



# FINAL TRANSCRIPT

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## **SCOX - The SCO Group Conference Call to Comment and Provide Q&A on Recent Red Hat Actions**

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*The SCO Group Inc - Director of Corporate Communications*

**Darl McBride**

*The SCO Group Inc - President and CEO*

**Christopher Sontag**

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## CONFERENCE CALL PARTICIPANTS

**Lee Gomez**

*Wall Street Journal - Analyst*

**David Becker**

*CNET - Analyst*

**Larry Greenemeier**

*Information Week - Analyst*

**Michael Singer**

*Jupiter Media - Analyst*

**Maureen O'Gara**

*Client Server News - Analyst*

**Reed Stevenson**

*Reuters - Analyst*

**Gary Rivlin**

*Wire Magazine - Analyst*

**Chris Gaither**

*Boston Globe - Analyst*

**Herbert Jackson**

*Renaissance Ventures - Analyst*

## PRESENTATION

### Operator

Good day everybody and welcome to the SCO Group Conference Call. Today's call is being recorded. At this time for opening remarks and introduction, I would like to turn the call over to Mr. Blake Stowell, please go ahead sir.

**Blake Stowell - The SCO Group Inc - Director of Corporate Communications**

Thank you and good day everyone. Thank you for hearing our call. We have on the line today our President and CEO, Darl McBride; and our Senior Vice President and General Manager of SCO Source, Chris Sontag. We will begin by reading a statement to you. Following our teleconference, we'll have a question-and-answer session and if you have

further questions or would like to access our press materials, we will point you to our press room on sco.com. With that I'll turn the time over to our President and CEO, Darl McBride.

**Darl McBride - The SCO Group Inc - President and CEO**

Thanks Blake and thanks you all for joining us here today. Yesterday Red Hat filed a legal action against the SCO Group in Delaware Federal Court and announced the formation of the Open Source Development Fund. The purpose of this call today is to comment on those actions and discuss SCO's new licensing plan going forward. Red Hat's loss has confirmed of what we've been saying all along. Linux developers are either unwilling or unable to screen the code in the Linux kernel to remove infringing code before customers buy and use it. Let me be clear, Red Hat is selling Linux that contains verbatim and obfuscated code from Unix system files. Red Hat is also selling Linux that contains derivative work from Unix that has been contributed to Linux in violation of Unix licensing agreements. Some of those companies like IBM and Sequent have now have the license agreement terminated for acting in violation of the terms of the license agreement. We've had the chance to preliminarily review the lawsuit and Red Hat's press statement from yesterday and we have several responses. I would like to go through those at this point.

First, Red Hat claims we have not shown examples of infringing code in Linux. This statement is simply not true; we have shown examples of infringing code in Linux to many different people including some Linux advocates. We set up reviewing center in Lindon, Utah; we had gone to companies around the world to show infringing code. In fact, this same offer was made to Red Hat but they chose instead to sue us. Red Hat is apparently trying to pretend that no problem exists. The code that the court will review in this case contains verbatim code from Unix and misappropriated derivative works from Unix. That has to be cleared to the people that have reviewed the sample code that we have shown -- in fact has been cleared.

Second point, Red Hat claims that SCO is at fault for its loss of recent Linux business. We believe that SCO is not at fault for Red Hat loss in business, rather we suggest that Red Hat has adopted a faulty business model. In its S-3 disclosure filed with the SEC on July 7, 2003, just a few weeks ago, Red Hat included very revealing risk factor disclosures that speak to its business model. The risk disclosure states that Red Hat relies on software developed by independent parties over whom it exercises no control. The disclosure statement

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1

# FINAL TRANSCRIPT

SCOX - The SCO Group Conference Call to Comment and Provide Q&A on Recent Red Hat Actions

continues to state that Red Hat lacks access to unpublished software patent applications and the copyright registrations. These are Red Hat's words about its own business. Red Hat's disclosure also warns that if infringing code is in Linux, it may need to stop product shipments. In fact this warning is consistent with the requirement of Section 7 in the General Public License under which Linux is shipped to end users.

The GPL states in Section 7 as follows -- if you cannot distribute so as to satisfy simultaneously your obligation under this license and any other patent obligations, then as a consequence you may not distribute the program at all; for example, if a patent license will not permit royalty redistribution of the program by all those who receive copies directly or indirectly through you, then the only way you can satisfy both it and the license would be to refrain entirely from distribution of the program. So, this is the main problem with Red Hat business model; it distributes under the GPL. It has no control to prevent infringing code from going into Linux, but if infringing code is found, Red Hat is required under the GPL to stop shipments of Linux. That business model seems unsustainable in the long run and we believe it is the real false side of Red Hat's business problems, not SCO. These issues were serviced eventually with or without SCO.

Third point, Red Hat has placed \$1m for Linux development fund. This pledge misses the mark. SCO has never considered suing Linux developers individually; only companies that employ them like IBM, who are taking improper advantage of the UNIX licenses with the SCO. Furthermore, Red Hat's pledge will not do anything for end users since there is still no indemnification for Linux end users. If Red Hat or other Linux players decide at some point in the future to reach all the defense fund, protect those who are really protecting, we will suggest they need to increase the size of the fund dramatically. With over 2.5m servers running infringing Linux 2.4, the price of indemnification is measured in the billions of dollars, an exposure which monumentally dwarfs the current [camouflage] of \$1m.

Fourth point, Red Hat thinks SCO should probably show them every line of infringing code. Why is this? So Red Hat can acknowledge SCO's legitimate claims and acknowledge the key role that Unix intellectual properties are playing in the growth of Linux? Not likely. Red Hat thinks we should show them every line of infringing code so they can make changes and go forward in a complete -- with a complete disregard for our business rights. Some Linux developers are so [inaudible] the SCO's infringing works that they seem to feel

an entitlement to keep doing it. SCO's brand is standing up for its valuable intellectual property rights because it has spent a great deal of money in purchase. That makes no sense. The issue here is more than just SCO and Red Hat. What is that issue? Whether intellectual property rights will have any value in the age of the internet? Whether intellectual property rights can be simply taken without regards for rightful ownership?

Some people think they have the right to do that. Linux companies seem to encourage that and have even made a business model. [They are] selling unwarranted software code developed under a ["Don't Ask Don't Tell"] policy. Our society is engaged in an important debate to decide whether intellectual property will remain proprietary or whether it will all become communal property according to Richard Stallman's vision for all software distributed under the General Public License such as Linux. There are so many current examples of intellectual property [tax] today that responsible corporations cannot disregard this as someone else's problem. SCO, one small company, intends to defend its intellectual property rights vigorously against Red Hat and all others.

In the only first half, the long term profitability and growth for any company in this internet era, and further from this agenda SCO has drawing out this week its new licensing plan for Linux. The runtime license permits the use of SCO's intellectual property in binary form only, as concerned in Linux distributions. By purchasing a SCO intellectual property license, customers avoid infringement of SCO's intellectual property rights in Linux 2.4 and Linux 2.5 kernels. Because it's so [wide] to operate with runtime use only, customers also comply with the General Public License under which Linux is distributed.

Okay. Those are my opening statements. So this would open up the phone lines to whatever questions that you might have.

## QUESTIONS AND ANSWERS

### Operator

Thank you. If you do have a question today, simply press the "\*" key followed by the digit "1" on your touchtone telephone. If you are using a speakerphone, please release your mute function to allow your signals to reach our equipment. And once again please press "\*" "1" to ask a question. And we'll

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2

# FINAL TRANSCRIPT

SCOX - The SCO Group Conference Call to Comment and Provide Q&A on Recent Red Hat Actions

pause for just a moment to assemble the roster. And we will go first to Lee Gomez with Wall Street Journal.

**Lee Gomez - Wall Street Journal - Analyst**

Hello.

**Darl McBride - The SCO Group Inc - President and CEO**

Hi Lee.

**Lee Gomez - Wall Street Journal - Analyst**

Hi Darl. How are you?

**Darl McBride - The SCO Group Inc - President and CEO**

Great.

**Lee Gomez - Wall Street Journal - Analyst**

Can you explain to me why you don't release the examples of infringement that you keep talking about so everyone can see this?

**Darl McBride - The SCO Group Inc - President and CEO**

Actually we have been releasing them, Lee, we have gone through--

**Lee Gomez - Wall Street Journal - Analyst**

Are there any website or something?

**Darl McBride - The SCO Group Inc - President and CEO**

What we've been doing is again going through these sessions and giving them -- the people -- these two factors of infringement here that relates to the derivative works code, actually we can be very open about that; it is not something a news under protective provision that we have in our context. But we have been very clear that the NUMA, the RCU contributions that have come from IBM into Open Source and into Linux -- into Linux Kernel are direct violations of our--

**Lee Gomez - Wall Street Journal - Analyst**

Have you have any specific examples in there?

**Darl McBride - The SCO Group Inc - President and CEO**

Absolutely. We have -- as long we think we have been showing is absolute--.

**Lee Gomez - Wall Street Journal - Analyst**

Why are you so shy? Do you -- could you give me making this publicly available to anyone?

**Darl McBride - The SCO Group Inc - President and CEO**

Yes. Absolutely. The only case is that it's been restricted is the piece -- are the pieces that we have basically controlled restrictions on the [sale basis] on our contracts. We can't just open it up. The moment we opened it up, we have in fact opened it up to the public and we can't restrict it in the future from a proprietary standpoint. So, we -- under that scenario we have shown it to over 100 people so far under NDA and the clear conclusion of people coming back is, you know, they get to see the direct line-by-line verbatim [copy of] the code.

**Lee Gomez - Wall Street Journal - Analyst**

Can you make available a list of the people that you have shown it to?

**Darl McBride - The SCO Group Inc - President and CEO**

I'll have to go back with my CR team. Some of the companies that we've shown it to don't necessarily want to have that revealed, if they --

**Lee Gomez - Wall Street Journal - Analyst**

You said you have -- you said you only made it available to some Linux and open source activists or something along those lines?

**Darl McBride - The SCO Group Inc - President and CEO**

Absolutely. He's gone out and written about it in fact that we can make, you know, that's what he said probably.

# FINAL TRANSCRIPT

SCOX - The SCO Group Conference Call to Comment and Provide Q&A on Recent Red Hat Actions

**Lee Gomez** - *Wall Street Journal - Analyst*

And who is that?

**Darl McBride** - *The SCO Group Inc - President and CEO*

I don't remember his name. Chris, if you can give--?

**Christopher Sontag** - *The SCO Group Inc - Senior VP and GM*

I don't have his name in front of me so that we can provide that to you. By the way, I just want to remind everyone that we're limiting everyone to one question. Thank you.

**Darl McBride** - *The SCO Group Inc - President and CEO*

I'll leave the other questions and response to that question there. So, yeah, we have gone through -- we have shown this code and whether it's in the verbatim side or -- that is more confidentially protected or on the other side which is open, we have done that. And just last week I met with a Linux developer who came in and admitted going into the discussion that he was skeptical. He was, you know, he's been watching the case for 4 months and actually went through a court hearing session. [inaudible] he said okay, you commit me what you really want me to do. So, it is really clear from everybody that we have met with -- almost with 100% hit rate in terms of the people, at least they are saying. "yeah, there is a problem." Next.

**Operator**

Thank you. Now we will hear from David Becker with CNET.

**David Becker** - *CNET - Analyst*

Hi, can you talk about the terms of the renewal of license pricing and how one would go about acquiring that?

**Darl McBride** - *The SCO Group Inc - President and CEO*

Sure, Chris, you want to give some detail on the announcement we made today on the licensing side.

**Christopher Sontag** - *The SCO Group Inc - Senior VP and GM*

Sure. The pricing initially for a single CPU commercial use Linux 2.4 or above is \$699 for an introductory price that will be good until October 15 after which it will climb to a higher price. We have decided to provide an introductory pricing to allow people to more readily purchase that intellectual property license from SCO to continue on with their business unaffected. The means by which they can obtain that license is to contact their SCO representative and they will place them in contact with appropriate people in my organization to set up appointments to facilitate the purchase of those licenses.

**Darl McBride** - *The SCO Group Inc - President and CEO*

Next question.

**Operator**

Thank you. We will go now to Larry Greenemeier with Information Week.

**Larry Greenemeier** - *Information Week - Analyst*

Hi, guys, I had a question about an email that had been sent out -- one of the things it refers to is a possibility of a global resolution of SCO's intellectual property claims. What else can you tell us about this, you know, what went into resolving this prior to the suit? What type of global resolution were you referring to?

**Darl McBride** - *The SCO Group Inc - President and CEO*

We have had discussions over the last several months. I can't get into details based on confidentiality provisions. We have had discussions; at a point in time we felt like those discussions were going somewhere in terms of where we are right now, you know, clearly at that point of time where we are going to take matters in our own hands and move forward. So, I guess best way to categorize it is there have been some discussions, but from where we stand right now it's starting to start marching onward again with our legal claims that we have.

**Operator**

Thank you. Our next question will come from Michael Singer with Jupiter Media.

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1

# FINAL TRANSCRIPT

SCOX - The SCO Group Conference Call to Comment and Provide Q&A on Recent Red Hat Actions

**Michael Singer** - Jupiter Media - Analyst

Yes, hi. So, to clarify -- are you also taking legal action like your counter suit against Red Hat at this point, or are you just considering it and kind of assessing your situation?

**Darl McBride** - The SCO Group Inc - President and CEO

Right, good question, we do have a number of options in terms of how we move forward on this. You know, in terms of how we move forward, what we do next, do we -- you know, we have questions about what it has -- Red Hat's complaint even face the claim upon which release may be granted due to the fact the way it's filed, we may find most of them dismissed, now we also have counterclaims against Red Hat that we could file according to rules established at the Federal courts -- it's probably a fair estimate that the Delaware case that was filed yesterday, we've got a trial sometime in 2005, which is about the same time that IBM case. IBM case, for your information, does have a court date now and that is in April, I believe, it's April 11th of 2005, and this one's probably tracking behind that one by a few months. So again we got this suit yesterday, David and his team are looking at the various options that we have, we're not here today to state which path we're going down, but I'm -- we know that based on the way that the suit was filed, there are a number of options we have, and we're looking at all of those options currently.

**Blake Stowell** - The SCO Group Inc - Director of Corporate Communications

Okay next question.

**Operator**

Next you will here from Maureen O'Gara with Client Server News.

**Maureen O'Gara** - Client Server News - Analyst

Thank you hi guys. Are you going to try and back build some of these people -- I mean when does the license pick-up as far as time goes, I'd like to know what the real price spin of a unit processor system is if it's not \$699, and that's only introductory, and I'd like to get some sort of an idea what the pricing for these rest of these kinds of systems on multiple

CPU's, the CPU add-on's to desktops and the embedded system? Can you help us out here?

**Darl McBride** - The SCO Group Inc - President and CEO

Sure, Chris I know we have more detail behind where we are on the pricing for the embedded systems and what not, do you want to --?

**Christopher Sontag** - The SCO Group Inc - Senior VP and GM

I -- sure I'm happy to answer that. Maureen the price after October 15th for a unit processor system will be \$1399, detail pricing of additional CPU's will be available on our website, I think it would be a rather boring list to read off to you right now, but tracking along that same level of pricing for additional CPU's.

**Operator**

We will go now to Reed Stevenson with Reuters.

**Reed Stevenson** - Reuters - Analyst

Hello just a couple of technical notes. Is it a one-time license or you -- are you going to charge yearly for something like this? And also given the timing of your announcement which is right at the start of the Linux world and this though -- I mean, is there something that you are trying to say to Linux?

**Darl McBride** - The SCO Group Inc - President and CEO

On the pricing side, that is a one-time license as it structures there. Now, with respect to the Linux world conference, we basically got -- served this suit yesterday and responding to the Red Hat suit, so, I am not sure if their timing was -- from Red Hat standpoint, I talked to Matthew Szulik, their CEO on Thursday, had very amicable discussion with him. We, in fact, thought we were on track to sit down and in fact volunteered to them that we could sell them the code; as we had volunteered to sell anybody that's come into this point. And actually walking right in the [call] on Thursday, I called my team and said, I think, we may be gaining some positive traction here, so this is interesting. So that was Thursday, and then on Monday morning, you know, we did serve the lawsuit. So, you know, I am not sure what their timing was related to Linux world, but first of all we're responding to where they are. Our pricing announcement -- we announced a couple

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# FINAL TRANSCRIPT

SCOX - The SCO Group Conference Call to Comment and Provide Q&A on Recent Red Hat Actions

weeks ago that we are going to go down this path, we were going to take a few weeks to do some checking and going through and validating with these various customers. And we've gone through that, we've got things both at down now, and in fact, have now launched the pricing of that.

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## Operator

Thank you. From Wire Magazine we will from Gary Rivlin (ph.)

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## Gary Rivlin - Wire Magazine - Analyst

Aren't you worried that even if you are right here, you lose because you could very well alienate every Linux program on the planet which is a large and influential group?

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## Darl McBride - The SCO Group Inc - President and CEO

Well, I think, the way we look at this is, if we're right here and we have every reason to believe that we are based on the evidence that we have, we think that it's the other way round. We think that there need to be a recognition here that investor's property rights do matter, the legal system, the copyright laws do matter, and in fact, that should be the recognition going forward that we need to step back and take a look at this business model that we have on the Open Source side, which in fact, doesn't have any inherent protections. It's a bit interesting as I talk to a lot of Linux developers, at the same they like the model of having, you know, things freely available. Virtually every one of them talks about their need to, in fact, have their own business interest projected; in fact, they have needs to put bread on the table. And then everybody is focused on, that I've talked to, how do I make money on path of this Linux model that's out there, and so I believe that's one of the things that this Linux creates going forward, I believe that is going to be the impetus for in fact adjusting the Open Source model in a way that people have a better ability to make profits from their hard work, their proprietary work that they've put into there coding efforts. Next question.

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## Operator

Thank you. We will go next to Chris Gaither with Boston Globe.

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## Chris Gaither - Boston Globe - Analyst

Yes, I was wondering if you have an estimate of how many roughly end-users just might apply for, and also whether you plan on suing end-users who don't sign up for the SCO intellectual property license?

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## Darl McBride - The SCO Group Inc - President and CEO

Right. The absolute number -- it's hard to get you arms around by virtue of the way Linux has been distributed, it's redistributable, really copyable etcetera. We have got our arms around the number that roughly 2.5m servers -- installed servers are out there in a sense the 2.4 kernel shift. And so, you know, obviously the numbers we think is in the thousands, we don't know how many, whether it is tens or hundreds or thousands of customers. The server shipments that are out there, they are in the millions. And with respect to where do we go with this next -- yes, we do have an ability to go down to the end-user with lawsuits if we have to. It is -- if you look at what has happened here, [inaudible] just hits the wire here just [inaudible] online. Now IBM has come out and said they in fact are not indemnifying their end-users. So the game here -- there is a shelving going on around legal Linux liability and the rocket is showing up under is the end-use customer. Now the question then is when it moved from IBM to Red Hat to an end-use customer, and in fact those companies have, in fact, shifted the liability, they admit they have shifted the liability to the end-use customer and have basically taunted to us to go sue them for to give release for our damages that we have. You know, at a certain point you are left with that card to play with. So that's what we are staring at. I think, as we move forward here, the big part of putting a licensing program in place was to in fact avoid these lawsuits. I was encouraged when I talked to Matthew last week, may be we are moving down a path where there will be some resolutions with a Red Hat, where we could start to work out some of these differences. Obviously, that all changed as of yesterday. So, yes we are absolutely 100% going to fight for our intellectual property rights. We paid hundreds of millions of dollars to the purchaser developed over the years, and our desire is that we can work through this in a licensing fashion, but if we don't get there with licensing, then we'll have to move to enforcement actions.

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## Blake Stowell - The SCO Group Inc - Director of Corporate Communications

Okay last question.

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6



# FINAL TRANSCRIPT

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## Operator

Thank you, and that will come from Herbert Jackson at Renaissance Ventures.

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## Herbert Jackson - Renaissance Ventures - Analyst

Hey guys, you have been busy.

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## Darl McBride - The SCO Group Inc - President and CEO

It has been a busy few months.

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## Herbert Jackson - Renaissance Ventures - Analyst

Could you comment on any discussions with other software vendors that might produce a street-legal version of Linux going forward?

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## Darl McBride - The SCO Group Inc - President and CEO

We have a variety of discussions going on, and I am not at liberty to go into the detail of the various discussions that are out there. I can say that there are companies we are dealing with that have seen the code, have seen the problems, they are stepping up. There are others that are taking an approach to really to come after us, and to try and take our legal rights we have and distort those rights. So, we are encouraged that we have some agreements we have signed already. We have other agreements that are in the works that we are encouraged about how they are working through the process and so we'll see how those go. I think the summary on the whole thing in terms of where we stand right now is the reality here IBM and Red Hat [inaudible] a Linux liability target on the back of their customers. And due to IBM and Red Hat acting, we have no choice but to fight the battle at the end-user level. Moving the place, we wanted to go fight the battle, so that's where we have ended up and they have pushed us in that direction; yesterday was another push in that direction.

It was very interesting that -- I think one of the biggest announcements yesterday was an announcement that, in fact, was not made. Same time Red Hat steps up and talks about a legal liability indemnification fund, they target that fund for someone who is not even under attack right now. We have never said once that we're considering to going after Linux developers per se. We have talked about, in fact, the

end use customers where the Linux legal liability is being held. The fact that Red Hat set up an indemnification fund and didn't even mention the customer was I thought a pretty loud statement. So there seems to be an elephant on the table here in the SCO-Linux debate, and its all around indemnification; and the fact that Red Hat ignored this issue in the press statement yesterday to me speaks volumes. And what they didn't say is becoming by now very loud and very clear and that is -- the legal liability for Linux truly rests with the end-users.

As we move down the path of resolving our issues, we recognize that we are in a broader world of intellectual property issues going on. If you look at what's happened in the music business over the last few months, the music fight is going on for a number of years and there have been billions of dollars that artists and the companies there have lost. And when they finally took the fight down to where the infringements are going on, the copyright infringement going on at the end-user level in the music business. One press report I read said that there was a 30% slowdown in downloading the illegal music on the internet after these customer lawsuits started. If we have to go down that path, then -- again we have been pushed there, we will go down there, that's why [Boyd's] team is engaged and David is ready to go, so that's what we have to do.

Our licensing programs announced today -- our clear preference is to not go down the legal path, but in fact, give companies the rights to the intellectual property that we have, give them a chance to get clean on this, and even though in yesterday's announcement Red Hat didn't step up with a solution for how to do this, we believe that that's what we are doing. The case that we are looking at now that was filed yesterday is on a, probably, a multi-year path to get resolved as is the IBM case. And so in the meantime what can users do, we do have a path for them and we have spent the last month training our sales team. They are ready to go, they are ready to work with customers to resolve their issues, and help everybody to be able to move forward. So, that's where we are today. Thanks for joining us to our call.

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## Operator

That does conclude today's conference call. Thank you all for your participation.

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7

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8