transition, unless very limited issues apply for which IFRS 1 requires restatement. Previous amortization and impairment losses of goodwill are not restated. Goodwill deducted directly from equity will not be reinstated on disposal of the related businesses.

As required by IFRS 1, any such goodwill were tested for impairment as of January 1, 2004, the date of transition to IFRSs, even though no indication of impairment existed. No impairment was identified.

b) Share-based compensation
As permitted under IFRS 1, IFRS 2 is not retrospectively applied to all share-based awards. Accordingly, the share-based compensation that was granted after November 7, 2002 and was not exercisable as of January 1, 2005 was recognized.

Changes in financial statement presentation

The financial information presented herein has been prepared in accordance with IAS 1, Presentation of Financial Statements. The application of IFRSs required Intershop to make only a limited number of adjustments to its financial statement presentation previously used for its U.S. GAAP reporting. Main changes include the following:

- Reclassification of accruals as defined by IFRSs: According to IAS 37, certain liability items require acertain degree of estimation, but are not as uncertain as a provision. Therefore, they are not reported as a provision. Rather they are they presented as liabilities.
- Deferred taxes: IFRSs require that all deferred tax items, including those that relate to current assets and liabilities, be presented as non-current items, whereas under U.S. GAAP the classification of deferred tax effects follows the classification of the underlying item. As a result, total current assets and total current liabilities as reported under IFRSs are lower by this amount.

Changes in recognition and measurement

Other intangible assets
Under IFRSs development costs are capitalized if specified criteria are met, while they are expensed under U.S. GAAP except for software development costs. For internally generated software all directly attributable costs (direct costs and directly attributable overheads) have to be recorded in the intangible assets under IFRSs, whereas under U.S. GAAP only direct costs are capitalized.

Compound financial instruments with conversion rights
Under both U.S. GAAP and IFRSs, compound financial instruments with conversion rights must be broken down into an equity and debt component at fair value at the acquisition date. Under U.S. GAAP, transaction costs related to convertible instruments are presented as prepaid expenses and will be charged to expense over the term of the convertible instrument. Under IFRSs, directly attributable transaction costs must be proportionately deducted from the equity and debt component, and accounted for as a deduction from the equity component or a deduction from the debt component. The debt component is then measured using the effective interest rate method.

Other provisions
Under U.S. GAAP, other provisions are not discounted except for asset retirement obligations and certain employee benefit liabilities. Under U.S. GAAP, asset retirement obligations are discounted using a historical interest rate when the obligation is initially recognized, whereas under IFRS the discount rate to be applied should reflect current market conditions prevailing at each balance sheet date.

Under IFRSs, all non current provisions are stated at their present value if the effect of discounting is significant.

Deferred taxes
Deferred taxes are recognised on all adjustments to IFRSs that represent a temporary difference between the tax base and the carrying amount of assets and liabilities in the consolidated financial statements based on IFRSs.

Impact of IFRS adjustments on the consolidated statement of cash flows

Most of the IFRS adjustments do not have any impact on consolidated statements of cash flow.

The only adjustment that has a material impact on the presentation of cash flows is the capitalization of product development expenses. Under U.S. GAAP, only development cost related to software development may be capitalized and therefore product development expenses related to other items are recognised in net income and presented in the consolidated statement of cash flows as part of the cash flow from operating activities. Under IFRSs, certain product development expenses are capitalized as intangible assets in addition to U.S. GAAP, and cash outflows are presented within cash flow from investing activities as additions to intangible assets.

Jena, March 23, 2006

The Management Board

Dr. Jürgen Schöttler | Ralf Männlein

General

The consolidated financial statements of INTERSHOP Communications AG were prepared in accordance with the pronouncements issued by the IASB and exempt the Company from preparing consolidated financial statements in accordance with section 292a of the Handelsgesetzbuch (HGB – German Commercial Code). At the same time, the consolidated financial statements and the Group management report comply with the European Union's Group Accounting Directive (83/349/EEC); this Directive was applied in accordance with its interpretation in German Accounting Standard 1 (GAS 1) "Exempting Consolidated Financial Statements in accordance with Sec. 292a of the Commercial Code" issued by the German Accounting Standards Committee e.V. (GASC). To ensure equivalence with consolidated financial statements prepared in accordance with German commercial law, all disclosures and explanatory notes required by the HGB and beyond the scope of those required by IFRSs have been published. The accounting policies and consolidation methods applied in accordance with IFRSs mainly differ from the HGB with regard to the following points:

Deferred taxes on loss carryforwards

Under the HGB, deferred tax assets arising from tax loss carryforwards may not be recognized in the balance sheet, as expected future tax savings are deemed to be not yet realized. Under IFRSs, such future tax benefit claims must be recognized if it is probable that the tax benefit from the loss carryforward will be realized. The Company has written off its recognized tax loss carryforwards in full as of December 31, 2005 due to uncertainties regarding their realization.

Employee stock options

Under IFRSs, payments made to employees in the form of equity interests (stock option plans) are carried at the fair value of the options issued and recognized under employee-related expenses, with a corresponding increase in equity. The prevailing opinion is that no expense would be recognized in the income statement in accordance with the HGB.

Revenue recognition

Under IAS 11, revenue and earnings from long-term construction contracts are recognized according to the stage of completion of the contract, if this can be reliably determined ("percentage of completion method"). Under the HGB, sales and earnings are not recognized until the contract is completed.

Convertible bond

The equity component of the convertible bond is reported as an increase in equity. The debt component is recognized as a liability at its discounted fair value. Under IFRSs, the transaction costs incurred by issuing the convertible bond reduce the equity component and the debt component. Under the HGB, the transaction costs represent expenses for the period.

Costs of the IPO

Under IFRSs, costs relating to the placement of shares on the stock exchange must be treated as a reduction of equity. Under the HGB, these costs represent expenses for the period.

Foreign currency transactions

Under IFRS, foreign currency transactions (for example, foreign currency denominated trade receivables or payables) are measured at the rate prevailing on the date on which they are initially recognized. These balance sheet items must be measured at the year-end rates at each subsequent balance sheet date. Foreign currency adjustments resulting from exchange rate fluctuations are recognized in income, with any unrealized gains being recorded in the income statement. Under HGB, revaluation losses are recognized in the income statement at each balance sheet date only, while gains are only recognized when realized (for example, upon payment of a foreign currency liability).

Goodwill

Acquisition accounting for companies acquired from third parties is performed at the date of acquisition using the purchase method in accordance with IFRS 3, Business Combinations. In subsequent periods, purchased goodwill is tested for impairment at least once a year, and if impaired, written down to the lower recoverable amount. Under HGB, the purchase method is used to measure combinations, and, in certain circumstances, the profits and losses of the acquired company may be recognized retroactively. Goodwill is amortized.

Software development costs

Under IFRSs, development costs are capitalized if they fulfill the above-mentioned requirements and are amortized over their standard useful life. The HGB does not permit internally generated software to be capitalized as a fixed asset.

Financial Statements
Intershop Communications AG

Balance Sheet Intershop Communications AG

As of December 31, (in EUR)	2005	2004
ASSETS		
Fixed assets		
Intangible assets		
Software licenses	21,896	52,962
Property and equipment		
Other facilities, office and operating equipment	470,686	588,684
Financial assets		
Investments in affiliated companies	8,872,229	10,670,003
	9,364,811	**11,311,649**
Current assets		
Inventories		
Work in process	10,828	184,252
Payments on account	8,659	8,659
	19,487	192,911
Receivables and other assets		
Accounts receivable	3,310,080	1,474,488
Receivables from affiliated companies	17,097	371,830
Other assets	685,050	602,341
	4,012,227	2,448,659
Cash-in-hand, bank balances	13,062,380	7,244,017
	17,094,094	**9,885,857**
Prepaid expenses	**184,406**	**106,809**
Total assets	**26,643,311**	**21,304,045**
SHAREHOLDERS' EQUITY AND LIABILITIES		
Shareholders' equity		
Common stock		
Conditional capital: EUR 25,418,317 (previous year: EUR 30,304,719)	17,662,052	25,551,412
Capital surplus	656,125	5,889,989
Accumulated deficit	(6,104,852)	(22,072,591)
	12,213,325	**9,368,810**
Contributions paid to implement the resolved capital increase	**15,840**	**15,840**
Accrued liabilities		
Other accrued liabilities	**2,688,920**	**5,993,714**
Liabilities		
Bonds		
thereof convertible bond: EUR 6,186,645 (previous year: EUR 0)	6,186,645	0
Advance payments received	-	457,740
Accounts payable	3,018,895	2,258,550
Other liabilities		
thereof from taxes: EUR 464,952 (previous year: EUR 202,175) thereof from social security benefits: EUR 245,793 (previous year EUR 262,250)	787,291	581,957
	9,992,831	**3,298,247**
Deferred charges	**1,732,395**	**2,627,434**
Total shareholders' equity and liabilities	**26,643,311**	**21,304,045**

Income Statement Intershop Communications AG

For the year ended December 31, (in EUR)	2005	2004
Revenues	15,066,333	13,753,746
Decrease in inventories of finished goods and work in progress	(173,424)	146,767
Other operating income	2,542,201	3,422,813
Cost of materials		
Cost of raw materials, consumables and supplies, and purchased merchandise	0	(3,096)
Cost of purchased services	(1,182,056)	(1,137,377)
Personnel costs		
Salaries	(10,050,663)	(10,555,851)
Social security contribution	(1,637,750)	(1,792,934)
Depreciation and amortization		
of intangible fixed assets and property and equipment,	(367,831)	(441,225)
of current assets to the extent it exceeds depreciation and amortization that is normal for the company	(5,472,273)	(7,322,334)
Other operating expenses	(9,318,336)	(12,257,180)
Other interest and similar income		
thereof from affiliated companies EUR 5,708,977 (previous year: EUR 7,127,398)	5,885,049	7,263,676
Write-downs of financial assets and short-term security investments	(1,806,551)	(5,058,896)
Interest and similar expenses		
thereof from affiliated companies EUR 0 (previous year: EUR 0)	(1,238,975)	(271,041)
Loss from ordinary operations	**(7,754,276)**	**(14,252,932)**
Taxes on income	0	(20,643)
Net income/loss	**(7,754,276)**	**(14,273,575)**
Accumulated deficit carried forward	(22,072,591)	(7,799,016)
Withdrawals from the capital reserve	6,687,703	0
Extraordinary income of capital reduction	17,034,312	0
Accumulated deficit	**(6,104,852)**	**(22,072,591)**

Notes to the Financial Statements
Intershop Communications AG

The annual financial statements of Intershop Communications AG were prepared in accordance with the provisions of the Handelsgesetzbuch (HGB – German Commercial Code) and the Aktiengesetz (AktG – German Public Companies Act).

Accounting Policies

Intangible fixed assets and property and equipment are stated at cost, less depreciation.

Financial assets are stated at cost, less necessary valuation allowances.

Inventories are measured at manufacturing costs.

Receivables and other assets are stated at face value, less any necessary valuation allowances.

Prepaid expenses and deferred charges are measured using the portion of expenses or income that relates to a period after the balance sheet date.

Common stock is stated at par value.

Other accrued liabilities cover all recognizable risks and are measured in the amount dictated by prudent business practice.

Liabilities are stated at their redemption amount.

Foreign currency receivables and liabilities are measured using the principle of lower of cost or market and the imparity principle, respectively.

Explanations on the Annual Financial Statements

Fixed assets changed as follows (in EUR):

	Intangible Assets	Tangible Assets	Financial Assets	Total
	Software licenses	Other equipment, operating and office equipment	Shares in affiliated companies	
Costs of purchase				
Balance at January 1, 2005	**2,849,634**	**2,775,388**	**49,424,281**	**55,049,303**
Additions	9,205	210,495	8,777	228,477
Disposals	–	(59,130)	(104,755)	(163,885)
Balance at December 31, 2005	**2,858,839**	**2,926,753**	**49,328,303**	**55,113,895**
Depreciation, amortization and write-downs				
Balance at January 1, 2005	**2,796,672**	**2,186,704**	**38,754,278**	**43,737,654**
Additions	40,271	327,560	1,806,551	2,174,382
Disposals	–	(58,197)	(104,755)	(162,952)
Balance at December 31, 2005	**2,836,943**	**2,456,067**	**40,456,074**	**45,749,084**
Net carrying amount at Dec. 31, 2004	**52,962**	**588,684**	**10,670,003**	**11,311,649**
Net carrying amount at Dec. 31, 2005	**21,896**	**470,686**	**8,872,229**	**9,364,811**

Effective January 1, 2003, Intershop Software Entwicklungs GmbH was merged with Intershop Communications AG. The merger entailed the transfer of goodwill with a carrying amount of EUR 0 to Intershop Communications AG. Since there was no longer a positive carrying amount, goodwill has not been shown in the balance sheet or in the statement of changes in fixed assets.

Receivables from affiliated companies and other assets have a maturity of up to one year. Receivables from affiliated companies result of the financing of the group.

Cash and cash equivalents totaling EUR 6,209,991 (previous year: EUR 6,754,169) reported under cash-in-hand and bank balances have been assigned as security (restricted cash).

The share capital in the amount of EUR 17,662,052 consists of 17,662,052 no-par value bearer shares.

The authorized capital totaling EUR 40,487,837 entitles the Management Board to issue an additional 40,487,837 no-par value bearer shares.

The resolution of the Annual Stockholders' Meeting on June 6, 2002 authorized the Management Board, with the approval of the Supervisory Board, to increase the Company's share capital by a total of up to EUR 35,093,887 on one or several occasions up to December 11, 2007, by issuing a maximum of 35,093,887 new no-par value bearer shares (Authorized Capital I). The Management Board is also authorized to exclude the shareholders' subscription rights with the approval of the Supervisory Board. A capital increase was made in the fiscal year from Authorized Capital I. A total of 4,258,550 new no-par value bearer shares were issued. Authorized Capital I was reduced to 30,835,337 as a consequence.

Furthermore, the resolution of the Annual Stockholders' Meeting on June 6, 2002 authorized the Management Board, with the approval of the Supervisory Board, to increase the Company's share capital by a total of up to EUR 9,652,500 for the purposes approved by the Annual Stockholders' Meeting on June 6, 2002. This increase may be carried out by issuing a maximum of 9,652,500 new no-par value bearer shares on one or several occasions up to December 11, 2007 (Authorized Capital II); shareholders' subscription rights have been excluded.

An amount totaling EUR 25,418,317 is available as conditional capital for the issuance of 25,418,317 no-par value bearer shares. Due to the reverse stock split and the lapsing of options, however, a maximum of 17,153,635 shares can be issued from conditional capital.

Of the conditional capital created for granting employee stock options, EUR 8,165,000 (Conditional Capital I) are reserved for options in compliance with section 192 (2) clause 3 of the German Stock Corporation Act (Aktiengesetz). Conditional Capital I is reserved for exercising the options based on the 1999 option model. These options must be exercised no earlier than two years and no later than five years from the time they were granted. The conversion price for the new shares is based upon the average price of the shares during the last ten trading days prior to the day the options were granted, plus 20%. Due to the 5:1 capital reduction resolved on October 30, 2002 that became legally effective on December 12, 2002, and the 3:1 capital reduction resolved on April 26, 2005 that became legally effective on June 28, 2005, the subscription rights arising from Conditional Capital I decreased at the same ratio, i.e., to 544,333 shares, in accordance with section 218 of the AktG.

Moreover, EUR 690,016 from Conditional Capital II created in compliance with section 192 (2) clause 3 of the German Stock Corporation Act is reserved to implement the rights granted to known holders of options to exchange shares in Intershop Communications, Inc., which was acquired by the Company in 1998, for shares in the Company at a ratio of 5:15. Due to the 5:1 capital reduction resolved on October 30, 2002 that became legally effective on December 12, 2002, and the 3:1 capital reduction resolved on April 26, 2005 that became legally effective on June 28, 2005, the subscription rights arising from Conditional Capital I decreased at the same ratio, i.e., to 46,001 shares, in accordance with section 218 of the AktG.

Conditional Capital III was cancelled by a resolution of the Annual Stockholders' Meeting of July 7, 2004. The conditional capital increase was used to meet the Company's obligation to issue shares of the Company to Stephan Schambach and Burgess Jamieson in exchange for shares of Intershop Inc. They exercised their conversion right in 2003.

The resolution of the Annual Stockholders' Meeting on June 13, 2001 authorized the Management Board to grant, on one or several occasions up to May 31, 2006, bearer convertible bonds as well as bonds with warrants for a total of up to 21,449,703 no-par value bearer shares of the Company, in which case shareholders' subscription rights can be excluded. In order to cover these convertible bonds, the Company's share capital was conditionally increased by up to EUR 21,449,703 (Conditional Capital IV). 4,886,402 bonds from the convertible bond were converted in fiscal year 2005. Accordingly, Conditional Capital IV was reduced from EUR 21,449,703 to EUR 16,563,301.

The capital reserve developed as follows in fiscal year 2005:

Balance at December 31, 2004	**5,889,989**
Addition of equity component of convertible bond	1,649,424
Reversal of the capital reserve due to the simplified capital reduction (section 229(2) of the AktG)	(6,687,703)
Reversal of equity component of convertible bond after conversion of 43.12% of the bonds	(195,585)
Balance at December 31, 2005	**656,125**

In 2004, the Company borrowed own shares to meet the exercise of an option as 9,600 shares. This option was a result of the stock option plan covered by Authorized Capital II. At the balance sheet date, no corresponding capital increase had been implemented. The proceeds resulting from the exercise of the option, including additional paid-in capital, have been recognized under the item "Contributions paid to implement the resolved capital increase". Due to the 3:1 capital reduction resolved on April 26, 2005, the capital increase was implemented in fiscal year 2006, but only in the amount of EUR 3,200 instead of EUR 9,600. The capital increase was entered in the commercial register on February 22, 2006.

Other accrued liabilities consist primarily of pending losses from ongoing obligations and litigation risks, year-end closing costs and the costs of the Annual Stockholders' Meeting, outstanding invoices, warranties, holiday entitlements, license fees, and commission.

Liabilities can be broken down as follows (in EUR thousands):

	Due within 1 year	Due in 1–5 years	Due after more than 5 years	Total	Mortgage-backed
Bonds		6,187		6,187	-
Trade payables	3,019			3,019	-
Other liabilities	787			787	-
	3,806	**6,187**		**9,993**	**-**

On November 24, 2004, Intershop announced its intention to issue a zero-coupon convertible bond with a total volume of up to EUR 20 million, as authorized by the resolution of the Annual Stockholders' Meeting on June 13, 2001, which created conditional capital of up to EUR 21,449,703 in order to allow the grant of conversion rights to holders of the bonds.

The zero-coupon convertible bond has a maturity date of December 14, 2008 and is composed of individual bonds with a nominal value of EUR 1 each. The principal features of the zero-coupon convertible bond are the repayment amount of EUR 1.46 per bond at maturity, if conversion has not taken place, corresponding to an effective interest rate of 10% p.a., and the right to convert into bearer voting ordinary shares of the Company during specified exercise periods (starting in November 2005). The conversion price on each occasion will be EUR 1.00, irrespective of any capital reductions. Automatic conversion will take place if the share price exceeds EUR 5.00 on ten consecutive trading days at any time after January 1, 2006. As collateral, Intershop will furnish a first-ranking lien on its worldwide copyright to the Enfinity Software.

Stockholders were granted an indirect right to subscribe at a ratio of 1.3 to 1 in the period from November 29 to December 14, 2004; they also received the right to subscribe for additional bonds. However, the minimum amount of EUR 5 million required for the issue of the convertible bond to proceed was not achieved during the subscription period. Additional bonds were offered to investors in the form of a private placement. On January 26, 2005, Intershop announced that the convertible bond had been successfully placed. Bonds arising from the convertible bond with a value of EUR 11,331,000 were subscribed.

The income from the issue of the convertible bond was divided into a debt and an equity component. In the first conversion window (November 1 to November 30, 2005), 4,886,402 convertible bonds were converted into shares of the Company; this corresponds to a proportion of 43.12%. A standard market interest rate of 15% was used for the calculation. The interest rate used corresponds to a standard market rate for debt financing for four-year maturities and a credit rating that is comparable with that of Intershop.
The effective interest rate is 18.026% per year.

The following table shows the development of convertible bonds in fiscal year 2005 (in EUR thousand):

1.	Subscribed bonds	11,331
	less equity component before conversion	-1,649
	Debt component before conversion	**9,682**
2.	Debt component before conversion	9,682
	Interest on the convertible bond	1,196
	Adjusted debt component before conversion	**10,878**
3.	Adjusted debt component before conversion	10,878
	Converted portion of the adjusted debt component (43.12%)	-4,691
	Debt component after conversion	**6,187**

Contingent Liabilities

The lessor of the Company's business premises in Jena gave notice of termination of the long-term lease on November 30, 2004, and notice to vacate the premises. The Company is of the opinion, however, that the notice to terminate is invalid. Nonetheless, the notice of termination and notice to vacate give rise to the possibility that occupation of our business premises will cease at the end of 2006. For fiscal 2006, the Company's financial obligations under the lease amount to EUR 1.7 million.
In the event that the Company's opinion that the notice to terminate is legally invalid is upheld, the financial obligations resulting from the lease as at December 31, 2005 amounted to EUR 17.1 million, which are due ratably until the end of the lease period on November 14, 2013.

Income statement of Operations

The following table shows a breakdown of revenues by region:

Germany	11,862,430
Rest of Europe	2,993,225
Rest of the world excluding Europe	210,678
	15,066,333

EUR 2,724,624 of revenues relates to license income and EUR 12,341,709 to income from consulting services.

Other operating income in the fiscal year 2005 includes prior-period income of EUR 1,725,889.

Other operating expenses for fiscal 2005 contain prior-period expenses amounting to EUR 196,493.

The write-downs charged in accordance with section 253 (2) of the HGB amount to EUR 1,806,551 (previous year: EUR 5,058,896); those charged in accordance with section 253 (3) of the HGB amount to EUR 5,472,273 (previous year: EUR 7,322,334).

EUR 5,708,977 of other interest and similar income relates to affiliated companies (previous year: EUR 7,127,398).

Other Disclosures

The Company had an average of 236 employees during the fiscal year 2005 (prior year: 260).

The Supervisory Board comprised the following members in 2005:

Hans W. Gutsch
- → Chairman of the Supervisory Board (from August 26, 2005)
- → Deputy Chairman of the Supervisory Board (till August 25, 2005)
- → Graduate in business administration
- → Former Senior VP Human Resources and Organization, Compaq Computer Corporation

Other supervisory board memberships:
- Sensomotion Inc., USA (Chairman of the Supervisory Board)
- El-Nets, Ltd., Singapore
- RYNEX Corporation New York, U.S.A.

Peter Mark Droste
- → Graduate engineer
- → Former Manager Central and Northern Europe, Siebel Systems
- → Former Manager of Compaq Germany
- → Partner at DV-Ratio Management Consulting GmbH
- → Senior Advisor 3i (Venture Capital)

Other board memberships:
- Ferrari Elektronik AG (Chairman of the Supervisory Board)
- Interhyp AG (Chairman of the Supervisory Board)
- Member of the Advisory Council of Aventeon Mobil Business Solution GmbH
- Amadee AG (Member of Management Board)

Wolfgang Meyer
(from October 1, 2005)
- → Graduate engineer
- → Chairman of the Management Board of Schott Jenaer Glas GmbH

Other memberships:
- Schott Lithotec AG (Member of the Management Board)
- Ernst-Abbe-Foundation in Jena (Member of the Management Board)
- Foundation for Technology, Innovation and Research Thuringia (Member of the Management Board)

Eckhard Pfeiffer
(till September 30, 2005)
→ Chairman of the Supervisory Board (till August 25, 2005)
→ Investor
→ Former President and Chief Executive Officer, Compaq Computer Corporation

Other supervisory board memberships:
- Accoona Corporation (Chairman of the Supervisory Board)
- General Motors Corporation
- LM Ericsson AB
- IFCO Systems NV
- Syntek Capital AG

The Management Board included the following persons in 2005:

Dr. Jürgen Schöttler
Chairman of the Management Board, Chief Executive Officer and Chief Financial

Ralf Männlein
Management Board member responsible for Sales and Marketing

The Management Board received remuneration from the Company totaling EUR 716,524. No stock options were granted in 2005. The remuneration for the members of the Supervisory Board for the fiscal year amounted to EUR 64,879.

Information on the shareholdings of the members of the executive bodies (Supervisory and Management Boards) as of December 31, 2005 can be found in the Note “Local Disclosure Requirements” of the notes to the consolidated financial statements.

As a listed company, Intershop Communications AG prepares consolidated financial statements in accordance with IFRS which, according to the provisions of section 292a of the German Commercial Code (HGB), exempt it from the need to file HGB consolidated financial statements. The consolidated financial statements are filed with the commercial register of the Local Court in Gera, Germany. These consolidated financial statements include the financial statements of the parent company and the following companies:

- Intershop Communications, Inc., San Francisco, USA
- Intershop Communications Ventures GmbH, Jena, Germany
- Intershop Communications s.r.o., Praque
- IS Nordic AB, Stockholm, Sweden
- Intershop Communications Australia Pty Ltd., North Sydney, Australia

The following list shows the subsidiaries of Intershop Communications AG and the Company's respective interest as of December 31, 2005:

	Interest in %	Currency	Nominal capital	Equity*	Net income/ net loss*
Intershop Communications, Inc., San Francisco, U.S.A.	100	Euro	7,332,682	(114,150,230)	(4,941,495)
Intershop Communications Ventures GmbH, Jena	100	Euro	1,000,000	(2,076,289)	(102,733)
Intershop (UK) Ltd., London, United Kingdom	100	Euro	1,586	0	22,966,086
Intershop Communications S.a.r.l., Paris, France	100	Euro	300,000	0	0
IS Nordic AB, Stockholm, Sweden	100	Euro	11,437	39,318	10,737
Intershop Communications Hongkong Co. Ltd., Hong Kong, China	99,99	Euro	1,378	0	(742,881)
Intershop Communications Korea Co, Ltd,, Seoul, Korea	99,98	Euro	50,940	0	347,100
Intershop Communications Taiwan, Taipeih, Taiwan	100	Euro	32,393	0	110,042
Intershop Communications Singapore Pte Ltd., Singapur	100	Euro	65,168	0	231,267
Intershop Communications Australia Pty Ltd,, Sydney, Australien	100	Euro	238,278	(1,670,720)	(91,676)
Intershop Communications s. r. o., Prag, Tschechien	100	Euro	6,746	(25,475)	(32,187)

**The above figures for equity and the net loss/net income for the year are provisional.*

Auditors' fees

In fiscal year 2005, the Company incurred expenses of EUR 132,500 for auditors' fees in respect of the audit of the annual and consolidated financial statements, as well as EUR 97,370 for other assurance services and EUR 62,064 for other services. There were no expenses for tax consulting services in 2005.

Declaration of Conformity in accordance with section 161 of the German Stock Corporation Act

The corporate governance declaration of conformity required under section 161 of the German Stock Corporation Act (Aktiengesetz) was submitted and has been permanently available to stockholders on the Company's web site at http://www.intershop.com/investors since February 8, 2006.

Appropriation of net income/loss

The Management Board of Intershop Communications AG proposes to carry forward the accumulated deficit of EUR 6,104,852 to new account.

Jena, March 23, 2006

The Management Board

Dr. Jürgen Schöttler   Ralf Männlein

Report of Independent Auditors
Intershop Communications AG

Auditor’s Report

We have audited the annual financial statements, comprising the balance sheet, the income statement and the notes to the financial statements, together with the bookkeeping system, and the management report of the INTERSHOP Communications AG, Jena, for the business year from January 1, 2005 to December 31, 2005. The maintenance of the books and records and the preparation of the annual financial statements and management report in accordance with Ger-man commercial law are the responsibility of the Company’s management. Our responsibility is to express an opinion on the annual financial statements, together with the bookkeeping system, and the management report based on our audit.

We conducted our audit of the annual financial statements in accordance with § 317 HGB [„Handelsgesetzbuch“: „German Commercial Code“] and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the annual financial statements in accordance with German principles of proper accounting and in the management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Company and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the books and records, the annual financial statements and the management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the annual financial statements and management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

In our opinion, based on the findings of our audit, the annual financial statements comply with the legal requirements and give a true and fair view of the net assets, financial position and results of operations of the Company in accordance with German principles of proper accounting. 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.

Leipzig, March 24, 2006

KPMG Deutsche Treuhand-Gesellschaft,
Aktiengesellschaft,
Wirtschaftsprüfungsgesellschaft

Dr. Georg Flascha
Wirtschaftsprüfer

Maik Pülmanns
Wirtschaftsprüfer

Report of the Supervisory Board

The Supervisory Board oversaw and monitored the activities of the Management Board in accordance with the tasks imposed upon it by law and the Articles of Association and assured itself that corporate governance standards were implemented and observed throughout the Company. The Supervisory Board convened for regular meetings on February 7, 2005, April 25, 2005, September 10, 2005 and November 10, 2005. Discussions were also held by telephone between the full Supervisory Board and the Management Board on March 10, 2005, August 25, 2005, and September 28, 2005.

In addition, the Management Board regularly reported to the Supervisory Board on the achievement of planned targets for the current year and on the forecast for future periods. The Supervisory Board held regular meetings with the CFO and the head of accounting to discuss, analyze, and monitor financial issues relating to ongoing business operations.

In 2005, all members of the Supervisory Board attended at least half of the Supervisory Board's meetings. No conflicts of interest arose for any of the Supervisory Board members during the year.

At the Supervisory Board meeting on August 25, 2005, the Chairman of the Supervisory Board, Eckhard Pfeiffer, resigned from this position with immediate effect for personal reasons; he also retired as a member of the Supervisory Board with effect from September 30, 2005. The Supervisory Board and the Company would like to thank Mr. Pfeiffer for his long association with and his commitment to the Company in the recent eventful years.
The Supervisory Board then elected the longstanding member Hans Gutsch as the new Chairman at the meeting on August 25, 2005.
Following Mr. Pfeiffer's retirement from the Supervisory Board, the Company filed an application with the competent Local Court for the appointment of Mr. Wolfgang Meyer as an additional member of the Supervisory Board; Mr. Meyer was appointed with effect from October 1, 2005.

The Supervisory Board's Audit Committee is now composed of the three members of the Supervisory Board and is chaired by Mr. Peter Mark Droste; the Human Resources/Compensation Committee also consists of the three members of the Supervisory Board and is chaired by Hans Gutsch.

KPMG Deutsche Treuhand-Gesellschaft AG Wirtschaftsprüfungsgesellschaft, which was elected by the Annual Stockholders' Meeting on April 26, 2005 as auditor for fiscal year 2005, audited the accounts, the annual and consolidated financial statements, and the combined management report and group management report of Intershop Communications AG and issued unqualified audit opinions. Following its own detailed review, the Supervisory Board concurred with the result of the audit and approved the annual and consolidated financial statements prepared by the Management Board on April 11, 2006. The annual financial statements of Intershop Communications AG have thus been adopted.
On behalf of the Supervisory Board, I would like to thank the Management Board and all our employees for their hard work and commitment in the past fiscal year.

Jena, April 11, 2006

Hans W.Gutsch
Chairman of the Supervisory Board
Intershop Communications AG

Corporate Governance Report

Corporate Governance Report

Intershop welcomes the German Corporate Governance Code presented by the Government Commission and most recently updated in July 2005. The recommendations of the German Corporate Governance Code were largely complied with in fiscal year 2005. The Supervisory Board and the Management Board issued the following joint Declaration of Conformity in accordance with section 161 of the Aktiengesetz on February 8, 2006:

1. Since its last declaration of conformity dated February 7, 2005, Intershop Communications AG complied with the recommendations of the Government Commission on the German Corporate Governance Code in the version dated May 21, 2003, in the period from February 7 to July 20, 2005, and in the version dated June 2, 2005 published on July 20, 2005 ("Code") from July 21, 2005 until the present, with the following exceptions:

   a) The documents convening the Annual Stockholders' Meeting were not sent via electronic chanels (section 2.3.2).
   b) Individualized information on the compensation components of Management Board salaries was not given in the notes to the consolidated financial statements (section 4.2.4).
   c) The recommended announcement of proposed candidates for the post of Chairman of the Supervisory Board was not made for practical reasons in relation to the election of Mr. Gutsch as Chairman of the Supervisory Board on August 25, 2005, as the election did not occur in connection with the appointment of new Supervisory Board members by the Annual Stockholders' Meeting and could not therefore be announced when the meeting was convened (section 5.4.3).
   d) The Supervisory Board does not receive performance-related compensation. Compensation was published as an aggregate amount (section 5.4.7).

2. Intershop Communications AG will comply with the recommendations of the Government Commission on the German Corporate Governance Code, as amended in the version dated June 2, 2005, with the following exceptions:

   a) The convention documents fort he stockholders´ meeting will not be sent via electronic channels (section 2.3.2)
   b) Individualized information on the compensation components of Management Board salaries is not given in the notes to the 2005 consolidated financial statements (section 4.2.4).
   c) The Supervisory Board will not receive performance-related compensation (section 5.4.7).
   d) The 2005 consolidated financial statements will be published 30 days after the deadline stated in the Code, in accordance with the deadline laid down in section 62(3) of the Exchange Rules of the Frankfurt Stock Exchange (section 7.1.2).

Jena, February 8, 2006

Intershop Communications AG

on behalf of the Management Board

Dr. Jürgen Schöttler

Ralf Männlein

on behalf of the Supervisory Board

Hans W. Gutsch

This declaration has been permanently available to stockholders on the Company's website at www.intershop.com/company/investor_relations/corporate_governance/ since February 8, 2006.

Compensation of the members of the Management Board and the Supervisory Board

The compensation of the Management Board comprises fixed and variable components. The variable remuneration is determined by the Supervisory Board on the basis of an assessment of the member's personal performance, the business situation, and successes achieved. The Management Board also participates in the Company's stock option plan.
The compensation of the Management Board for fiscal year 2005 amounted to EUR 716,524; of this amount, a provision of EUR 309,052 was recognized for unpaid performance-related remuneration. No stock options were granted in 2005. This disclosure creates sufficient transparency from the Company's perspective.

The current compensation rules for the Supervisory Board are laid down in Article 13 of the Company's Articles of Association. In addition to the reimbursement of their expenses, the individual members of the Supervisory Board receive fixed compensation payable at the end of the fiscal year. The compensation takes into account the positions of Chairman and Deputy Chairman. The members of the Management Board and the Supervisory Board believe that the existing compensation of the Supervisory Board is better suited to ensuring the independence of the Supervisory Board in the performance of its oversight function.

The Supervisory Board received the following compensation for 2005:

Name	Compensation in EUR thousand
Hans W. Gutsch (Chairman)	25
Peter Mark Droste	15
Wolfgang Meyer	4
Retired Supervisory Board members	21
Total Supervisory Board compensation	65

Securities transactions subject to reporting requirements (Directors´ dealings)

In fiscal year 2005, the members of the Company's executive bodies made the following purchases and sales of Intershop ordinary bearer shares or shares in the 2004/2008 zero-coupon convertible bond issued by the Company.

Name	Date	Type of security	Type of transaction	Amount	Total value (EUR)
Supervisory Board:					
Eckhard Pfeiffer	January 25, 2005	Bond	Purchase	120,000	120,000
Hans W. Gutsch	January 25, 2005	Share	Sale	23,333*	52,990
	January 25, 2005	Bond	Purchase	152,990	152,990
	November 11, 2005	Bond	Conversion	152,990	152,990
Peter Mark Droste	January 26, 2005	Bond	Purchase	100,000	100,000
	November 11, 2005	Bond	Conversion	100,000	100,000
Management Board:					
Dr. Jürgen Schöttler	January 25, 2005	Share	Sale	5,027*	11,519
	January 25, 2005	Bond	Purchase	111,519	111,519
	November 11, 2005	Bond	Conversion	111,519	111,519
Ralf Männlein	January 26, 2005	Bond	Purchase	50,000	50,000
	November 11, 2005	Bond	Conversion	50,000	50,000

** reverse stock split adjusted.*

As of December 31, 2005, the following members of the Company's executive bodies held Intershop Communications AG ordinary bearer shares or options to purchase such shares, as well as shares in the 2004/2008 zero-coupon convertible bond issued by the Company.

Name	Title, Function	Shares held *	Stock options held*, **	Convertible bonds
Hans W. Gutsch	Chairman of the Supervisory Board	155,018	-	-
Peter Mark Droste	Member of the Supervisory Board	100,000	-	-
Wolfgang Meyer	Member of the Supervisory Board	-	-	-
Dr. Jürgen Schöttler	Chairman of the Management Board	111,519	53,333	-
Ralf Männlein	Member of the Management Board	50,000	23,333	-

** All information post 5:1 reverse stock split in 2002 and the 3:1 reverse stock split in 2005.*
*** The stock options were granted at the conditions of the 1999 stock option plan. Details on the 1999 stock option plan can be found in section entitled "Stock option plans". Jürgen Schöttler's stock options have an average reverse stock split adjusted exercise price of EUR 12.48 per share, and Ralf Männlein's stock options have an exercise price of EUR 5.67 per share.*

Stock option plans

Stock option plans allow employees to acquire shares in the Company. Intershop has the following Stock Option Plans:

1997 Stock Option Plan

The Company had originally reserved 2,000,000 ordinary shares for issuance to employees, directors, and consultants under its 1997 Stock Option Plan (the 1997 Plan). The Supervisory Board may grant incentive or non-statutory stock options at prices not less than 100% or 85%, respectively, of the fair value as determined by the Supervisory Board at the grant date. Options vest ratably over periods determined by the Board, generally three years. The Management Board also has the authority to set exercise dates (no longer than ten years from the grant date), payment terms, and other provisions. The Company had the right of first refusal for all ordinary shares issued under the 1997 Plan should the holder intend to sell or otherwise transfer any of the shares. The Company's right of first refusal terminated at the effective date July 16, 1998, of the Company's initial public offering.

1999 Stock Option Plan

With effect from June 21, 1999, the Company adopted a new stock option plan (the 1999 Plan) for the issuance of shares to Management Board members, executives, and various employees. The options under the 1999 Plan vest ratably over a four-year period, beginning six months from the grant date; however, in accordance with the Aktiengesetz (German Stock Corporation Act), no options will be exercisable, even though a portion is vested, prior to the second anniversary of the grant date. The exercise price of the options is equal to 120% of the market price of the shares at the grant date, where the market price is determined to be the average closing price as quoted on the Prime Standard for the 10 trading days prior to the grant date.

There are two pools of shares authorized under the 1999 Plan. There are 44,333 shares for grants of stock options to members of the Management Board and general managers of subsidiaries and 500,000 shares for grants of stock options to all other employees.

2001 Stock Option Plan

As of January 1, 2001, the Company adopted a new stock option plan (the 2001 Plan) for the issuance of shares to all employees. No options under this plan have been allocated to the Management Board. The options under the 2001 Plan vest ratably over a fifty-month period beginning from the grant date; however, in accordance with the Aktiengesetz, no options will be exercisable, even though a portion is vested, prior to the six months after the grant date. The exercise price of the options is the fair value at the grant date, defined as equivalent to the XETRA closing price on the Frankfurt Stock Exchange for voting shares of stock of the Company.

The Company has reserved 643,500 ordinary shares for issuance to employees under its 2001 Stock Option Plan.

Stock market data on Intershop shares

ISIN	DE000A0EPUH1
WKN	A0EPUH
Stock market symbol	ISH2
Admission segment	Prime Standard / Regulated market
Prime sector	Software
Membership of Deutsche Börse indices	CDAX, Prime All Share, Technology All Share

Key figures for Intershop shares		2005
Closing price*	in EUR	1.00
High*	in EUR	2.46
Low*	in EUR	0.68
Number of shares outstanding (as of Dec. 31)	Number	17,662,052
Number of shares – diluted (as of Dec. 31)	Number	24,106,650
Market capitalization (as of Dec. 31)	in EUR million	17.7
Market capitalization (as of Dec. 31) – diluted	in EUR million	24.1
Free float	in %	100
Average trading volume per day*	Number	178,094

** in Xetra*

Financial Calendar 2006

Date	Event
February 9, 2006	Release of Q4/05 and FY 2005 financials
April 27, 2006	Release of Q1/06 financials
July 27, 2006	Release of Q2/06 and 6-month financials
August 1, 2006	Annual stockholders´meeting
October 26, 2006	Release of Q3/06 and 9-month financials

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