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This is a translated copy of the original Swedish Annual Report  
The Board of Directors and Chief Executive Officer of

# **Transmode Holding AB**

Corporate Identity Number 556588-9101

hereby present the

## **Annual Report**

for the financial year 1 January - 31 December 2010

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# Directors' Report

The Board of Directors of Transmode Holding AB hereby submits the following Annual Accounts and Consolidated Accounts for the financial year January 1, 2010 - December 31, 2010. Unless specifically stated otherwise, all amounts in the Directors' Report are stated in millions of Swedish kronor (SEK m) and then in thousands of Swedish kronor (SEK 000). The information in brackets is for the previous year.

## The Group's Operating Activities and Structure

Transmode is a leading provider of optical network solutions for transporting data, voice and video traffic based on CWDM and DWDM (coarse/dense wavelength division multiplexing) technology.

Transmode's unique concept Intelligent WDM (iWDM™) has resulted in over 20,000 installed systems with over 300 fixed and mobile telecom operators, cable TV operators, Internet service providers and large corporations and public institutions across Europe, the Americas and Asia.

With its broad product portfolio addressing regional, metro core, access and large corporate networks, as well as secure global organizational resources, Transmode helps its customers enhance their network capacity, quality of service and functionality in a cost-efficient manner.

Transmode conducts its operating activities from its head office located in southern Stockholm, Sweden, where product development, production, marketing, sales, logistics, administration and corporate management are located. Transmode also has local resources in the UK, Germany, Poland, the Netherlands, Belgium, Italy, Spain, France, the US, Russia and Malaysia. The company sells its products direct to end-customers or via resellers.

At year-end 2010, Transmode had 197 employees, an increase of 35 on year-end 2009. Most of the increase was in development and sales resources.

## Significant Events in the Financial Year

### Geographical Expansion

The market returned to growth in 2010, and independent analyst Infonetics estimates that Transmode's core market of Metro WDM equipment grew by some 12% worldwide. The same analysts estimate that growth was highest in North America and in the Asia and Pacific region (APAC). To enable its geographical expansion to continue, the company extended its American and Asian sales resources further, while also hiring a regional Sales Vice President for APAC. The collaboration with NEC of Japan continued, resulting in more new business and business opportunities, primarily in Eastern Europe, APAC and Latin America. The company also extended its sales resources in Europe to expand its presence in selected countries. Thanks to these and previous initiatives, the company judges that it outgrew the market across all regions in 2010.

### Customers

Transmode's customer base passed the 300 customers mark in the year. Customer engagements announced in 2010 included Netnod (Internet Exchange), Net4Mobility and Teracom of Sweden, Telenor (MetroCore networks) and Ishavslink of Norway, German cable TV operator KBW, Gencat (ROADM) of Spain FarEasTone of Taiwan. The company announced business with LMT of Latvia and Starnet of Moldavia via NEC. Moreover, utilizing the company's products, ESB of Ireland was able to launch a mobile backhaul offering addressing Irish mobile operators. Virgin Media Business of the UK also launched high-capacity services for business customers, which include Transmode's transponder products.

### Product Development

In 2010, Transmode continued the launch of a series of new, innovative products. The main activities centered on the company's Ethernet offering. The company launched an EDU (Ethernet Demarcation Unit) and a range of EMXs (Ethernet Muxponders) within its Native Packet Optical architecture, which are used to aggregate Ethernet traffic and manage a raft of Ethernet services. Existing and new customers gave these products a very positive reception.

### Other

Transmode strengthened its management team by hiring Britt Alexandersson as HR Director and Dan Rydberg has taken on the role as Operations & Customer Services Vice President on a consultancy basis.

Transmode also secured official recognition as a Red Herring finalist in the European Technology Awards, as one of Sweden's representatives in the European Business Awards, and was nominated for Sweden's *Stora Exportpriset* (Great Export Prize) 2010.

## Ownership Structure

At the end of the financial year, Transmode Holding AB's share capital was SEK 4,879,817, divided between 487,981,740 shares (see Note 23 regarding the division between share classes) with a quotient value of SEK 0.01. At the end of the financial year there were also 61,540,590 issued share warrants, which when fully exercised, would result in share capital increasing by SEK 644,433, and the number of shares would increase by 64,443,287, dilution of 13.2%.

The shareholders of Transmode holding AB as of December 31, 2010 were:

	No. of Outstanding Shares	Proportion of Equity and Votes (%)
Pod Venture Partners AB	202,664,198	41.5
Amadeus Capital Partners Ltd.	104,724,382	21.5
HarbourVest IV LP	57,128,838	11.7
EEP Managers Ltd.	44,332,571	9.1
Santec Corporation	11,290,259	2.3
Other	67,841,492	13.9
Total	487,981,740	100.0

For more information on share capital, refer to Note 23 of the Annual Report.

## Shareholders' Meetings and Work of the Board of Directors

### Annual General Meeting

The AGM on 12 April 2010 re-elected Kent Sander as Chairman of the Board of Transmode Holding AB and Eva Lindqvist, Simon Cornwell, Tom Nyman, Alex Rogers, Gerd Tenzer and Karl Thedéen as Board members. For the first time in Transmode's history, the AGM also resolved to pay dividends of SEK 0.88 per class F preference share. Later in the year, Karl Thedéen put his Board position at the disposal of a further external member, Torbjörn Nilsson.

### Extraordinary General Meeting, September 28, 2010

An EGM on 28 September 2010 resolved to authorize the Board of Directors to decide on the new issue of a maximum of 80,000,000 ordinary shares that can be used in tandem with acquisitions of other companies or operations, for example on one or more occasions until the end of the following AGM, and waiving shareholders' preferential rights. Her hand as shares shall be paid foreign cash, through payment in kind or set off. In addition, on one or more occasion until the end of the following AGM, and waiving shareholders' preferential rights, the Board of Directors was authorized to issue a maximum of 18,600,000 share warrants with entitlement to subscribe for shares, to senior management, other key staff and other employees in, or attributable to, other companies, or other operations that may be acquired.

The above authorizations have not been utilized.

### Extraordinary General Meeting, December 13, 2010

An EGM of December 13, 2010 resolved to pay a further dividend of SEK 1.61 per class F preference share and SEK 0.33 per class E preference share. Accordingly, total dividends for 2010 amount to SEK 200,414,469.

### Board of Directors and Committees

The Board of Directors consists of seven regular members and two deputies elected by the AGM. In the year, CEO Karl Thedéen put his Board position at the disposal of a further external member, Torbjörn Nilsson. Nicolas Brusson also replaced Pat Burtis as a deputy. The Board held 18 (14) meetings during the financial year. The work of the Board is formalized by special rules of procedure the Board has prepared regarding the division of responsibilities between the Board and Chief Executive Officer.

The Board has a Remuneration Committee and an Audit Committee. The main duty of the Remuneration Committee is to deal with decisions and guidelines regarding salaries and other remuneration and employment terms for the Chief Executive Officer and other members of the company's management, and such other related matters the Board assigns the Committee to consider. The members of the Remuneration Committee are Simon

Cornwell (Chairman), Tom Nyman and Kent Sander. The Remuneration Committee held one meeting in 2010. The Audit Committee is a body within the company's Board whose duty is to deal with matters regarding tendering for auditors and fees, monitoring audit work and the company's internal control systems, monitoring the current risk outlook, monitoring the external audit, the company's financial information, for example, and other matters the Board assigns the Committee to deal with, on behalf of the Board. The members of the Audit Committee are Tom Nyman (Chairman), Eva Lindqvist and Kent Sander. Apart from through the Audit Committee, contact with the company's auditors is maintained by the company's auditor participating in at least one Board meeting each year. The Audit Committee held three meetings in 2010.

### **Other**

At the end of 2010, the Board of Directors decided to start preparations for a potential listing of the company's shares on Nasdaq OMX Stockholm.

## **Sales and Profits**

Transmode's order intake in 2010 was SEK 723.4 (599.3) m, i.e. an increase of 20.7 (-4.5)% on 2009.

Total sales amounted to SEK 699.3 (570.1) m in 2010, i.e. an increase of 22.7 (-6.1)% on 2009. Exchange rates exerted a negative effect in 2010 compared to 2009, mainly due to depreciation of the euro against the Swedish krona. Adjusted for exchange rate effects, revenues increased by approximately 33% (-11) over the previous year. Sales growth was positive in all three regions: EMEA, the Americas and APAC, especially in the Americas, where invoicing more than doubled. In total, invoicing on markets outside Europe was SEK 105.4 (43.0) m.

Invoicing to the company's five largest customers increased to 48.8 (43.7)% of total.

Gross profit for 2010 amounted to SEK 358.6 (281.6) m. The improvement is mainly a result of a combination of higher sales and wider gross margins at 51.3 (49.4)%. The higher gross margins are mainly a result of an improved customer and product mix, lower purchasing prices and higher volumes. Overall for sales and purchasing, exchange rate fluctuations had a negative effect on gross profit of some SEK 37 (9) m net compared to 2009.

Operating expenses were SEK 248.9 (219.5) m in the period. The cost increase is mainly a result of the company's expansion, and thereby, primarily increased personnel expenses.

In the period January - December 2010, a total of SEK 21.2 (7.7) m was capitalized and SEK 5.6 (3.7) m of capitalized development expenses were amortized.

Almost exclusively, other operating income and expenses consist of exchange rate differences, net of income and expenses. First and foremost, other operating expenses consist of consulting fees and expenses related to the potential initial public offering (IPO).

EBITDA for 2010 was SEK 122.3 (77.3) m, excluding SEK 0.8 (7.3) m expenses attributable to the potential IPO and SEK 121.4 (70.3) including the aforementioned expenses. Operating profit for 2010 was SEK 107.6 (57.4) m.

Net profit after tax for the year was SEK 81.4 (44.3) m.

In 2010, the company had SEK -0.2 (-) m of transactions with related parties. The whole of this expense related to Directors' fees to Board member Gerd Tenzer's wholly owned German company.

## **Cash Flow and Investments**

Transmode's cash flow from operating activities was SEK 133.6 (154.9) m in 2010. Cash flow after financing activities was SEK -90.6 (116.0) m including dividends paid totaling SEK 200.4 (-) m and the net of payments for options received and re-purchased options of a total of SEK 0.6 (1.4) m.

Investments in tangible fixed assets amounted to SEK 3.5 (1.6) m, and in intangible assets, SEK 21.2 (7.7) m.

## Cash and Cash Equivalents, Financing

The group's cash and cash equivalents were SEK 206.0 (299.0) m at year-end 2010. There was an additional SEK 0.5 (1.3) m in blocked funds and unutilized credit facilities of SEK 30.0 (30.0) m. As in 2009, at year-end 2010 there were no interest-bearing liabilities to credit institutions or for finance leases.

## Research and Development

Transmode developed a series of new products and functionality in 2010 so it can address new segments and markets. As previously, product development largely focused on higher capacity and increased coverage, greater flexibility, integrated Ethernet functionality and WDM access.

Migration to access technologies for mobile broadband like HSPA+ and LTE demand the cost-efficient transport of Ethernet traffic right the way to base stations, which has created opportunities for fiber-based solutions. The company's first products in this segment were launched at year-in 2009, and are now being delivered to the majority of customers. These products consist of EMXPs (Ethernet muxponders) and EDUs (Ethernet demarcation units), used to aggregate traffic and create a variety of services at Ethernet level.

The Ethernet products are based on Transmode's Native Packet Optical architecture and enable customers to transport Ethernet traffic cost-efficiently. The company launched several new products including an 80G muxponder in the year. Apart from being able to offer effective transport, these products have qualities that create benefits for financial applications, for example, and for solutions transporting TV and video.

In the access segment, Transmode already has its TG series products, which alongside EDU's and EMXPs, for example, can be used to deliver Gbit and 10 Gbit access.

In terms of increased capacity, the company has launched its first products for transmission speeds of 40 Gbit/s per wavelength.

To enhance the flexibility of networks, the company has now launched an 8-degree ROADM (reconfigurable optical add drop multiplexor). So that customers can get the full benefit from these new units, it is important to be able to offer them good support from a management and maintenance perspective. Accordingly, the TNM (Transmode Network Manager) initiative is a priority segment, where increased resources were allocated in the year.

To participate in and support Swedish research projects within broadband communications, Transmode renewed its membership of SICT Center IBBC, a center of excellence at the ACREO contract research institute. Transmode is also a member of TM Forum—a trade organization promoting standardization in the management and maintenance segment, and MEF, which standardizes and accredits Ethernet products.

The number of employees in R&D including technology and product management as of December 31, 2010 was 89, an increase of 18 on December 2009.

## Quality and Environment

Transmode designs, develops and delivers high-end optical networking solutions. The common feature of all our customers and their applications is that the performance of their optical networks is critical. Accordingly, Transmode has always prioritized quality-related issues in development, production and implementation with the ambition for the company's customers to get the most reliable products and services available on the market.

Transmode's management system has ISO 9001:2008 and ISO 14001:2004 certification. This means that operations are controlled, monitored and improved continuously in accordance with these standards. Quality and environmental goals are an integrated part of the management system of its business, and established and monitored alongside other goals within the company's management activities. Transmode's improvement work is delegated to all groups in the company, with status consolidated at departmental level and reported regularly to management.

Transmode conducts a yearly customer satisfaction survey, achieving an index of 79 on a scale of 1-100 in 2010, which according to research provider Claes Fornell International, CFI Group, is a world-class result.

Transmode worked on mapping the company's environmental impact through its CO<sub>2</sub> emissions in the year. The aim of this work was to be able to monitor and set relevant goals for the long term. The company has chosen to work in accordance with the Greenhouse Gas protocol, a global model to calculate a company's CO<sub>2</sub> impact. In the quality segment, the company implemented a database to rationalize its work on variances and improvements in its business.

Transmode is also continuing to develop products under its 'Low Power Design' banner. They have been well received by customers, thanks to their reduced environmental impact and lower cost.

## **Human Resources**

Transmode's expansion in 2010 meant that by December 31, the company had 197 employees, up by 35 since December 2009. Of this increase, 18 staff are in research and development, including technology and product management, and 9 are in its sales organization. Of the total employee headcount, 31 staff are employed in foreign countries. The average number of full-time employees in 2010 was 181, against 155 in 2009.

In 2010, Transmode strengthened its management team by hiring Britt Alexandersson as HR Director and Dan Rydberg has taken on the role as Operations & Customer Services Vice President on a consultancy basis.

The employee satisfaction survey conducted at year-end 2009 resulted in a global ESI (Employee Satisfaction Index) of 93, a very positive result according to the company's collaboration partner Netsurvey Bolinder AB.

In 2010, Transmode entered agreement to lease new office premises for its head office in Liljeholmen, Stockholm. Transmode plans to start using these new, more contemporary and functional premises at the end of the first quarter of 2011.

## **Operating Risks and Uncertainty Factors**

In its operations, Transmode is exposed to certain risks that can affect its business, earnings or financial position. Some of these risks, and how they are managed, are reviewed below.

The company's sector is changing rapidly, and competition is very intense. Thus, the company's capacity to anticipate market needs and to modify its technology solutions accordingly, is of central significance to its continued success. This is why Transmode has dedicated R&D and marketing resources to monitor market trends, so the company's products remain at the leading edge of technological progress, satisfying customer standards and needs.

The sales cycle of Transmode's products to new customers is fairly lengthy, while its advance planning for customer orders is short. However, Transmode has a broad customer base, which is highly stable, and a significant portion of the company's total sales are sourced from regular repeat orders from existing customers. Transmode diversifies risks further through its end-customers operating different business models and being active on differing geographical markets.

By the nature of its operations, Transmode is dependent on its capacity to hire and retain skilled staff. The company endeavors to be an attractive employer, with a favorable working environment and employment terms at market levels.

In the short term, Transmode is dependent on a limited group of external suppliers of components and product assembly. Transmode reduces this dependency by retaining its core technology skills in-house and endeavoring to collaborate with alternative suppliers.

A global shortage of electrical and optical components applied in 2010. In the year, Transmode strengthened some of its purchasing collaborations and had extra resources in its purchasing function to manage the situation. The company judges that the global component shortage has been managed to minimize delivery delays.

Operations are also dependent on smoothly functioning IT infrastructure, partly for the company's ongoing research and development, and partly to ensure an effective delivery process. Accordingly, IT security is a high priority.

## Financial Risks and Risk Management

Through its international operations, the Transmode group is exposed to financial risks, which are managed according to policies prepared by the Board of Directors. Exposure primarily consists of funding, credit and currency risks. More information on risk exposure is provided in Note 31 of the Annual Report.

To mitigate the extent of short-term effects of exchange rate fluctuations, Transmode enters currency forward contracts to hedge parts of its expected EUR and GBP-denominated inflows, and parts of its expected USD-denominated outflows.

## Parent Company

Transmode Holding AB is the parent company of the Transmode group. The parent company is primarily a holding company, which owns and manages shares in subsidiaries and also sells certain intra-group services to subsidiaries. At year-end 2010, the parent company had 9 (8) employees.

In the period January-December 2010, parent company total sales were SEK 19.7 (14.5) m, all of which relates to invoicing of services sold to subsidiaries. The operating loss was SEK -8.2 (-9.8) m including an expense of SEK 0.8 (7.3) m attributable to the possible IPO. At the end of the calendar year, the parent company had SEK 108.0 (222.3) m of cash and cash equivalents.

## Significant Events after the End of the Financial Year

Kai Hollensett, whose background is with companies including Juniper Networks, was hired as a new Vice President of Sales for Central Europe in early-2011.

## Market Outlook for 2011

The fundamental uncertainties in demand, namely the continued expansion of video and data traffic in fixed and mobile telecom networks, continue. Accordingly, there is also a need to invest in equipment that increases the capacity of optical fiber networks, which also creates opportunities for the company's new solutions such as Mobile Backhaul. Independent researcher Infonetics judges that Transmode's core market, Metro WDM, will grow by an average of 12% annually through the coming years.

Going forward, Transmode's objective remains to outgrow the Metro WDM market, and accordingly, it has continued to invest in segments like product development and sales.

## Proposed Appropriation of Profits of Transmode Holding AB

The following funds are at the disposal of the Annual General Meeting (SEK):

Share premium reserve	100,914,753
Retained profits	-99,358,992
Net profit/loss	<u>91,947,520</u>
Total	93,503,281

The Board of Directors proposes that the funds at the disposal of the Annual General Meeting are appropriated as follows:

- Dividend to holders of class E preference shares (SEK 0.22 per share)	29,846,780
- Dividend to holders of class C, D and F preference shares	-
- Dividend to holders of ordinary shares	-
- Carried forward	<u>63,656,501</u>
Total	93,503,281

Consolidated equity has been stated pursuant to IFRS standards and their IFRIC interpretation statements, and pursuant to Swedish law through application of RFR's (the Swedish Financial Reporting Board) recommendation

RFR 1 (Supplementary Accounting Rules for Groups). Parent company equity has been stated pursuant to Swedish law and by applying RFR 2 (Accounting for Legal Entities).

The Board of Directors' proposed distribution of profits of SEK 29,846,780 to holders of class E preference shares is pursuant to its Articles of Association, which stipulate preferential rights for preference shares. Accordingly, the Board is proposing no dividend to holders of other preference shares (classes C, D and F) or to holders of ordinary shares.

The Board of Directors considers that there is full coverage for the company's restricted equity after the proposed distribution of profits. The Board of Directors considers that the proposed dividend to shareholders is justifiable in terms of the parameters stated in chap. 17 § 3 second and third paragraphs of the Swedish Companies Act (concerning the nature, scope and risks of operations and need to strengthen the Balance Sheet, liquidity and financial position otherwise).

The Board of Directors judges that the company's and the group's equity after the proposed distribution of profits will be sufficient in relation to the nature, scope and risks of operations. In this context, the Board considers factors including the company's and group's historical performance, budgeted performance, investment plans and economic conditions.

The proposed dividend represents 32% of the parent company's non-restricted equity and 5% and 7% of the parent company's and group's total equity respectively. The company's and group's equity/assets ratio is good in the context of prevailing circumstances in the sector. Against this background, the Board thinks that the company and group have good prospects to take future business risks and also to withstand potential losses. Planned investments have been considered when determining the proposed distribution of profits. Nor will the distribution of profits adversely affect the company's and group's capacity to make further business-motivated investments according to its adopted plans.

The proposed distribution of profits will not affect the company's or group's capacity to fulfill their payment obligations on time. The Board has considered other known circumstances that may be significant to the company's and group's financial position and that are not considered within the above framework. Accordingly, no circumstances have arisen that would imply that the proposed dividend does not appear justifiable.

Regarding the company's results of operations and financial position otherwise, the reader is referred to the following Income Statements and Balance Sheets with associated notes. The Annual Accounts and Consolidated Accounts were approved for issue by the Board of Directors on February 25, 2011. The Parent Company and Consolidated Income Statement and Balance Sheet will be subject to adoption at the Annual General Meeting on March 15, 2011.

## Board of Directors' Certification and Signatures

The undersigned hereby certify that the Consolidated Financial Statements and Annual Accounts have been prepared pursuant to IFRS (International Financial Reporting Standards) as endorsed by the EU and generally accepted accounting practice, and give a true and fair view of the group's and the company's financial position and profits, and that the Group Directors' Report and Directors' Report give a true and fair view of the progress of the group's and company's operations, financial position and profits, and review the essential risks and uncertainty factors facing the companies in the group.

Stockholm, Sweden, February 25, 2011

Kent Sander  
*Chairman*

Simon Cornwell

Eva Lindqvist

Tom Nyman

Torbjörn Nilsson

Alex Rogers

Gerd Tenzer

Karl Thedéen  
*CEO*

Our Audit Report was presented on February 25, 2011

PricewaterhouseCoopers AB

Ulf Pettersson  
Authorized Public Accountant

## Summary Consolidated Income Statement

for the financial year as of 31 December

	Note	2010	2009
Sale of goods		662,094	537,942
Sale of services		37,208	32,144
<b>Total sales</b>	3	<b>699,302</b>	<b>570,086</b>
Cost of goods and services provided	5	-340,705	-288,519
<b>Gross profit</b>		<b>358,597</b>	<b>281,567</b>
Other income	4	4,171	2,782
Research and development expenses		-92,119	-78,068
Selling expenses		-130,923	-120,628
Administrative expenses		-25,882	-20,948
Other operating expenses		-6,272	-7,297
<b>Operating profit/loss</b>	5, 6, 7, 8	<b>107,572</b>	<b>57,408</b>
Financial income	9	-336	1,125
Financial expenses	9	-359	-2,394
<b>Net financial income/expenses</b>		<b>-695</b>	<b>-1,269</b>
Taxes	10	-25,478	-11,862
<b>Profit/loss for the year</b>		<b>81,399</b>	<b>44,277</b>
Attributable to:			
Equity holders of the parent company		81,399	44,277
Earnings per share:	11		
– basic		0.868	0.377
– diluted		0.148	0.067

## Summary Consolidated Statement of Comprehensive Income

For the financial year as of December 31

	Note	2010	2009
<b>Profit/loss for the year</b>		<b>81,399</b>	<b>44,277</b>
<b>Other comprehensive income</b>			
Translation difference		-216	259
<b>Other comprehensive income for the period, net after tax</b>		<b>-216</b>	<b>259</b>
<b>Total comprehensive income for the period</b>		<b>81,183</b>	<b>44,536</b>
Attributable to:			
Equity holders of the parent company		81,183	44,536

## Summary Consolidated Balance Sheet

as of December 31

	Note	2010	2009
<b>ASSETS</b>			
<b>Fixed assets</b>			
<i>Intangible assets</i>	14		
Goodwill	15	88,388	88,388
Capitalized development expenses		29,136	14,074
Technology		19,975	24,675
Customer relations		-	250
		<b>137,499</b>	<b>127,387</b>
<i>Tangible assets</i>	13		
Machinery and equipment		6,122	5,976
		<b>6,122</b>	<b>5,976</b>
<i>Financial assets</i>			
Deferred tax asset	10	29,786	55,865
Other financial assets	16	1,156	1,674
		<b>30,942</b>	<b>57,539</b>
<b>Total non-current assets</b>		<b>174,563</b>	<b>190,902</b>
<b>Current assets</b>			
Inventories	18	75,508	34,081
Accounts receivable	19	93,127	148,302
Other current receivables	20	16,129	9,405
Prepaid expenses and accrued income	21	5,682	5,641
Cash and cash equivalents	22	206,047	298,980
<b>Total current assets</b>		<b>396,493</b>	<b>496,409</b>
<b>TOTAL ASSETS</b>		<b>571,056</b>	<b>687,311</b>
<b>EQUITY AND LIABILITIES</b>			
<b>Equity attributable to equity holders of the parent company</b>			
	12, 17, 23		
Share capital		4,880	4,816
Unregistered share capital		-	63
Other contributed capital		619,912	619,343
Other reserves		-721	-505
Accumulated profit or loss		-201,881	-82,865
<b>Total equity</b>		<b>422,190</b>	<b>540,852</b>
<b>Long-term liabilities</b>			
Borrowings	24	-	76
Pension commitments	25, 26	815	499
Other provisions	25	102	-
Deferred tax liability	10	5,253	6,555
<b>Total long-term liabilities</b>		<b>6,170</b>	<b>7,130</b>
<b>Current liabilities</b>			
Accounts payable	27	70,714	66,909
Tax liability		1,858	1,409
Provisions	25	12,130	12,731
Other current liabilities	27	11,775	7,861
Accrued expenses and deferred income	28	46,219	50,419
<b>Total current liabilities</b>		<b>142,696</b>	<b>139,329</b>
<b>TOTAL EQUITY AND LIABILITIES</b>		<b>571,056</b>	<b>687,311</b>

For information on the group's pledged assets and contingent liabilities, see Note 29.

## Summary Consolidated Cash Flow Statement

as of December 31

	Note	2010	2009
<b>Cash flow from operating activities</b>			
Profit/loss after financial items		106,877	56,139
Adjustment for non-cash items			
Depreciation and amortization		13,781	12,644
Profit/loss from disposals and obsolescence of non-current assets		634	-
Change in provisions		-4,695	5,044
Net financial income/expense		695	1,269
Interest paid		-353	-3,089
Interest received		2,448	2,775
Other paid/received financial income/expense		-473	-1,366
Income tax paid		-429	-135
<b>Cash flow from operating activities before changes in working capital</b>		<b>118,485</b>	<b>73,281</b>
Increase(-)/decrease(+) in inventories		-39,341	25,685
Increase(-)/decrease(+) in trade receivables		50,801	16,418
Increase(+)/decrease(-) in trade payables		3,682	39,516
<b>Cash flow from operating activities</b>		<b>133,627</b>	<b>154,900</b>
<b>Cash flow from investing activities</b>			
Acquisitions of intangible assets		-21,170	-7,673
Acquisition of tangible assets		-3,530	-1,565
Change in other financial assets		302	300
<b>Cash flow from investing activities</b>		<b>-24,398</b>	<b>-8,938</b>
<b>Cash flow from financing activities</b>			
Repayment of debt		-	-31,476
New share issue		-	108
Payment for options		689	1,441
Repurchase of options		-119	-26
Dividend to equity holders of the parent		-200,415	-
<b>Cash flow from financing activities</b>		<b>-199,845</b>	<b>-29,953</b>
<b>Decrease/increase in cash and cash equivalents</b>		<b>-90,616</b>	<b>116,009</b>
Cash and cash equivalents, at beginning of year		298,980	184,713
Exchange rate difference in cash and cash equivalents		-2,317	-1,742
<b>Cash and cash equivalents, at end of year</b>		<b>206,047</b>	<b>298,980</b>

## Summary Consolidated Changes in Equity

	Share Capital	Un- registered Share Capital	Other Contributed Capital	Other Reserves	Accum- ulated Profit/loss	Total Equity
<b>Opening balance, January 1, 2009</b>	4,758	57	617,884	-764	-127,142	494,793
<b>Total comprehensive income for the period</b>	-	-	-	259	44,277	44,536
Transactions with shareholders:						
Registration of share capital	57	-57	-	-	-	-
Share exchange/non-cash issue	-	63	-63	-	-	-
New share issue	1	-	107	-	-	108
Payment for options	-	-	1,441	-	-	1,441
Repurchase of options	-	-	-26	-	-	-26
Total transactions with shareholders	58	6	1,459	-	-	1,523
<b>Closing balance, December 31, 2009</b>	4,816	63	619,343	-505	-82,865	540,852
<b>Opening balance, January 1, 2010</b>	4,816	63	619,343	-505	-82,865	540,852
<b>Total comprehensive income for the period</b>	-	-	-	-216	81,399	81 183
Transactions with shareholders:						
Registration of share capital	64	-63	-1	-	-	-
Share exchange/non-cash issue	-	-	-	-	-	-
New share issue	-	-	-	-	-	-
Payment for options	-	-	689	-	-	689
Repurchase of options	-	-	-119	-	-	-119
Dividend to equity holders of the parent	-	-	-	-	-200,415	-200,415
Total transactions with shareholders	64	-63	569	-	-200,415	-199,845
<b>Closing balance December 31, 2010</b>	4,880	-	619,912	-721	-201,881	422,190

## Parent Company Income Statement

for the financial year as of December 31

	Note	2010	2009
Sale of services		19,651	14,508
<b>Total sales</b>		<b>19,651</b>	<b>14,508</b>
Other revenues		53	-
Administrative expenses		-27,858	24,235
Other operating expenses		-	-42
<b>Operating profit/loss</b>	6,7	<b>-8,154</b>	<b>-9,769</b>
Financial income	9	99,652	6,513
Financial expenses	9	0	-9
<b>Net financial income/expenses</b>		<b>99,652</b>	<b>6,504</b>
Taxes	10	450	807
<b>Profit/loss for the year</b>		<b>91,948</b>	<b>-2,458</b>

## Summary Parent Company Statement of Comprehensive Income

For the financial year as of December 31

	Note	2010	2009
<b>Profit/loss for the year</b>		<b>91,948</b>	<b>-2,458</b>
<b>Other comprehensive income</b>			
Translation difference		-	-
Income taxes attributable to components of other comprehensive income		-	-
<b>Other comprehensive income for the period, net after tax</b>		<b>-</b>	<b>-</b>
<b>Total comprehensive income for the period</b>		<b>91,948</b>	<b>-2,458</b>
Attributable to:			
Equity holders of the parent company		91,948	-2,458

## Parent Company Balance Sheet

as of December 31

	Note	2010	2009
<b>ASSETS</b>			
<b>Fixed assets</b>			
<i>Financial assets</i>			
Participations in group companies	33	369,377	369,377
Receivables from group companies		95,742	95,742
Deferred tax asset	10	8,999	8,549
Other financial assets		469	252
<b>Total non-current assets</b>		<b>474,587</b>	<b>473,920</b>
<b>Current assets</b>			
Receivables from group companies		11,053	-
Other current receivables		309	259
Prepaid expenses and accrued income		91	127
Cash and cash equivalents		108,027	222,329
<b>Total current assets</b>		<b>119,480</b>	<b>222,715</b>
<b>TOTAL ASSETS</b>		<b>594,067</b>	<b>696,635</b>
<b>EQUITY AND LIABILITIES</b>			
<b>Equity</b>	17, 23		
<i>Restricted equity</i>			
Share capital		4,880	4,816
Unregistered share capital		-	63
Statutory reserve		482,921	482,921
		<b>487,801</b>	<b>487,800</b>
<i>Non-restricted equity</i>			
Share premium reserve		100,914	100,345
Profit/loss brought/carried forward		-99,359	103,514
Profit/loss for the year		91,948	-2,458
		<b>93,503</b>	<b>201,401</b>
<b>Total equity</b>		<b>581,304</b>	<b>689,201</b>
<b>Provisions</b>			
Provisions for pensions		582	314
Other provisions		2,290	1,282
<b>Total provisions</b>		<b>2,872</b>	<b>1,596</b>
<b>Current liabilities</b>			
Accounts payable		902	325
Tax liabilities		445	659
Other current liabilities		1,471	1,807
Accrued expenses and deferred income	28	7,073	3,047
<b>Total current liabilities</b>		<b>9,891</b>	<b>5,838</b>
<b>TOTAL EQUITY AND LIABILITIES</b>		<b>594,067</b>	<b>696,635</b>
<b>Pledged assets and contingent liabilities – parent company</b>			
<i>Pledged assets</i>			
		None	None
<i>Contingent liabilities</i>			
		None	None

## Parent Company Cash Flow Statement

as of December 31

	Note	2010	2009
<b>Cash flow from operating activities</b>			
Profit/loss after financial items		91,498	-3,265
Adjustment for non-cash items			
Change in provisions		1,276	344
Net financial income/expense		-99,652	-6,504
Interest paid		-	-
Interest received		6,264	6,505
Other paid/received financial income/expense		-1	-9
<b>Cash flow from operating activities before changes in working capital</b>		<b>-615</b>	<b>-2,929</b>
Increase(-)/decrease(+) in trade receivables		82,323	5,500
Increase(+)/decrease(-) in trade payables		4,053	-257
<b>Cash flow from operating activities</b>		<b>85,761</b>	<b>2,314</b>
<b>Cash flow from investing activities</b>			
Change in other financial assets		-217	126,891
<b>Cash flow from investing activities</b>		<b>-217</b>	<b>126,891</b>
<b>Cash flow from financing activities</b>			
Payment for options		689	1,441
Repurchase of options		-119	-26
New share issue		-	108
Dividend to equity holders of the parent		-200,415	-
<b>Cash flow from financing activities</b>		<b>-199,845</b>	<b>1,523</b>
<b>Decrease/increase in cash and cash equivalents</b>		<b>-114,301</b>	<b>130,728</b>
Cash and cash equivalents, at beginning of year		222,329	91,603
Exchange rate difference in cash and cash equivalents		-1	-2
<b>Cash and cash equivalents, at end of year</b>		<b>108,027</b>	<b>222,329</b>

## Parent Company Changes in Equity

	Share Capital	Unreg. Share Capital	Statutory Reserve	Share Premium Reserve	Accum- ulated Profit/loss	Total Equity
<b>Opening balance, January 1, 2009</b>	4,758	57	482,921	96,985	103,514	688,235
Profit/loss for the year	-	-	-	-	-2,458	-2,458
Total recognized income and expenses	-	-	-	-	-2,458	-2,458
Transactions with equity holders:						
Registration of new share issue	57	-57	-	-	-	-
Non-cash issue in progress	-	63	-	1,838	-	1,901
New share issue	1	-	-	107	-	108
Payment for options	-	-	-	1,441	-	1,441
Repurchase of options	-	-	-	-26	-	-26
Total transactions with equity holders	58	6	-	3,360	-	3,424
<b>Closing balance, December 31, 2009</b>	4,816	63	482,921	100,345	101,056	689,201
<b>Opening balance, January 1, 2010</b>	4,816	63	482,921	100,345	101,056	689,201
Profit/loss for the year	-	-	-	-	91,948	91,948
Total recognized income and expenses	-	-	-	-	91,948	91,948
Transactions with equity holders:						
Registration of new share issue	64	-63	-	-1	-	-
Payment for options	-	-	-	689	-	689
Repurchase of options	-	-	-	-119	-	-119
Dividend to equity holders of the parent	-	-	-	-	-200,415	-200,415
Total transactions with equity holders	64	-63	-	569	-200,415	-199,845
<b>Closing balance, December 31, 2010</b>	4,880	-	482,921	100,914	-7,411	581,304

## Note 1 Corporate Information

The Consolidated Accounts of Transmode Holding AB (556588-9101) for the financial year 2010 were approved for issue in accordance with a decision by the Board of Directors on February 25, 2011. Transmode Holding AB is a limited company incorporated and domiciled in Stockholm, Sweden.

Transmode is a leading provider of optical network solutions for transporting data, voice and video traffic based on CWDM and DWDM (coarse/dense wavelength division multiplexing) technology.

Transmode's unique concept Intelligent WDM (iWDM™) has resulted in over 20,000 installed systems with over 300 fixed and mobile telecom operators, cable TV operators, Internet service providers and large corporations and public institutions across Europe, the Americas and Asia. With its broad product portfolio addressing regional networks, metro core, access and large corporate networks, as well as secure global organizational resources, Transmode helps customers enhance network capacity, quality of service and functionality in a cost-efficient manner.

## Note 2.1 Basis of Preparation of the Consolidated Accounts and Annual Accounts

The Consolidated Accounts and Annual Accounts have been prepared according to the cost method. The Consolidated Accounts are presented in Swedish kronor and all values are rounded to the nearest thousand Swedish kronor (SEK 000) unless otherwise indicated.

### Statement of Compliance

The Consolidated Accounts have been prepared in accordance with the Swedish Annual Accounts Act, RFR 1 Supplementary Accounting Rules for Groups and IFRS (International Financial Reporting Standards) as endorsed by the EU.

The parent company Annual Accounts have been prepared pursuant to the Swedish Annual Accounts Act and RFR 2, Accounting for Listed Legal Entities, implying the parent company reporting pursuant to the same principles as the group subject to the exemptions stated in "parent company accounting principles".

### New and Revised Standards Applied by the Group

A review of the standards and interpretation statements on existing standards that have been published and are obligatory for the group for financial years starting January 1, 2010 or later follows. These standards and amendments have not been applied in advance. The review covers those standards and interpretation statements that management considers relevant for the group but have not yet had any effect on the group as of the reporting date.

IAS 27 (amendment), "Consolidated and Separate Financial Statements." This revised standard requires that the effects of all transactions with holders with non-controlling influence are reported in equity if they do not imply any change to the controlling influence and the transactions no longer give rise to goodwill or gains or losses. The standard also states that when a parent company relinquishes the controlling influence potential residual participation should be restated at fair value and a gain or loss reported in the Income Statement.

IFRS 3 (revised), "Business Combinations." This revised standard continues to prescribe that the purchase method of accounting is used for business combinations but with some material changes. For example, all payments to acquire an operation at fair value are reported as of the acquisition date, while subsequent conditional payments classified as liabilities that are subsequently restated via the Income Statement. There is freedom of choice regarding measuring holdings with non-controlling influence in the acquired operation at fair value or the proportional share of the acquired operation's net assets held by the holder with non-controlling influence. All transaction expenses regarding business combinations should be expensed. This amendment did not have any material effect on the Consolidated Accounts.

Other standards and interpretation statements to be applied from 2010 onwards are not judged to be relevant and have no effect on the group.

## **Standards, Amendments and Interpretation Statements on Existing Standards where the Amendment Has Not Yet Come into Effect and Has Not Been Applied in Advance by the Group**

IFRS 9, "Financial Instruments" (published November 2009). This standard will replace IAS 39, "Financial Instruments: Recognition and Measurement." IFRS 9 introduces two new requirements for the recognition and measurement of financial assets, and will probably affect the group's reporting of financial assets. This standard is not applicable before financial years that start January 1, 2013 but is available for advance adoption. However, the standard has not yet been endorsed by the EU. The group still has to evaluate the full impact of IFRS 9 on its financial statements.

IAS 24 (revised), "Related Party Disclosures," issued in November 2009. This replaces IAS 24 "Related Party Disclosures," issued in 2003. IAS 24 (revised) should be applied for financial years that start on January 1, 2011 or later. Advance adoption of the standard is permitted, wholly or partly. The revised standard clarifies and simplifies the definition of a related party.

Several other amendments of standards and new statements have been published, but at present, they are not judged to have any impact on the company's financial statements.

## **Note 2.2 Significant Accounting Judgments and Estimates**

### **Judgments**

When applying the group's accounting principles, management and the Board of Directors have made the following judgments in addition to those encompassing calculations, which have the greatest effect on the amounts recognized in the financial statements:

#### **Basis for Consolidation**

The Consolidated Accounts encompass the legal parent Transmode Holding AB and its subsidiaries as of December 31, each year. Because Transmode Holding AB (formerly Lumentis AB) was acquired in a reverse acquisition in 2005, the Consolidated Accounts have been prepared based on Transmode Holding AB being the actual subsidiary. The subsidiaries' Annual Accounts are prepared for the same financial year as the parent company's, using consistent accounting principles.

#### **Classification of Lease Arrangements**

Lease arrangements where Transmode is the lessee and bears the majority of the risks and rewards associated with the assets are treated as finance leases and recognized as assets in the Balance Sheet.

#### **Estimation Uncertainty**

The key assumptions concerning the future and other sources of estimation uncertainty at the reporting date that have a significant risk of causing a material adjustment of carrying amounts of assets and liabilities within the next financial year are discussed below:

#### **Impairment Testing of Goodwill**

The group determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the recoverable amount of cash-generating units to which the goodwill is allocated. Estimating the value in use requires the group making an estimate of the expected future cash flows from the cash-generating unit and also selecting a suitable discount rate to calculate the present value of these cash flows. The carrying amount of goodwill at December 31, 2010 was 88,388 (88,388). See Note 15.

#### **Capitalized Development Expenses**

The company has capitalized its development expenses from the financial year 2008 onwards pursuant to IAS 38. In product development there is primarily an inherent risk of whether development will result in future revenues. The company makes regular assessments of projects on an aggregate level. Capitalized development expenses are amortized during product's estimated economic lives, although subject to a maximum of 3 years. The carrying amount of capitalized development expenses as of December 31, 2010 was 29,136 (14,074). See Note 14.

**Deferred Tax Assets**

As of December 31, 2010, Transmode had un-utilized tax losses for Transmode Holding AB and Transmode Systems AB in Sweden of a total of 107,623 (201,556). The Board of Directors' judgment as of December 31, 2010 is that it remains likely that for the foreseeable future, the company's taxable income in Sweden will exceed total tax losses. The background to this judgment is partly in the continued positive profit performance the company has achieved historically, with, for example, positive consolidated profit before tax in all quarters of 2007-2010. Additionally, in those assumptions regarding the company's future progress that are also the basis of the company's potential testing for impairment of goodwill. As of December 31, 2010, the company reported a tax asset of 29,786 (55,865) under the balance sheet item "Deferred tax assets." See Note 10.

**Inventory Obsolescence**

Inventory is reported at the lower of cost, in accordance with the first in first out (FIFO) method, and net realizable value. The estimated net realizable value includes management's consideration of outdated items, over-stocking, physical damage, inventory lag-time, handling and other selling costs. If the estimated net realizable value is lower than historical cost, a valuation allowance for inventory obsolescence is established. The total inventory value, net of inventory obsolescence is 75,508 (34,081) as of December 31, 2010. The provision for obsolescence amounts to 17,778 (19,864). See Note 18.

**Credit Loss Reserves**

The establishment of credit loss reserves on accounts receivable is dependent on estimates including assumptions regarding past dues, repossession rates and the recovery rate on underlying collateral. As of December 31, 2010, Transmode's total credit loss reserve was 1,762 (4,112). See Note 19.

## Note 2.3 Summary of Significant Accounting Principles

### **Consolidation**

All subsidiaries are entities whose financial and operating principles the group is authorized to control. Generally the parent company has a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the group. They are de-consolidated from the date that control ceases.

The purchase method of accounting is used to recognize the acquisition of subsidiaries by the group. The transferred remuneration for an acquisition consists of the fair value of assets submitted as payment and liabilities arising or taken over as of the transfer date. Transaction expenses attributable to the acquisition are expensed as they arise. For each acquisition, the group decides if all holdings with non-controlling influence in the acquired company are reported at fair value or the holding's proportional share of the acquired company's net assets. The amount whereby the transferred remuneration, potential holdings with non-controlling influence and fair value at the acquisition date of previous shareholdings exceeds the fair value of the group's share of the identifiable net assets is reported as goodwill. If the transferred remuneration is less than the fair value of the net assets acquired, the difference is recognized directly in the Income Statement.

All intra-group balances, income, profits and losses from intra-group transactions are fully eliminated.

### **Foreign Currency Translation**

The Consolidated Accounts are presented in Swedish kronor (SEK), which is the company's functional and presentation currency. Each entity in the group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency. Transactions in foreign currencies are initially reported at the functional currency rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are re-translated at the functional currency rate of exchange ruling at the reporting date. All differences are recognized in the Income Statement. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions.

The results of operations and financial position of all group entities that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- Assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet.
- Income and expense for each income statement are translated at average exchange rates.
- All exchange differences are recognized as a separate component of equity.

### **Revenue Recognition**

Revenue covers the fair value of what has been received or will be received for sold goods and services in the group's operating activities. Revenues are recognized excluding VAT, returns and discounting and after eliminating intragroup sales.

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognized:

#### **Sale of Goods**

Revenue is recognized when the significant risks and rewards associated with ownership of the goods have passed to the buyer.

#### **Rendering of Services**

Revenue from services is recognized according to the percentage of completion method by reference to the stage of completion. Stage of completion depends upon the service provided, i.e. measured with reference to labor hours incurred to date as a percentage of total estimated labor hours for each contract or equally divided by month during the period which each contract covers. Where the contract outcome cannot be measured

reliably, revenue is recognized only to the extent of the expenses recognized that are recoverable. In cases of doubtful debt, the full loss is immediately expensed.

### **Government Assistance**

Government subsidies are recognized as revenue when there is reasonable certainty that the company satisfies the conditions for receiving the subsidy.

### **Interest Income**

Interest income is recognized as interest accrues using the effective interest method, that is the rate that exactly discounts estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset.

## **Segment Reporting**

Operating segments should be reported in the same way as internal reporting to the senior executive decision-maker. In Transmode, this party has been identified as the company's Chief Executive Officer. The CEO mainly monitors the company's operations at customer and product levels. From Transmode's perspective, the risks and opportunities are similar for its various customers, which means that Transmode has a single segment.

Operations are conducted from the starting-point of Sweden, from where all invoicing to customers is executed and where, almost exclusively, all assets are located.

## **Income Statement Classified by Function**

Transmode reports research & development, selling and administrative expenses. Each function includes its own direct expenses as well as an allocated part of common expenses. The cost of goods sold and services rendered includes direct costs and an allocated part of common costs connected with the generation of revenue. Amortization of the intangible assets Technology and Capitalized Development Expenses is included in Research & Development Expenses and amortization of the intangible asset Customer Relations is included in Selling Expenses.

## **Tangible Fixed Assets**

Tangible fixed assets are stated at cost, less accumulated depreciation and accumulated impairment in value. Expenditure that arises after acquisition is included in the carrying amount of the asset only to the extent it is likely that the group will receive significant future economic benefits from the asset. Depreciation is calculated on a straight-line basis over the economic life of assets.

The carrying amounts of the tangible fixed assets are reviewed for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable.

A tangible fixed asset is derecognized upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognizing the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the Income Statement in the year the asset is derecognized.

The residual values and economic lives are reviewed, and adjusted if appropriate, at least at each financial year-end.

## Taxes

### Current Tax

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws utilized to compute the amount are those that are enacted or substantively enacted by the reporting date.

### Deferred Tax

Deferred tax is stated on temporary differences between the tax bases of assets and liabilities at the reporting date and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognized for all taxable temporary differences, except:

- where the deferred tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognized for all deductible temporary differences and unutilized tax losses, to the extent that it is probable that a taxable profit will be available against which the deductible temporary differences and the carrying amount of un-utilized tax credits and un-utilized tax losses can be utilized except:

- where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the reported profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries, deferred tax assets are recognized only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilized.

The carrying amount of deferred income tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilized. Unrecognized deferred income tax receivables are re-assessed at each reporting date and are recognized to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the reporting date.

Income tax relating to items recognized directly in equity and other comprehensive income is recognized in equity and other comprehensive income and not in the Income Statement.

Deferred tax assets and deferred tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

### Value-added Tax

Revenues, expenses, assets and liabilities are recognized net of the amount of VAT except:

- Where the VAT incurred on a purchase of assets or services is not recoverable from the taxation authority, in which case the VAT (sales tax) is recognized as part of the cost of acquisition of the asset or as part of the expense item as applicable and
- Accounts receivable and accounts payable that are stated with the amount of VAT included.

The amount VAT recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the Balance Sheet.

## Goodwill

Goodwill acquired in a business combination is initially measured at cost, being the excess of the transferred remuneration of the business combination over the group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that the carrying amount may be impaired.

For the purpose of impairment testing, from the acquisition date, goodwill acquired in a business combination is allocated to each of the group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the group are assigned to those units or groups of units. Each unit or group of units which the goodwill is so allocated:

- represent the lowest level within the group at which the goodwill is monitored for internal management purposes and
- is not larger than a segment based on the group's primary segment reporting.

Impairment is determined by assessing the recoverable amount of the cash-generating unit (group of cash-generating units) to which the goodwill relates. When the recoverable amount of the cash-generating unit (group of cash-generating units) is less than the carrying amount, impairment is recognized. Where goodwill forms part of a cash-generating unit (group of cash-generating units) and part of the operation within that Unit is disposed of, goodwill is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

## Intangible Assets apart from Goodwill

Intangible assets acquired separately are initially recognized at cost. The cost of intangible assets acquired in a business combination is the fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses.

An intangible asset originating from development expenses of products for commercial or internal use is reported on the basis of the product judged to be technically and economically sound until the product is ready for commercial launch or starts usage in the company. The capitalized development expenses are primarily internally generated, and consist of direct expenses incurred for labor and the related portion of indirect expenses. The amortization of capitalized development expenses starts coincident with the commercial launch, or when the product comes into internal use.

The economic lives of intangible assets, excluding goodwill, are assessed to be finite, amortized over economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method for an intangible asset are reviewed at least at each financial year-end. Changes in the expected economic life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for by changing the amortization period or method, as appropriate, and treated as changes in accounting estimates.

Gains or losses arising from derecognizing an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognized in the Income Statement when the asset is derecognized.

## Impairment of Assets

The group assesses at each reporting date whether there is an indication that an asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the group makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use and is determined for an individual asset, if the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risk specific to the asset. Impairment losses of continuing operations are recognized in the Income Statement.

An assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognized impairment loss is reversed only if there has been a change in the estimates utilized to determine the asset's recoverable amount since the impairment loss was recognized. Goodwill impairment cannot be reversed. If that is the case, the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in the Income Statement unless the asset is carried at revalued amount, in which case the reversal is treated as a revaluation increase. After such a reversal, the depreciation charge is adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining economic life.

## **Investments and Other Financial Assets**

When financial assets are recognized initially, they are measured at fair value less directly attributable transaction costs apart from for financial assets, which are measured at fair value in the Income Statement where transaction expenditure is immediately expensed. The group determines the classification of its financial assets on initial recognition.

### **Loans and Accounts Receivable**

Loans and accounts receivable are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are carried at amortized cost. Gains and losses are recognized in the Income Statement when the loans and receivables are derecognized or impaired. The group primarily holds financial instruments in this category.

## **Derivative Instruments**

Derivative instruments consist of currency forward contracts used to limit the risk of exchange rate fluctuations. The actual value of derivative instruments is reported as Other current receivables or Other current liabilities. Value increases and decreases on derivatives are reported as revenues or expenses respectively in operating profit/loss or in net financial income/expense depending on the purpose of the derivative instrument and whether its usage relates to a trading item or a financial item. Exchange gains and exchange losses are reported net in operating profit/loss and net financial income/expense respectively. The Company has not applied hedge accounting when utilizing currency forward contracts.

## **Inventories**

Inventories are valued at the lower of cost, in accordance with the first in first out method, and net realizable value.

## **Accounts Receivable**

Accounts receivable, which have 30-day payment terms as standard adjusted for local market conditions, are recognized at original invoiced amount less an allowance for any uncollectible amounts. A provision is recognized when there are strong indications that the group will not be able to receive payment. Bad debt is written off when it is definitively determined that no payment will be received.

## **Cash and Cash Equivalents**

Cash and cash equivalents in the Balance Sheet encompass cash at bank and in hand and short-term deposits with an original maturity of three months or less. For the purpose of the Consolidated Cash Flow Statement, cash and cash equivalents consists of cash and cash equivalents as defined above, net of outstanding bank overdrafts.

## **Interest-bearing Loans and Borrowings**

All loans and borrowings are initially recognized at the fair value of the consideration received. After initial recognition, interest-bearing loans and borrowings are subsequently recognized at amortized cost.

## **Borrowing Costs**

Borrowing costs directly attributable to the purchase, completion or production of a qualifying asset are capitalized as a part of the cost of the asset. Other borrowing costs are charged to profit as an expense for the period to which they relate.

## **Provisions**

Provisions are recognized when the group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. When the group expects some or all of the provision to be reimbursed, for example in an insurance contract, the reimbursement is recognized as a separate asset, but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the Income Statement net of any reimbursement. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liability. Where discounting is utilized, the increase in the provision due to the passage of time is recognized as a borrowing cost.

## **Pensions and Other Post-employment Benefits**

In the group there are mainly defined contribution plans. The group has one defined benefit plan, which is a multi-employer plan.

### **Defined Contribution Plans**

The group's payments relating to defined contribution plans are reported as an expense during the period the employee has rendered services to which the contribution relates.

### **Defined Benefit Plan**

Pension obligations for employees in Sweden are vested partly through insurance with Alecta. According to pronouncement UFR 3 Issued by the Swedish Financial Reporting Board (*Rådet för finansiell rapportering*) the plan is to be classified as a multi-employer defined benefit plan. Transmode does not have access to such information that makes it possible to report this plan as a defined benefit plan. The ITP pension plan that is vested through insurance with Alecta is therefore reported as a defined contribution plan.

## **Share-based Payment Transactions**

There are equity settled option schemes. For all option schemes, the participants have paid fair value for the options; hence the programs have no effect on the profit or loss of the Transmode group.

## **Leases**

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement and requires an assessment of whether the fulfillment of the arrangement is dependent on the use of a specific asset and the arrangement conveys a right to use the asset.

### **The Group as Lessee**

Finance leases, which transfer to the group substantially all the risks and rewards incidental to ownership of the leased item, are capitalized at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charge directly to the Income Statement.

Capitalized leased assets are depreciated over the shorter of the estimated economic life of the asset and the lease term, if there is no reasonable certainty that the group will obtain ownership by the end of the lease term.

Operating lease payments are recognized as an expense in the Income Statement on a straight-line basis over the lease term.

## **Earnings per Share**

*Basic earnings per share* are calculated by dividing the profit/loss attributable to equity holders of the parent company, adjusted by stipulated preference dividends for cumulative preference shares entitled to dividends for the period, by the weighted average number of ordinary shares in issue during the year.

*Diluted earnings per share* are calculated by adjusting the weighted average number of ordinary shares for the dilution effect of all potential ordinary shares. Potential dilution effects arise through the convertible preference shares and share options. If outstanding convertible preference shares were converted, this would result in a reduction of preference dividends, if applicable, and an increase in the number of shares that may have a net dilution effect on earnings per share. For the share options, a calculation is made in order to determine the number of shares that could have been acquired at fair value, determined as the last used issued ordinary share price of the parent company's shares, based on the monetary value of the subscription rights attached to outstanding share options. The number of shares calculated as above is compared with the number of shares that would have been issued assuming the exercise of the share options. Dilution effects are only considered when they have an adverse effect on earnings per share.

## **Note 2.4 Parent Company Accounting Principles**

The difference in accounting principles in the parent company's Annual Accounts and the Consolidated Accounts are due to the fact that the parent company must observe the Swedish Annual Accounts Act and the Swedish Financial Reporting Board's recommendation RFR 2, Accounting for Legal Entities. The accounting principles of the parent company that differ from the group's are reviewed below. Apart from differences in accounting principles, there are some differences in disclosure requirements, which to some extent, limit disclosures regarding the parent company.

### **Shares in Subsidiaries**

Shares in subsidiaries are carried in the Balance Sheet at cost less any impairment charges. An impairment test is conducted if there is indication that recoverable value is less than book value.

### **Group contributions**

Group contributions are reported in accordance with UFR 2. Group contributions that have been paid or received by the parent company with the aim of minimizing the group's total tax are recognized directly against accumulated profit or loss after deducting for current tax. Shareholders' contributions made by the parent company are reported in shares and participations.

### **Presentation of Equity**

In the parent company's financial statements, equity is divided into restricted and unrestricted equity due to the stipulation in the Swedish Annual Accounts Act, which is not required under IFRS and therefore, no division is effected in the Consolidated Accounts.

### Note 3 Sales

<i>Group</i>	2010	2009
Sweden	101,253	85,576
EMEA excluding Sweden	492,464	440,840
Americas	93,889	41,324
APAC	11,696	2,346
Total	<u>699,302</u>	<u>570,086</u>

There are 3 (2) customers that each represent over 10% of total sales. Together, these customers' share amounts to 37 (25)% of total sales.

### Note 4 Other Income

Other income is 4,171 (2,782), of which 4,155 (2,584) consists of net exchange rate gains attributable to trade receivables and trade liabilities, 15 (198) consists of insurance claims and other items amount to 1 (-).

### Note 5 Expenses by Category

	2010	2009
Cost of goods and services provided	-340,705	-288,519
Other expenses	-59,734	-64,294
Personnel expenses	-181,681	-150,003
Depreciation and amortization of intangible and tangible fixed assets	-13,781	-12,644
Total operating expenses	<u>-595,901</u>	<u>-515,460</u>

### Note 6 Auditors' Fees

<i>Group</i>	2010	2009
<b>PricewaterhouseCoopers</b>		
Audit assignment	925	803
Auditing services over and above audit assignment	42	167
Tax advisory services	69	236
Other services	41	225
Total, PricewaterhouseCoopers	<u>1,077</u>	<u>1,431</u>
<b>The MGroup</b>		
Audit assignment	47	-
Auditing services over and above audit assignment	-	-
Tax advisory services	-	-
Other services	210	-
Total, MGroup	<u>257</u>	<u>-</u>
Total	<u>1,334</u>	<u>1,431</u>

Auditing means the auditor's reimbursement for the statutory audit, i.e. the work necessary to submit the Audit Report. This also includes fees for audit advisory services provided in tandem with the audit assignment.

In principle, auditing services over and above the audit assignment relate to quality-assurance services pursuant to the Swedish Auditors' Act. This Act stipulates that auditing activities are partly the review of administration or accounting information to be conducted according to constitution, statute or contract and should result in a report or other documentation intended for parties other than the client, and advisory services ensuring from observations from a review assignment.

Tax advisory services are evident from the statement itself. Other services means advisory services that are not related to any of the stated services assignments.

*Parent company*

The audit of the parent company for the financial years 2010 and 2009 was conducted by PricewaterhouseCoopers and invoiced to Transmode Systems AB. However, in the year, the parent company incurred audit expenses of 21 (-) and purchased 100 (47) of other services from PricewaterhouseCoopers, consisting of 33 (-) of auditing services over and above the audit assignment, 37 (-) of tax advisory services and 30 (47) of other services.

## Note 7 Employee Benefits

### Ave. Number of Employees

<i>Group</i>	2010	Of which Men	2009	Of which Men
Sweden	160	81%	145	83%
UK	8	100%	7	100%
Germany	6	100%	-	-
USA	5	100%	1	100%
Canada	1	100%	1	100%
Italy	1	100%	1	100%
Group total	181	83%	155	85%

<i>Parent company</i>	2010	Of which Men	2009	Of which Men
Sweden	8	50%	8	50%
Parent company total	8	50%	8	50%

### Division between the Sexes, Group (incl. Subsidiaries) for Board Members and other Senior Management

<i>Group</i>	2010	Of which Men	2009	Of which Men
Board members apart from CEO Chief Executive Officer and other senior management	7	86%	6	83%
Group total	8	88%	7	100%
Group total	15	87%	13	92%

### Salary and Other Benefits, Social Security Contributions

<i>Group</i>	2010	2009		
	Salary and Benefits	Social Security Contributions	Salary and Benefits	Social Security Contributions
(of which pension expenses) <sup>1</sup>	123,919	50,210 (14,263) <sup>1</sup>	107,813	44,846 (12,839) <sup>1</sup>

<sup>1</sup> No pension expenses relate to the Board of Directors for 2010 or 2009.

<i>Parent company</i>	2010	2009		
	Salary and Benefits	Social Security Contributions	Salary and Benefits	Social Security Contributions
(of which pension expenses)	11,357	6,525 (1,704)	8,392	5,127 (1,583)

## Salary and Benefits by Country and between Chief Executive Officer, Board of Directors and Other Employees

<i>Group</i>	2010		2009	
	CEO and Board	Other Employees	CEO and Board	Other Employees
Sweden	5,089	90,019	3,661	91,203
Germany	-	7,827	-	-
UK	-	7,656	-	8,068
USA	-	9,344	-	1,780
Canada	-	2,366	-	2,283
Italy	-	718	-	818
Group total	<u>5,089</u>	<u>118,830</u>	<u>3,661</u>	<u>104,152</u>

For more information, see Note 30.

<i>Parent company</i>	2010		2009	
	CEO and Board	Other Employees	CEO and Board	Other Employees
Sweden	5,089	6,268	3,661	4,731
Parent company total	<u>5,089</u>	<u>6,268</u>	<u>3,661</u>	<u>4,731</u>

### Incentive Schemes

The group has a total of 48,658,989 (40,149,989) share warrants issued to employees. For more information, refer to Note 17.

<b>Sickness absence group</b>	2010	2009
Total sickness absence as a proportion of scheduled working-hours	2%	3%
Proportion of total sickness absence relating to continuous sickness absence of 60 days or more	61%	52%
Sickness absence by sex:		
Men	2%	3%
Women	1%	2%
Sickness absence by age group:		
Up to 29	1%	2%
30-49	2%	2%
50 or above	5%	6%

### Sickness Absence, Parent Company

Not disclosed because the number of employees does not exceed 10.

## Note 8 Depreciation, Amortization and Impairment Losses

<b>Group</b>	2010	2009
<i>Depreciation and amortization by asset</i>		
Capitalized development expenses	5,609	3,666
Technology	4,700	4,700
Customer relations	250	1,000
Machinery and equipment	3,222	3,278
Total	<u>13,781</u>	<u>12,644</u>
<i>Depreciation and amortization by function</i>		
Cost of goods and services provided	733	871
Research and development expenses	12,135	10,122
Selling and marketing expenses	877	1,614
Administrative expenses	36	37
Total	<u>13,781</u>	<u>12,644</u>

## Note 9 Financial Income and Expenses

<b>Group</b>	2010	2009
<i>Financial income</i>		
Interest income	2,462	2,760
Exchange losses	-2,798	-1,635
Total	-336	1,125
<i>Financial expenses</i>		
Interest expenses to credit institutions	-	-1,868
Other interest and financial expenses	-366	-347
Exchange gains/losses	7	-179
Total	-359	-2,394
<b>Parent company</b>		
	2010	2009
<i>Financial income</i>		
Interest income	1,897	1,509
Interest income from group companies	4,359	5,005
Anticipated dividend from group companies	93,397	-
Exchange losses	-1	-1
Total	99,652	6,513
<i>Financial expenses</i>		
Other interest expenses and financial expenses	-1	-9
Exchange gains/losses	1	0
Total	0	-9

## Note 10 Taxes

### Group

The dominant constituent components of tax expenses for the financial years are:

	2010	2009
<i>Current tax</i>		
Tax on profit/loss for the year	-634	-273
Tax attributable to previous year	-68	-105
<i>Deferred tax</i>		
Occurrence and reversal of temporary differences	-24,776	-11,484
Effect of change in Swedish tax rate	-	-
Total tax	-25,478	-11,862

Reconciliation between tax expense and recognized profits multiplied by the Swedish tax rate for the financial years as of December 31 is as follows:

	2010	2009
Recognized profit before tax	106,877	56,139
Tax calculated on Swedish enacted tax rate, 26.3 (26.3)%	-28,109	-14,764
Tax attributable to previous year	-68	-105
Utilized loss carry-forwards previously not recognized	-134	291
Non-taxable income	0	5
Non-deductible expenses	-707	-627
Effect of higher/lower tax rates for foreign subsidiaries	131	-70
Tax effect of goodwill amortization, group companies	3,409	3,409
Deductible deficits for which no deferred tax asset is reported	-	-1
Tax recognized in the Consolidated Income Statement	-25,478	-11,862

<i>Current tax</i>	2010	2009
Sweden	26.3%	26.3%
UK	21.0%	21.0%
Singapore	17.0%	17.0%
USA	30.7%	23.8%
Canada	30.0%	33.0%
Italy	31.4%	31.4%
Germany	29.8%	30.0%

Deferred tax assets are attributable to the following:

<i>Deferred tax asset</i>	2010	2009
Income taxes recoverable to offset against future tax expenses	28,305	53,009
Provisions for pensions	198	131
Provisions for guarantees	526	526
Other	757	2,199
Total	29,786	55,865

	2010	2009
Opening balance at beginning of year	55,865	68,848
Loss carry-forwards	-24,704	-12,498
Tax on provisions for pensions for the year	67	49
Other	-1,442	-534
Total	29,786	55,865

<i>Deferred tax liability</i>	2010	2009
Technology	5,253	6,489
Customer relations	-	66
Total	5,253	6,555

	2010	2009
Opening balance at beginning of year	6,555	8,054
Tax on the year's amortization of Technology	-1,236	-1,236
Tax on the year's amortization of Customer Relations	-66	-263
Total	5,253	6,555

The group has deductible loss carry-forwards that have arisen in Transmode Holding AB and Transmode Systems AB of 107,623 (201,556) available to offset against future taxable earnings in those companies where the losses have arisen. The deductible loss carry-forwards correspond to a deferred tax asset of 28,305 (53,009). There is no time limit to when loss carry-forwards can be utilized. There are no tax consequences for the company upon potential dividends.

### **Parent Company**

<i>Deferred tax asset</i>	2010	2009
Cost at beginning of year	8,549	7,742
Change in the year	450	807
Cost at end of year	8,999	8,549

## Note 11 Earnings per Share

	2010	2009
Profit attributable to equity holders of the parent	81,399	44,277
Preference dividends for cumulative preference shares	<u>-15,802</u>	<u>-15,803</u>
Net earnings used to determine earnings per share basic and after dilution <sup>1</sup>	<u>65,597</u>	<u>28,474</u>
Weighted average number of outstanding ordinary shares used to calculate basic earnings per share (000)	75,598	75,498
Adjustments for:		
– Assumed conversion of preference shares to ordinary shares (000)	349,876	349,876
– assumed exercise of stock options (000)	<u>18,575</u>	<u>2,471</u>
Weighted average no. of outstanding ordinary shares utilized to calculate diluted earnings per share (000)	<u>444,049</u>	<u>427,845</u>
Basic earnings per share	0.868	0.377
Diluted earnings per share <sup>1, 2</sup>	0.148	0.067

<sup>1</sup> Pursuant to the current Articles of Association, at a possible stock market listing, all preference shares would be converted to ordinary shares, assuming the satisfaction of certain conditions. This implies that no compensation would be paid to preference shareholders. Assuming a stock market listing at year-end, diluted earnings per share for 2010 would have been SEK 0.183 (0.103) because the key ratios would not have been charged with the aforementioned interest and nor would the weighted average number of shares been affected.

<sup>2</sup> Dilution effects are only considered when they imply a deterioration of earnings per share.

## Note 12 Dividends

	2010	2009
Dividend paid on class E and F preference shares	<u>-200,415</u>	-
	<u>-200,415</u>	-

The Board of Directors is proposing to the Annual General Meeting 2010 that dividends of 29,847 are paid to holders of class E preference shares.

## Note 13 Machinery and Equipment

### December 31, 2009

	Machinery and Equipment
January 1, 2009	
Cost	23,485
Cumulative depreciation	<u>-15,796</u>
Carrying amount	<u>7,689</u>
January 1, 2009, opening carrying amount	7,689
Purchases	1,565
Disposals and obsolescence	-
Depreciation for the year	<u>-3,278</u>
December 31, 2009, closing carrying amount	<u>5,976</u>
December 31, 2009	
Cost	25,032
Cumulative depreciation	<u>-19,056</u>
Carrying amount	<u>5,976</u>

No impairment losses were taken in 2009. Obsolescence in 2009 reduced cost by 18 and cumulative depreciation by 18, - net.

**December 31, 2010**

	Machinery and Equipment
January 1, 2010, opening carrying amount	5,976
Purchases	3,530
Disposals and obsolescence	-162
Depreciation for the year	<u>-3,222</u>
December 31, 2010, closing carrying amount	<u>6,122</u>

December 31, 2010	
Cost	26,287
Cumulative depreciation	<u>-20,165</u>
Carrying amount	<u>6,122</u>

No impairment losses were taken in 2010. Obsolescence in the year reduced costs by 2,275 and cumulative depreciation by 2,113, 162 net.

The estimated economic lives of the assets are as follows:	<u>2010</u>	<u>2009</u>
Machinery and equipment	3 – 5 yr.	3 – 5 yr.

**Note 14 Intangible Assets****December 31, 2009**

	Goodwill	Capitalized Dev. Exp.	Technology	Customer Relations
January 1, 2009				
Cost	88,388	11,072	47,000	5,000
Cumulative amortization	-	-1,005	-17,625	-3,750
Carrying amount	<u>88,388</u>	<u>10,067</u>	<u>29,375</u>	<u>1,250</u>
January 1, 2009, opening carrying amount	88,388	10,067	29,375	1,250
Acquisitions	-	7,673	-	-
Amortization in the year	-	-3,666	-4,700	-1,000
December 31, 2009, closing carrying amount	<u>88,388</u>	<u>14,074</u>	<u>24,675</u>	<u>250</u>
December 31, 2009				
Cost	88,388	18,745	47,000	5,000
Cumulative amortization	-	-4,671	-22,325	-4,750
Carrying amount	<u>88,388</u>	<u>14,074</u>	<u>24,675</u>	<u>250</u>

No impairment losses or obsolescence was taken in 2009.

**December 31, 2010**

	Goodwill	Capitalized Dev. Exp.	Technology	Customer Relations
January 1, 2010, opening carrying amount	88,388	14,074	24,675	250
Acquisitions	-	21,170	-	-
Disposals and obsolescence	-	-499	-	-
Amortization in the year	-	-5,609	-4,700	-250
December 31, 2010, closing carrying amount	<u>88,388</u>	<u>29,136</u>	<u>19,975</u>	<u>-</u>
December 31, 2010				
Cost	88,388	37,121	47,000	5,000
Cumulative amortization	-	-7,985	-27,025	-5,000
Carrying amount	<u>88,388</u>	<u>29,136</u>	<u>19,975</u>	<u>-</u>

No impairment losses or obsolescence was taken in 2010.

Obsolescence of capitalized development expenses in the year reduced costs by 2,794 and cumulative amortization by 2,295, -499 net.

The economic lives of the assets are estimated as follows:	<u>2010</u>	<u>2009</u>
Technology	10 yr.	10 yr.
Customer relations	5 yr.	5 yr.
Capitalized development expenses	3 yr.	3 yr.

Transmode acquired Lumentis AB in 2005. Intangible assets attributable to Technology and Customer Relations were identified when valuing the company. Technology is amortized on a straight-line basis over 10 years, which is the economic life assessed by the Board of Directors. Customer Relations are amortized on a straight-line basis over 5 years, which is the economic life assessed by the Board of Directors. Capitalized development expenses are amortized over a maximum of 3 years.

## Note 15 Impairment Test of Goodwill

Goodwill acquired in business combinations is allocated to a cash-generating unit, which is synonymous with Transmode's only business segment; optical network solutions. The carrying amount of goodwill is allocated as follows:

	<u>2010</u>	<u>2009</u>
Optical networking solutions	<u>88,388</u>	<u>88,388</u>
Total goodwill	<u>88,388</u>	<u>88,388</u>

The impairment test for Transmode's cash-generating unit is based on calculated value in use. The cash flow forecast utilized in the impairment test 2010 is based on financial forecasts approved by management and the Board of Directors, for the four-year period 2011 - 2014.

Expected market growth and Transmode's opportunities to increase market shares were used when preparing these forecasts. Margins are based on estimates, analyzed against historical profits. In the impairment test, the growth rate utilized to extrapolate cash flows after year 2014 is 3.0 (3.0)%. A discount rate of 7.9 (9.8)% was utilized when calculating the present value of cash flow.

Nor was any impairment identified when a sensitivity analysis was conducted.

## Note 16 Other Financial Assets

### December 31, 2009

	Blocked Bank Funds	Endowment Insurance	Total
Opening balance, January 1, 2009	1,211	250	1,461
New deposit/premiums paid	23	151	174
Interest received	39	-	39
Closing balance, December 31, 2009	<u>1,273</u>	<u>401</u>	<u>1,674</u>

### December 31, 2010

	Blocked Bank Funds	Endowment Insurance	Total
Opening balance, January 12010	1,273	401	1,674
Released funds	-778	-	-778
New deposit/premiums paid	-	160	160
Value change	-	95	95
Interest received	5	-	5
Closing balance, December 31, 2010	<u>500</u>	<u>656</u>	<u>1,156</u>

Blocked bank funds are collateral for bank guarantees issued.

## Note 17 Share warrants

### 1 Share warrants for Board Members and Employees

#### 1.1 Option plan 2007

In March 2007, the Board of Directors decided on an option plan for Board members and employees comprising a maximum of 39,897,145 share warrants. The offered granting and terms and conditions of the share warrants were made known to, and determined for, participants in April and May 2007. The commitment to issue share warrants was formalized through a resolution at the AGM in June 2007 to issue share warrants, and by the participants then subscribing for/acquiring share warrants in June and July 2007.

Of the subscribed/acquired share warrants, 18,450,000 share warrants were subscribed at a subscription price of SEK 0.065 per share warrant, with entitlement to subscribe for a total of 18,450,000 ordinary shares until May 31, 2010 inclusive at an exercise price of SEK 1.14 per ordinary share. Another 11,013,603 share warrants were acquired at a price of SEK 0.06 per share warrant, with entitlement to subscribe for 11,013,603 ordinary shares until November 30, 2009 at an exercise price of SEK 1.08 per ordinary share.

The price of the share warrants was based on assessed market value, with price calculated by an external valuer by applying the Black & Scholes valuation model. As an individual un-listed share, volatility was assessed as above the Stockholm Stock Exchange average for the OMX Index over recent years, at approximately 25%. Because the price of the share warrants corresponded to the assessed fair value, consolidated profit was not charged.

Input data used in the valuation:

Expected dividend, SEK	0.00
Volatility	30%
Term, years	2.5/3.0
Share price at grant date, SEK	0.72
Annual risk-free interest	3.9%
Exercise price, SEK	1.08/1.14

In the subscription period, Transmode held an option to re-purchase the share warrants at market value if the holder's employment terminates before subscription is consummated.

a) Holdings and changes in the number of share warrants for the option plan 2007, with subscription period until November 30, 2009 are as follows:

	<u>2010</u>	<u>2009</u>
As of January 1	-	10,537,203
Granted	-	-
Forfeited	-	-
Re-purchased	-	-9,463,503
Exercised	-	-100,000
Expired	-	-973,700
As of December 31	<u>-</u>	<u>-</u>

b) Holdings and changes in the number of share warrants for the option plan 2007, with subscription period until May 31, 2010 are as follows:

	<u>2010</u>	<u>2009</u>
As of January 1	-	18,250,000
Granted	-	-
Forfeited	-	-
Re-purchased	-	-18,250,000
Exercised	-	-
Expired	-	-
As of December 31	<u>-</u>	<u>-</u>

### 1.2 Option plan 2009

The AGM in April 2009 authorized the Board of Directors to decide on the issue of a maximum of 55,000,000 share warrants with the right to subscribe for a maximum of 55,000,000 ordinary shares for certain Board members and employees of the company on one or more occasions in the period until the next AGM, waiving shareholders' preferential rights.

The offered granting and terms and conditions of the share warrants of the option plan 2009:I were delivered to participants in May 2009. In June 2009, the Board of Directors took a decision to issue a total of 43,071,858 share warrants to the participants in the option plan.

The offered granting and terms and conditions of the share warrants of the option plan 2009:II were delivered to participants in June 2009. In July 2009, the Board of Directors took a decision to issue a total of 4,966,280 share warrants to the participants in the option plan.

All the share warrants in the above option plans, totaling 48,038,138, were subscribed at a subscription price of SEK 0.03 per share warrant, with entitlement to subscribe for a total of 48,038,138 ordinary shares at an exercise price of SEK 0.45 per ordinary share. The subscription period for the option plan 2009:I is the period October 2009 to April 30, 2012. Subscription for shares in the option plan 2009:II is possible in the period April 1-30, 2012, coincident with and after a possible initial public offering of the company's share and other periods that the Board of Directors may decide. Otherwise, the terms and conditions of the options are the same for both plans.

The price of the share warrants was based on assessed market value, proceeding from a price calculated by an external valuer by applying the Black & Scholes valuation model. As an individual un-listed share, volatility was assessed as above the Stockholm Stock Exchange average for the OMX Index over recent years. Because the price of the share warrants is judged to correspond to the assessed fair value, consolidated profit was not charged at granting. However, provisioning is conducted for social security contributions on an ongoing basis in accordance with each country's regulations.

Input data used in the valuation of both plans:

Expected dividend, SEK	0.00
Volatility	30%
Term, years	3.0
Share price at grant date, SEK	0.30
Annual risk-free interest	3.2%
Exercise price, SEK	0.45

In the subscription period, Transmode holds an option to re-purchase the share warrants at market value if the holder's employment terminates before subscription is consummated.

In accordance with existing share warrant terms, due to the dividends paid by Transmode in 2010, the above exercise price was restated from SEK 0.45 to SEK 0.30 per ordinary share.

Holdings and changes in share warrants in the 2009:I plan are as follows:

	<u>2010</u>	<u>2009</u>
As of January 1	43,071,858	-
Granted	-	43,071,858
Forfeited	-	-
Re-purchased	-64,000	-
Exercised	-	-
Expired	-	-
As of December 31	<u>43,007,858</u>	<u>43,071,858</u>

Given full exercise of share warrants as above, share capital would increase by 430.

The share warrants re-purchased in 2010 are retained by the company.

Holdings and changes in share warrants in the 2009:II plan are as follows:

	<u>2010</u>	<u>2009</u>
As of January 1	4,966,280	-
Granted	-	4,966,280
Forfeited	-	-
Re-purchased	-292,000	-
Exercised	-	-
Expired	-	-
As of December 31	<u>4,674,280</u>	<u>4,966,280</u>

Given full exercise of the above share warrants, share capital would increase by 47.

The share warrants re-purchased in 2010 are retained by the company.

The AGM 2010 resolved to extend the Board of Directors' authorization from the AGM 2009 for the remaining share warrants up to an aggregate maximum of 55,000,000.

The offered granting and terms and conditions of the share warrants in the 2009:III option plan were delivered to participants in February 2010. In May 2010, the Board of Directors took the decision to issue a maximum total of 2,900,000 share warrants to participants in the option plan.

The offered granting and terms and conditions of the share warrants in the 2009:IV option plan were delivered to participants in May 2010. In May 2010, the Board of Directors took the decision to issue a maximum total of 3,995,000 share warrants to participants in the option plan.

All the share warrants in the 2009 III – IV option plans, totaling 6,895,000, were subscribed at a subscription price of SEK 0.10 per share warrant, with entitlement to subscribe for a total of 6,895,000 ordinary shares at an exercise price of SEK 0.75 per ordinary share. The subscription period for the option plan 2009:III is the period May 2010 to April 30, 2012. Subscription for shares in the option plan 2009:IV is possible in the period April 1-30, 2012, coincident with and after a possible initial public offering of the company's share and other periods that the Board of Directors may decide. Otherwise, the terms and conditions of the options are the same for both plans.

The price of the share warrants was based on assessed market value, proceeding from a price calculated by an external valuer by applying the Black & Scholes valuation model. As an individual un-listed share, volatility was assessed as above the Stockholm Stock Exchange average for the OMX Index over recent years. Because the price of the share warrants is judged to correspond to the assessed fair value, consolidated profit was not charged at granting. However, provisioning is conducted for social security contributions on an ongoing basis in accordance with each country's regulations.

Input data used in the valuation of both plans:

Expected dividend, SEK	0.00
Volatility	30%
Term, years	2.4
Share price at grant date, SEK	0.66
Annual risk-free interest	2.5%
Exercise price, SEK	0.75

In the subscription period, Transmode holds an option to re-purchase the share warrants at market value if the holder's employment terminates before subscription is consummated.

In accordance with existing share warrant terms, due to the dividends paid by Transmode in 2010, the above exercise price was restated from SEK 0.75 to SEK 0.60 per ordinary share.

Holdings and changes in share warrants in the 2009:III and 2009:IV plans are as follows:

	2009:III	2009:IV
As of January 1	-	-
Granted	2,900,000	3,995,000
Forfeited	-	-
Re-purchased	-500,000	-
Exercised	-	-
Expired	-	-
As of December 31	2,400,000	3,995,000

Given full exercise of share warrants as above, share capital would increase by 64.

The share warrants re-purchased in 2010 are retained by the company.

## 2 Share Warrants Issued to Lenders

In 2006, 3,517,760 share warrants were issued to European Partners II Leveraged Venture Leasing Company Limited ("EVP") coincident with entering a finance leasing arrangement with EVP (now Kreos Capital). These options conferred entitlement to subscribe for 3,517,760 class E preference shares, or the corresponding number of ordinary shares if Transmode Holding AB's shares are listed, at an exercise price of SEK 1.1785 per share. The terms of the options give the holder the possibility of utilizing potential value growth of the options as part-payment for shares upon subscription.

Subscription can take place in the period from 7 February 2006 to the earliest of:

- i) 7 February 2016,
- ii) The fifth anniversary of the listing of Transmode Holding AB's shares or;
- iii) The day holders of at least 90% of all Transmode Holding AB's shares accept an offering on market terms to transfer their shares of the company in a single transaction.

In 2006, 1,972,846 share warrants were issued to Proventus AB and Kreos Capital (formerly "EVP") each, totaling 3,945,692 share warrants, coincident with raising a venture capital loan from Proventus AB. These options confer entitlement to subscribe for a total of 3,945,692 class E preference shares, or the corresponding number of ordinary shares if Transmode Holding AB's shares are listed, at an exercise price of SEK 1.1785 per ordinary share. The terms of the options give the holder the possibility of utilizing potential value growth of the options as part-payment for shares upon subscription.

Subscription can take place in the period from 3 August 2006 to the earliest of:

- i) 3 August 2016,
- ii) The fifth anniversary of the listing of Transmode Holding AB's shares or;
- iii) The day holders of at least 90% of all Transmode Holding AB's shares accept an offering on market terms to transfer their shares of the company in a single transaction.

In accordance with existing share warrant terms, due to the dividends paid by Transmode in 2010, which the above options, totaling 7,463,452 entitle subscription to, have been restated to a total of 10,366,149 class E preference shares, or the corresponding number of ordinary shares in the event of Transmode Holding AB's shares being listed. Simultaneously, the exercise price has been restated to SEK 0.8485 per share.

The finance lease arrangement and venture capital loan were fully amortized before 2010.

Holdings and changes in share warrants to lenders are as follows:

	2010	2009
As of January 1	7,463,452	7,463,452
Granted	-	-
Forfeited	-	-
Re-purchased	-	-
Exercised	-	-
Expired	-	-
As of December 31	7,463,452	7,463,452

Given full exercise of the share warrants as above, share capital would increase by 104

## Note 18 Inventories

Inventories of 75,508 (34,081) comprise finished goods, products in progress and raw materials.

Expensed impairment losses on inventories amount to 2,364 (7,700). Impairment losses have been conducted for established and assessed obsolescence. The expense is included in cost of goods and services provided in the Income Statement.

No impairment losses were reversed in the years 2009 - 2010.

Provisioning to obsolescence reserve is based on age and rate of turnover and is 17,778 (19,864).

	<u>2010</u>	<u>2009</u>
Raw materials	18,353	18,258
Products in progress	3,795	6,815
Finished goods	71,138	28,872
Obsolescence	-17,778	-19,864
Total	<u>75,508</u>	<u>34,081</u>

## Note 19 Accounts Receivable

	<u>2010</u>	<u>2009</u>
Accounts receivable	94,889	152,414
Less: provision for bad debt	-1,762	-4,112
Accounts receivable, net	<u>93,127</u>	<u>148,302</u>

Changes in the provision for bad debt in the years 2009 to 2010 are stated in the following table.

	<u>2010</u>	<u>2009</u>
Opening balance, January 1	-4,112	-6,353
Receivables written off in the year	-	47
Reversed unutilized amounts	4,112	6,353
New provisioning for bad debt	-1,762	-4,159
Closing balance, December 31	<u>-1,762</u>	<u>-4,112</u>

An age analysis of the group's outstanding accounts receivable as of December 31, for 2009 and 2010 is stated in the following table. The amounts exclude debt written off. Net accounts receivable thus correspond to the maximum credit risk for the group in addition to that provisioned in the financial statements. The group has no pledges as collateral for these credit risks.

	<u>2010</u>	<u>2009</u>
Non-overdue accounts receivable	77,066	132,770
Overdue by 1 – 30 days	13,434	13,055
Overdue by 31 – 90 days	3,764	3,056
Overdue by 91 – 180 days	-954	-93
Overdue by over 180 days	-183	-486
Accounts receivable, net	<u>93,127</u>	<u>148,302</u>

## Note 20 Other Current Receivables

	<u>2010</u>	<u>2009</u>
Income taxes recoverable	503	259
Sales tax recoverable	14,225	8,488
Other receivables	1,401	658
Total	<u>16,129</u>	<u>9,405</u>

## Note 21 Prepaid Expenses and Accrued Income

	<u>2010</u>	<u>2009</u>
Prepaid rent	-	1,441
Accrued interest income	23	9
Accrued income	2,294	1,220
Prepaid staff-related insurance policies	889	808
Prepaid licensing expenses	1,119	530
Other prepaid expenses	<u>1,357</u>	<u>1,633</u>
Total	<u>5,682</u>	<u>5,641</u>

## Note 22 Cash and Cash Equivalents

	<u>2010</u>	<u>2009</u>
Bank balances	<u>206,047</u>	<u>298,980</u>
Total	<u>206,047</u>	<u>298,980</u>

Bank balances accrue interest at varying rates, based on daily deposit rates. The fair value of cash and cash equivalents is the same as book value.

On December 31, 2010, the group had access to an unutilized credit facility of 30,000 (30,000) for which all covenants are satisfied.

In the Consolidated Cash Flow Statement, cash and cash equivalents consist of bank balances.

## Note 23 Share Capital and Reserves

### Share Capital

As of December 31, 2010, there are 487,981,740 shares of Transmode Holding AB, of which 75,597,679 ordinary shares and 412,384,061 preference shares (class C 28,923,078, class D 185,286,052, class E 135,667,180 and class F 62,507,751), with a quotient value of SEK 0.01.

All shares are fully paid-up.

If the company is liquidated or pays dividends, the Articles of Association stipulate the following order of priority:

- preference for holders of class F over holders of all other shares
- preference for holders of class E over holders of class D and C
- preference for holders of class D over holders of class C
- preference for holders of class C over holders of ordinary shares

All preference shares would be converted to ordinary shares on a one-to-one basis if the company was listed on a stock market.

### Option plans

Upon full exercise of the outstanding share warrants as of December 31, 2010, share capital would increase by 644 (555). More information in Note 17.

### Other reserves

Other reserves consist of translation differences attributable to equity in foreign subsidiaries.

## Note 24 Interest-bearing Loans

	<u>2010</u>	<u>2009</u>
Long Term		
Other long-term liabilities	-	76
Total	<u>-</u>	<u>76</u>

<b>Interest and Other Borrowing Costs</b>	2010	2009
Loans from credit institution	-	1,868
Currency contracts	300	270
Other interest not attributable to interest-bearing loans	66	77
<b>Total</b>	<b>366</b>	<b>2,215</b>

#### *Bank Credits/Pledging Customer Invoices*

Pledging customer invoices functions as collateral for bank credit/pledging customer invoices. As of December 31 the unutilized credit facility was 30,000 (30,000). A 0.15% credit agreement commission has been paid for the credit facility.

There are covenants related to the group's equity/assets ratio and EBITDA level for rolling 12-month periods per quarter. These covenants have not been exceeded.

#### *Loans from Credit Institutions*

The loan from a credit institution, which was fully amortized in 2009, was interest-bearing with variable interest of EURIBOR + 8.0% at the beginning of 2009, the interest rate was 2.93 + 8.0%.

## **Note 25 Provisions**

### **December 31, 2009**

	Compensation,				Total
	Pensions	Guarantees	Founders	Other	
January 1, 2009	310	6,208	3,227	-	9,745
Additional provisions	189	5,343	-	155	5,687
Utilized in the year	-	-1,078	-	-	-1,078
Reversed unutilized amounts	-	-1,124	-	-	-1,124
<b>December 31, 2009</b>	<b>499</b>	<b>9,349</b>	<b>3,227</b>	<b>155</b>	<b>13,230</b>
Short term	-	9,349	3,227	155	12,731
Long term	499	-	-	-	499
<b>Total</b>	<b>499</b>	<b>9,349</b>	<b>3,227</b>	<b>155</b>	<b>13,230</b>

### **December 31, 2010**

	Compensation,				Total
	Pensions	Guarantees	Founders	Other	
January 1, 2010	499	9,349	3,227	155	13,230
Additional provisions	316	2,763	-	1,110	4,189
Utilized in the year	-	-2,436	-	-	-2,436
Reversed unutilized amounts	-	-1,936	-	-	-1,936
<b>December 31, 2010</b>	<b>815</b>	<b>7,740</b>	<b>3,227</b>	<b>1,265</b>	<b>13,047</b>
Short term	-	7,740	3,227	1,163	12,130
Long term	815	-	-	102	917
<b>Total</b>	<b>815</b>	<b>7,740</b>	<b>3,227</b>	<b>1,265</b>	<b>13,047</b>

#### *Provisions for Pensions*

Provisions for pensions relate to an endowment insurance that is described in more detail in Note 26.

#### *Provisions for Guarantees*

The provision relates to expected expenditure for guarantee commitments to customers. Partly for commitments relating to specific customer projects and partly for general commitments according to standard agreements, but also for expected expenditure of a goodwill nature. The provision is based on historical and forward-looking information regarding expenses and guarantee periods, for example. The majority of the guarantee expenses during the remaining guarantee period are expected to occur within the next 12 months. The commitment regarding one specific customer project ceases after the end of March 2011, for which the company provisioned 2,000 in 2008.

#### *Provision for Compensation to Founders*

This provision relates to expected compensation to founders of Transmode Systems AB and Transmode Holding AB (formerly Lumentis AB). This compensation was agreed coincident with Transmode Holding AB acquiring Transmode Systems AB. The payment for the company is expected within 12 months from the founders

potentially selling shares in Transmode Holding AB. Payment will be conducted at one or more occasions depending on when and how many shares are sold on each occasion.

## Note 26 Pensions

Commitments for old-age and survivors' pensions for salaried employees in Sweden are vested through an insurance policy with Alecta. According to pronouncement UFR 3 issued by the Swedish Financial Reporting Board, this is a multi-employer defined benefit plan. For the financial year 2010, the group did not have access to such information that makes it possible to report this plan as a defined benefit plan. Thus the ITP pension plan secured through insurance with Alecta is reported as a defined contribution plan. Expenditure for pension policies in the year insured with Alecta amount to 7,934 (7,301)). Alecta's surplus can be distributed to policyholders and/or insured parties. At year-end 2010, Alecta's surplus expressed as its collective consolidation ratio was 146 (141)%. The collective consolidation ratio comprises the market value of Alecta's assets as a percentage of its insurance commitments, calculated according to Alecta's actuarial calculation assumptions, which are not consistent with IAS 19.

As part of his pension plan, the Chief Executive Officer has chosen an endowment insurance held by Transmode Holding AB and Transmode Systems AB. This policy is recognized as a financial asset. The expected pension payments and employer's contributions on it are stated as a long-term provision in the Consolidated Balance Sheet.

Commitments for foreign pensions are reported in accordance with local regulations in each country.

## Note 27 Accounts Payable and Other Current Liabilities

	<u>2010</u>	<u>2009</u>
Accounts payable	70,714	66,909
Advances from customers	4,656	1,219
VAT liability	1,117	1,626
Social security contributions and employee withholding taxes	5,499	4,571
Other current liabilities	505	445
Total	<u>82,491</u>	<u>74,770</u>

Accounts payable are non interest-bearing and normally settled on their stated due date, usually within 30 - 60 days from invoice date. See Note 29 for liabilities to related parties. Other current liabilities are non interest-bearing and settled within 12 months.

## Note 28 Accrued Expenses and Deferred Income

<b>Group</b>	<u>2010</u>	<u>2009</u>
Accrued personnel expenses	31,915	25,370
Dismissal pay	-	123
Prepaid income	3,676	18,985
Other accrued expenses	<u>10,628</u>	<u>5,941</u>
Total	<u>46,219</u>	<u>50,419</u>
<b>Parent Company</b>	<u>2010</u>	<u>2009</u>
Accrued personnel expenses	5,730	2,942
Other accrued expenses	<u>1,343</u>	<u>105</u>
Total	<u>7,073</u>	<u>3,047</u>

## Note 29 Commitments, Pledged Assets and Contingent Liabilities

### Operating Lease Commitments—the Group as Lessee

The group has entered commercial lease agreements regarding computers and premises.

The lease agreements have differing terms, indexation clauses and extension options.

Future minimum lease payments for irrevocable operating lease agreements as of December 31 are as follows:

	2010	2009
Within one year	9,105	3,600
After more than one year but within five years	44,532	-
After more than five years	2,008	-
Total	<u>55,645</u>	<u>3,600</u>

Expenses for operating lease commitments	5,918	5,381
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### Pledged Assets

	2010	2009
Blocked funds	500	1,273
Total	<u>500</u>	<u>1,273</u>

### Floating Charge

	2010	2009
Priority 1	9,002	10,353
Priority 2	3,000	3,000
Priority 3	27,006	31,059
Total	<u>39,008</u>	<u>44,412</u>

Of outstanding floating charges, the company holds 27,006 (31,059).

### Pledges

The group's endowment insurance, which is part of the pension plan for the Chief Executive Officer, is pledged. The pledgee is the Chief Executive Officer.

### Contingent Liabilities

The group has no contingent liabilities requiring any disclosure for the years 2009 and 2010.

## Note 30 Transactions with Related Parties

The Consolidated Accounts include the financial statements of Transmode Holding AB and the subsidiaries in the following table:

	Corporate ID No.	Country	Equity Holding
Directly owned subsidiaries			
– Transmode Systems AB	556587-0028	Sweden	100%
Indirectly owned subsidiaries			
– Transmode Incentive AB	556599-4596	Sweden	100%
– Transmode Systems Inc	3457703	USA	100%
– Transmode (UK) Ltd	4968653	UK	100%
– Transmode Systems Germany GmbH	00724618305	Germany	100%
– Transmode Systems Asia Pte Ltd	200413703N	Singapore	100%
– Transmode Systems Canada Inc	6562281	Canada	100%
– Transmode Systems Italy S.r.l.	06189330969	Italy	100%

No subsidiaries were incorporated in 2010. In the previous year, a new indirectly owned subsidiary was incorporated in Germany, Transmode Systems Germany GmbH.

Transmode Holding AB is the group parent company.

### Transactions with Related Parties

The company conducted transactions with related parties amounting to -200 (-) in the year. This wholly relates to fees to Board member's Gerd Tenzer's wholly owned German company.

## Salary and Benefits to Senior Management

### 2010

	Basic Salary/ Director's Fee	Performance- related Pay	Pension Expense	Other Benefits	Total
Chairman of the Board	200	-	-	-	200
Other Board members	533	-	-	-	533
Chief Executive Officer	2,144	2,212	598	-	4,954
Other senior management (6 people)	7,589	3,325	2,185	735	13,834
Total	10,466	5,537	2,783	735	19,521

### 2009

	Basic Salary/ Director's Fee	Performance- related Pay	Pension Expense	Other Benefits	Total
Chairman of the Board	300	-	-	-	300
Other Board members	433	-	-	-	433
Chief Executive Officer	2,017	911	570	-	3,498
Other senior management (6 people)	7,158	1,509	1,895	-	10,562
Total	9,908	2,420	2,465	-	14,793

#### *Chief Executive Officer*

The current Chief Executive Officer took up his position in March 2007. Basic annual salary is 2,079 (1,980). Maximum performance-related pay is 100 (100)% of basic annual salary. Pension is defined contribution and amounts to 28 (28)% of basic annual salary. Upon termination initiated by the employee, a notice period of six months applies, and upon termination initiated by the company, a notice period of six months applies. For termination initiated by the company, extra remuneration of six months' salary may be payable if certain conditions are satisfied.

#### *Other Senior management*

Other senior management have maximum performance-related pay at 20 - 75% of basic annual salary. One senior manager has a defined-contribution pension amounting to 30% of basic annual salary. Other senior management pensions are based on the ITP pension plan. Other benefits are remuneration to people whose employment has ceased or have been on leave. For the group consisting of other senior management, notice periods are between three and six months for termination initiated by themselves. For termination initiated by the company, notice periods are between 3 and 12 months.

#### *Share-based Payments*

In the event of the sale of over 90% of the shares of the company to an external buyer, the company will pay performance-related pay corresponding to the potential difference between the value of the company's ordinary shares in a stock market listing and in a trade sale, on a total of 16,595,681 of the share warrants or ordinary shares senior management are eligible to subscribe for as a result of their share options held coincident with the aforementioned trade sale.

Share-based payments are stated in Note 17.

## Note 31 Financial Risk Management

### 1. Financial Risk Factors

The group has various financial assets and liabilities such as accounts receivable, accounts payable and other assets and liabilities that arise in operating activities. In addition, the group's financial assets and liabilities primarily comprise bank balances. In 2005 to 2010, the capital structure was altered from being exclusively owner financed to being primarily funded via equity.

Through its operations, the group is exposed to various financial risks; market risks (including interest risks on cash flows and currency risk), credit risks and liquidity risks.

The Board of Directors has prepared a finance policy for overall financial risk management and for specific segments including financial risks within the group. The Board of Directors has delegated responsibility for ongoing observance of its policy to the group management.

Generally, considering global economic conditions, financial risks are considered to have been relatively unchanged at year-end 2010 compared to year-end 2009. Nor, apart from volatile exchange rates, has the group being affected by this.

### Interest Risks on Cash Flows

The group's interest-bearing assets, in the form of bank balances, reduced in 2010 due to dividends paid to shareholders.

The company did not have any borrowings from credit institutions in the year, and accordingly, the group's exposure to interest risks as of the reporting date consists of bank balances exclusively. Note 24 states the interest terms and currencies of the group's previous interest-bearing liabilities. Pursuant to the prevailing finance policy, the Board of Directors takes decisions on interest fixings for each individual major funding facility based on a general risk assessment. Pursuant to the current policy, at least 50% of potential new borrowings should have fixed interest for at least three years. In the years 2009 and 2010, the group did not use any interest derivatives.

The following table illustrates how changes in interest rates on the net of interest-bearing assets and liabilities with variable interest, with all other variables unchanged, would have affected consolidated profit before tax.

	Change in Basis Points	Effect on Profit before Tax, SEK m (approx.)
2010	+/-100	+/- 3
2009	+/-100	+/- 3

### Currency Risk

The group has business with counterparties in countries other than Sweden. Accordingly, the group is exposed to transaction exposure where exchange rates between the transaction currency and Transmode's functional currency (SEK) change over time. Currency risks arise when future business transactions or recognized assets or liabilities are expressed in one currency, usually EUR, GBP and USD, which is not the entity's functional currency, which almost exclusively means Swedish kronor (SEK) for the Transmode group.

The group's ambition is to attempt to control its cash flows in foreign currencies by matching payments made and received, for example, the funding arranged in EUR that was fully amortized in 2009. Bank balances are usually almost exclusively in SEK, whereupon cash exposure is limited.

Pursuant to its finance policy, unmatched net flows can be hedged using financial derivatives. However, with the aim of reducing certain short-term effects of fluctuations in exchange rates, in 2009 and 2010, the Board of Directors decided that parts of accounts receivable denominated in EUR and GBP and parts of the net outflow, of goods purchases less good sales, denominated in USD should be hedged by currency forward contracts pursuant to the adopted policy.

At year-end 2010, the company had currency forward contracts regarding commitments to sell currencies totaling EUR 6.4 m at an average spot rate of SEK/EUR 8.97, a total of GBP 1.1 m at a spot rate of SEK/GBP 10.77 and a total of EUR 0.2 m linked to purchases of USD 0.3 m at a spot rate of EUR/USD 1.33. The company also had currency forward contracts for commitments to purchase currency of a total of USD 3.0 m at an average spot rate of SEK/USD 6.90. The remaining maturity of outstanding currency forward contracts was less than 12 months and has been classified as other current receivables and other current liabilities.

	<u>2010</u>	<u>2009</u>
Other current receivables	248	624
Other current liabilities	-433	-317
Net receivable/(liability)	<u>-185</u>	<u>307</u>

For those transactions made in EUR, GBP and USD, the following table illustrates how exchange rate variations, all other variables unchanged, would have affected consolidated profit before tax, excluding the effect of currency forward contracts.

	Change in Exchange Rate	Effect on Profit before Tax, SEK m (approx.)
2010 EUR	+/-1%	+/- 4
2010 GBP	+/-1%	+/- 1
2010 USD	+/-1%	-/+ 1
2009 EUR	+/-1%	+/- 3
2009 GBP	+/-1%	+/- 1
2009 USD	+/-1%	-/+ 1

The effect of translation differences on consolidated equity is marginal because operations and net investments in foreign subsidiaries are limited.

### Credit Risk

Primarily, the group's end-customers are network operators, services providers, corporations and public institutions in Europe. Sales to end-customers are mainly direct, but also through resellers. Outstanding accounts receivable are monitored continuously, and the group's exposure to credit risks is judged to be fairly low, as in the previous year. The need for provisioning of doubtful debt is effected continuously at customer level. The maximum credit risk for accounts receivable is the same as the carrying amount stated in Note 19. This Note also provides an age analysis of overdue accounts receivable for which payment had not been received as of the reporting date. In 2010, the company made provisions for doubtful debt totaling 1,762 (4,112). There was no bad debt in 2010. In the previous year, bad debt was 47.

The group has a large number of customers, although a small number of them represent a relatively sizeable part of outstanding accounts receivable. The following summary states the share of total accounts receivable attributable to the five customers with the largest outstanding balances as of the reporting date, December 31.

Concentration of Accounts Receivable as of December 31	Total Accounts Receivable, SEK 000	Of which Outstanding Balance for 5 Customers with the Largest Balances, SEK 000	Share of Total Accounts Receivable
2010	93,127	39,459	42.4%
2009	148,302	72,103	48.6%

The credit risk on cash and cash receivables is judged as low because surplus liquidity is deposited in bank accounts and time-finite investment at three banks in Sweden.

### Liquidity Risk

The group has surplus liquidity, which is continuously deposited in bank accounts, on fixed-term deposits of a maximum of six months. This implies that only a negligible share of the group's investments of surplus liquidity could be at risk of reducing the group's flexibility in terms of liquidity. Additionally, the group has the option to utilize committed credit facilities to reduce its liquidity risk further, see Note 24.

The group's policy is to endeavor normally to maintain a liquidity reserve of a minimum of 8% of the forthcoming 12 month's sales. The group management also monitors forecasts of the group's liquidity reserves in the short and long term.

The following table illustrates maturities of the group's financial liabilities based on contracted terms. Disclosures on interest and other borrowing terms are stated in Note 24.

As of December 31, 2010	<12 months	12-60 months	>60 months	Total
Liabilities to credit institutions	-	-	-	-
Accounts payable	70,714	-	-	70,714
Other liabilities*	57,994	-	-	57,994

As of December 31, 2009	<12 months	12-60 months	>60 months	Total
Liabilities to credit institutions	-	76	-	76
Accounts payable	66,909	-	-	66,909
Other liabilities*	58,280	-	-	58,280

\* Includes other current liabilities and accrued expenses and deferred income.

## 2. Managing Capital Risks

In 2007 and until mid-2009, the group was largely financed by equity and interest-bearing loans. The group has monitored and analyzed this capital continuously on the basis of changes in items including net debt, equity/assets ratio and cash flow. The general objective of capital risk management has been to ensure the group's ability to continue its expansion and simultaneously maintain an optimal capital structure with the aim of limiting the cost of capital. In July 2009, the group amortized the final portion of a EUR 3 m interest-bearing loan.

To maintain or alter its capital structure, the group can pay out capital to shareholders or otherwise re-pay capital to shareholders. The group can also issue new shares or sell assets to alter its debt/equity ratio. In 2010, the company paid dividend to shareholders totaling SEK 200.4 m.

The following table reviews the group's debt/equity ratio and equity/assets ratio in the years 2009 to 2010.

	2010	2009
Interest-bearing loans	-	-
Shareholders' equity	422,190	540,852
Total assets	571,056	687,311
Debt/equity ratio	-	-
Equity/assets ratio	73.9%	78.7%

## Note 32 Financial Instruments

### Fair Values of Financial Instruments

There were no finance lease liabilities at the end of 2009 or 2010.

For other financial instruments, such as accounts receivable, accounts payable and other assets and liabilities, carrying amounts are considered a close approximation of fair values, because their term is short.

### Classification of Financial Instruments

<i>December 31, 2010</i>	Loan Receivables and	Derivative Non-financial		Total
	Accounts Receivable	Instruments	Assets	
Goodwill and other intangible assets	-	-	137,499	137,499
Machinery and equipment	-	-	6,122	6,122
Deferred tax asset	-	-	29,786	29,786
Other financial assets	1,156	-	-	1,156
Inventories	-	-	75,508	75,508
Accounts receivable	93,127	-	-	93,127
Other current receivables	-	248	15,881	16,129
Prepaid expenses and accrued income	-	-	5,682	5,682
Cash and cash equivalents	206,047	-	-	206,047
Total assets	300,330	248	270,478	571,056

	Financial Liabilities			
	Recognized at			
	Amortized Cost	Derivative Instruments	Non-financial Liabilities	Total
<i>December 31, 2010</i>				
Borrowings, long term	0	-	-	0
Provisions, long term	917	-	-	917
Deferred tax liability	-	-	5,253	5,253
Accounts payable	70,714	-	-	70,714
Tax liability	-	-	1,858	1,858
Provisions, short term	4,390	-	7,740	12,130
Other current liabilities	-	433	11,342	11,775
Accrued expenses and deferred income	46,219	-	-	46,219
Total liabilities	122,240	433	26,193	148,866

	Financial Assets			
	Recognized at			
	Loan Receivables and Accounts Receivable	Derivative Instruments	Non-financial Assets	Total
<i>December 31, 2009</i>				
Goodwill and other intangible assets	-	-	127,387	127,387
Machinery and equipment	-	-	5,976	5,976
Deferred tax asset	-	-	55,865	55,865
Other financial assets	1,674	-	-	1,674
Inventories	-	-	34,081	34,081
Accounts receivable	148,302	-	-	148,302
Other current receivables	-	624	8,781	9,405
Prepaid expenses and accrued income	9	-	5,632	5,641
Cash and cash equivalents	298,980	-	-	298,980
Total assets	448,965	624	237,722	687,311

	Financial Liabilities			
	Recognized at			
	Amortized Cost	Derivative Instruments	Non-financial Liabilities	Total
<i>December 31, 2009</i>				
Borrowings, long term	76	-	-	76
Provisions, long term	499	-	-	499
Deferred tax liability	-	-	6,555	6,555
Accounts payable	66,909	-	-	66,909
Tax liability	-	-	1,409	1,409
Provisions, short term	3,382	-	9,349	12,731
Other current liabilities	-	317	7,544	7,861
Accrued expenses and deferred income	50,419	-	-	50,419
Total liabilities	121,285	317	24,857	146,459

## Note 33 Participations in Group Companies

	2010	2009
OB at beginning of year	369,377	367,476
Investments in the year	-	1,901
Carrying amount at end of period	<u>369,377</u>	<u>369,377</u>

	Corporate ID Number	Country	Equity Holding	Book Value
Directly owned subsidiaries				
– Transmode Systems AB	556587-0028	Sweden	100%	369,377
Indirectly owned subsidiaries				
– Transmode Incentive AB	556599-4596	Sweden	100%	
– Transmode Systems Inc	3457703	USA	100%	
– Transmode (UK) Ltd	4968653	UK	100%	
– Transmode Systems Germany GmbH	00724618305	Germany	100%	
– Transmode Systems Asia Pte Ltd	200413703N	Singapore	100%	
– Transmode Systems Canada Inc	6562281	Canada	100%	
– Transmode Systems Italy S.r.l.	06189330969	Italy	100%	

## Three-year Summary

	2010	2009	2008
Total sales (SEK m)	699.3	570.1	607.1
Gross profit (SEK m)	358.6	281.6	329.7
EBITDA (SEK m)*	122.1	77.3	116.7
Operating profit/loss (SEK m)	107.6	57.4	104.9
Profit/loss for the period	81.4	44.3	73.3
Working capital (SEK m)	47.6	58.1	144.0
Net debt (-)/cash (+) (SEK m)	206.5	300.3	153.1
Cash flow from operating activities (SEK m)	133.6	154.9	69.5
Change in total sales (%)	22.7%	-6.1%	31.7%
Gross margin (%)	51.3%	49.4%	54.3%
EBITDA margin (%)*	17.5%	13.6%	19.2%
Operating margin (%)	15.4%	10.1%	17.3%
Working capital/total sales (%)	8.8%	13.4%	20.2%
Equity/assets ratio (%)	73.9%	78.7%	78.2%

\* For 2008, 2009 and 2010, operating expenses were adjusted by SEK 1.7 m, 7.3 m and 0.8 m for expenses related to the possible stock market listing.

## **Definitions**

### **Regions**

Americas: North and South America  
EMEA: Europe, Middle East and Africa  
APAC: Asia and Pacific region

### **Total sales**

Income from sale of goods and services.

### **Invoicing**

Non-allocated income from sale of goods and services.

### **Growth**

Change in total sales:  
Change from the corresponding preceding period as a percentage of total sales.

### **Earnings measures**

EBITDA:  
Operating profit/loss before amortization and depreciation of intangible and tangible fixed assets.

### **Margin measures**

Gross margin:  
Gross profit as a percentage of total sales.

EBITDA margin:  
Operating profit/loss before amortization and depreciation of intangible and tangible fixed assets (EBITDA) as a percentage of total sales.

Operating margin:  
Operating profit/loss as a percentage of total sales.

### **Capital structure**

Working capital:  
Inventories, accounts receivable and other non interest-bearing current assets less accounts payable and other interest-free current liabilities, excluding interest-free loans from shareholders. The working capital percentage measurement is based on the average of data as of the end of each quarter for the last 12-month period (five measurements) and is stated as a percentage of total sales calculated on a rolling 12-month period.

Net debt/cash:  
Interest-bearing liabilities less cash and cash equivalents and interest-bearing financial fixed assets.

Equity/assets ratio:  
Shareholders' equity as a percentage of total assets.

Debt/equity ratio:  
Interest-bearing liabilities divided by equity.