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Madison Covered Call & Equity Strategy Fund

Form N-CSR

February 28, 2014

OMB APPROVAL

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM N-CSR

CERTIFIED SHAREHOLDER REPORT OF REGISTERED

MANAGEMENT INVESTMENT COMPANIES

Investment Company Act file number 811-21582

Madison Covered Call & Equity Strategy Fund

(Exact name of registrant as specified in charter)

550 Science Drive, Madison, WI 53711

(Address of principal executive offices)(Zip code)

Pamela M. Krill

Madison Legal and Compliance Department

550 Science Drive

Madison, WI 53711

(Name and address of agent for service)

Registrant's telephone number, including area code: 608-274-0300

Date of fiscal year end: December 31

Date of reporting period: December 31, 2013

Form N-CSR is to be used by management investment companies to file reports with the Commission not later than 10 days after the transmission to stockholders of any report that is required to be transmitted to stockholders under Rule 30e-1 under the Investment Company Act of 1940 (17 CFR 270.30e-1). The Commission may use the information provided on Form N-CSR in its regulatory, disclosure review, inspection, and policymaking roles.

A registrant is required to disclose the information specified by Form N-CSR, and the Commission will make this information public. A registrant is not required to

respond to the collection of information contained in Form N-CSR unless the Form displays a currently valid Office of Management and Budget ("OMB") control number. Please direct comments concerning the accuracy of the information collection burden estimate and any suggestions for reducing the burden to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-0609. The OMB has reviewed this collection of information under the clearance requirements of 44 U.S.C. s 3507.

Item 1. Certified Financial Statement

ANNUAL REPORT

December 31, 2013

Madison Covered Call & Equity Strategy Fund (MCN)

Active Equity Management combined with a Covered Call Option Strategy

Madison
www.madisonfunds.com

MCN | Madison Covered Call & Equity Strategy Fund | December 31, 2013

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Discussion of Fund's Performance

What happened in the market during 2013?

Despite modest economic growth, U.S. equities had one of the best years in history and led the world's stock markets, as the S&P 500 advanced 32.39% in 2013. Domestic mid-cap and small-cap indices showed even stronger returns, with the Russell Midcap® Index up 34.76% and the Russell 2000® Index of small-cap stocks up 38.82%. Developed international markets were also robust, as the broad MSCI EAFE Net Index advanced 22.78%. Emerging markets, on the other hand, lagged the developed world badly, with the Russell Emerging Market Index barely positive with a 0.2% return.

Despite an array of challenges, the resilient U.S. economy grew by nearly 2% in 2013, with the rate of this growth appearing to accelerate through the final quarters. Europe seemed to be working through the worst of its problems, while emerging markets showed signs of slowing growth, putting selling pressure on what had been an investor favorite for much of the past decade.

Returns for bond investors were not as satisfying, as the broad Barclays Aggregate Index dropped -2.02%. During the final quarter of 2013, fixed income investors continued to focus on the timing of a much awaited shift in monetary policy from the Federal Reserve Board (the "Fed"). Throughout 2013 strengthening economic fundamentals and hints from the Fed created expectations for a tapering in Fed open-market bond purchasing. These expectations for what was widely viewed as the first stage towards monetary tightening put steady pressure on interest rates. The yield on the bellwether 10-year Treasury began the year below 2% and climbed close to 3% in early September before drifting back to 2.6% at the end of the third quarter. At year's end the 10-year yield was just over 3%, marking its highest level for 2013.

How did the fund perform given the marketplace conditions during 2013?

For the year ending December 31, 2013, on a Net Asset Value (NAV) basis, Madison Covered Call and Equity Strategy Fund ("MCN" or the "Fund") rose 17.9%, compared to the 13.3% return of the CBOE S&P BuyWrite Index (BXM). The BXM, the Fund's primary index, represents the passive version of a covered call equity strategy. On a share price basis, MCN advanced 17.1%. The fund's share price discount to the NAV widened slightly throughout the year, starting at an 11.7% discount and ending the year at a 13.2% discount. In mid-March, the discount was at

its narrowest level at 9.2%. MCN distributed \$0.72 per share for the full year, on par with the 2012 distribution level. We earned \$1.50 from investment operations as our NAV increased from \$8.63 to \$9.41. Using year-end values, the Fund's yield was 7.7% on NAV or 8.8% on market price.

The Fund outperformed the BXM by over 460 basis points on a NAV basis. The Fund was positively impacted by stock selection and sector allocation that were stronger than the S&P 500, which is the underlying asset in the BXM. In addition, the Fund's equity exposure was not fully "covered" by call options during the year which resulted in the Fund being less hedged relative to the BXM, which is fully covered at all times. Being less hedged in a rising market environment allowed the Fund to participate in the positive market move to a greater extent. Partially offsetting these positive attributes was the impact of the Fund's cash exposure, which detracted from performance in a rising market relative to BXM, which has no cash exposure. The impacts of stock selection, sector allocation and cash holdings is discussed below.

Typically, a covered call strategy will lag the overall market during periods of strong upward movement in stock prices as the sale of call options against stock positions limits full participation in favor of higher income potential and downside protection. This certainly impacted the Fund's ability to keep up with the S&P 500 strong returns over the past 12 months.

The strong full year performance of the S&P 500 was broad-based and led by lower quality, higher risk companies. From a sector perspective for the Fund, the Consumer Discretionary, Health Care and Industrial Sectors were the top performers. The Fund benefited from its overweighted positioning in consumer companies with particularly strong performance coming from Best Buy,

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Advance Auto Parts and Amazon, and only minimally offset by weakness in a few mid-cap companies such as Lululemon and Panera Bread Company. The Fund had a neutral weight in health care stocks although the positioning declined throughout the year as individual holdings were trimmed or sold due to strong performance. Biotechnology companies were the best of breed performers within this sector and the Fund benefited from owning Celgene and Allergan. Generic drug manufacturers were mixed with Mylan Labs' strong performance offset by weakness in Teva Pharmaceuticals. The Industrials Sector was under-represented in the Fund and individual stocks underperformed, led by weakness in C. H. Robinson and Expeditors International. Strength in United Technologies partially offset weakness elsewhere. The weakest sectors during the year were the relatively small Telecom and Utilities Sectors in which the fund had no exposure. The Information Technology Sector was up over 26% but technically underperformed the overall market. The Fund has had a consistent overweighted position in this sector so this hindered relative performance to a small degree. The Fund's individual technology holdings fared well during the year with particularly strong contribution coming from Flextronics, Microsoft, Linear Technology, Applied Materials, Symantec and Yahoo. Weaker performance came from Broadcom, Altera, Nuance Communications and eBay. With respect to cash levels, a rising stock market typically results in a high level of stock assignments which can occur when a holding's market price moves above the call option's strike price. A high level of assignments will lead to higher cash levels until the cash is reinvested into other appropriate equity holdings. During 2013, assignment activity was very high given the stock market's strong advance and cash levels were consistently elevated as the fund managers prudently awaited reinvestment opportunities without the benefit of meaningful market pullbacks. The higher than normal cash levels were a hindrance to performance given the market's strong advance. At year end, cash levels were at 11.6%.

**SHARE PRICE AND NAV PERFORMANCE FOR
MADISON COVERED CALL & EQUITY STRATEGY FUND**

Describe the Fund's portfolio equity and option structure.

As of December 31, 2013, the Fund held 45 equity securities and unexpired covered call options had been written against 87.9% of the Fund's stock holdings. It is the strategy of the Fund to write "out-of-the-money" call options, yet, as of December 31, only 25% of the Fund's call options (18 of 72 different options) remained "out-of-the-money." The sharp market rally late in the year caused many options to move into the money although they were originally written out-of-the-money. (Out-of-the-money means the stock price is below the strike price at which the shares could be called away by the option holder.) Given concerns that the overall market had moved ahead of fundamentals, in mid-year, the Fund's managers begun writing options "closer-to-the-money" in order to capture higher premium income and provide the fund added protection from a reversal in the market's most recent upward trend. With a very high percentage of the equity holdings covered by options written closer-to-the-money, the fund took on a greater "hedged" posture as the year wound down. Clearly, as the market continued to move higher, this was a drag on relative performance.

Which sectors are prevalent in the Fund?

From a sector perspective, MCN's largest exposure as of December 31, 2013 was to the Information Technology (and technology related) Sector, followed by Consumer Discretionary, Health Care, Industrials, and Financials.

The Fund had no representation in the Telecommunication Services and Utilities Sectors as of year-end.

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ALLOCATION AS A PERCENTAGE OF TOTAL INVESTMENTS

AS OF 12/31/13

Consumer Discretionary	16.5	%
Consumer Staples	4.6	%
Energy	5.3	%
Financials	6.3	%
Health Care	8.9	%
Industrials	8.5	%
Information Technology†	25.5	%
Materials	4.3	%
Exchange Traded Funds	8.0	%
U.S. Government and Agency Obligations	5.2	%
Short-Term Investments	6.9	%

†Information Technology includes securities in the following industries:

Communications Equipment; Computers and Peripherals; Internet Software & Services; IT services; Semiconductors & Semiconductor Equipment; and Software.

Discuss the Fund's security and option selection process.

The Fund is managed by primarily focusing on active stock selection before adding the call option overlay utilizing individual equity call options rather than index options. We use fundamental analysis to select solid companies with good growth prospects and attractive valuations. We then seek attractive call options to write on those stocks. It is our belief that this partnership of active management of the equity and option strategies provides investors with an innovative, risk-moderated approach to equity investing. The Fund's portfolio managers seek to invest in a portfolio of common stocks that have favorable "PEG" ratios (Price/Earnings Ratio to Growth Rate), as well as financial strength and industry leadership. As bottom-up investors, we focus on the fundamental businesses of our companies. Our stock

selection philosophy strays away from the “beat the street” mentality, as we seek companies that have sustainable competitive advantages, predictable cash flows, solid balance sheets and high-quality management teams. By concentrating on long-term prospects and circumventing the “instant gratification” school of thought, we believe we bring elements of consistency, stability and predictability to our shareholders.

Once we have selected attractive and solid names for the Fund, we employ our call writing strategy. This procedure entails selling calls that are primarily out-of-the-money, meaning that the strike price is higher than the common stock price, so that the Fund can participate in some stock appreciation. By receiving option premiums, the Fund receives a high level of investment income and adds an element of downside protection. Call options may be written over a number of time periods and at differing strike prices in an effort to maximize the protective value to the strategy and spread income evenly throughout the year.

Discuss how risk is managed through the Fund’s investment process.

Risk management is a critical component of the investment manager’s overall philosophy and investment process. The primary means for managing risk are as follows:

1. Focus on the underlying security. The manager’s bottom-up stock selection process is geared toward investing in companies with very strong fundamentals including market leadership, balance sheet strength, attractive growth prospects, sustainable competitive advantages, predictable cash flows, and high-quality management teams.

Purchasing such companies at attractive valuations is vital to providing an added margin of safety and the manager’s “growth-at-a-reasonable-price” (GARP) philosophy is specifically tuned to such valuation discipline.

2. Active covered call writing. The manager actively sells (writes) individual equity call options on equities that are owned by the Fund. The specific characteristics of the call options (strike price, expiration, degree of coverage) are dependent on the manager’s outlook on the underlying equity and/or general market conditions. If equity prices appear over-valued due to individual company strength or surging markets, the manager may choose to become more defensive with the Fund’s option strategy by selling call options that are closer to the current equity market price, generating larger option premiums which would help defend against a market reversal. The manager

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may also sell call options on a greater percentage of the portfolio in an effort to provide for more downside protection. Following a market downturn, the manager may sell options further out of the money in order to allow the fund to benefit from a market recovery. In such an environment, the manager may also determine that a lesser percentage of the portfolio should be covered by call options in order to more fully participate in market upside.

3. Cash management and timing. Generally, the manager believes that the Fund should be fully invested under normal market conditions. A covered call strategy is rather unique relative to most equity portfolios as the short term nature of call options can lead to the assignment or sale of underlying stock positions on a fairly regular basis. As a result, the Fund's cash levels are likely to frequently fluctuate based on the characteristics of the call options and the market conditions. The thoughtful reinvestment of cash levels adds a layer of risk management to the investment process. This is most evident following a strong surge in equity prices above the strike prices of call options written against individual stocks in the Fund (call options move in-the-money). This could lead to a larger than normal wave of stock sales via call option assignment, which would increase the Fund's cash position following a period of very strong stock. Given the manager's disciplined focus on purchasing underlying securities at appropriate valuation levels, the immediate reinvestment of cash may be delayed until market conditions and valuations become more attractive. If market conditions continue to surge for a period of time, the Fund may underperform due to higher than normal cash levels, however, it is the manager's belief that maintaining a strong valuation discipline will provide greater downside protection over a full market cycle.

What is the management's outlook for the market and Fund in 2014?

In our view, the slow but steady improvement in the U.S. real economy bodes well for 2014. Our cautiously upbeat outlook is largely based on an improving fiscal backdrop, with 2013's federal government headwind expected to recede in 2014. Relative to other countries, the U.S. enjoys favorable demographics, has strong energy and agricultural resources, good national security, a strong rule of law, and a robust consumer base. In addition, the U.S. federal budget deficit has declined from 10% to near 4% of GDP over the past four years. We remain watchful regarding still-high debt levels with governmental entities and consumers, lower labor force participation, unclear long-term fiscal and monetary policies, and lower levels of

capital investments by businesses. On balance, though, the U.S. looks strong compared to the rest of the world. In terms of the equity markets, following incredibly strong performance in 2013, U.S. equity markets are more susceptible to short term volatility stemming from some wavering in the emerging markets and/or the negative impact from severe winter weather. There are also growing signs of complacency and greed with investors, so we would view the short term risk/reward environment as skewed toward risk. This has been evident in the growing “hedged” positioning of the Fund in late 2013. However, looking beyond some potential near-term uncertainty, we view corporate America as being in relatively solid health with good balance sheets, excessive cash, and low but positive earnings growth. Given the recent run-up in equities, valuations have become somewhat extended but not excessive. We expect that volatility will be higher in 2014 and this should provide an improved premium environment for selling call options.

TOP TEN HOLDINGS AS OF 12/31/13

% of net assets

eBay Inc.	3.7	%
Powershares QQQ Trust Series 1 ETF	3.4	%
DIRECTV	3.4	%
Apple Inc.	3.1	%
SPDR S&P 500 ETF Trust	2.9	%
Oracle Corp.	2.9	%
Advance Auto Parts Inc.	2.8	%
T. Rowe Price Group Inc.	2.8	%
Accenture PLC, Class A	2.8	%
QUALCOMM Inc.	2.7	%

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INDEX DEFINITIONS

Indices are unmanaged, reflect no expenses and it is not possible to invest directly in an index.

The S&P 500 Index is an unmanaged, capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The Chicago Board Options Exchange (CBOE) Market Volatility Index, often referred to as the VIX (its ticker symbol), the fear index or the fear gauge, is a measure of the implied volatility of S&P 500 Index options. It represents a measure of the market's expectation of stock market volatility over the next 30-day period. Quoted in percentage points, the VIX represents the expected daily movement in the S&P 500 Index over the next 30-day period, which is then annualized.

The CBOE S&P 500 Buy/Write Index (BXM) is a benchmark index designed to show the hypothetical performance of a portfolio that purchases all the constituents of the S&P 500 Index and then sells at-the-money (meaning same as purchase price) call options of one-month duration against those positions.

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Portfolio of Investments

	Shares	Value (Note 2)
COMMON STOCKS - 84.1%		
Consumer Discretionary - 17.4%		
Advance Auto Parts Inc. (A)	46,000	\$ 5,091,280
Amazon.com Inc.* (A)	9,000	3,589,110
CBS Corp., Class B (A)	32,000	2,039,680
DIRECTV* (A)	88,000	6,079,920
Discovery Communications Inc., Class C* (A)	38,000	3,186,680
Home Depot Inc./The (A)	52,000	4,281,680
Lululemon Athletica Inc.* (A)	60,000	3,541,800
Panera Bread Co., Class A* (A)	21,000	3,710,490
		31,520,640
Consumer Staples - 4.9%		
Costco Wholesale Corp. (A)	35,000	4,165,350
CVS Caremark Corp. (A)	65,000	4,652,050
		8,817,400
Energy - 5.6%		
Apache Corp. (A)	42,500	3,652,450
Canadian Natural Resources Ltd. (A)	80,000	2,707,200
Petroleo Brasileiro S.A., ADR	60,000	826,800
Schlumberger Ltd. (A)	32,000	2,883,520
		10,069,970
Financials - 6.6%		
BB&T Corp. (A)	107,000	3,993,240
Morgan Stanley (A)	95,000	2,979,200
T. Rowe Price Group Inc. (A)	60,000	5,026,200
		11,998,640
Health Care - 9.4%		
Allergan Inc. (A)	36,900	4,098,852
Baxter International Inc. (A)	60,000	4,173,000
Mylan Inc.* (A)	60,000	2,604,000
Teva Pharmaceutical Industries Ltd., ADR (A)	60,000	2,404,800
Varian Medical Systems Inc.* (A)	48,000	3,729,120
		17,009,772
Industrials - 8.9%		
C.H. Robinson Worldwide Inc. (A)	45,000	2,625,300
Expeditors International of Washington Inc. (A)	70,000	3,097,500
Rockwell Collins Inc. (A)	52,000	3,843,840

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Stericycle Inc.* (A)	24,000	2,788,080
United Technologies Corp. (A)	34,000	3,869,200
		16,223,920
Information Technology - 26.8%		
Communications Equipment - 2.6%		
QUALCOMM Inc. (A)	65,000	\$ 4,826,250
	Shares	Value (Note 2)
Computers & Peripherals - 4.7%		
Apple Inc. (A)	10,000	\$ 5,611,100
EMC Corp. (A)	116,500	2,929,975
		8,541,075
Internet Software & Services - 3.7%		
eBay Inc.* (A)	121,000	6,641,690
IT Services - 3.4%		
Accenture PLC, Class A (A)	61,000	5,015,420
Visa Inc., Class A (A)	5,000	1,113,400
		6,128,820
Semiconductors & Semiconductor Equipment - 6.7%		
Altera Corp.	110,000	3,578,300
Broadcom Corp., Class A (A)	130,000	3,854,500
Linear Technology Corp. (A)	103,000	4,691,650
		12,124,450
Software - 5.7%		
Microsoft Corp. (A)	95,000	3,555,850
Nuance Communications Inc.*	99,000	1,504,800
Oracle Corp. (A)	137,000	5,241,620
		10,302,270
		48,564,555
Materials - 4.5%		
Freeport-McMoRan Copper & Gold Inc. (A)	70,000	2,641,800
Monsanto Co. (A)	27,000	3,146,850
Mosaic Co./The (A)	49,800	2,354,046
		8,142,696
Total Common Stocks (Cost \$141,523,956)		152,347,593
INVESTMENT COMPANIES - 8.3%		
Powershares QQQ Trust Series 1 ETF (A)	70,000	6,157,200
SPDR S&P 500 ETF Trust (A)	28,800	5,318,496
SPDR S&P MidCap 400 ETF Trust (A)	15,000	3,663,000
Total Investment Companies(Cost \$14,483,826)		15,138,696
	Par Value	
U.S. GOVERNMENT AND AGENCY OBLIGATIONS - 5.5%		

U.S. Treasury Bill (B) (C) - 5.5%		
0.038%, 2/6/14	\$10,000,000	9,999,625
Total U.S. Government and Agency Obligations		9,999,625
(Cost \$9,999,625)		

See accompanying Notes to Financial Statements.

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MCN | Madison Covered Call & Equity Strategy Fund | Portfolio of Investments - continued | December 31, 2013

	Shares	Value (Note 2)
SHORT-TERM INVESTMENTS - 7.2%		
State Street Institutional U.S. Government Money Market Fund	13,046,372	\$ 13,046,372
Total Short-Term Investments		13,046,372
(Cost \$13,046,372)		
TOTAL INVESTMENTS - 105.1% (Cost \$179,053,779**)		190,532,286
NET OTHER ASSETS AND LIABILITIES - (0.1%)		(99,943)
TOTAL CALL & PUT OPTIONS WRITTEN - (5.0%)		(9,097,322)
TOTAL NET ASSETS - 100.0%		\$181,335,021

* Non-income producing.

** Aggregate cost for Federal tax purposes was \$179,679,253.

(A) All or a portion of these securities' positions represent covers (directly or through conversion rights) for outstanding options written.

(B) All or a portion of these securities are segregated as collateral for put options written. As of December 31, 2013, the total amount segregated was \$9,999,625.

(C) Rate noted represents annualized yield at time of purchase.

ADR American Depository Receipt

ETF Exchange Traded Fund

PLC Public Limited Company

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Call Options Written	Contracts (100 Shares Per Contract)	Expiration Date	Strike Price	Value (Note 2)
Accenture PLC, Class A	410	January 2014	\$ 75.00	\$297,250
Accenture PLC, Class A	200	February 2014	75.00	153,000
Advance Auto Parts Inc.	460	March 2014	100.00	598,000
Allergan Inc.	369	January 2014	95.00	601,470
Amazon.com Inc.	90	February 2014	385.00	251,775
Apache Corp.	175	January 2014	90.00	4,025
Apache Corp.	250	January 2014	92.50	1,625
Apple Inc.	25	January 2014	550.00	43,938
Apple Inc.	75	February 2014	565.00	166,125
Baxter International Inc.	300	February 2014	70.00	45,000
BB&T Corp.	600	January 2014	35.00	145,800
BB&T Corp.	400	January 2014	36.00	60,800
Broadcom Corp., Class A	500	January 2014	28.00	89,500
Broadcom Corp., Class A	500	February 2014	28.00	117,000
C.H. Robinson Worldwide Inc.	200	January 2014	60.00	5,000
C.H. Robinson Worldwide Inc.	250	February 2014	57.50	61,875
Canadian Natural Resources Ltd.	400	January 2014	33.00	46,000
CBS Corp., Class B	160	January 2014	55.00	140,000
CBS Corp., Class B	160	January 2014	60.00	62,400
Costco Wholesale Corp.	250	January 2014	118.00	52,250
Costco Wholesale Corp.	100	January 2014	120.00	10,100
CVS Caremark Corp.	300	January 2014	62.50	274,500
CVS Caremark Corp.	350	February 2014	62.50	320,250
DIRECTV	300	January 2014	62.50	198,750
DIRECTV	400	January 2014	65.00	170,000
Discovery Communications Inc., Class C	300	March 2014	80.00	172,500
eBay Inc.	600	January 2014	52.50	168,600
eBay Inc.	500	January 2014	55.00	59,500
EMC Corp.	200	January 2014	26.00	2,000
EMC Corp.	500	February 2014	25.00	44,500
Expeditors International of Washington Inc.	400	January 2014	45.00	15,000
Expeditors International of Washington Inc.	300	February 2014	45.00	28,500

See accompanying Notes to Financial Statements.

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Call Options Written	Contracts (100 Shares Per Contract)	Expiration Date	Strike Price	Value (Note 2)
Freeport-McMoRan Copper & Gold Inc.	200	January 2014	\$ 33.00	\$ 95,000
Freeport-McMoRan Copper & Gold Inc.	250	January 2014	37.00	27,875
Freeport-McMoRan Copper & Gold Inc.	250	February 2014	38.00	28,750
Home Depot Inc./The	220	January 2014	75.00	162,250
Home Depot Inc./The	300	January 2014	77.50	148,500
Linear Technology Corp.	500	January 2014	40.00	277,500
Linear Technology Corp.	500	February 2014	41.00	232,500
Lululemon Athletica Inc.	300	March 2014	62.50	68,250
Microsoft Corp.	600	January 2014	35.00	152,400
Microsoft Corp.	350	February 2014	36.00	76,300
Monsanto Co.	270	January 2014	110.00	183,600
Morgan Stanley	450	January 2014	29.00	112,725
Morgan Stanley	500	January 2014	30.00	83,000
Mosaic Co./The	198	January 2014	47.50	17,028
Mosaic Co./The	300	January 2014	50.00	5,700
Mylan Inc.	380	January 2014	39.00	171,000
Mylan Inc.	220	January 2014	40.00	78,100
Oracle Corp.	700	January 2014	34.00	297,500
Oracle Corp.	500	March 2014	35.00	183,750
Panera Bread Co., Class A	210	January 2014	170.00	160,650
Powershares QQQ Trust Series 1	700	January 2014	82.00	432,950
QUALCOMM Inc.	350	January 2014	70.00	152,250
QUALCOMM Inc.	300	January 2014	72.50	63,600
Rockwell Collins Inc.	400	January 2014	70.00	168,000
Schlumberger Ltd.	160	February 2014	90.00	45,280
Schlumberger Ltd.	160	May 2014	92.50	57,200
SPDR S&P 500 ETF Trust	38	January 2014	175.00	38,456
SPDR S&P 500 ETF Trust	250	March 2014	184.00	120,625
SPDR S&P MidCap 400 ETF Trust	150	January 2014	235.00	146,250
Stericycle Inc.	120	February 2014	115.00	42,600
T. Rowe Price Group Inc.	400	January 2014	75.00	348,000
T. Rowe Price Group Inc.	200	January 2014	80.00	79,000
Teva Pharmaceutical Industries Ltd.	300	January 2014	42.50	5,700

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United Technologies Corp.	200	January 2014	110.00	83,000
United Technologies Corp.	140	February 2014	110.00	71,750
Varian Medical Systems Inc.	188	February 2014	75.00	80,840
Varian Medical Systems Inc.	112	February 2014	80.00	18,760
Varian Medical Systems Inc.	180	May 2014	80.00	57,600
Visa Inc., Class A	50	January 2014	200.00	113,750
Total Call Options Written (Premiums received \$5,020,573)				\$9,095,022
Put Options Written				
Monsanto Co.	200	January 2014	97.50	2,300
Total Put Options Written (Premiums received \$49,199)				\$ 2,300
Total Value of Options Written (Premiums received \$5,069,772)				\$9,097,322

See accompanying Notes to Financial Statements.

MCN | Madison Covered Call & Equity Strategy Fund | December 31, 2013

Statement of Assets and Liabilities as of December 31, 2013

Assets:

Investments in securities, at cost	
Unaffiliated issuers	\$179,053,779

Net unrealized appreciation

Unaffiliated issuers	11,478,507
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Total investments at value	190,532,286
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Receivables:

Investments sold	9,499
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Dividends and interest	53,380
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Total assets	190,595,165
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Liabilities:

Payables:

Advisory agreement fees	122,885
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Service agreement fees	39,937
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Options written, at value (premiums received \$5,069,772) (Note 6)	9,097,322
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Total liabilities	9,260,144
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Net assets applicable to outstanding capital
stock

For sales that offer future discounts, revenues are deferred in amounts equal to the discount and subsequently recognized over the period in which discounted services are provided.

Advance payments are recorded as deferred revenue until the services are delivered or obligations are met. Deferred revenue represents the difference between amounts invoiced and amounts recognized as revenues.

Cash and Cash Equivalents

The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

Restricted Cash

At December 31, 2003 and December 31, 2002, approximately \$619,000 and \$640,000, respectively, of cash were classified as restricted cash on the consolidated balance sheets. As of December 31, 2003 and 2002, \$619,000 was related to a compensating balance arrangement associated with a debt facility (see Note 5). As of December 31, 2002, approximately

\$20,000 served as collateral for a letter of credit furnished by a bank pursuant to an equipment lease, which expired during 2003. At June 30, 2004, \$0 (unaudited), of cash was classified as restricted cash on the consolidated balance sheets.

Fair Value of Financial Instruments

The consolidated balance sheets include various financial instruments, primarily cash and cash equivalents, accounts receivable, accounts payable, accrued expenses, and debt. The carrying values of these financial instruments approximate their fair values.

B2eMarkets, Inc.

Notes to Consolidated Financial Statements

Property and Equipment

The Company's property and equipment consist primarily of equipment and leasehold improvements. These assets are recorded at cost. Maintenance and repair costs are expensed as incurred. Fixed assets are depreciated on a straight-line basis over their estimated useful lives, generally ranging from three years for computer equipment to seven years for furniture and fixtures. Leasehold improvements are amortized on a straight-line basis over their estimated useful lives, or the life of the lease, whichever is shorter.

Capitalized Software

Management intends on selling its developed software licenses in future periods and, as a result, accounts for software development costs in accordance with SFAS No. 86, *Accounting for the Costs of Computer Software to Be Sold, Leased, or Otherwise Marketed*. SFAS No. 86 provides that software development costs are expensed as incurred until technological feasibility has been established, at which time such costs are capitalized until the product is available for general release to customers. For the years ended December 31, 2003 and 2002, the Company capitalized approximately \$307,000 and \$735,000 of software development costs, respectively. The Company amortizes the capitalized amounts over a two-year period. Amortization expense of software amounted to \$469,000 and \$754,000 for the years ended December 31, 2003 and 2002, respectively. Additionally, as a result of the acquisition of Diligent Software Systems, Inc. (Diligent) (see Note 3), the Company charged \$399,000 to expense to write down certain software previously capitalized by the Company to its net realizable value.

Intangible Assets

Intangible assets (see Note 3) are amortized using the straight-line method over the following estimated useful lives of the assets:

Acquired technology	2 years
Contracts and customer lists	2 years

Impairment of Goodwill and Intangibles

In 2001, the FASB issued SFAS No. 141, *Business Combinations* (SFAS 141) and SFAS No. 142, *Goodwill and Other Intangible Assets* (SFAS 142). SFAS 141 was effective for the Company for purchase business combinations consummated after June 30, 2001 (see Note 3). The Company has chosen September 30 as the date to perform its annual impairment analysis. There was no impairment for goodwill or intangibles during 2002 or 2003.

Impairment of Long-Lived Assets

The Company evaluates its long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable.

Recoverability of assets to be held and used is measured by a comparison of the carrying amount of any asset to future net undiscounted cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by future discounted cash flows compared to the carrying amount of the asset. No such impairment existed at December 31, 2003 and 2002 or at June 30, 2004 (unaudited).

Income Taxes

The Company recognizes deferred taxes using the liability approach pursuant to which deferred income taxes are calculated based on the differences between the financial and tax bases of assets and liabilities based upon enacted tax laws and rates applicable to the periods in which the taxes become payable. The Company provides a valuation allowance against deferred tax assets, if necessary, based on a number of factors, including available objective evidence.

Significant Customers

For the years ended December 31, 2003 and 2002, one customer accounted for approximately 17% and 40% of revenues, respectively. Additionally, two customer balances accounted for approximately 62% and 60% of the accounts receivable balance as of December 31, 2003 and 2002, respectively.

Advertising Costs

Costs incurred for advertising are charged to expense as incurred. Advertising expense amounted to \$0 and \$19,376 for the years ended December 31, 2003 and 2002, respectively.

Foreign Currency Translation

The reporting currency of the Company is the U.S. dollar. In accordance with SFAS No. 52, *Foreign Currency Translation*, all assets and liabilities in the balance sheets of entities whose functional currency is a currency other than the U.S. dollar are translated into U.S. dollar equivalents at exchange rates as follows: (1) asset and liability accounts at year-end rates, (2) statement of operations accounts at exchange rates approximating the rate in effect on the date recognized, and (3) stockholders' deficit accounts at historical exchange rates.

Translation gains or losses are recorded in stockholders' deficit and transaction gains and losses are reflected in net loss, including the unrealized foreign exchange gains and losses on long-term intercompany advances that are expected to be settled in the foreseeable future.

B2eMarkets, Inc.

Notes to Consolidated Financial Statements

Comprehensive Loss

Comprehensive loss includes net loss, combined with unrealized gains and losses not included in operations and reflected as a separate component of stockholders' deficit.

Recent Accounting Pronouncements

In November 2002, the EITF published Issue No. 00-21, *Revenue Arrangements with Multiple Deliverables* (EITF 00-21), which addresses certain aspects of the accounting by a vendor for arrangements under which it will perform multiple revenue-generating activities. EITF 00-21 addresses how to determine whether an arrangement involving multiple deliverables contains more than one unit of accounting. EITF 00-21 is effective for the Company for revenue arrangements entered into beginning on January 1, 2004. The Company is analyzing the provisions of EITF 00-21 and has yet to determine if the adoption of EITF 00-21 will have a material impact on its 2004 consolidated financial statements.

In May 2003, the FASB issued SFAS No. 150, *Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity* (SFAS 150). SFAS 150 requires that an issuer classify certain financial instruments as a liability because they embody an obligation of the issuer. The remaining provisions of SFAS 150 revise the definition of a liability to encompass certain obligations that a reporting entity can or must settle by issuing its own equity shares, depending on the nature of the relationship established between the holder and the issuer. The provisions of this statement require that any financial instruments that are mandatorily redeemable on a fixed or determinable date or upon an event certain to occur be classified as liabilities. The Company's redeemable convertible preferred stock may be converted into common stock at the option of the stockholder and, therefore, it will not be classified as a liability under the provisions of SFAS 150.

3. Business Combination

Adaptivetrade, Inc.

On February 27, 2004, the Company executed an Asset Purchase Agreement and completed the acquisition of substantially all the assets of Adaptivetrade, Inc. (Adaptive). The Company had previously utilized software technology and consulting services of Adaptive to provide optimization solutions to its customers through a reseller agreement since March of 2002. The assets of Adaptive, including its intellectual property, were acquired by B2e Sourcing Optimization, Inc., a wholly owned subsidiary of B2eMarkets, Inc., in exchange for 200,000 shares of B2eMarkets, Inc. Series B Preferred Stock and 200,000 shares of B2eMarkets, Inc. Common Stock, such shares in total representing approximately 1.2% of the fully diluted shares of the Company.

The acquisition was accounted for as a purchase and, accordingly, the results of operations have been included in the accompanying consolidated statements of operations since the effective date of the acquisition. The fair value attributed to the identifiable intangible assets acquired included \$120,000 in acquired technology and \$50,000 in non-compete agreements. The excess of the purchase price consideration over the amount attributable to assets acquired and liabilities assumed of \$14,000 was recorded as goodwill.

Diligent Software Systems, Inc.

In May 2003, the Company executed an Asset Purchase Agreement and completed the acquisition of substantially all the assets of Diligent. Diligent provided contract management and negotiation software and services to its customers prior to the acquisition. The assets of Diligent, including its intellectual property, were acquired by B2e Contract Management, Inc., a wholly owned subsidiary of B2eMarkets, Inc., in exchange for 2,600,000 shares of B2eMarkets, Inc. Series A Preferred Stock valued at \$2,889,113, the assumption by B2eMarkets of net liabilities of approximately \$209,008 and transaction costs of approximately \$144,252 for total purchase price consideration of \$3,242,373. The Company purchased Diligent to acquire existing client relationships and certain technologies.

The acquisition was accounted for as a purchase and, accordingly, the results of operations have been included in the accompanying consolidated statements of operations since the effective date of the acquisition. The fair value attributed to the identifiable intangible assets acquired included \$242,468 in customer lists and \$463,460 in acquired technology. The excess of the purchase price consideration over the amount attributable to assets acquired and liabilities assumed of \$2,536,445 was

recorded as goodwill. Amortization expense associated with identifiable intangible assets was \$205,895 during the year ended December 31, 2003.

4. Balance Sheet Details

Accounts receivable, net consists of the following (in thousands):

	December 31,		June 30,
	2002	2003	2004
			(unaudited)
Accounts receivable trade	\$ 1,806	\$ 1,475	\$ 794
Less: Allowance for doubtful accounts	(30)	(39)	(39)
	\$ 1,776	\$ 1,436	\$ 755

B2eMarkets, Inc.

Notes to Consolidated Financial Statements

Property and equipment, net consists of the following (in thousands):

	December 31		June 30,
	2002	2003	2004
			(unaudited)
Computer equipment and internal-use software	\$ 4,550	\$ 2,736	\$ 2,789
Office equipment and furniture	524	547	553
Leasehold improvements	105	124	125
	<u>5,179</u>	<u>3,407</u>	<u>3,467</u>
Less accumulated depreciation and amortization	<u>(3,341)</u>	<u>(2,757)</u>	<u>(2,949)</u>
	<u>\$ 1,838</u>	<u>\$ 650</u>	<u>\$ 518</u>

Depreciation and amortization expense for the years ended December 31, 2002 and 2003 and the six months ended June 30, 2003 and 2004 was \$1,524,00, \$1,254,000, \$663,000 (unaudited), and \$194,000 (unaudited) respectively.

5. Debt

On December 1, 2002, the Company obtained a \$600,000 line of credit from a bank to be used to repay the balance of the existing bank line of credit with a former bank. The Company borrowed \$590,000 under this line of credit. Interest is payable at the prime rate (4.00% and 5.25% at December 31, 2003 and 2002, respectively) per annum. Interest payments are due monthly and the principal is due in a lump sum on December 31, 2005. The bank line of credit is collateralized by a cash account with a value not less than 105% of the then outstanding principal balance of the term debt. This cash account was a money market fund of \$619,000 as of December 31, 2003 and is classified as restricted cash on the balance sheet. As of December 31, 2003, the Company had an unpaid principal balance of \$590,000 and accrued interest of \$2,000. In March 2004, the Company fulfilled the obligations on the line of credit

in full.

During 2002, the Company issued a warrant to purchase 26 shares of the Company's Series A Preferred stock with an exercise price of \$40 per share after giving effect to the May 2003 recapitalization in conjunction with the bank line of credit. The warrant is exercisable for a period of 10 years from the date of issuance. The value of the warrant was insignificant.

As of December 31, 2003, principal maturities of debt are scheduled to be repaid as follows, although the full amount was paid during March 2004 (in thousands):

2004	\$
2005	590
	<u>590</u>
	<u>\$ 590</u>

6. Redeemable Convertible Preferred Stock

Preferred Class	Per share liquidation value	Authorized	Issued and Outstanding		
			December 31,		June 30,
			2002	2003	2004
					(unaudited)
Series A	\$ 2.69	1,021,355	204,271		
Series B	\$ 6.00	17,003,407	3,400,681		
Series C	\$ 2.27	157,300,000	18,842,500		
Series C-3	\$ 3.07	11,275,202	2,505,600		
		<u>186,599,964</u>	<u>24,953,052</u>		
New Series A	\$ 1.47	49,786,730		21,832,452	21,832,452
New Series B	\$ 1.45	4,834,818		1,847,186	2,624,531
		<u>54,621,548</u>		<u>23,679,638</u>	<u>24,456,983</u>

B2eMarkets, Inc.

Notes to Consolidated Financial Statements

Recapitalization

In May 2003, the Company completed a recapitalization of its equity structure. All classes of preferred stock were converted into Redeemable New Series A Convertible Preferred Stock (the New Series A Preferred Stock). After recapitalization, the Company had 21,391,165 shares of New Series A Preferred Stock, which had a preference value of \$1.40 per share. All dividends accrued prior to the recapitalization were eliminated as part of the recapitalization. The excess of the carrying value of the preferred stock prior to the recapitalization over the redemption value of the New Series A Preferred Stock was reclassified to additional paid-in capital.

New Series A Preferred Stock

The New Series A Preferred Stock has a cumulative dividend of 8% per annum, which is to be paid in cash, unless at least a majority of the holders of the New Series A Preferred Stock consent to such dividends being paid in securities of the Company. At December 31, 2003 and June 30, 2004, the Company had accrued \$1,461,000 and \$2,661,000, respectively, of unpaid dividends, which are included in the carrying value of the New Series A Preferred Stock. The New Series A Preferred Stock has full voting rights, and the holders vote separately as a class as to certain rights set forth in the Company's Amended and Restated Certificate of Incorporation (the Certificate) and the Recapitalization Agreement and its related agreements.

Upon a Liquidation Event, as defined, the holders of the New Series A Preferred Stock shall be entitled to receive, prior and in preference to any distribution of any of the assets or surplus funds of the Company to the holders of any other class or series of stock, excepting only the New Series B Preferred Stock, an amount equal to \$1.40 per share for each share of New Series A Preferred Stock then held, plus all unpaid accumulated dividends.

Each share of New Series A Preferred Stock is convertible into an equal number of shares of common stock, at the option of the holder, at any time after the date of issuance. The New Series A Preferred Stock will be automatically converted into

shares of common stock, at the then effective New Series A Conversion Price (as defined in the Certificate), immediately upon an Automatic Conversion Event. The shares of New Series A Preferred Stock are redeemable at any time on or after November 19, 2004, at a price per share equal to the original price per share plus accrued dividends, upon the written request of at least a majority of the outstanding shares of the New Series A Preferred Stock, voting as a single class, that all, or any portion of, the New Series A Preferred Stock shall be redeemed.

New Series B Preferred Stock

In July 2003, the Company raised \$2.6 million, net of issuance costs of \$11,635, through the sale of Redeemable New Series B Convertible Preferred Stock (the New Series B Preferred Stock). The shares of New Series B Preferred Stock have certain voting, anti-dilutive, redemption, liquidation and other rights as defined in the New Series B Preferred Stock Purchase Agreement.

In March 2004, the Company raised an additional \$808,000 through the sale of Redeemable New Series B Preferred Stock under terms provided for as part of the July 2003 New Series B Preferred Stock financing.

The New Series B Preferred Stock has a cumulative dividend of 8% per annum, which is to be paid in cash, unless at least a majority of the holders of the New Series B Preferred Stock consent to such dividends being paid in securities of the Company. At December 31, 2003 the Company had accrued \$99,000 and \$277,000, respectively, of unpaid dividends, which are included in the carrying value of the New Series B Preferred Stock. The New Series B Preferred Stock has full voting rights, and the holders vote separately as a class as to certain rights set forth in the Certificate and its related agreements.

Upon a Liquidation Event, as defined, the holders of the New Series B Preferred Stock shall be entitled to receive, prior and in preference to any distribution of any of the assets or surplus funds of the Company to the holders of any other class or series of stock, an amount equal to \$1.40 per share for each share of New Series B Preferred Stock then held, plus all unpaid accumulated dividends.

Under the terms of the New Series B Preferred Stock agreements, each holder of New Series A Preferred Stock could choose to invest their pro rata share, or any portion thereof, in

the New Series B Financing or, in accordance with the agreements, all or a proportionate share of their New Series A Preferred Stock would convert into shares of common stock. 2,158,921 shares of New Series A Preferred Stock were converted to an equal number of common shares pursuant to this provision of the New Series B Preferred Stock agreements.

Each share of New Series B Preferred Stock is convertible into an equal number of shares of common stock, at the option of the holder, at any time after the date of issuance. The New Series B Preferred Stock will be automatically converted into shares of common stock, at the then effective New Series B Conversion Price, as defined in the Certificate, immediately upon an Automatic Conversion Event, as defined. The shares of New Series B Preferred Stock are redeemable at any time on or after November 19, 2004, at a price per share equal to the original price per share plus accrued dividends, upon the written request of at least a majority of the outstanding shares of the New Series B Preferred Stock, voting as a single class, that all, or any portion of, the New Series B Preferred Stock shall be redeemed.

Series A Convertible Preferred Stock

In May 1999, the Company raised \$550,000 through the issuance of 204,271 shares of Series A Convertible Preferred Stock (the Series A Preferred Stock). The offering price of these shares was \$2.6925 per share. The Series A Preferred Stock had a noncumulative 10% dividend rate and was payable only when, as and, if declared by the Board of Directors. The dividends may be paid in cash or securities of the Company, at the option of the Company. The Series A Preferred Stock had voting rights equal to those provided to the holders of the common stock, and voted separately as a class as to certain rights set forth in the Certificate. In May 2003, all then-outstanding shares of Series A Preferred Stock were converted to New Series A Preferred Stock at a rate of 0.5 shares of New Series A Preferred Stock for each share of Series A Preferred Stock.

Upon a Liquidation Event, the holders of the Series A Preferred Stock were entitled to receive prior and in preference to any distribution of any of the assets or surplus funds of the Company to the holders of common stock, an amount equal to \$2.6925 per share for each share of Series A Preferred Stock then held, plus a further amount equal to all declared but unpaid dividends on such shares.

Each share of Series A Preferred Stock was convertible into an equal number of shares of common stock, at the option of the

holder, at any time after the date of issuance. The Series A Preferred Stock was to be automatically converted into shares of common stock, at the then effective Series A Conversion Price (as defined in the Certificate), immediately upon: (i) the closing of the Company's initial public offering where the offering price of the common stock is not less than \$8.00 per share with aggregate proceeds of at least \$30,000,000, (ii) a sale of all the outstanding shares of the Company for cash at a price per share of not less than the Series C-1 Liquidation Amount (as defined in the Certificate) on an as-converted per share basis, or (iii) the merger of the Company with another entity in which (A) the Company's common stock is valued at not less than the Series C-1 Liquidation Amount on an as-converted per share basis, (B) the holders of the Company's common stock receive shares listed on the NASDAQ National Market or other comparable exchange, or (C) the merger partner's shares are sufficiently liquid in the marketplace,

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Notes to Consolidated Financial Statements

as determined by a majority of the holders of the Series C Preferred Stock (as defined below), voting together as a single class (each of (i), (ii), and (iii), an Automatic Conversion Event). In the event that less than 25% of the Series A Preferred Stock that was issued and outstanding as of the Series C Issue Date (as defined in the Certificate) was issued and outstanding, the remaining shares of Series A Preferred Stock would be automatically converted into shares of common stock at the then effective Series A Conversion Price at the election of the holders of at least 50% of the then-outstanding Series A Preferred Stock, Series B Preferred Stock (as defined below), and Series C Preferred Stock, voting together as a single class.

The shares of Series A Preferred Stock were redeemable at any time on or after November 19, 2004, at a price per share equal to the original price per share plus accrued dividends, upon the written request of at least a majority of the outstanding shares of the Series A Preferred Stock, voting as a single class, that all, or any portion of, the Series A Preferred Stock shall be redeemed.

Series B Convertible Preferred Stock

In November 1999, the Company raised an additional \$13,400,000, net of issuance costs of \$35,476, through the issuance of 3,400,681 shares of Series B Convertible Preferred Stock (the Series B Preferred Stock). The offering price of the Series B Preferred Stock was \$3.9595 per share. The Series B Preferred Stock had a cumulative dividend of 8% per annum, which was to be paid in cash, unless at least a majority of the holders of Series B Preferred Stock consent to such dividends being paid in securities of the Company. The Series B Preferred Stock had voting rights equal to those provided to the holders of the common stock, and voted separately as a class as to certain rights set forth in the Certificate and the Series B Stock Purchase Agreement and its related agreements. In May 2003, all then-outstanding shares of Series B Preferred Stock were converted to New Series A Preferred Stock at a rate of 0.5 shares of New Series A Preferred Stock for each share of Series B Preferred Stock.

Upon a Liquidation Event, the holders of the Series B Preferred Stock were entitled to receive prior and in preference to any distribution of any of the assets or surplus funds of the Company to the holders of the Series A Preferred Stock or

common stock, an amount equal to \$3.9595 per share for each share of Series B Preferred Stock then held, plus all unpaid accumulated dividends. During 2003 and prior to the conversion of the Series B Preferred Stock to New Series A Preferred Stock, the Company accrued dividends of \$422,026. At December 31, 2002, the Company had accrued \$3,411,133 of unpaid dividends.

Each share of Series B Preferred Stock was convertible into an equal number of shares of common stock, at the option of the holder, at any time after the date of issuance. The Series B Preferred Stock was to be automatically converted into shares of common stock, at the then effective Series B Conversion Price (as defined in the Certificate), immediately upon an Automatic Conversion Event. The shares of Series B Preferred Stock were redeemable at any time on or after November 19, 2004, at a price per share equal to the original price per share plus accrued dividends, upon the written request of at least a majority of the outstanding shares of the Series B Preferred Stock, voting as a single class, that all, or any portion of, the Series B Preferred Stock shall be redeemed.

Series C Convertible Preferred Stock

During 2001, the Company raised an additional \$25,200,000, net of issuance costs of \$156,873, through the issuance of 12,617,500 shares of Series C-1 and Series C-2 Redeemable Convertible Preferred Stock (the Series C Preferred Stock). Additionally, the Company converted the outstanding balance and accrued interest of \$11,850,000 and \$600,000, respectively, of convertible notes into Series C Preferred Stock. The offering price of the Series C Preferred Stock was \$2.00 per share. The Series C Preferred Stock had a cumulative dividend of 8% per annum, which is to be paid in cash, unless at least a majority of the holders of the Series C Preferred Stock consent to such dividends being paid in securities of the Company. The Series C Preferred Stock had voting rights equal to those provided to the holders of the common stock, and vote separately as a class as to certain rights set forth in the Certificate and the Series C Stock Purchase Agreement and its related agreements. In May 2003, all then-outstanding shares of Series C Preferred Stock were converted to New Series A Preferred Stock at a rate of one share of New Series A Preferred Stock for each share of Series C-1 Redeemable Convertible Preferred Stock and 0.5 shares of New Series A Preferred Stock for each share of Series C-2 Redeemable Convertible Preferred Stock.

Upon a Liquidation Event, the holders of the Series C Preferred Stock were to be equivalent to Series B Preferred Stockholders and would be entitled to receive prior and in preference to any distribution of any of the assets or surplus funds of the Company to the holders of the Series A Preferred Stock, Series B Preferred Stock, or common stock, an amount equal to \$2.00

per share for each share of Series C Preferred Stock then held, plus all unpaid accumulated dividends. During 2003 and prior to the conversion of the Series C Preferred Stock to New Series A Preferred Stock, the Company accrued dividends of \$1,181,141. At December 31, 2002, the Company had accrued \$5,222,900 of unpaid dividends.

Each share of Series C Preferred Stock was convertible into an equal number of shares of common stock, at the option of the holder, at any time after the date of issuance. The Series C Preferred Stock was to be automatically converted into shares of common stock, at the then effective Series C Conversion Price (as defined in the Certificate), immediately upon an Automatic Conversion Event. The shares of Series C Preferred Stock are redeemable at any time on or after November 19, 2004, at a price per share equal to the original price per share plus accrued dividends, upon the written request of at least a majority of the outstanding shares of the Series C Preferred Stock, voting as a single class, that all, or any portion of, the Series C Preferred Stock shall be redeemed.

Series C-3 Convertible Preferred Stock and Series C-3 Warrants

In August 2002, the Company raised an additional \$4,900,000, net of issuance costs of \$75,628, through the issuance of 2,505,600 shares of Series C-3 Convertible Preferred Stock (the Series C-3 Preferred Stock). In addition, 672,768 warrants (the Series C-3 Warrants) to purchase additional Series C-3 Preferred Stock shares were issued to the investors and were exercisable at any time after issuance. The Company allocated \$3,950,475 of the proceeds from this offering to the Series C Preferred Stock and \$1,060,725 to the Series C-3 Warrants based upon their relative fair value. The Company recorded a beneficial conversion feature associated with the issuance of the Series C-3 Preferred Stock of \$1,060,725 and a beneficial conversion feature of \$284,811 associated with the Series C-3 Warrants. In May 2003, all then-outstanding shares of Series C-3 Preferred Stock were converted to New Series A Preferred Stock at a rate of 1.5 shares of New Series A Preferred Stock for each share of Series C-3 Preferred Stock and the warrants to purchase additional Series C-3 Preferred Stock were cancelled.

The offering price of the Series C-3 Preferred Stock was \$2.00 per share. The Series C-3 Preferred Stock has a cumulative dividend of 8% per annum, which is to be paid in cash, unless at least a majority of the holders of Series C-3 Preferred Stock consent to such dividends being paid in securities of the Company. The Series C-3 Preferred Stock had voting rights equal to those provided to the holders of the common stock, and voted separately as a class as to certain rights set forth in the Certificate and the Series C-3 Stock Purchase Agreement and its related agreements.

Upon a Liquidation Event, the holders of the Series C-3 Preferred Stock were entitled to receive prior and in preference to any distribution of any of the assets or surplus funds of the Company to the holders of the Series A Preferred Stock, Series B Preferred Stock, Series C-1 or Series C-2, or common stock, an amount equal to \$3.00 per share for each share of Series C-3 Preferred Stock then held, plus all unpaid accumulated dividends. During 2003 and prior to the conversion of the Series C-3 Preferred Stock to New Series A Preferred Stock, the Company accrued dividends of \$157,063. At December 31, 2002, the Company had accrued \$167,038 of unpaid dividends.

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Each share of Series C-3 Preferred Stock is convertible into an equal number of shares of common stock, at the option of the holder, at any time after the date of issuance. The Series C-3 Preferred Stock will be automatically converted into shares of common stock, at the then effective Series C-3 Conversion Price (as defined in the Certificate), immediately upon an Automatic Conversion Event. The shares of Series C-3 Preferred Stock are redeemable at any time on or after November 19, 2004, at a price per share equal to the original price per share plus accrued dividends, upon the written request of at least a majority of the outstanding shares of the Series C-3 Preferred Stock, voting as a single class, that all, or any portion of, the Series C-3 Preferred Stock shall be redeemed.

7. Common Stock

In May 2003, the Company completed a recapitalization of its equity structure. All common stock was converted into New Series A Preferred Stock at a rate of 0.05 shares of New Series A Preferred Stock for each then-outstanding share of common stock. In July 2003, 2,158,921 shares of New Series A Preferred Stock were converted to an equal number of shares of common stock pursuant to the provisions of the New Series B Preferred Stock agreements (see Note 6). The carrying value of the 2,158,921 shares of New Series A Preferred Stock at the conversion date was \$3,022,489. The \$3,022,274 excess carrying value of the New Series A Preferred Stock over the par value of the common stock was recorded as additional paid-in capital upon conversion.

8. Stock Options and Warrants

The Company has established the 1999 Long-Term Incentive Plan and the 2003 Long-Term Incentive Plan (the Plans) for granting stock options to employees, officers, and directors. The options are granted at or above the estimated fair market value of the Company's stock and expire no later than 10 years from the date of grant. The options are exercisable in accordance with vesting schedules that generally provide for them to be fully exercisable four years after the date of grant. As of December 31, 2003 and 2002, the Company had 4,295,500 and 5,949,850 shares, respectively, of common stock, and 355,350 and 0 shares, respectively, of New Series A Preferred stock reserved for options pursuant to the Plan.

The exercise prices are equal to or exceed the estimated fair market value of the common stock as determined by the Board of Directors on the grant dates. The options expire at various dates through 2013. The exercise price for all options outstanding as of December 31, 2003 ranged from \$0.28 to \$12.00 per share. The weighted-average remaining contractual life of those options outstanding at December 31, 2003 is nine years.

A summary of the Company's option and warrant activity related to the Company's common stock for the two years ended December 31, 2003 is presented below:

	Number of Shares	Weighted- Average Exercise Price
Balance at December 31, 2002	244,632	\$ 7.20
Granted	3,327,176	0.32
Exercised	(208)	12.00
Forfeited	(303,877)	0.56
Balance at December 31, 2003	3,267,723	\$ 0.47
Granted	93,750	0.28
Exercised	(4,350)	0.28
Forfeited	(41,399)	0.44
Balance at June 30, 2004 (unaudited)	3,315,724	\$ 0.47
Options exercisable at end of period	2,012,755	

At December 31, 2003, 1,992,287 options were exercisable at prices ranging from \$0.32 to \$12.00

During 2003, the Company granted 13,000 options to purchase common stock at \$0.28 per share to a nonemployee in addition to payment for services rendered. The options were fully vested upon issuance. The Company deemed the value of the options to be insignificant.

During 2002, the Company granted 948 options to purchase common stock at \$12.00 per share to a nonemployee in addition

to payment for services rendered. The options were fully vested upon issuance. The Company valued the options at \$5,134 and recorded this amount in general and administrative expenses in 2002.

During 2002 and 2003, the Company issued to one of its customers a warrant for the purchase of 5,000 shares of New Series A Preferred stock at an exercise price of \$40.00 per share after giving effect to the May 2003 recapitalization (see Note 6) and a warrant to purchase 139,000 shares of common stock at an exercise price of \$1.40 per share. The warrants are exercisable for a period of 10 years from the date of issuance. The Company deemed the value of the warrants to be insignificant.

B2eMarkets, Inc.

Notes to Consolidated Financial Statements

9. Income Taxes

For the years ended December 31, 2003 and 2002, there is no current provision or benefit for income taxes and the deferred tax benefits have been entirely offset by valuation allowances.

The differences between the amounts of income tax benefit that would result from applying domestic federal statutory income tax rates to the net loss and the net deferred tax assets, related to certain nondeductible expenses, state income taxes, and, most significantly, the changes in the valuation allowance.

The Company's net deferred tax asset consists of the following:

	December 31	
	2003	2002
Gross deferred tax assets:		
Net operating loss	\$ 21,232,528	\$ 18,965,903
Deferred revenue	1,369,280	1,188,128
Start-up and organization costs	459,080	765,134
Accrued vacation		96,370
Depreciation and amortization	899,519	219,354
Other	135,636	107,405
	24,096,043	21,342,294
Gross deferred tax liabilities:		
Capitalized software	(187,526)	(281,890)
Less valuation allowance	(23,908,517)	(21,060,404)
Net deferred tax asset	\$	\$

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some or all of the deferred tax asset will not be realized. The ultimate realization of the deferred tax asset is dependent upon the generation of future taxable income during the periods in which the net operating loss carryforwards are available. Management considers projected future taxable income, the scheduled reversal of deferred tax liabilities, and available tax planning strategies that can be implemented by the Company in making this assessment. Based upon the projected level of historical taxable income over the periods in which the net operating loss carryforwards are available to reduce income taxes payable, management has established a full valuation allowance.

At December 31, 2003, the Company has net operating loss carryforwards of approximately \$52,400,000. The Company's NOL carryforwards will begin to expire in tax year 2019. The timing and manner in which these net operating loss carryforwards may be utilized in any year by the Company will be limited by certain provisions of the U.S. tax code.

10. Commitments and Contingencies

Lease Commitments

Future minimum rental payments associated with noncancelable lease obligations are as follows at December 31, 2003:

	Gross Rentals Under Operating Leases	Sublease Rentals	Net Operating Leases
2004	\$ 918,940	\$ (284,080)	\$ 634,860
2005	489,006	(199,456)	289,550
2006	17,728		17,728
2007			
2008 and thereafter			
	<u>\$ 1,425,674</u>	<u>\$ (483,536)</u>	<u>\$ 942,138</u>

Assets recorded under capital leases aggregated \$0 and \$2,131,528 as of December 31, 2003 and 2002, respectively. Accumulated depreciation of assets under capital leases totaled \$0 and \$1,294,797 at December 31, 2003 and 2002, respectively. Depreciation of the assets under capital lease is included in depreciation and amortization expense.

Rent expense for the years ended December 31, 2003 and 2002 was \$633,119 and \$692,190, respectively. Rent expense is net of sublease income, which was approximately \$261,745 and \$151,649 as of December 31, 2003 and 2002, respectively.

B2eMarkets, Inc.

Notes to Consolidated Financial Statements

Renegotiation of Leases

In February 2004, the Company renegotiated the operating lease for its primary location, reducing its total leased space at that location and returning to the landlord certain space the Company had subleased to another tenant. The new lease extends through 2008.

Litigation

The Company is party to certain legal actions arising in the ordinary course of business. In the opinion of the Company's management, the liability, if any, under these claims will not have a material effect on the Company's consolidated financial position or the results of its operations.

In March 2003, the Company reached a settlement of its patent infringement litigation with FreeMarkets, Inc. (FreeMarkets). The payments to be made to FreeMarkets under this settlement have been included in the balance of accrued expenses as of December 31, 2002.

11. Employee Benefit Plan

During 2000, the Company established a contributory employee savings plan under Section 401(k) of the Internal Revenue Code, which is available to all employees. The Company may contribute discretionary amounts to individual participant accounts based on specific provisions of the plan. The Company has made no contributions since the plan's inception.

12. Subsequent Events

Sale of Company to Verticalnet, Inc.

On July 19, 2004, the Company was merged with and into Popcorn Acquisition Sub, Inc., a wholly-owned subsidiary of Verticalnet, Inc., pursuant to an Agreement of Merger, by and among Verticalnet, Inc., Popcorn Acquisition Sub, Inc. and the Company dated July 16, 2004. Under the agreement, the holders of shares of preferred stock of the Company received an aggregate of 5.1 million shares of Verticalnet common stock and a note. The note has a face amount of \$5,925,603 and is convertible at the option of Verticalnet or the noteholder into 2,949,204 shares of Verticalnet common stock if such conversion feature is approved by the shareholders of Verticalnet at its 2004 annual shareholders meeting.

PRO FORMA FINANCIAL STATEMENTS

VERTICALNET, INC.

**PRO FORMA CONDENSED CONSOLIDATED
FINANCIAL STATEMENTS**

BASIS OF PRESENTATION

Tigris Corp. (Tigris) was acquired by Verticalnet on January 30, 2004 and B2eMarkets, Inc. (B2eMarkets) was acquired by Verticalnet on July 19, 2004. The accompanying unaudited pro forma condensed consolidated balance sheet as of June 30, 2004, and the related unaudited pro forma condensed consolidated statements of operations for the six months ended June 30, 2004 and the year ended December 31, 2003, give effect to the acquisitions of Tigris and B2eMarkets, as described in Note 2 of the Notes to Pro Forma Condensed Consolidated Financial Statements, as if the transactions had occurred as of June 30, 2004 in the case of the unaudited pro forma condensed consolidated balance sheet, and as of January 1, 2003 in the case of the unaudited pro forma condensed consolidated statements of operations.

The accompanying unaudited pro forma condensed consolidated balance sheet as of June 30, 2004 also reflects the \$3.0 million private placement completed in August 2004, as described in Note 3 of the Notes to Pro Forma Condensed Consolidated Financial Statements.

The unaudited pro forma condensed consolidated financial statements have been prepared by management of Verticalnet and should be read in conjunction with Verticalnet's historical consolidated financial statements, which have been previously filed in Verticalnet's Annual Report on Form 10-K, as amended, for the year ended December 31, 2003 and its Quarterly Report on Form 10-Q for the period ended June 30, 2004, and the historical financial statements of B2eMarkets, which are included elsewhere in this Form 8-K/A and the historical financial statements of Tigris, which were previously filed on Form 8-K/A by Verticalnet on April 13, 2004. Since the unaudited pro forma condensed consolidated financial statements which follow are based upon the financial condition and operating results of both B2eMarkets and Tigris during periods when it was not under the control or management of Verticalnet, the information presented may not be indicative of the results which would have actually been obtained had the acquisitions been completed on January 1, 2003 nor is it indicative of future financial or operating results.

Verticalnet, Inc.
Unaudited Pro Forma Condensed Consolidated Balance Sheet
June 30, 2004

(in thousands)

	Historical (Note 1)			Pro Forma August Private Placement Adjustments (Note 3)	(Note 2)	Pro Forma
	Verticalnet	B2eMarkets				
Assets						
Current assets:						
Cash and cash equivalents	\$ 6,966	\$ 698	\$ 3,000	\$ (2,430)(a)		\$ 8,234
Accounts receivable, net	6,181	755				6,936
Prepaid expenses and other current assets	873	185				1,058
Total current assets	14,020	1,638	3,000	(2,430)		16,228
Property and equipment, net	1,037	518		(143)(c)		1,412
Goodwill	4,924	2,550		11,134(b)		16,058
				(2,550)(c)		
Other intangible assets, net	3,442	552		3,780(b)		7,222
				(552)(c)		
Other assets	1,078	19				1,097
Total assets	\$ 24,501	\$ 5,277	\$ 3,000	\$ 9,238		\$ 42,017
Liabilities and shareholders equity (deficit)						
Current liabilities:						
Current portion of long-term debt and	\$ 1,259	\$	\$	\$		\$ 1,259

convertible notes					
Accounts payable and accrued expenses	4,045	1,744	212	(11)(c)	\$ 5,990
Deferred revenue	1,146	4,344		(2,030)(c)	3,460
Total current liabilities	6,450	6,088	212	(2,041)	10,709
Long-term debt	61	1			62
Convertible promissory notes				3,899(a)	3,899
Total liabilities	6,511	6,089	212	1,858	14,669
Redeemable convertible preferred stock		37,074		(37,074)(d)	
Total shareholders equity (deficit)	17,990	(37,886)	2,788	6,569(a)	27,347
				37,886(d)	
Total liabilities and shareholders equity (deficit)	\$ 24,501	\$ 5,277	\$ 3,000	\$ 9,238	\$ 42,017

The accompanying notes are an integral part of these statements.

Verticalnet, Inc.
**Unaudited Pro Forma Condensed Consolidated Statement
of Operations**
For the year ended December 31, 2003

(in thousands, except per share data)

	Historical (Note 1)		Pro Forma Adjustments		
	Verticalnet	B2eMarkets	Tigris	(Note 2)	Pro Forma
Revenues	\$ 9,633	\$ 8,108	\$ 9,786	\$	\$ 27,527
Cost of revenues	3,147	4,357	5,810		13,314
Gross profit	6,486	3,751	3,976		14,213
Operating expenses:					
Research and development	4,070	3,457			7,527
Selling, general, and administrative	6,847	7,160	4,380	(83)(k) (474)(l)	17,830
Restructuring reversals	(480)				(480)
Stock-based compensation	544				544
Amortization of other intangible assets		206		1,224(e) 1,386(m)	2,816
Total operating expenses	10,981	10,823	4,380	2,053	28,237
Operating loss	(4,495)	(7,072)	(404)	(2,053)	(14,024)
Interest and other expense, net	6,520	23	34	474(f) 507(g)	7,558
Loss before income tax benefit	(11,015)	(7,095)	(438)	(3,034)	(21,582)
Income tax benefit			32	(32)(n)	
Net loss	\$ (11,015)	\$ (7,095)	\$ (406)	\$ (3,066)	\$ (21,582)

Net loss per share - basic and diluted	\$	(0.70)		\$ (0.96)
Weighted average common shares outstanding used in basic and diluted per share calculation (Note 4)		15,675	6,883	22,558

The accompanying notes are an integral part of these
statements.

Verticalnet, Inc.
**Unaudited Pro Forma Condensed Consolidated Statement
of Operations**
For the six months ended June 30, 2004

(in thousands, except per share data)

	Historical (Note 1)			Pro Forma Adjustments (Note 2)	Pro Forma
	Verticalnet	B2eMarkets	Tigris		
Revenues	\$ 11,071	\$ 3,883	\$ 982	\$	\$ 15,936
Cost of revenues	5,131	1,746	539		7,416
Gross profit	5,940	2,137	443		8,520
Operating expenses:					
Research and development	2,445	1,836			4,281
Selling, general, and administrative	5,360	2,643	306	4(o) (40)(p)	8,273
Stock-based compensation	921				921
Amortization of other intangible assets	377	206		592(h) 92(q)	1,267
Total operating expenses	9,103	4,685	306	648	14,742
Operating loss	(3,163)	(2,548)	137	(648)	(6,222)
Interest and other expense, net	318	3	1	237(i) 278(j)	837
Net loss	\$ (3,481)	\$ (2,551)	\$ 136	\$ (1,163)	\$ (7,059)
Net loss per share - basic and diluted	\$ (0.14)				\$ (0.24)
Weighted average common	24,500			5,398	29,898

shares outstanding used in basic and diluted per share calculation (Note 4)			
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The accompanying notes are an integral part of these statements.

Note 1: HISTORICAL FINANCIAL STATEMENTS

The historical balances of Verticalnet, Inc. ("Verticalnet" or the "Company") reflect the consolidated balance sheet as of June 30, 2004, and the consolidated results of operations for the year ended December 31, 2003 and six months ended June 30, 2004, as reported in the consolidated financial statements which have been previously filed in the Company's SEC filings. The historical balances of B2eMarkets, Inc. ("B2eMarkets") as of June 30, 2004 and for the year ended December 31, 2003 and six months ended June 30, 2004 were derived from B2eMarkets historical consolidated financial statements. The historical statements of operations balances of Tigris Corp ("Tigris") represent the results for Tigris, prior to the acquisition date of January 30, 2004.

Note 2: ACQUISITIONS

B2eMarkets, Inc.

On July 19, 2004, Verticalnet, through its direct, wholly-owned subsidiary Popcorn Acquisition Sub, Inc., a Delaware corporation ("Acquisition Sub"), acquired B2eMarkets through a merger. The acquisition of B2eMarkets was made pursuant to an Agreement of Merger (the "Merger Agreement") dated July 16, 2004 by and among Verticalnet, Acquisition Sub and B2eMarkets. Pursuant to the terms of the Merger Agreement, B2eMarkets was merged with and into Acquisition Sub on July 19, 2004, with Acquisition Sub being the surviving corporation. Thereafter, Acquisition Sub changed its name to Verticalnet Employees II. As a result of the merger, B2eMarkets's wholly-owned subsidiaries, B2e Sourcing Optimization, Inc., B2e Contract Management, Inc., B2eMarkets, B.V., B2eMarkets France S.A.R.L., and B2eMarkets UK Limited (together referred to as "B2e Subsidiaries") are now indirect, wholly-owned subsidiaries of Verticalnet.

B2eMarkets' business consists of the development of an eSourcing software suite which includes strategy formulation, negotiation management, contract management and compliance, and performance management. The combined company, which operates under the Verticalnet® name, brings together Verticalnet's top rated Spend Analysis and Advanced Sourcing solutions with B2eMarkets' leading eSourcing suite. Benefits of this combination include:

B2eMarkets brings proven best of breed competence in program management, eSourcing, contract management, and performance management capabilities, which when combined with Verticalnet's existing capabilities, provides a comprehensive suite of supply management solutions.

The combination of B2eMarkets and Verticalnet creates a company with increased scale from a financial, customer, and product standpoint. B2eMarkets generated approximately \$8.1 million in revenues in the year ended December 31, 2003.

A majority of B2eMarkets' customers operated via an on-demand software model with long-term subscription agreements. The subscription model provides Verticalnet with a more balanced software and services revenue mix and enhanced visibility of future revenues.

With over 35 software customers with registered users on six continents using B2eMarkets' solutions, Verticalnet has expanded its base of software customers. In addition, the combined company has more than ten European customers in France, the United Kingdom, and Northern Europe.

Having been partners for the six months prior to the merger, the companies worked closely together in go-to-market efforts and in joint product planning. Prior to the merger, Verticalnet and B2eMarkets had several common customers and had been jointly selected in multiple competitive sales processes.

The consideration for the purchase transaction was approximately \$12.9 million, including transaction costs of approximately \$2.4 million. Pursuant to the Merger Agreement, Verticalnet agreed to issue an aggregate amount of 5,100,000 shares of common stock, valued on the date of closing at approximately \$6.6 million, and a promissory note (the Promissory Note) in the principal amount of approximately \$5.9 million (valued at approximately \$3.9 million by an independent appraiser) to the holders of shares of preferred stock of B2eMarkets. The Promissory Note accrues interest at the rate of 8% per annum. Half of the outstanding principal amount of the Promissory Note is payable on July 16, 2007 and the remaining outstanding principal amount and interest earned thereon is payable on July 16, 2008. Subject to approval by Verticalnet's shareholders, the Promissory Note is convertible into 2,949,204 shares of Verticalnet common stock. Upon obtaining such approval, either Verticalnet or the noteholders can require the conversion of the Promissory Note into Verticalnet common stock.

The acquisition will be accounted for under the purchase method of accounting. Under this method, the purchase price is allocated to the assets acquired and liabilities assumed based on

their fair values at the acquisition date. Such allocation has been based on estimates that may be revised at a later date. Therefore, actual amounts may differ from those in the unaudited pro forma condensed consolidated financial statements. The excess of the purchase price over the fair value of the net tangible assets acquired was approximately \$14.9 million, which has been allocated to the covenants not-to-compete, customer contracts, customer relationships, technology and goodwill in the amounts of \$40,000, \$610,000, \$1.5 million, \$1.7 million and \$11.1 million, respectively. The following are the estimated useful lives for each intangible asset:

Covenants not-to-compete	1.0 year
Customer contracts	1.5 years
Customer relationships	6.5 years
Technology	3.0 years

The following pro forma adjustments for the B2eMarkets acquisition are reflected in the unaudited pro forma condensed consolidated balance sheet as of June 30, 2004, and the unaudited pro forma condensed consolidated statements of operations for the year ended December 31, 2003 and for the six months ended June 30, 2004:

Unaudited Pro Forma Adjustments to Condensed Consolidated Balance Sheet

(a) Reflects the consideration issued by the Company to consummate the acquisition (in thousands):

Issuance of common stock	\$ 6,569
Issuance of convertible promissory note	3,899
Transaction costs	2,430
	<hr/>
Total consideration	\$ 12,898
	<hr/>

(b) Reflects the recording of the purchase transaction (in thousands):

Total consideration per above	\$ 12,898
Fair value of net liabilities assumed	2,016
	<hr/>
Excess purchase price to be allocated	\$ 14,914
	<hr/>

The excess purchase price was allocated as follows (in thousands):

Covenant not-to-compete	\$ 40
Customer contracts	610
Customer relationships	1,480
Technology	1,650
Goodwill	11,134
	<hr/>
	\$ 14,914
	<hr/>

(c) Reflects opening balance sheet adjustments.

(d)

Reflects the elimination of the preferred stock and shareholders' deficit accounts of B2eMarkets.

Unaudited Pro Forma Adjustments to Condensed Consolidated Statement of Operations for the year ended December 31, 2003

(e) Reflects amortization expense for the intangible assets.

(f) Reflects the interest expense accrued on the convertible promissory note.

(g) Reflects the accretion on the carrying value of the convertible promissory note.

Unaudited Pro Forma Adjustments to Condensed Consolidated Statement of Operations for the six months ended June 30, 2004

(h) Reflects amortization expense for the intangible assets.

(i) Reflects the interest expense accrued on the convertible promissory note.

(j) Reflects the accretion on the carrying value of the convertible promissory note.

Tigris Corp.

On January 30, 2004, Verticalnet, through its direct, wholly-owned subsidiary, River Acquisition Co., Inc., a Delaware corporation ("Acquisition Co. "), acquired through a merger Tigris Corp., a New York corporation, from Brent Habig (the "Stockholder "). The merger was made pursuant to an Agreement of Merger (the "Tigris Merger Agreement ") dated January 30, 2004 by and among Verticalnet, Acquisition Co. and the Stockholder. Pursuant to the terms of the Tigris Merger Agreement, Tigris was merged with and into Acquisition Co. on January 30, 2004, with Acquisition Co. being the surviving corporation. Thereafter, Acquisition Co. changed its name to Tigris I Corp. As a result of the merger, Tigris 's wholly-owned subsidiary, Tigris Consulting UK, Ltd. ("Tigris UK "), is now an indirect, wholly-owned subsidiary of Verticalnet.

As a result of this acquisition, the Company has enhanced its capability to serve enterprise customers by expanding its spend analysis and strategic sourcing domain expertise while adding additional technology tools in the area of bid optimization and advanced sourcing tools.

The consideration for the purchase transaction was approximately \$12.1 million, including transaction costs of approximately \$300,000. The consideration included \$3.5 million in cash, 1,870,450 shares of Verticalnet 's common stock valued on the date of closing at approximately \$5.7 million (355,029 shares were held in escrow until they were released to the Stockholder on April 30, 2004), issuance of employee options to purchase 751,670 shares of Verticalnet 's common stock valued as of the date of acquisition at \$2.2 million, and assumed debt of approximately \$346,000. The acquisition was accounted for under the purchase method of accounting. Under this method, the purchase price was allocated to the assets acquired and liabilities assumed based on their fair values at the acquisition date. The excess of the purchase price over the fair value of the net tangible assets acquired was approximately \$8.5 million, which has been allocated to customer contracts and relationships, a strategic relationship, a non-compete agreement and goodwill in the amounts of \$1.8 million, \$1.5 million, \$200,000 and \$4.9 million, respectively. The amortization of the customer contracts and relationships and the strategic relationship intangible assets are based on an attrition analysis and the non-compete intangible asset is being amortized on a straight line basis. The following are the amortization percentages by year:

<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>	<u>Year 4</u>	<u>Year 5</u>
47.3%	37.6%	15.1%		

Customer contracts and relationships					
Strategic relationship	31.1%	24.3%	19.9%	13.9%	10.8%
Non-compete agreement	20.0%	20.0%	20.0%	20.0%	20.0%

The following pro forma adjustments for the Tigris acquisition are reflected in the unaudited pro forma condensed consolidated statements of operations for the year ended December 31, 2003 and for the six months ended June 30, 2004:

Unaudited Pro Forma Adjustments to Condensed Consolidated Statement of Operations for the year ended December 31, 2003:

- (k) Reflects the change in compensation for Tigris Chief Executive Officer and sole shareholder, based on the amount per his new employment agreement.
- (l) Represents the effect of the renegotiated operating lease for a New York City office, which was negotiated in concert with the transaction.
- (m) Reflects amortization expense for the intangible assets.
- (n) Reflects the elimination of Tigris historical tax benefit.

Unaudited Pro Forma Adjustments to Condensed Consolidated Statement of Operations for the six months ended June 30, 2004:

- (o) Reflects the change in compensation for Tigris Chief Executive Officer and sole shareholder, based on the amount per his new employment agreement.
- (p) Represents the effect of the renegotiated operating lease for the New York City office, which was negotiated in concert with the transaction.
- (q) Reflects amortization expense for the intangible assets.

Note 3: PRIVATE PLACEMENT

In August 2004, the Company completed a \$3.0 million private placement of its common stock. The Company issued 3,000,000 shares of common stock along with warrants to purchase 1,200,000 shares of common stock at an exercise price of \$1.25 per share. The Company received approximately \$2.8 million in net proceeds from this transaction.

Note 4: PRO FORMA BASIC AND DILUTED NET LOSS PER SHARE

The weighted average shares outstanding used in the pro forma basic and diluted net loss per share calculations for the year ended December 31, 2003 and for the six months ended June 30, 2004 includes 1,870,450 and 5,100,000 shares of Verticalnet's common stock issued in the acquisitions of Tigris and B2eMarkets, respectively, as if the acquisitions had occurred on January 1, 2003. In addition, 355,029 common shares held in escrow in connection with the acquisition of Tigris have been excluded from the loss per share calculation and are only included in the loss per share calculation subsequent to their deemed release date of March 31, 2003.

For the purposes of the proforma, the shares are deemed to be released on March 31, 2003 (i.e., 3 months after their deemed issuance date of January 1, 2003) rather than their actual release date of April 30, 2004.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned thereunto duly authorized.

VERTICALNET, INC.

Date: October 1, 2004

By: /s/ GENE S. GODICK

Name: Gene S. Godick

Title: Executive Vice President
and Chief Financial Officer

EXHIBIT INDEX

Exhibit No.	Exhibit
2.1	Agreement of Merger, by and among Verticalnet, Inc., Popcorn Acquisition Sub., Inc. and B2eMarkets, Inc. dated July 16, 2004. (1)
4.1	Form of Registration Rights Agreement by and among Verticalnet, Inc. and certain former stockholders of B2eMarkets, Inc. dated July 16, 2004. (1)
4.2	Convertible Promissory Note dated July 16, 2004 from Verticalnet, Inc. to FBR Investment Management, Inc. (1)
23.1	Consent of Ernst & Young LLP *
99.1	Press release dated July 19, 2004. (2)

* Filed herewith

(1) Filed as an exhibit to the registrant's report on Form 8-K dated August 3, 2004.

(2) Filed as an exhibit to the registrant's report on Form 8-K dated July 21, 2004.