

Notes to the financial statements

1 Basis of preparation

These financial statements comprise the consolidated interim balance sheets as of 31 October 2006 and 31 October 2005 and related consolidated interim statements of income and cash flows for the six months then ended of Micro Focus International Plc (hereinafter referred to as “the interim financial statements”). These interim financial statements have been prepared on a basis consistent with the accounting policies set out in Micro Focus International Plc’s annual report for the year ended 30 April 2006. The interim financial statements should therefore be read in conjunction with the 2006 annual report. The interim financial statements have been issued in accordance with the Listing Rules of the Financial Services Authority. The Group has chosen not to adopt IAS 34 “Interim financial statements” in preparing these interim financial statements.

These interim financial statements have been prepared under the historical cost convention.

The preparation of financial statements require estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although the estimates are based on management’s best knowledge of the amounts, events or actions, actual results may differ from those estimates.

Copies of the interim results for the six months ended 31 October 2006 will be sent to all shareholders. Details can also be found on the Company’s website at www.microfocus.com. Further copies of the interim results and copies of the accounts for the year ended 30 April 2006 can be obtained by writing to the Company Secretary, Micro Focus International Plc, Old Bath Road, Newbury, Berkshire RG14 1QN.

This announcement was approved by the board of Micro Focus International Plc on 7 December 2006.

2 Reclassification of expenditure

The directors have reviewed the classification of certain expenditure within the income statement and believe, to be consistent with software industry accounting practices, in order to aid comparison, it is more appropriate to classify the following costs differently than was reported in prior periods.

a) *Cost of customer support* – these costs were previously included within administrative expenses and have been reclassified as cost of sales. The impact of the change is to increase cost of sales by \$4,651,000 (H1 2006: \$5,302,000, FY 2006: \$10,074,000) and decrease administrative expenses by a corresponding amount.

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b) *Amortisation of research and development* – these costs relating to capitalised salaries were previously amortised through cost of sales. The amortisation has been reclassified as research and development expenditure. The impact of the change is to decrease cost of sales by \$2,470,000 (H1 2006: \$2,508,000, FY 2006: \$4,626,000) and increase research and development expenditure by a corresponding amount.

3 Functional currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The consolidated financial statements are presented in US Dollars, which is the Company's functional currency.

4 Earnings per share

The calculation of basic earnings per share has been based on the earnings attributable to ordinary shareholders of the Company and the weighted average number of shares for each period. The weighted average number of shares used in the calculation was 199,558,000 (31 October 2005: 192,990,000; 30 April 2006: 196,709,000).

The diluted earnings per share has been calculated after taking account of the share options. The weighted average number of shares used in the calculation was 201,889,000 (31 October 2005: 195,394,825; 30 April 2006: 198,711,000).

Diluted earnings per share excluding exceptional items was 11.18 cents (H1 2006: 7.20 cents, FY 2006: 14.23 cents). Diluted earnings per share is calculated after adjusting for the post-tax effect of exceptional items of \$277,000 (H1 2006: \$5,064,000, FY 2006: \$12,059,000).

5 Reconciliation of operating profit to EBITDA

	Six months ended 31 October 2006 (unaudited) \$'000	Six months ended 31 October 2005 (unaudited) \$'000	Year ended 30 April 2006 (audited) \$'000
Operating profit	30,022	13,657	22,733
Depreciation	514	475	1,006
Amortisation of software	364	426	806
EBITDA	30,900	14,558	24,545
Exceptional items:			
IPO-related costs	–	6,458	6,909
Reorganisation costs	–	–	7,403
Share-based compensation	390	(500)	(224)
Management charges	–	–	125
EBITDA before exceptional items	31,290	20,516	38,758

In calculating EBITDA the amortisation of research and development expenditure is not added back to operating profit, as the directors believe by doing so EBITDA provides a better measure of the cash generation of the business. Amortisation of research and development expenditure in the current period was \$2,470,000 (H1 2006: \$2,508,000, FY 2006: \$4,626,000).

6 Segmental information

	Six months ended 31 October 2006 (unaudited) \$'000	Six months ended 31 October 2005 (unaudited) \$'000	Year ended 30 April 2006 (audited) \$'000
Geographical analysis of turnover			
North America	35,704	35,023	68,847
Europe and the Middle East	30,167	25,740	54,038
Rest of the world	13,095	12,096	20,803
Total	78,966	72,859	143,688

There is no material difference between turnover by origin above and turnover by destination. All turnover is derived from external customers.

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7 Supplemental information

Set out below is an analysis of turnover recognised between the principal product categories, which the directors use to assess the future revenue flows from the current portfolio of customers.

Turnover	Six months ended 31 October 2006 (unaudited) \$'000	Six months ended 31 October 2005 (unaudited) \$'000	Year ended 30 April 2006 (audited) \$'000
Licence fees	37,675	35,160	67,985
Maintenance fees	39,115	35,388	71,860
Consultancy fees	2,176	2,311	3,843
Total	78,966	72,859	143,688

8 Taxation

Tax for the half year ended 31 October 2006 was \$7.4 million (2005: \$3.9 million) based on increased profits. The Group's effective tax rate is 23.5% (2005: 30%). As a result of the significant increase in the share price in the six-month period to 31 October 2006, a tax deduction has arisen on the stock options in issue. Excluding the effects of this beneficial tax deduction, the underlying effective tax rate was 26.8%.

9 Trade and other receivables

	31 October 2006 (unaudited) \$'000	31 October 2005 (unaudited) \$'000	30 April 2006 (audited) \$'000
Trade debtors	34,500	27,596	29,377
Prepayments	3,213	3,089	3,959
Accrued income	4,629	5,636	4,293
Total	42,342	36,321	37,629

10 Trade and other payables

	31 October 2006 (unaudited) \$'000	31 October 2005 (unaudited) \$'000	30 April 2006 (audited) \$'000
Trade payables	1,762	2,058	1,944
Other tax and social security payable	2,720	2,593	2,468
Accruals	15,456	10,010	20,511
Deferred income	42,926	38,507	45,593
Total	62,864	53,168	70,516

11 Post balance sheet events

On 2 November 2006, Micro Focus announced that it had agreed to acquire HAL Knowledge Solutions SPA ("HAL KS"), a leading provider of Application Portfolio Management software in order to enhance the Company's enterprise application modernisation capabilities. The deal successfully closed on 10 November 2006. HAL KS has been acquired by Micro Focus for a total consideration of \$3.5 million in cash, subject to a net asset adjustment.

In the year to 31 December 2005, HAL KS reported a net loss before tax of \$4.5 million and its gross assets as at 31 December 2005 were \$9.5 million. Following the acquisition, we are now restructuring the business to reduce costs, with an expected restructuring charge of approximately \$4.0 million, falling in the current financial year. HAL KS was acquired with net balance sheet liabilities of approximately \$4.5 million.