

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

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FORM 10-K

(X) ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934  
FOR THE FISCAL YEAR ENDED DECEMBER 31, 1999

OR

( ) TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934  
FOR THE TRANSITION PERIOD OF \_\_\_\_\_ TO \_\_\_\_\_

COMMISSION FILE NUMBER 1-11388

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PLC SYSTEMS INC.  
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

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YUKON TERRITORY, CANADA  
(STATE OR OTHER JURISDICTION OF  
INCORPORATION OR ORGANIZATION)

04-3153858  
(I.R.S. EMPLOYER  
IDENTIFICATION NO.)

10 FORGE PARK, FRANKLIN, MASSACHUSETTS  
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES)

02038  
(ZIP CODE)

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(508) 541-8800  
(REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE)

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SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

TITLE OF EACH CLASS -----	NAME OF EACH EXCHANGE ON WHICH REGISTERED -----
COMMON STOCK, NO PAR VALUE	AMERICAN STOCK EXCHANGE

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT:

NONE  
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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes X No  
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Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [ ]

The aggregate market value of the voting stock held by non-affiliates of the registrant, based on the last sale price for such stock on March 8, 2000, was \$82,192,815. As of March 8, 2000, 21,223,385 shares of Common Stock, no par value per share, were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement, which will be issued in connection with the 2000 Annual Meeting of Shareholders, are incorporated by reference in Part III of its Annual Report in Form 10-K.

FORWARD-LOOKING STATEMENTS

This report (including certain information incorporated herein by

reference) contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements include statements in Item 1. "Business"; Item 3. "Legal Proceedings"; Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations"; and Item 7A. "Quantitative and Qualitative Disclosures about Market Risk". Statements containing terms such as "believes", "plans", "expects", "anticipates", "intends", "estimates" and similar expressions contain uncertainty and are forward-looking statements. Forward-looking statements are based on current plans and expectations and involve known and unknown risks and uncertainties that could cause actual results to differ materially from those described in the forward-looking statements. Such factors and uncertainties include, but are not limited to: the successful ability to secure any required financing; the ability to convince health care professionals and third party payers of the medical and economic benefits of the Company's products; the absence of reimbursement for health care providers who use the Company's products, or the risk that reimbursement, if provided, will be inadequate; restrictions imposed by regulatory agencies such as the U.S. Food and Drug Administration; competitive developments; business conditions, growth in certain market segments, and the general economy; uncertainty that any patent protection will exclude competitors or that the Company's products do not infringe any intellectual property rights of others; and the risk factors set forth in Item 7, Item 7A, the Company's other SEC reports and the Company's press releases.

#### PART I

#### ITEM 1. BUSINESS.

##### General

PLC Systems Inc. ("PLC" or the "Company") has developed a patented high-powered carbon dioxide ("CO(2)") laser system known as The Heart Laser-TM-System for use in the treatment of coronary artery disease in a surgical laser procedure, pioneered by the Company and its clinical investigators, known as transmyocardial revascularization ("TMR").

TMR is a new laser based treatment for relieving debilitating pain in patients suffering from severe coronary artery disease ("CAD"). Each TMR procedure requires a sterile, single use, TMR kit containing assorted TMR handpieces, drapes and other disposable items. The Company's CO(2) laser is used by a cardiovascular surgeon to create between 20 and 40 tiny channels in the heart wall of a patient suffering from severe CAD. The Company's Heart Laser System was developed specifically for TMR and it is believed to be the only TMR system that can create a channel completely through the heart wall with a single laser pulse. In addition, the Company's Heart Laser System uses patented technology to fire this single laser pulse in the fraction of a second between a patient's heartbeats. This patented "synchronization" technology ensures that The Heart Laser System will only fire at a relatively safe point in a patient's heartbeat cycle when the heart is relatively still and unresponsive to stimuli. The procedure does not require a heart-lung bypass machine and is performed through a small incision between the patient's ribs while the patient's heart is beating.

The Company estimates that each year approximately 120,000 patients worldwide are diagnosed with severe CAD which is not treatable by conventional revascularization techniques. CAD is a form of heart disease caused by the blockage of blood flow into the coronary arteries which supply oxygen-rich blood to the heart. Typically, severe CAD patients experience excruciating spasmodic attacks of chest pain, or "angina", and often shortness of breath and fatigue. No longer candidates for traditional surgery, these patients are generally on maximum drug therapy. U.S. clinical studies have demonstrated The Heart Laser System to be safe and effective in decreasing angina by two or more classes (angina is measured in classes from one to four, one being the least painful and four being the most) in nearly 75% of the patients studied; in fact, TMR using The Heart Laser System eliminated all angina in one-third of the patients studied.

Over 5,500 patients have been treated with the Company's Heart Laser System in the United States and abroad. As of December 31, 1999, the Company had shipped 135 Heart Laser Systems worldwide.

##### RECENT DEVELOPMENTS

Since the Company's last annual report on Form 10-K, the following significant events and accomplishments have occurred:

**MEDICARE REIMBURSEMENT BEGINS.** On July 1, 1999, the Health Care Financing Administration ("HCFA") implemented nationwide coverage for Medicare patients receiving TMR with devices approved by the U.S. Food and Drug Administration (the "FDA"). The decision allows health care providers who use the PLC Heart Laser System to receive payment for TMR procedures performed on patients insured by Medicare. During the previous two years, HCFA had denied all coverage for Medicare patients receiving TMR. In October 1999, HCFA further announced that its TMR coverage policy included cases where TMR is used as an adjunct to coronary artery bypass grafting ("CABG").

**MANAGEMENT CHANGES AT PLC.** During 1999, PLC's chief executive officer and chief financial officer resigned. A new chief financial officer was appointed in November 1999 and a new chief executive officer was appointed in December 1999. Mark R. Tauscher was appointed president, chief executive officer and a director of PLC on December 22, 1999. Mr. Tauscher has over 20 years of

experience in medical product sales, marketing and management at companies including Quinton Instrument Company, Marquette Medical Systems and Hewlett Packard.

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James G. Thomasch was appointed senior vice president of finance and administration, chief financial officer and treasurer on November 8, 1999. Mr. Thomasch is a certified public accountant with over 18 years of experience. Mr. Thomasch has served as chief financial officer for XRE Corporation and Angiographic Devices Corporation and as an audit manager for Arthur Andersen LLP. Most recently, Mr. Thomasch was the XRE division president and chief operating officer for Trex Medical Corporation.

**NEW DIRECTORS JOIN PLC'S BOARD.** In September 1999, two new directors were appointed to PLC's Board of Directors, Alan H. Magazine and Kevin J. Dunn. For the past 10 years, Mr. Magazine served as president and chief executive officer of the Health Industry Manufacturer's Association, the largest worldwide association for medical technology companies. Prior to this, Mr. Magazine was the president and chief executive officer of the Foundation for American Economic Competitiveness and its operating arm, the Council on Competitiveness. Mr. Dunn is the senior managing director for the Boston office of The Robinson Humphrey Company, an investment banking firm. Previously, Mr. Dunn worked for Tucker Anthony Incorporated for over 15 years, most recently as senior managing director for the investment banking group and a director of the firm. In May 1999, Harold Capozzi, a PLC director since 1991, retired from the Board.

**PLC RECEIVES PMR PATENT.** In 1999 PLC received U.S. Patent No. 5,893,848 covering a gauging system for monitoring the depth of channels created in percutaneous myocardial revascularization, known as "PMR" or "PTMR". Knowing the depth of channels created during PMR is believed to be important to performing PMR procedures safely and effectively.

**PLC RECEIVES ISO 9001 CERTIFICATION.** In March 1999, PLC received ISO 9001 certification, allowing the Company to place the CE Mark on its products.

**PLC HEART LASER SYSTEM APPROVED FOR SALE IN SOUTH KOREA.** In July 1999, the Korean Food and Drug Administration approved the PLC Heart Laser System for commercial distribution throughout South Korea.

#### BACKGROUND

In 1981, the Company's former Chairman, Dr. Robert I. Rudko, formed Laser Engineering, Inc. ("LEI"), now PLC Medical Systems, Inc., to develop and commercialize sealed-off carbon dioxide ("CO(2)") lasers. Dr. Rudko, who holds a Ph.D. in electrical engineering from Cornell University, had spent over twenty-five years designing and developing CO(2) laser systems for Raytheon Company. In the late 1980s, a heart surgeon at the San Francisco Heart Institute, Dr. John Crew, was performing early studies of TMR on hearts that had been stopped and placed on a heart-lung machine. Although these early studies appeared promising, the efficacy of the TMR treatment could not be proven unless the procedure could be performed on a beating heart. Since no laser existed at that time which could perform such a medical procedure, the San Francisco Heart Institute turned to Dr. Rudko and LEI to design and develop such a laser. The result of that effort was The Heart Laser System, a high-powered laser system capable of creating a channel completely through a human heart wall with a single laser pulse delivered in the fraction of a second between heartbeats.

In November 1990, the Company received a Phase I Investigational Device Exemption ("IDE") for its Heart Laser System from the FDA. In approving the Phase I study, the FDA permitted the use of The Heart Laser System for patients considered not suitable for any other intervention. Phase I trials were performed by Dr. John Crew and completed in October 1991. In April 1992, the Company received Phase II clearance from the FDA to perform TMR on 50 patients at four clinical sites. This clearance was expanded to eventually include 201 patients at eight clinical sites. In 1995, the FDA approved three new IDEs for studies of TMR using The Heart Laser System. The first was a 100 patient randomized study (Phase III) comparing TMR patients to patients receiving medical management. The study was later expanded to 200 patients. The second study was a 400 patient randomized trial comparing TMR patients to patients receiving a second bypass surgery. The third study compared patients receiving TMR in conjunction with bypass surgery to patients receiving only bypass surgery.

The Company recently undertook an effort to gather long-term (more than 12 months) data on its clinical study

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patients. The long-term TMR analysis included 70 patients at eight hospitals. Each patient had been suffering from severe coronary artery disease, including chronic angina, before receiving treatment with The Heart Laser System. The average age of the patients at enrollment was 63. The average preoperative angina class for the group was 3.8. Angina is measured in classes ranging from one to four, with one being the least painful and four being the most painful. After an average of 34 months following the TMR procedure, the group's average angina class was improved from 3.8 to 1.5. This was virtually unchanged from the 1.4 average angina class reported at 12 months postoperatively. In fact, three

years after TMR with The Heart Laser System, 23% of the patients reported having no angina and 58% were in class 1 or 2.

Since April 1992, the Company has received 21 U.S. patents relating to the underlying laser technology, the use of a laser on a beating heart, The Heart Laser System handpiece and other laser accessories. The Company also has 11 U.S. patent applications pending that cover various aspects of the technology for The Heart Laser System and the process by which a laser is used to revascularize the myocardium, as well as other laser technologies. The Company also holds a number of foreign patents and patent applications.

On August 20, 1998, the Company received approval from the FDA to market The Heart Laser System throughout the U.S. to treat the estimated 80,000 domestic patients each year who suffer from severe coronary artery disease but cannot be treated with conventional coronary revascularization techniques such as bypass surgery or angioplasty. PLC was the first company to receive FDA approval to commercialize a product to perform TMR.

The Company was incorporated pursuant to the COMPANY ACT of British Columbia, Canada on March 3, 1987. The Company transferred its jurisdiction of incorporation to the Yukon Territory of Canada in March 1999. The Company's principal offices and manufacturing facilities are located at 10 Forge Park, Franklin, Massachusetts 02038. The Company's telephone number is (508) 541-8800. As used herein, the term "Company" means, unless the context requires otherwise, PLC and its subsidiaries, PLC Medical Systems, Inc., PLC Sistemas Medicos Internacionais GmbH, PLC Medical Systems AG, PLC Medical Systems Asia/Pacific Pte Ltd and PLC Medical Systems Australia Pty Ltd.

#### CARDIOVASCULAR DISEASE AND CURRENT THERAPIES

Today 60 million Americans are suffering from cardiovascular disease with over 12.2 million Americans suffering from coronary heart disease. Cardiovascular disease is the leading cause of death in the U.S., resulting in over 41% (or 950,000) of all deaths in the U.S. annually. Arteriosclerosis, the principal form of cardiovascular disease and primary cause of heart attacks, is characterized by a progressive accumulation of fatty deposits known as "plaque" in the walls of arteries and the resulting narrowing of the interior of the arteries. Arteriosclerosis reduces blood flow to the muscle wall ("myocardium") of the heart, causing ischemia and resulting angina and can further lead to a complete occlusion of the artery causing a heart attack. According to the 2000 Heart and Stroke Facts Statistics published by the American Heart Association (the "AHA"), approximately 607,000 coronary bypass operations and 447,000 balloon angioplasty procedures were performed in the U.S. in 1997. The AHA estimates the cost of cardiovascular disease in the year 2000 at \$326.6 billion, including physician and nursing services, hospital and nursing home services, the cost of medications and lost productivity resulting from disability.

Traditional treatment of atherosclerosis includes drug therapy, surgery and angioplasty. Drug therapy alleviates some of the symptoms of atherosclerosis but is often ineffective in serious cases. Conventional bypass surgery involves cutting open the patient's chest, cutting through the sternum, connecting the patient to a heart-lung machine, stopping the heart, attaching a vein or artery removed from another part of the patient's body to create a bypass around the diseased blood vessel and restarting the heart. Certain patients are not suitable for bypass procedures, including some who have previously undergone bypass surgery, patients with extremely diffuse diseases, patients with vessels that are too small to graft, patients with chronic obstructive pulmonary disease, some diabetics, and others who are too ill to survive the use of a heart lung machine.

A less invasive alternative to bypass surgery is balloon angioplasty. The most common form of angioplasty involves inserting a catheter with a balloon at the tip into a diseased artery. By inflating the balloon at the site of blockage, the arterial plaque can be pressed against the arterial walls and reshaped, resulting in increased blood flow.

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Metallic stents were developed to help prevent the sudden closures that sometimes occur after angioplasty and to help reduce restenosis. These stents are inserted into the artery after balloon angioplasty to hold the expanded plaque in place. Because it is less traumatic and less costly, balloon angioplasty is preferred over bypass surgery when the blockages are not complicated and involve few coronary arteries. While offering certain benefits compared to bypass surgery, certain studies including the 1991 Coronary Artery Descriptors and Restenosis Study ("CADRE") and the 1993 Emory Angioplasty vs. Surgery Trial ("EAST") suggest restenosis or reocclusion is a serious problem with traditional angioplasty treatment. While stents have been shown to help reduce restenosis, and are used extensively, restenosis continues to occur at a significant rate. Atherectomy, another angioplasty-type treatment, involves the use of a catheter that contains a rotating mechanical device to cut, grind away and remove the plaque.

Management believes that TMR using The Heart Laser System is useful as a treatment for patients who have severe, stable angina and who are no longer candidates for either angioplasty or bypass because of either extensive disease or small coronary arteries. The FDA has approved The Heart Laser System for such patients. TMR is designed to be less invasive and less expensive than traditional bypass surgery, and may avoid the restenosis problem common with bypass surgery and balloon angioplasty by not targeting the coronary arteries

for treatment. Also, with additional clinical research, TMR may be proven useful in conjunction with angioplasty or bypass surgery to obtain more complete revascularization.

In addition to the more conventional treatments described above, there are a number of newer treatments and therapies including minimally invasive direct coronary artery bypass ("MIDCAB"), "off-pump" coronary artery bypass ("OPCAB") and the use of angiogenic growth factors. Some of these techniques and therapies may offer certain improvements in relation to conventional treatments. Management believes that with further clinical research, TMR may be found useful in conjunction with these less invasive procedures to more effectively revascularize the heart.

#### TMR USING THE HEART LASER SYSTEM

The main challenge in treating atherosclerosis is to allow adequate blood to flow to the heart muscle without significantly damaging the heart. The conventional and newer techniques described above are used to bypass, reopen or widen blocked or narrowed arteries and could eventually fail due to restenosis or natural disease progression. TMR using The Heart Laser System involves a different technique where channels are created into the myocardium as a means of supplying oxygen-rich blood from the left ventricular chamber into the ischemic myocardium. TMR does not target the coronary arteries for treatment.

Heart muscle, like all tissues of the body, must be constantly supplied with oxygen in order to function effectively. Oxygen is delivered to the myocardium by the blood, which is distributed to the myocardium through the right and left coronary arteries. If these arteries are narrowed or blocked as a result of atherosclerosis, sufficient oxygen-rich blood may be unable to reach the heart to satisfy the metabolic demands of the myocardium. Cardiovascular disease eventually may cause myocardial ischemia, often evidenced by severe and debilitating angina caused by lack of oxygen to the heart muscle, which can progress to myocardial infarction (the death of an area of the heart muscle). Advanced multi-vessel ischemic heart disease is typically treated with bypass surgery.

During the TMR procedure, the patient is given general anesthesia. An incision is made in the patient's side between the ribs, exposing the heart. The Heart Laser System is computer synchronized with the patient's heartbeat, firing only when the left ventricle is filled with blood and is electrically insensitive. The Company believes that synchronization may reduce the risk of arrhythmias (irregular heartbeats) and their associated morbidity and mortality. Research studies conducted by the Texas Heart Institute in animal models indicated that performing TMR without synchronization may be associated with an increase in life threatening arrhythmias. The synchronization technology is covered under a patent owned by the Company. The Heart Laser System is capable of drilling a transmural channel in less than 0.05 seconds with a single laser pulse in a patient whose heart has not been stopped and who has not been placed on a heart-lung bypass machine. The surgeon can vary the pulse width of the laser using a touch key control panel to accommodate for the thickness of the patient's heart wall. Transesophageal Echocardiography (TEE) is used to confirm that complete channels are made by the laser. Generally, 20 to 40 new channels are created during the procedure. Each TMR procedure requires a sterile, single use, TMR kit containing assorted TMR hand pieces, drapes

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and other disposable items.

#### POTENTIAL BENEFITS OF TMR

Based on clinical results to date, the Company believes that TMR using The Heart Laser System provides a number of benefits, although no assurance can be given that any of the mentioned benefits will be received by patients and no assurance can be given that the FDA will approve additional indications for use of The Heart Laser System.

These current anticipated benefits include:

**THERAPY FOR PATIENTS NOT SUITABLE FOR CORONARY BYPASS.** The FDA has approved the use of The Heart Laser System for patients who have severe, stable angina and would otherwise not be suitable for coronary bypass surgery, and for whom other surgical or interventional techniques may not be available or advisable to alleviate the effects of atherosclerotic illness.

**POTENTIAL USE IN CONJUNCTION WITH BOTH CONVENTIONAL AND MINIMALLY INVASIVE CORONARY BYPASS.** TMR may allow the surgeon to provide oxygenated blood to areas of the heart muscle that are not accessible by coronary bypass grafts. With the advent of the MIDCAB and OPCAB procedures, in which coronary artery bypass graft surgery is performed on a beating heart, Management believes that with additional clinical research, TMR may be found to be an effective complement to these procedures. TMR can be performed on the anterior, posterior and lateral walls of the heart while the MIDCAB procedure usually is only performed on the anterior wall of the heart. Further, although the OPCAB procedure can be performed on posterior and lateral walls of the heart, it generally entails great technical difficulty.

**POTENTIALLY A THIRD REVASCLARIZATION OPTION.** In the future, with additional clinical research, TMR may be found to be useful as an alternative to bypass or angioplasty procedures.

**POTENTIAL THERAPY FOR HEART TRANSPLANT PATIENTS.** With additional clinical research, TMR could potentially be found useful for post-transplant patients suffering from chronic rejection atherosclerosis. Presently, the only treatment for this condition is re-transplantation.

**POTENTIALLY LOWER MEDICAL COSTS.** Management believes the medical costs associated with TMR using The Heart Laser System will be less than the costs of traditional bypass surgery which requires a larger surgical team, more supporting equipment and a longer hospital stay. The cost of TMR in some situations may also be less than angioplasty when combinations of additional devices such as atherectomy catheters, stents or intravascular ultrasound are required.

**POTENTIALLY QUICKER RECOVERY.** Because TMR using The Heart Laser System is less invasive and does not involve stopping and starting the heart, the patient may recover more quickly than if conventional bypass techniques were used, with potentially reduced risks of complications.

**NOT DEPENDENT ON PLAQUE TYPE OR LOCATION AND POTENTIALLY LESS RISK OF RESTENOSIS.** Unlike angioplasty, atherectomy devices and stents, which may be more or less effective, depending on the composition, extent or location of the plaque occluding the artery and which have evidenced high restenosis rates, TMR is not dependent upon plaque type or location.

#### DEVELOPMENT OF MARKETING STRATEGY

The Company's strategy is to establish TMR using The Heart Laser System as a standard of care for treating patients suffering from coronary artery disease. Currently, The Heart Laser System is commercially available in the U.S., the European Community (except France), China, South Korea, Taiwan and certain countries that do not require governmental approval for commercialization. The Company has submitted applications for government approval to sell The Heart Laser System in other countries including Japan.

The Company has also developed a procedural kit, which includes single use surgical products to be used with

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The Heart Laser System in performing TMR. The TMR procedure kit contains a set of handpieces, drapes and other TMR surgical accessories.

The Company has developed a strategy to address the challenges of marketing high cost capital equipment by offering the Heart Laser System on a usage basis to hospitals. The structure of a particular usage based contract, including the length of contract, price billed per procedure and end of term options for purchase, depends primarily on whether the hospital is willing and able to commit to a certain minimum volume of procedures over a defined period of time. If the hospital cannot commit to a sufficient number of procedures, The Heart Laser System may be installed with usage fees billed as agreed upon with the hospital. The Company refers to this type of usage arrangement as a retained placement contract. Under a retained placement contract, placement and service fee revenue is recorded over the term of the usage agreement, and The Heart Laser System remains the property of the Company and is depreciated over the term of the usage agreement.

If the hospital is willing and able to commit to a sufficient number of procedures such that the substantial risks and benefits of ownership of The Heart Laser System have transferred to the hospital, then the Company classifies the usage agreement as a minimum procedure sales contract. Under a minimum procedure sales contract, the Company records product revenue at a discounted present value of the guaranteed minimum procedure payments, and records product cost of sale at the time of acceptance of The Heart Laser System.

Retained placement and minimum procedure sales contracts are appealing to hospitals when capital equipment funds are scarce or unavailable or when it is difficult to predict early usage as is the case with new technology such as TMR. The Company's financing arrangements with leasing vendors enables the Company to monetize future payment streams associated with certain placements. If utilization becomes more predictable, the Company expects a significant number of new accounts to opt for conventional leasing or direct purchase.

The Heart Laser System is also sold to customers, and the related sterile handpieces and other disposables are sold separately for each procedure. These sales are classified as product sales.

The Company has several different marketing strategies to sell or place The Heart Laser System and accessories depending upon the particular circumstances, including direct sales, sales through distributors, minimum procedure sales contracts, retained placements, rental, and leasing. Pricing varies depending upon the particular marketing strategy used and the country in which The Heart Laser System is sold.

**UNITED STATES.** The Company is primarily using a direct sales force in the United States to market The Heart Laser System. The sales force is comprised of personnel with a high degree of professionalism and experience in the cardiovascular device business. The Company invested considerable resources in recruiting and training of the sales force in 1998 and 1999. Initial marketing efforts following FDA approval were directed at The Heart Laser System user, the

cardiothoracic surgeon, whose influence is believed to be critical in a hospital's decision to purchase The Heart Laser System. Subsequent marketing efforts are expected to shift to hospital administration and referring physicians, with a focus on promoting the economics and viability of TMR as a new hospital technology and driving the growth of TMR procedures. No assurance can be given that such programs will be implemented successfully, or at all.

Supporting the direct sales force is a promotional program that consists of electronic media advertising, public relations, direct mail, trade shows and educational symposia, all focused on disseminating critical information to decision makers and key purchase influencers.

In 1999, PLC expanded its Center of Excellence training program to Texas Heart Institute in Houston. Since 1998, PLC and Rush Presbyterian Medical Center in Chicago have hosted a training program focused on educating prospective surgeons as well as surgeons from new and existing customer sites in the use of The Heart Laser System. These comprehensive programs facilitate interaction among experienced users enabling them to discuss best practices and focus on ensuring the best possible patient outcomes, including intensive discussions on patient selection and management. Course participants view live, narrated procedures via closed circuit television. Actual hands on training is also provided during the laboratory session.

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**INTERNATIONAL.** The Company currently markets The Heart Laser System overseas both directly and through distributors. International Sales (by origin) accounted for 12%, 30% and 54% of the Company's total revenues in 1999, 1998 and 1997 respectively. The Company had no sales by origin in Canada, its principle business location.

PLC received the CE Mark for The Heart Laser System in the third quarter of 1995. The CE Mark allows the Company to sell The Heart Laser System commercially in European Community countries. Despite receiving the CE Mark, the French Ministry of Health instituted a commercial moratorium on TMR procedures in France in October 1997 (See "Government Regulation").

In March 1999, PLC received ISO 9001 certification, allowing the Company to self certify and place the CE Mark on its products.

In early 1999, the Company renewed its distribution agreement in Japan with Imatron Japan, Inc. ("Imatron") to distribute The Heart Laser System in Japan and complete the Japanese regulatory approval process. Along with the United States and Germany, Japan is believed to be one of the three largest markets in the world for products used in the treatment of cardiovascular disease. Imatron also distributes medical equipment in Japan for its parent, Imatron, Inc. a U.S. based manufacturer of diagnostic imaging equipment. Between 1995 and 1997, Imatron purchased 12 Heart Laser Systems from PLC to conduct clinical studies in Japan. PLC and Imatron submitted data from these studies to the Japanese Government in December 1998 in support of their application to market The Heart Laser System in Japan. The joint application is believed to be the first submitted by a laser revascularization company seeking to market its product in Japan. No assurance can be given that Japanese regulatory approval will be granted to The Heart Laser System.

As of December 31, 1999, the Company had shipped 78 Heart Laser Systems to international markets. Foreign sales may be subject to certain risks, including foreign medical, electrical and safety regulations, export and import restrictions, tariffs and currency fluctuations.

#### PRODUCTS AND CUSTOMERS

The Company develops and markets one principal product: The Heart Laser System. Approximately 89% of the Company's revenue in the fiscal year ended December 31, 1999, 90% in the fiscal year ended December 31, 1998 and 93% in the fiscal year ended December 31, 1997 was derived from The Heart Laser System. No single customer accounted for more than 10% of the Company's revenues in fiscal 1999 or 1998. In 1997, Imatron, the Company's exclusive distributor in Japan, accounted for approximately 20% of the Company's revenues.

#### MANUFACTURING

The Company manufactures and tests its products at its 37,000 square foot facility in Franklin, Massachusetts, approximately 40 miles west of Boston. The Company moved to this facility in September 1996 and believes that its manufacturing capacity will be sufficient to meet market demands anticipated in the coming year.

The Company purchases components for its laser systems and its related disposables from a number of sources, and management believes that most components are available from multiple sources. The Company's manufacturing facilities are subject to periodic inspection by regulatory authorities to ensure compliance with FDA and European Community quality regulations. The Company's business is not subject to seasonal fluctuations.

#### GOVERNMENT REGULATION

The Heart Laser System, as well as other medical devices that have been and are being developed by the Company, are subject to extensive regulation by the FDA. Pursuant to the Federal Food, Drug and Cosmetic Act,

as amended, (the "FDC Act"), the FDA regulates the design, development, manufacturing and clinical testing, installation, servicing, labeling, distribution and promotion of medical devices in the U.S. The Company's laser products are subject to

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additional FDA regulation under the radiation health and safety provisions of the FDC Act, which imposes labeling and other safety requirements related to radiation hazards. In addition, various foreign countries in which the Company's products are or may be sold impose additional regulatory requirements.

On August 20, 1998, the Company received approval from the FDA to market The Heart Laser System throughout the U.S. to treat the estimated 80,000 domestic patients each year who suffer from severe coronary artery disease but cannot be treated with conventional coronary revascularization techniques such as bypass surgery or angioplasty. PLC was the first company to receive FDA approval to commercialize a product to perform TMR. FDA imposed certain post-approval requirements as conditions of its August clearance. These requirements include a 600 patient post-market study to further assess mortality, a specific "TMR" surgical informed consent and certain disclaimers placed on all promotion and advertising materials.

Once a product obtains market approval, any material modifications to the existing design or manufacturing process as well as any desire to change its labeling (i.e., intended use) must be approved by the FDA. The Company intends to continuously improve The Heart Laser System after market introduction and may therefore submit future Investigational Device Exemption ("IDE"), Pre-Market Approval ("PMA") and PMA supplement applications to the FDA. No assurance can be given that approval of such new IDEs, PMAs or PMA supplements will be received from the FDA on a timely basis, or at all.

The international regulatory approval process varies from country to country and is subject to change in a given country as regulatory requirements change. There is no assurance that foreign regulatory authorities will allow (or will continue to allow) the use or sale of The Heart Laser System in a particular country on a timely basis, or at all.

In addition, regulatory authorities can suspend or modify approvals previously granted in certain circumstances. For example, the French Ministry of Health instituted a commercial moratorium on TMR procedures in France in October 1997. The French Ministry of Health deemed the procedure to be "experimental", although The Heart Laser System had been approved for commercial distribution in the European Community since 1995. As a result, TMR can only be performed within the context of a clinical study in France. An evaluation of the safety of The Heart Laser System is currently under review by a panel of French experts. There can be no assurance that the Company will be successful in having the moratorium lifted or that other countries will not impose restrictions on the use or sale of the Company's products.

As a device manufacturer, the Company is also required to register with the FDA. As such, the Company is subject to inspection on a routine basis for compliance with the FDA's Quality Systems regulations. These regulations require that the Company manufacture its products and maintain its documents in a prescribed manner with respect to manufacturing, testing and control activities. Further, the Company is required to comply with various FDA requirements for reporting. The FDC Act and medical device reporting regulations require that the Company provide information to the FDA on death or serious injuries alleged to have been caused or contributed to by the use of its products, as well as product malfunctions that would likely cause or contribute to death or serious injury if the malfunction were to recur. The FDA also prohibits an approved device from being marketed for unapproved uses. The Company's laser products are subject to periodic inspection under the radiation health and safety provisions of the FDC Act for compliance with labeling and other safety regulations. If the FDA believes that a company is not in compliance with the law, proceedings can be instituted to detain or seize products or force notification and correction of hazards or defects (including a recall), enjoin future violations and assess civil and criminal penalties against the Company, its officers, directors or employees. Failure to comply with regulatory requirements could have a material adverse effect on the Company's business, financial condition and results of operations.

#### THIRD PARTY REIMBURSEMENT

Health care providers, such as hospitals and physicians, that purchase medical devices such as The Heart Laser System for use on their patients generally rely on third party payers, principally Medicare, Medicaid and private health insurance plans, to reimburse all or part of the costs associated with the procedures performed with these devices.

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In February 1997, the Health Care Financing Administration ("HCFA") published a national non-coverage instruction for TMR. It is not unusual for HCFA to deny reimbursement for procedures performed using devices that have not yet received FDA approval. The non-coverage instruction applied to procedures performed on or after May 19, 1997 on Medicare beneficiaries.

On August 20, 1998, the Company received approval from the FDA to market The Heart Laser System throughout the U.S. to treat the estimated 80,000 domestic patients each year who suffer from severe coronary artery disease but cannot be treated with conventional coronary revascularization techniques such as bypass surgery or angioplasty. PLC was the first company to receive FDA approval to commercialize a product to perform TMR.

In January 1999, the Blue Cross and Blue Shield Association Technology Evaluation Center ("TEC") completed a favorable assessment of TMR. The TEC concluded that TMR meets all five criteria used to evaluate new medical technologies: (1) final approval from the FDA; (2) scientific evidence of improvement in health outcomes; (3) net benefit in health outcomes; (4) health outcomes at least as beneficial with any established alternative; and (5) improvements achievable outside investigational settings. The TEC's determination that TMR meets its criteria is a significant step in obtaining reimbursement for TMR by major payers. The TEC's conclusion was based upon a review of data showing the safety and effectiveness of TMR by the TEC program staff, and the TEC's assessment was approved by its panel of independent medical advisors. The TEC program is sponsored by the national Blue Cross and Blue Shield Association, whose members include local Blue Cross and Blue Shield plans nationwide, as well as other major managed care organizations. TEC assessments are released as reports to TEC program subscribers. Nearly all major payers in the US, including governmental payers, private third party payers and managed care organizations, subscribe to the TEC program and receive TEC assessment reports for use in their own coverage and payment policy making.

In February 1999, HCFA rescinded the national non-coverage instruction for TMR implemented in May 1997 and announced that Medicare will provide coverage for TMR procedures performed with devices approved by the FDA. The decision set a new coverage policy to allow payment for TMR consistent with FDA-approved uses of TMR devices effective July 1, 1999.

In October 1999, HCFA issued an addendum clarifying Medicare coverage for TMR procedures. In response to questions from practicing physicians, HCFA announced that Medicare coverage would be provided in cases where TMR is used as an adjunct to coronary artery bypass grafting (CABG).

Economic data derived from the Company's clinical studies indicates that TMR using The Heart Laser System may result in a significant reduction in the cost of treating patients with severe CAD. Potentially, this could mean that TMR performed with The Heart Laser System is a procedure that offers real economic advantages to the managed care market, in particular, in which over 70% of all privately insured Americans are covered at least in part. No assurance can be given that such economic benefits will be realized by customers.

Certain private insurance companies and health maintenance organizations currently provide reimbursement for TMR procedures performed with the Company's products. No assurance can be given, however, that these payers will continue to reimburse health care providers who perform TMR procedures using the Company's products. Further, no assurance can be given that additional payers will reimburse health care providers who perform TMR procedures using the Company's products or that reimbursement, if provided, will be timely or adequate. In addition, the market for the Company's products could be adversely affected by future legislation to reform the nation's health care system or by changes in industry practices regarding reimbursement policies and procedures.

#### PRODUCT LIABILITY AND INSURANCE

The Company's business involves the risk of product liability claims. No claims have been made against The Heart Laser System to date. The Company maintains product liability insurance with per claim and aggregate coverage limits of \$10 million, subject to a \$50,000 per occurrence and \$250,000 aggregate self-insured deductible. No

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assurance can be given that product liability claims, if brought, will not exceed such insurance coverage limits, that such claims will not have a material adverse effect on the Company or that such insurance will be available on commercially reasonable terms or at all.

#### PROPRIETARY PROCESSES, PATENTS, LICENSES AND OTHER RIGHTS

The Company's policy is to file patent applications to protect its technology, inventions and product improvements. The Company also relies on trade secret protection for certain confidential and proprietary information.

Since April 1992, the Company has received 21 U.S. patents, of which 16 involve The Heart Laser System and its related technologies. These patents have terms which expire from 2009 through 2017 and cover the underlying laser technology needed to create a pulsed, fast flow laser system, the use of a laser on a beating heart to revascularize the heart using TMR, and the system used to time the heart's contractions to synchronize the laser firing at the correct time. The Company also has eleven U.S. patent applications pending relating to The Heart Laser System handpiece, other technology used in The Heart Laser System, technology associated with minimally invasive surgical techniques and technologies associated with percutaneous myocardial revascularization.

In April 1996, the Company received patents from the European Patent Office and the Japanese Patent Office providing patent protection on its heart

synchronization technology. A patent covering this technology was also issued in April 1997 in Canada. Additional Japanese-issued patents cover a TMR handpiece, a self-aligning coupler for a laser endoscope, laser beam manipulation and a laser beam status indicator. In December 1996, a patent was issued in Canada covering a self-aligning coupler for a laser endoscope. The Company has numerous patents pending related to The Heart Laser System and its components in various international patent offices. The Company expects to file additional patent applications in the next year, although there can be no assurance that any additional applications will be filed or that any additional patents will be issued.

In January 1999, CardioGenesis Corporation ("CardioGenesis"), a competitor of the Company that subsequently merged with Eclipse Surgical Technologies, Inc., agreed to the validity and enforceability of certain of the Company's patents in connection with a settlement of certain litigation between the companies. The patents, U.S. Patent No. 5,125,926 and related international patents, cover the Company's proprietary synchronization technology, which the Company believes is a critical factor in increasing the safety of TMR and PMR procedures. PLC granted CardioGenesis a non-exclusive worldwide license to the patents in exchange for payment of a license fee and ongoing royalties over the life of the patents. A minimum of \$2.5 million will be paid to the Company in connection with this license agreement. (See Item 3. "Legal Proceedings").

Although the Company believes its patents to be strong, successful litigation against these patents by a competitor could have a material adverse effect on the Company's business, financial condition and results of operations. No assurance can be given that the existing patents will be held valid if challenged, that any additional patents will be issued or that the scope of any patent protection will exclude competitors. The breadth of claims in medical technology patents involve complex legal and factual issues and therefore can be highly uncertain.

The Company also relies upon unpatented proprietary technology and trade secrets that it seeks to protect, in part, through confidentiality agreements with employees and other parties. No assurance can be given that these agreements will not be breached, that the Company will have adequate remedies for any breach, that others will not independently develop or otherwise acquire substantially equivalent proprietary technology and trade secrets or disclose such technology or that the Company can meaningfully protect its rights in such unpatented technology. In addition, others may hold or receive patents, which contain claims that may cover products developed by the Company.

The Company believes its patents to be valid and enforceable. However, there has been substantial litigation regarding patent and other intellectual property rights in the medical device industry. Litigation, which could result in substantial cost to and diversion of effort by the Company, may be necessary to enforce patents issued to the Company, to protect trade secrets or know-how owned by the Company, to defend the Company against claimed infringement of the rights of others and to determine the scope and validity of the proprietary rights of others. Adverse determinations in

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litigation could subject the Company to significant liabilities to third parties, require the Company to seek licenses from third parties and prevent the Company from manufacturing, selling or using its products, any of which could have a material adverse effect on the Company's business, financial condition and results of operations.

#### COMPETITION

The Company believes that the majority of TMR procedures completed worldwide to date have been performed using The Heart Laser System. As of December 31, 1999, over 5,500 TMR procedures had been performed using The Heart Laser System. In addition, the Company believes that the majority of peer reviewed medical articles on TMR report results of TMR procedures performed with The Heart Laser System.

A number of other companies have entered or are attempting to enter the TMR market. These companies are believed to be using other types of lasers such as holmium and excimer lasers. Holmium and excimer lasers have different physical properties and interact differently with human tissue than the Company's CO(2) laser. The Company believes that The Heart Laser System is the only TMR product that can create a channel completely through the heart wall with a single laser pulse. Research conducted at the Texas Heart Institute in animal models has indicated that the Company's synchronized, single pulse CO(2) laser may cause significantly less damage to the heart than a holmium laser used to perform TMR. Holmium lasers currently used for TMR are not capable of creating a patent channel in one pulse, and must therefore use a fiber-optic probe that "drills" its way from the outside of the heart to the blood-filled left ventricle. The presence of the probe within the heart muscle may contribute to an increased risk of arrhythmias. Moreover, since four to seven firings are required to create a channel, channels formed in the heart wall by such holmium systems have been observed to be jagged and segmented. The Company believes that there is an opportunity to successfully differentiate its CO(2) laser and plans to implement an appropriate marketing effort accordingly. No assurance can be given that such a marketing effort will be implemented successfully, or at all.

The Company believes several companies are developing "percutaneous"

methods of performing TMR, known as "PMR". PMR procedures are performed via a catheter inserted through an incision in a patient's leg. The Company has a proprietary PMR development program underway. PMR may provide a less invasive method of creating channels in a human heart if it can be proven safe and effective. No assurance can be given that the Company's PMR development program will be successful.

The Company's two principal competitors, Eclipse Surgical Technologies, Inc. ("Eclipse") and CardioGenesis Corporation ("CardioGenesis"), merged on March 17, 1999. Both companies have holmium laser systems. In February 1999, Eclipse received FDA approval to market its holmium laser in the U.S. to perform TMR. According to public information, the laser revascularization systems developed by Eclipse and CardioGenesis may be adaptable to be used to perform both TMR and PMR procedures.

Many treatments are available for coronary artery disease. The Company believes that the primary competitive factors in the medical treatment of coronary artery disease are clinical safety and efficacy, product safety and reliability, regulatory approval, availability of reimbursement from insurance companies and other payers, product quality, price, reputation for quality, customer service and ease of use. The Company believes that its competitive success will be based on its ability to create and maintain scientifically effective and safe technology, obtain required regulatory approvals, obtain third party reimbursement for use of its products, attract and retain key personnel, obtain patent or other protection for its products and successfully differentiate, price, manufacture and market its products either directly or through outside parties.

The Company believes that the primary competitive factors within the interventional cardiovascular market are the ability to treat safely and effectively various types of coronary disease, physician familiarity with and acceptance of the procedure, third party reimbursement policies, and to a lesser extent, ease of product use, product reliability and price.

The medical care products industry is characterized by extensive research efforts and rapid technological

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progress. New technologies and developments are expected to continue at a rapid pace in both industry and academia. Competition in the market for surgical lasers and for the treatment of cardiovascular disease is intense and is expected to increase. Management believes that The Heart Laser System must compete not only with TMR and PMR systems, but also with medical management (drugs) and other coronary procedures (e.g. coronary bypass, balloon angioplasty, atherectomy, laser angioplasty and stents). Many of the companies manufacturing these products have substantially greater resources and experience than the Company and represent significant competition for the Company. Such companies may succeed in developing products that are more effective or less costly in treating coronary disease than The Heart Laser System and may be more successful than the Company in manufacturing and marketing their products. No assurance can be given that the Company's competitors or others will not succeed in developing technologies, products or procedures that are more effective than any being developed by the Company or that would render the Company's technology and products obsolete or noncompetitive. Although the Company will continue to work to develop new and improved products, the advent of either new devices or new pharmaceutical agents could hinder the Company's ability to compete effectively and have a material adverse effect on its business, financial condition and results of operations.

#### RESEARCH AND DEVELOPMENT

Research and development expenses were \$2,672,000, \$4,468,000 and \$5,158,000 for the years ended December 31, 1999, 1998 and 1997, respectively. Since The Heart Laser System received final approval from the FDA in late August 1998, there has been a significant reduction in research and development expenses related to clinical trials. The Company continues to refine The Heart Laser System and is currently designing and developing next generation products and technologies, including less invasive methods of performing myocardial revascularization including catheters and other percutaneous delivery devices. Several other companies are developing "percutaneous" methods of performing TMR, known as "PMR". PMR procedures are performed via a catheter inserted through an incision in a patient's leg. The Company has a proprietary PMR development program underway. PMR may provide a less invasive method of creating channels in a human heart if it can be proven safe and effective. No assurance can be given that the Company's PMR development program will be successful.

The Company continues to monitor all technologies that may be applicable to TMR to keep it at the forefront of this field. No assurance can be given that the Company's research and development goals will be implemented successfully or that the Company will maintain its position in this market.

#### EMPLOYEES

As of March 13, 2000, the Company had 48 full-time domestic employees, including its executive officers. Of these, 16 are employed in general and administrative activities, 19 are involved in sales and marketing, 7 are involved in research and development and 6 are involved in manufacturing. The Company also employs one part-time employee. None of the Company's employees are represented by a union. In addition, the Company has 9 full time

employees/consultants for its international operations. Management considers its relations with employees to be satisfactory.

ITEM 2. DESCRIPTION OF PROPERTY.

Since September 1996, the Company has leased its current 37,000 square foot facility in Franklin, Massachusetts where it maintains its principal executive offices and manufacturing operations. The lease expires in August 2001. The lease provides for two renewal periods of three years each. The total base rental payments for the term of the lease are approximately \$296,400 per year plus operating and maintenance costs and real estate taxes.

ITEM 3. LEGAL PROCEEDINGS.

In September 1996, CardioGenesis filed a civil lawsuit in the United States District Court for the Northern District of California asking the court to declare the Company's synchronization patent (U.S. Patent No. 5,125,926) invalid and unenforceable, or, alternatively, to find that CardioGenesis' TMR and PMR lasers do not infringe this

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patent. The Company filed a counterclaim alleging that all of CardioGenesis' TMR and PMR lasers infringe U.S. Patent No. 5,125,926. In January 1997, CardioGenesis filed an opposition in the European Patent Office to have the Company's German synchronization patent declared invalid. In April 1997, the Company filed an infringement lawsuit against CardioGenesis and one of its distributors in the Munich District Court alleging that CardioGenesis' TMR and PMR lasers infringe the Company's German synchronization patent. The PLC patents at issue in these lawsuits cover the Company's synchronization technology, which the Company believes is a critical factor in increasing the safety of TMR and PMR procedures.

In January 1999, the Company settled its outstanding patent infringement litigation with CardioGenesis who subsequently merged with Eclipse Surgical Technologies, Inc. Under the settlement, CardioGenesis agreed that U.S. Patent No. 5,125,926 and related international patents of the Company are valid and enforceable. PLC granted CardioGenesis a non-exclusive worldwide license to these patents in exchange for the payment of a license fee and ongoing royalties over the life of the patents (at least 10 years unless the patents are all held invalid in future lawsuits). As part of the settlement, CardioGenesis agreed to pay the Company:

- a minimum of \$2.5 million over the next 42 months; and
- license fees and ongoing royalties on sales of all covered products for at least 10 years (unless the patents are all held invalid in future lawsuits).

In July 1997, an FDA advisory panel recommended against approval of the Company's application to market The Heart Laser System in the United States. Following this recommendation, the Company was named as defendant in 21 purported class action lawsuits filed between August 1997 and November 1997 in the United States District Court for the District of Massachusetts. The lawsuits seek an unspecified amount of damages in connection with alleged violations of the federal securities laws based on the Company's failure to obtain a favorable FDA panel recommendation in 1997. Nineteen of these complaints have been consolidated by the court into a single action for pretrial purposes (hereafter referred to as the "federal suit"). Two of these suits were voluntarily dismissed. The Company moved to dismiss all claims in the federal suit. On March 26, 1999, the court issued an order dismissing some, but not all, of the claims in the federal suit. The parties filed cross motions for reconsideration and on October 12, 1999, the court dismissed additional, but not all remaining claims in the federal suit. The Company has also been named as a defendant in a lawsuit filed in Massachusetts Superior Court in September 1998 (hereafter referred to as the "state suit") seeking over \$2 million in damages for alleged negligent misrepresentations and fraud arising from the Company's failure to obtain a favorable FDA recommendation in 1997. The Company cannot make a meaningful estimate of the amount or range of loss that could result from an unfavorable outcome of these lawsuits, but an unfavorable outcome could have a material adverse effect on the Company's business, financial position and results of operations. The Company believes that it has meritorious defenses to these litigation matters and continues to vigorously defend itself in these matters.

In August 1997, the Company received from the United States Securities and Exchange Commission (the "Commission") an informal request for information relating to the decision by the FDA Advisory Panel not to recommend approval of The Heart Laser System in July 1997. The Company has responded and has not received any further communication from the Commission regarding this matter since June 1998.

In February 1996, PLC Medical Systems, Inc. filed suit against Eclipse Surgical Technologies, Inc. ("Eclipse") in the United States District Court for the District of Massachusetts alleging copyright infringement and unfair and deceptive trade practices based on Eclipse's misappropriation and copying of one of PLC's confidential clinical study protocols. The Company settled this suit in April 1999 on confidential terms. The settlement of the lawsuit did not have a material impact on the Company's financial statements.

In November 1998, a hospital in France, Centre Medico Chirurgical Foch ("Foch Hospital"), sued the Company's Portuguese subsidiary, PLC Sistemas Medicos Internacionais Lda., and a third party, Johnson & Johnson Leasing GmbH, in Paris, France alleging breach of contract. In October 1997, the French Ministry of

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Health suspended commercial use of TMR devices in France. Foch Hospital is seeking reimbursement of lease payments made for The Heart Laser System. The Company intends to vigorously defend itself in this matter. A hearing on the merits of the case has been held, however no decision has been rendered and a meaningful estimate of the loss that could result from this matter has not been made. However, the Company does not believe that the loss, if any, would have a material adverse impact on the Company's financial condition.

The Company is not involved in any other litigation of a material nature.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

Not applicable.

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PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS.

Since September 17, 1992, the Company's Common Stock has traded on the American Stock Exchange ("AMEX") under the symbol "PLC". From March 3, 1992 through September 16, 1992, the Company's Common Stock was traded on the over-the-counter market through the National Association of Securities Dealers Automated Quotation System ("NASDAQ"). On March 13, 2000 the closing sale price of the Company's Common Stock was \$3.75 per share.

For the periods indicated, the following table sets forth the range of high and low sales prices for the Common Stock from January 1, 1998.

<TABLE>  
<CAPTION>

	SALES	
	HIGH	LOW
	----	---
1998		
-----		
<S>	<C>	<C>
First Quarter.....	\$19.50	\$7.75
Second Quarter.....	\$22.00	\$9.13
Third Quarter.....	\$12.88	\$3.25
Fourth Quarter.....	\$7.13	\$2.75
1999		
-----		
First Quarter.....	\$7.44	\$2.38
Second Quarter.....	\$4.88	\$2.31
Third Quarter.....	\$4.88	\$2.63
Fourth Quarter.....	\$3.19	\$1.81
2000		
-----		
First Quarter (through March 13, 2000).....	\$4.63	\$2.06
</TABLE>		

As of March 13, 2000, there were approximately 728 record holders of the Company's Common Stock. Management believes that there are approximately 16,000 beneficial owners of the Company's Common Stock.

DIVIDENDS

The Company has never paid cash dividends. The Company currently intends to retain all future earnings, if any, for use in its business and does not anticipate paying any cash dividends in the foreseeable future.

ITEM 6. SELECTED FINANCIAL DATA.

The following selected financial data with respect to the Company for the five years ended December 31, 1999, are derived from the audited financial statements of the Company. The data should be read in conjunction with the financial statements, related notes and other financial information included elsewhere herein.

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SELECTED FINANCIAL DATA

<TABLE>  
<CAPTION>

FOR THE YEARS ENDED DECEMBER 31

	1999	1998	1997	1996	1995
(ALL AMOUNTS ARE IN THOUSANDS EXCEPT PER SHARE DATA)					
<S>	<C>	<C>	<C>	<C>	<C>
STATEMENT OF OPERATIONS DATA:					
Revenue:					
Product sales.....	\$ 8,400	\$ 3,088	\$ 5,687	\$9,082	\$11,938
Placement and service fees....	3,236	2,605	3,254	2,790	1,407
Costs and expenses:					
Cost of product sales.....	3,615	1,945	2,721	2,911	4,177
Cost of placement and service fees	2,061	2,622	2,595	1,155	386
Selling, general and administrative	10,054	13,718	13,049	7,023	5,035
Research and development .....	2,672	4,468	5,158	2,835	2,246
Income (loss) from operations.	(6,766)	(17,060)	(14,582)	(2,052)	1,501
Other income.....	211	457	178	512	588
Income (loss) before income taxes	(6,555)	(16,603)	(14,404)	(1,540)	2,089
Provision for income taxes....	--	--	--	--	85
Net income (loss).....	\$ (6,555)	\$ (16,603)	\$ (14,404)	\$ (1,540)	\$2,004
Net income (loss) per share - Basic	\$ (.32)	\$ (.86)	\$ (.84)	\$ (.09)	\$ .13
Net income (loss) per share - Diluted	\$ (.32)	\$ (.86)	\$ (.84)	\$ (.09)	\$ .12
Shares used to compute net income (loss) per share - Basic	20,675	19,218	17,050	16,376	15,868
Shares used to compute net income (loss) per share - Diluted	20,675	19,218	17,050	16,376	16,590

</TABLE>

<TABLE>  
<CAPTION>

As of December 31

	1999	1998	1997	1996	1995
<S>	<C>	<C>	<C>	<C>	<C>
BALANCE SHEET DATA:					
Working capital .....	\$5,459	\$5,050	\$12,793	\$11,245	\$13,541
Total assets.....	15,319	16,257	27,017	19,417	18,290
Long term obligations.....	--	37	121	27	32
Secured borrowings .....	2,082	--	--	--	--
Stockholders' equity .....	8,885	10,662	19,009	16,467	15,508

</TABLE>

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

OVERVIEW

The Company offers placement, purchase and leasing alternatives to customers interested in acquiring The Heart Laser System. The Company has developed a strategy to address the challenges of marketing high cost capital equipment by offering The Heart Laser System on a usage basis to hospitals. The particular structure of a usage based contract, including the length of contract, price billed per procedure and end of term options for purchase, depends primarily on whether the hospital is willing and able to commit to a certain minimum volume of procedures over a defined period of time. If the hospital cannot commit to a sufficient number of procedures, The Heart Laser System may be installed with usage fees billed as agreed upon with the hospital. The Company refers to this type of usage arrangement as a retained placement contract. Under a retained placement contract, placement and service fee revenue

is recorded over the term of the usage agreement and The Heart Laser System remains the property of the Company and is depreciated over the term of the usage agreement.

If the hospital is willing and able to commit to a sufficient number of procedures such that the substantial risks and benefits of ownership of The Heart Laser System have transferred to the hospital, then the Company classifies the usage agreement as a minimum procedure sales contract. Under a minimum procedure sales contract, the Company records product revenue, at a discounted present value of the guaranteed minimum procedure payments, and records product cost of sale at the time of acceptance of The Heart Laser System.

The Company believes that retained placement and minimum procedure sales contracts are appealing to hospitals when capital equipment funds are scarce or unavailable or when it is difficult to predict early usage as is the case with new technology such as TMR. The Company's financing arrangements with leasing vendors enables the Company to monetize future payment streams associated with certain agreements. If utilization becomes more predictable, the Company expects a significant number of new accounts to opt for conventional leasing, or direct purchase.

The Heart Laser System is also sold to customers, and the related sterile handpieces and other disposables are sold separately for each procedure. These sales are classified as product sales.

Customers are given the option to purchase service contracts to cover the cost of maintaining The Heart Laser System beyond the applicable warranty period. These service revenues are recorded ratably over the service contract and are classified as a component of placement and service fees.

#### RESULTS OF OPERATIONS

##### YEAR ENDED DECEMBER 31, 1999 COMPARED TO YEAR ENDED DECEMBER 31, 1998

Total revenues of \$11,636,000 for the year ended December 31, 1999 increased \$5,943,000 or 104% when compared to total revenues of \$5,693,000 for the year ended December 31, 1998. For the year ended December 31, 1999, product sales of \$8,400,000 increased \$5,312,000 or 172% when compared to product sales of \$3,088,000 for the year ended December 31, 1998. The major factors in both increases are primarily due to the 1999 periods reflecting increased sales of The Heart Laser System and related disposables due to the Company's receipt of FDA approval to market the Heart Laser System in August 1998, as well as license and royalty fees associated with the CardioGenesis settlement.

Placement and service fees of \$3,236,000 for the year ended December 31, 1999 increased 24% from placement and service fees of \$2,605,000 for the year ended December 31, 1998. In May 1997, the Health Care Financing Administration ("HCFA") instituted a non-coverage policy for transmyocardial revascularization ("TMR") procedures performed on Medicare patients in the United States. The HCFA announcement, coupled with delays in the FDA Pre-Market Approval ("PMA") process, caused the Company to examine its contractual requirements during 1997 and amend substantially all of its retained placement contracts, temporarily replacing contractual minimum billings with actual usage billings. Following approval of the PMA by the FDA on August 20, 1998, the Company renegotiated usage agreements with its customers on a case-by-case basis. The 1999 period reflects revenue from these retained placement contracts with the renegotiated usage agreements following FDA approval. The 1998 period reflects revenue primarily from retained placement contracts with actual usage billings.

Total gross profit increased to \$5,960,000 or 51% of total revenues for the year ended December 31, 1999

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as compared with the gross profit of \$1,126,000 or 20% of total revenues for the year ended December 31, 1998. In the 1998 period, the Company did not generate sufficient sales volume to efficiently cover manufacturing costs, resulting in lower gross margins. In 1999, gross margins improved as a result of an increase in sales volumes and manufacturing cost reductions implemented by the Company.

Selling, general and administrative expenses of \$10,054,000 for the year ended December 31, 1999 decreased \$3,664,000 or 27% when compared with expenses of \$13,718,000 for the year ended December 31, 1998. This reduction is primarily due to a restructuring of the Company's workforce in April 1999. The 1999 periods reflect reduced headcount and compensation and related benefits related to the reduced workforce.

Research and development expenditures of \$2,672,000 decreased \$1,796,000 or 40% for the year ended December 31, 1999 when compared with expenditures of \$4,468,000 for the year ended December 31, 1998. The decreases in 1999 compared to 1998 reflect the reduced demands for clinical study compilation and data preparation following the FDA approval for The Heart Laser System in August 1999. In addition, in April 1999, the Company reduced its workforce, and the 1999 periods reflect reduced headcount and compensation and related benefits related to the reduced workforce.

Other income of \$211,000 for the year ended December 31, 1999 decreased \$246,000 or 54% when compared to other income of \$457,000 for the year ended

December 31, 1998, primarily due to lower interest income as a result of lower average cash balances in 1999 as compared to 1998.

There was no provision for income tax for the years ended December 31, 1999 or 1998 due to the net losses of \$6,555,000 and \$16,603,000, respectively.

The Company incurred a net loss for the year ended December 31, 1999 of \$6,555,000 compared with a net loss of \$16,603,000 for the year ended December 31, 1998. The smaller net loss resulted from higher total revenues and higher gross margin dollars coupled with lower overall operating expenses in 1999 when compared with 1998.

#### YEAR ENDED DECEMBER 31, 1998 COMPARED TO YEAR ENDED DECEMBER 31, 1997

Total revenues of \$5,693,000 for the year ended December 31, 1998 decreased \$3,248,000 or 36% when compared to total revenues of \$8,941,000 for the year ended December 31, 1997. For the year ended December 31, 1998, product sales of \$3,088,000 decreased \$2,599,000 or 46% when compared to product sales of \$5,687,000 for the year ended December 31, 1997. The major factor in these decreases is the decline in the number of sales transactions in 1998. In 1998, the Company recorded revenue on six sales compared with revenue recognition on ten sales in 1997.

Placement and service fees of \$2,605,000 for the year ended December 31, 1998 decreased 20% from placement and service fees of \$3,254,000 for the year ended December 31, 1997. Although the Company increased the number of its retained placement contracts in 1998, revenue from these contracts decreased. In May 1997, HCFA instituted a non-coverage policy for TMR procedures performed on Medicare patients in the United States. The HCFA announcement, coupled with delays in the FDA PMA process, caused the Company to examine its contractual requirements during 1997 and amend substantially all of its retained placement contracts, temporarily replacing contractual minimal billings with actual usage billings. Following receipt of the PMA from the FDA on August 20, 1998, the Company renegotiated usage agreements with the customer based on a case-by-case basis.

Total gross profit decreased to \$1,126,000 or 20% of total revenues for the year ended December 31, 1998

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as compared with total gross profit of \$3,625,000 or 41% of total revenues for the year ended December 31, 1997. This decrease resulted from three factors. First, the decrease in revenue in 1998 generated fewer gross margin dollars as compared to 1997. Second, the Company produced fewer of The Heart Laser Systems than planned in 1998, resulting in unfavorable manufacturing variances. These unfavorable manufacturing variances would continue until production increases to levels which will fully absorb manufacturing overhead. Third, depreciation on The Heart Laser Systems shipped pursuant to placement contracts increased at a greater rate than the corresponding revenue generated from placement contracts.

Selling, general and administrative expenses of \$13,718,000 for the year ended December 31, 1998 increased \$669,000 or 5% when compared with expenses of \$13,049,000 for the year ended December 31, 1997. The increase in 1998 reflects sales and marketing expenses incurred to initiate rapid commercialization of The Heart Laser System upon receipt of the PMA.

Research and development expenditures of \$4,468,000 decreased \$690,000 or 13% for the year ended December 31, 1998 when compared with expenditures of \$5,158,000 for the year ended December 31, 1997. The decrease in 1998 compared to 1997 reflects the reduced demands for clinical study compilation and data preparation following the FDA panel recommendation of approval for The Heart Laser System, offset in part by higher costs associated with the development of new products.

Other income of \$457,000 for the year ended December 31, 1998 increased \$279,000 or 157% when compared to other income of \$178,000 for the year ended December 31, 1997, primarily because of gains recorded in connection with foreign currency transactions.

There was no provision for income tax for the years ended December 31, 1998 or 1997 due to the net losses of \$16,603,000 and \$14,404,000, respectively.

The Company incurred a net loss for the year ended December 31, 1998 of \$16,603,000 compared with a net loss of \$14,404,000 for the year ended December 31, 1997. The larger net loss resulted from lower total revenues and lower gross margin dollars in 1998 when compared with 1997.

#### LIQUIDITY AND CAPITAL RESOURCES

At December 31, 1999, the Company had cash and cash equivalents of \$4,467,000

Over the past three years, the Company incurred significant operating losses and utilized significant amounts of cash to fund operations. The Company is in a critical stage in its growth as it continues to transition from a research and development company to a commercial company with complete sales, marketing and production capabilities.

During 1999, the Company implemented a number of programs to reduce its consumption of cash, including operating expense reductions and establishment of third party financing alliances to enable the Company to obtain an upfront cash payment on certain of its minimum procedure sales contracts. In April 1999, the Company announced a workforce restructuring to further reduce operating expenses and concentrate the Company's resources on its sales efforts. The restructuring eliminated 27 of the 91 positions within the Company as of April 23, 1999. During 1999, the Company also sold 1,316,140 shares of common stock resulting in proceeds to the Company (net of all issuance costs) of approximately \$3,800,000 to fund working capital requirements.

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Most recently, on March 28, 2000, the Company closed an equity financing with two institutional investors at \$2.00 per share. In conjunction with this offer, the Company sold 2,683,000 shares of common stock, resulting in proceeds to the Company (net of all issuance costs) of approximately \$5,000,000 and issued the placement agent a three year warrant for 61,326 shares of common stock at \$3.15 per share. The Company may seek additional financing through the issuance and sale of debt or equity securities, bank financing, joint ventures or by other means. The availability of such financing and the reasonableness of any related terms in comparison to market conditions cannot be assured.

While the Company is encouraged by recent developments with respect to FDA approval and Medicare coverage for TMR procedures, the historical absence of widespread reimbursement for the TMR procedure by third party payers has limited demand for and use of The Heart Laser System. Although Medicare reimbursement began in July 1999, and some private insurance plans have begun reimbursing health care providers for TMR procedures using The Heart Laser System, the Company believes that operating losses are likely to continue until such time as third party payers begin to provide widespread reimbursement to healthcare providers for use of The Heart Laser System. Management believes that its existing cash resources and cash from operations will meet working capital requirements over the next twelve months. However, unanticipated decreases in operating revenues, increases in expenses or further delays in the process of third party payers providing reimbursement to healthcare providers, may adversely impact the Company's cash position and require further cost reductions or the need to obtain additional financing. No assurance can be given that the Company will be successful in achieving broad commercial acceptance of The Heart Laser System or that the Company will be able to operate profitably on a consistent basis. Should additional financing not be available on terms and conditions acceptable to the Company, additional actions may be required that could adversely impact the Company's ability to continue to realize assets and satisfy liabilities in the normal course of business. The financial statements do not include any adjustments to reflect the possible future effects of these uncertainties.

During the year ended December 31, 1999, the Company incurred a net loss of \$6,555,000, which resulted in the use of approximately \$3,793,000 to support operations. Cash used by investing activities was approximately \$585,000 and primarily related to PLC's retained placement contract activity. Cash provided by financing activities was approximately \$3,979,000 and primarily related to the net proceeds of \$3,803,000 obtained from the sale of the Company's common stock, \$242,000 in secured borrowings, offset by principal payments on capital lease obligations of \$66,000.

At December 31, 1999, the Company had U.S. net operating loss carryforwards of approximately \$40.8 million available to reduce future taxable income, which expire at various dates through 2013, and the Company had foreign net operating loss carryforwards of approximately \$4.4 million. In addition, various other deferred tax assets have been generated related primarily to intercompany profit, accruals, and research and development tax credits. Because the Company believes that, as of December 31, 1999, it is more likely than not, that all of the deferred tax assets will not be realized, no tax benefit for prior year losses and other deferred items has been provided. These amounts could provide a benefit to the Company in the future in profitable years, subject to the expirations noted.

The Company and certain of its officers have been named as defendants in 21 purported class action lawsuits filed between August 1997 and November 1997. See Note 5 in the accompanying consolidated financial statements for further discussion.

#### YEAR 2000

In prior years, the Company discussed the nature and progress of its plans to become Year 2000 ready. In late 1999, the Company completed its remediation and testing of systems. As a result of those planning and implementation efforts, the Company experienced no significant disruptions in mission critical information technology and non-information technology systems and believes those systems successfully responded to the Year 2000 date change. The Company did not incur material expenses in 1999 in connection with remediating its systems to become Year 2000 ready. The Company is not aware of any material problems resulting from Year 2000 issues, either with its products, its internal systems, or the products and services of third parties. The Company will continue to monitor its mission critical computer applications and those of its suppliers and vendors through the year 2000 to ensure that any latent Year 2000 matters that may arise are addressed completely.

**RISK FACTORS****OUR COMPANY HAS A HISTORY OF OPERATING LOSSES**

PLC Systems Inc. was founded in 1987. We have incurred operating losses in every year of our existence except 1995. We have incurred net losses of \$6,555,000 for the year ended December 31, 1999, \$16,603,000 for the year ended December 31, 1998 and \$14,404,000 for the year ended December 31, 1997. As of December 31, 1999, we had an accumulated deficit of \$74,691,000. We have not achieved profitability and expect to continue to incur net losses for at least the next fiscal year. Moreover, although our business is not seasonal in nature, our revenues tend to vary significantly from fiscal quarter to fiscal quarter.

**OUR COMPANY IS DEPENDENT ON ONE PRINCIPAL PRODUCT**

We develop and market one principal product: a patented high-powered carbon dioxide laser system known as The Heart Laser System and related disposables. Approximately 89% of our revenue in the fiscal year ended December 31, 1999 and 90% in the fiscal year ended December 31, 1998 was derived from The Heart Laser System.

**OUR COMPANY MAY BE UNABLE TO RAISE NEEDED FUNDS**

As of December 31, 1999, we had cash and cash equivalents totaling \$4,467,000, a decrease of \$379,000 from the balance of \$4,846,000 we had as of December 31, 1998. Based on our current operating plan, we anticipate that our existing capital resources, together with cash from operations, should be sufficient to meet our working capital requirements over the next twelve months. If our business does not progress in accordance with our current business plan, we may need to raise additional funds. We are currently exploring a number of alternatives to raise additional capital. We may not be able to raise additional capital upon satisfactory terms or at all, and our business, financial condition and results of operations could be materially and adversely affected. To the extent that we raise additional capital by issuing equity or convertible securities, ownership dilution to our stockholders will result.

**IN ORDER TO COMPETE EFFECTIVELY, THE HEART LASER SYSTEM NEEDS TO GAIN COMMERCIAL ACCEPTANCE**

The Heart Laser System is designed for use in the treatment of coronary artery disease in a surgical laser procedure we pioneered known as transmyocardial revascularization. Transmyocardial revascularization is commonly referred to in our industry as "TMR." TMR is a new technology that is only recently becoming known. We may never achieve widespread commercial acceptance. To be successful, we need to:

- demonstrate to the medical community in general, and to heart surgeons and cardiologists in particular, that TMR procedures and The Heart Laser System are effective, relatively safe and cost effective;
- train heart surgeons to perform TMR procedures using The Heart Laser System; and
- obtain widespread insurance reimbursement for the TMR procedure.

To date, we have trained only a limited number of heart surgeons and will need to expand our marketing and training capabilities.

Although The Heart Laser System has received FDA approval and the CE Mark, it has not yet received widespread commercial acceptance. If we are unable to maintain regulatory approvals or to achieve widespread commercial acceptance of The Heart Laser System, our business, financial condition and results of operations will be materially and adversely affected.

**RESULTS OF LONG-TERM CLINICAL STUDIES MAY ADVERSELY AFFECT OUR BUSINESS**

Patients have only been treated with The Heart Laser System since January 1990, and, as a result, there have been few long-term follow-up studies. If patients suffer harmful, long-term consequences from The Heart Laser System,

our business, financial condition and results of operations will be materially and adversely affected.

**RAPID TECHNOLOGICAL CHANGES IN OUR INDUSTRY COULD MAKE THE HEART LASER SYSTEM OBSOLETE**

Our industry is characterized by rapid technological change and intense competition. New technologies and products and new industry standards will develop at a rapid pace. They could make The Heart Laser System obsolete. The advent of new devices and procedures and advances in new drugs and genetic engineering are especially threatening. Our future success will depend upon our ability to develop and introduce product enhancements to address the needs of our customers. Material delays in introducing product enhancements may cause

customers to forego purchases of our product and purchase those of our competitors.

Many of our competitors have substantially greater financial resources and are in a better financial position to exploit marketing and research and development opportunities. Our competitors' products use different types of lasers than we use in The Heart Laser System, including holmium and excimer lasers that may gain more widespread market acceptance than The Heart Laser System. In addition, we believe that several companies are attempting to develop less invasive methods of performing TMR procedures. These new methods may eliminate the need to make an incision in the patient's chest, reducing costs and speeding recovery. These new technologies and methods may erode the potential TMR market, which could have a material adverse effect on our business, financial condition and results of operations.

#### WE MUST RECEIVE AND MAINTAIN GOVERNMENT APPROVAL IN ORDER TO MARKET OUR PRODUCT

##### GENERAL

The Heart Laser System and our manufacturing activities are subject to extensive, rigorous and changing federal and state regulation in the United States and to similar regulatory requirements in other major markets, including the European Community and Japan. To date, we have received regulatory approval in the United States and have the ability to market The Heart Laser System in the European Community (excluding France). We have not received regulatory approval in Japan. Without regulatory approval, we cannot market The Heart Laser System in Japan. Even if granted, regulations may significantly restrict the use of The Heart Laser System. The process of obtaining and maintaining required regulatory approval is lengthy, expensive and uncertain.

UNITED STATES -- ALTHOUGH WE HAVE RECEIVED FDA APPROVAL, THE FDA HAS RESTRICTED THE USE OF THE HEART LASER SYSTEM AND COULD REVERSE ITS APPROVAL AT ANY TIME

In August 1998, we received FDA approval to market a laser system for TMR procedures. However, the FDA:

- has not allowed us to market The Heart Laser System to treat patients whose condition is amenable to conventional treatments, such as heart bypass surgery and angioplasty; and
- could reverse its ruling and prohibit use of The Heart Laser System at any time.

EUROPE -- ALTHOUGH WE HAVE THE ABILITY TO MARKET OUR PRODUCT IN THE EUROPEAN COMMUNITY, THE MEMBERS OF THE EUROPEAN COMMUNITY COULD, AND FRANCE HAS, PROHIBITED COMMERCIAL USE OF THE HEART LASER SYSTEM

The Heart Laser System received the CE Mark from the European Community in 1995. However:

- the European Community could reverse its ruling and prohibit use of The Heart Laser System at any time;
- we cannot market The Heart Laser System in France; and
- other European Community countries could prohibit or restrict use of The Heart Laser System.

Despite receiving the CE Mark, The French Ministry of Health instituted a commercial moratorium on TMR procedures in October 1997. In its opinion, the procedure is considered to be experimental and should only be

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performed within the context of a clinical study. An evaluation of the safety of The Heart Laser System is currently under review by a panel of French experts. There can be no assurance that this moratorium will be lifted on a timely basis or at all.

ASIA -- WE CANNOT MARKET OUR PRODUCT IN MAJOR ASIAN MARKETS UNTIL WE RECEIVE GOVERNMENT APPROVAL

We believe that Japan represents the largest potential market for The Heart Laser System in Asia. Prior to marketing The Heart Laser System in Japan, we must receive approval from the Japanese Government. This approval requires a clinical study in Japan with at least 60 patients. This study was completed in 1998. Although the results of this study have been submitted to the Japanese Government, we do not know whether the clinical study will be sufficient or when, if ever, we will receive approval to sell The Heart Laser System in Japan.

Additional regulatory applications are pending in Taiwan. We cannot be sure when, if at all, we will obtain regulatory approval in any particular country.

ASSERTING AND DEFENDING INTELLECTUAL PROPERTY RIGHTS MAY IMPACT OUR RESULTS OF OPERATIONS

In our industry, competitors often assert intellectual property

infringement claims against one another. The success of our business depends on our ability to successfully defend our intellectual property. Future litigation may have a material impact on our financial condition even if we are successful in marketing The Heart Laser System. We may not be successful in defending or asserting our intellectual property rights.

An adverse outcome in any litigation or interference proceeding could subject us to significant liabilities to third parties and require us to cease using the technology that is at issue or to license the technology from third parties. In addition, a finding that any of our intellectual property is invalid could allow our competitors to more easily and cost-effectively compete with us. Thus, an unfavorable outcome in any patent litigation or interference proceeding could have a material adverse effect on our business, financial condition or results of operations.

The cost to us of any patent litigation or interference proceeding could be substantial. Uncertainties resulting from the initiation and continuation of patent litigation or interference proceedings could have a material adverse effect on our ability to compete in the marketplace. Patent litigation and interference proceedings may also absorb significant management time.

#### WE MAY BE SUBJECT TO PRODUCT LIABILITY LAWSUITS; OUR INSURANCE MAY NOT BE SUFFICIENT TO COVER DAMAGES

We may be subject to product liability claims. The United States Supreme Court has stated that compliance with FDA regulations will not shield a company from common-law negligent design claims or manufacturing and labeling claims based on state rules. Such claims may absorb significant management time and could degrade the reputation of PLC and the marketability of The Heart Laser System. If product liability claims are made with respect to our products, we may need to recall the implicated product which could have a material adverse effect on our business, financial condition and results of operations. In addition, although we maintain product liability insurance with a per claim and yearly aggregate maximum of \$10 million, subject to a \$50,000 per occurrence and \$250,000 aggregate self-insured deductible, we cannot be sure that our insurance will be adequate to cover potential product liability lawsuits. Our insurance is expensive and in the future may not be available on acceptable terms, if at all. If a successful product liability claim or series of claims exceeded our insurance coverage, it could have a material adverse effect on our business, financial condition and results of operations.

#### WE ARE DEPENDENT ON CERTAIN SUPPLIERS

We believe that some of the components for our laser systems, most notably the laser head, may only be available from one or a limited number of suppliers. Any interruption in supply from these suppliers could prevent us from meeting commercial demands for The Heart Laser System, which could have a material adverse effect on our business, financial condition and results of operations.

#### RISKS ASSOCIATED WITH INTERNATIONAL OPERATIONS

A portion of our product sales are generated from operations outside of the United States. Establishing and expanding international sales can be expensive. Managing and overseeing foreign operations may be difficult and products may not receive market acceptance. Risks of doing business outside the U.S. include the following: agreements may be difficult to enforce and receivables difficult to collect through a foreign country's legal system; foreign customers may have longer payment cycles; foreign countries may impose additional withholding taxes or otherwise tax PLC's foreign income, impose tariffs or adopt other restrictions on foreign trade; U.S. export licenses may be difficult to obtain; and the protection of intellectual property in foreign countries may be more difficult to enforce. There can be no assurance that our international business will grow or that any of the foregoing risks will not result in a material adverse effect on PLC.

#### WE HAVE BEEN SUED FOR ALLEGED VIOLATIONS OF SECURITIES LAW

In July 1997, an FDA advisory panel recommended against approval of our application to market The Heart Laser System. Following this recommendation, we were named as defendant in 21 purported class action lawsuits filed between August 1997 and November 1997 in the United States District Court for the District of Massachusetts. The lawsuits seek an unspecified amount of damages in connection with alleged violations of the federal securities laws based on our failure to obtain a favorable FDA panel recommendation in 1997. Nineteen of these complaints have been consolidated by the court into a single action for pretrial purposes and two suits were voluntarily dismissed. The Company moved to dismiss all of the remaining claims. On March 26, 1999, the court issued an order dismissing some, but not all of the remaining claims. The parties both filed motions for reconsideration and on October 12, 1999, the court dismissed additional, but not all remaining claims. We cannot make a meaningful estimate of the amount or range of loss that could result from an unfavorable outcome of these lawsuits. We may not be able to pay the amount of any judgment against us. An unfavorable outcome in this litigation could have a material adverse effect on our business, financial position and results of operations.

#### BECAUSE WE ARE INCORPORATED IN CANADA, YOU MAY NOT BE ABLE TO ENFORCE JUDGMENTS

AGAINST US AND OUR CANADIAN DIRECTORS

Under Canadian law, you may not be able to enforce a judgment issued by courts in the United States against us or our Canadian directors. The status of the law in Canada is unclear as to whether a U.S. citizen can enforce a judgment from a U.S. court in Canada for violations of U.S. securities laws. A separate suit may need to be brought directly in Canada.

ANTITAKEOVER PROVISIONS MAY PREVENT YOU FROM REALIZING A PREMIUM RETURN

Provisions of Canadian law could make it more difficult for a third party to acquire us, even if the acquisition would be beneficial to you. Specifically, Canadian law requires any person who makes a tender offer that would increase the person's stock ownership to more than 20% of our outstanding common stock to make a tender offer for all of our common stock. These provisions could prevent you from realizing the premium return that stockholders may realize in conjunction with corporate takeovers.

In addition, the Company has three classes of directors, with approximately one-third elected each year for a three-year term. These provisions may have the effect of delaying or preventing a corporate takeover or a change in our management. This could adversely affect the market price of your common stock.

THE MARKET PRICE OF OUR STOCK MAY FALL IF OTHER STOCKHOLDERS SELL THEIR STOCK

If our stockholders sell substantial amounts of our common stock in the public market, the market price of our common stock could fall. Such sales also might make it more difficult for us to sell equity or equity-related securities in the future at a price we deem appropriate.

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THE VALUE OF YOUR COMMON STOCK MAY DECREASE IF OTHER SECURITY HOLDERS EXERCISE THEIR OPTIONS AND WARRANTS

As shown in the table below, we have reserved an additional 3,023,026 shares of common stock for future issuance upon exercise or conversion of outstanding options and redeemable warrants.

<TABLE>  
<CAPTION>

	Range of Exercise/ Conversion Prices	Weighted Average Exercise/ Conversion Price	Shares Reserved for Future Issuance
	-----	-----	-----
<S>	<C>	<C>	<C>
Options	\$2.00 - \$8.88	\$3.84	2,868,162
Redeemable Warrants	\$15.78 - \$27.81	\$21.33	154,864
			-----
Total			3,023,026
			=====

</TABLE>

We may issue additional options and warrants in the future. If any of these securities are exercised, you may experience significant dilution in the market value and earnings per share of your common stock.

WE HAVE NO INTENTION TO PAY DIVIDENDS

We have never paid any cash dividends on our common stock. We currently intend to retain all future earnings, if any, for use in our business and do not expect to pay any dividends in the foreseeable future.

OUR ACTUAL RESULTS COULD DIFFER MATERIALLY FROM THOSE ANTICIPATED IN FORWARD-LOOKING STATEMENTS

This annual report and information incorporated by reference contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements deal with our current plans and expectations and involve known and unknown risks and uncertainties. Statements containing terms such as:

- believes,
- does not believe,
- plans,
- expects,
- intends,
- estimates,
- anticipates,

and other phrases of similar meaning are considered to contain uncertainty and are forward-looking statements.

No forward-looking statement is a guarantee of future performance. Our actual results could differ materially from those anticipated in these

forward-looking statements. We make cautionary statements in certain sections of this annual report, including in the risk factors identified above, and in materials incorporated herein by reference. You should read these cautionary statements as being applicable to all related forward-looking statements, wherever they appear in this annual report, in the materials referred to in this annual report, in the materials incorporated by reference into this annual report or in our press releases. You should not place undue reliance on any forward-looking statement.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

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A portion of the Company's operations consists of sales activities in foreign jurisdictions. The Company manufactures its products exclusively in the United States and sells the products in the United States and abroad. As a result, the Company's financial results could be significantly affected by factors such as changes in foreign currency exchange rates or weak economic conditions in the foreign markets in which the Company distributes its products. The Company's operating results are exposed to changes in exchange rates between the U.S. dollar and foreign currencies, especially the Swiss Franc and the German Mark. When the U.S. dollar strengthens against the Franc or Mark, the value of nonfunctional currency sales decreases. When the U.S. dollar weakens, the functional currency amount of sales increases. Overall, the Company's support of its foreign operations results in a benefit of a stronger U.S. dollar, but is adversely affected by a weaker U.S. dollar relative to major currencies worldwide. The Company does not believe that its exposure is significant.

The Company's interest income and expense are most sensitive to changes in the general level of U.S. interest rates. In this regard, changes in U.S. interest rates affect the interest earned on the Company's cash equivalents as well as interest paid on its debt.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

All financial statements required to be filed hereunder are filed as Appendix A hereto, are listed under Item 14(a) and are incorporated herein by reference.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

Not applicable.

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PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

This information required by this item is incorporated herein by reference from the Company's Definitive Proxy Statement to be filed with the Securities and Exchange Commission in connection with the Company's 2000 Annual Meeting of Stockholders (the "Definitive Proxy Statement") under the caption "Item No. 1 - Election of Directors".

ITEM 11. EXECUTIVE COMPENSATION

This information required by this item is incorporated herein by reference from the Company's Definitive Proxy Statement under the caption "Item No. 1 - Election of Directors".

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

This information required by this item is incorporated herein by reference from the Company's Definitive Proxy Statement under the caption "Item No. 1 - Election of Directors - Beneficial Ownership of Common Stock.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

This information required by this item is incorporated herein by reference from the Company's Definitive Proxy Statement under the caption "Certain Relationships and Related Transactions".

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PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K.

(a) FINANCIAL STATEMENTS. The following documents are filed as Appendix A hereto and are included as part of this Annual Report on Form 10-K.

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PLC SYSTEMS INC.

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	Consolidated Statements of Operations for the years ended December 31, 1999, 1998 and 1997.....		F-4
	Consolidated Statements of Stockholders' Equity for the years ended December 31, 1999, 1998 and 1997.....		F-5
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All other schedules for which provision is made in the applicable accounting regulation of the Securities and Exchange Commission are not required under the related instructions or are inapplicable, and therefore have been omitted.

(b) REPORTS ON FORM 8-K

(1) On December 30, 1999, PLC filed a Current Report on Form 8-K with the Securities and Exchange Commission announcing that Mark R. Tauscher had been appointed president, chief executive officer and a director of PLC.

(c) EXHIBITS. The list of Exhibits filed as part of this Annual Report on Form 10-K are set forth on the Exhibit Index immediately preceding such exhibits, and is incorporated herein by this reference.

(d) FINANCIAL STATEMENT SCHEDULES. See Item 14(a) above.

SIGNATURES

PURSUANT TO THE REQUIREMENTS OF SECTION 13 OR 15(d) 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.

PLC SYSTEMS INC.

Date: March 30, 2000

By: /s/ Mark R. Tauscher

-----  
Mark R. Tauscher  
President and Chief Executive Officer

PURSUANT TO THE REQUIREMENTS OF THE SECURITIES EXCHANGE ACT OF 1934, THIS REPORT HAS BEEN SIGNED BY THE FOLLOWING PERSONS ON BEHALF OF THE REGISTRANT AND IN THE CAPACITIES AND ON THE DATE INDICATED.

<TABLE>

Name ----	Capacity -----	Date ----
<S> /s/ Mark R. Tauscher ----- Mark R. Tauscher	<C> President and Chief Executive Officer (Principal Executive Officer)	<C> March 30, 2000
/s/ James G. Thomasch ----- James G. Thomasch	Chief Financial Officer (Principal Financial and Accounting Officer)	March 30, 2000
/s/ Edward H. Pendergast ----- Edward H. Pendergast	Chairman of the Board of Directors	March 30, 2000
/s/ William C. Dow ----- William C. Dow	Director	March 30, 2000
/s/ Kevin J. Dunn ----- Kevin J. Dunn	Director	March 30, 2000
/s/ Alan H. Magazine ----- Alan Magazine	Director	March 30, 2000
/s/ H.B. Brent Norton, M.D. ----- H.B. Brent Norton, M.D.	Director	March 30, 2000
/s/ Kenneth J. Pulkonik ----- Kenneth J. Pulkonik	Director	March 30, 2000

/s/ Robert I. Rudko, PH.D.

Director

March 30, 2000

-----  
Robert I. Rudko, Ph.D.

/s/ Roberts A. Smith, PH.D.

Director

March 30, 2000

-----  
Roberts A. Smith, Ph.D.

</TABLE>

APPENDIX A

PLC SYSTEMS INC.  
CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE YEARS ENDED DECEMBER 1999, 1998, 1997

PLC SYSTEMS INC.  
INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

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REPORT OF INDEPENDENT AUDITORS

To The Board of Directors and Stockholders of  
PLC Systems Inc.

We have audited the accompanying consolidated balance sheets of PLC Systems Inc. as of December 31, 1999 and 1998, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 1999. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of PLC Systems Inc. at December 31, 1999 and 1998, and the consolidated results of its operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 1999 in conformity with accounting principles generally accepted in the United States.

/s/ Ernst & Young LLP

Ernst & Young LLP

Boston, Massachusetts  
February 18, 2000,  
except for Note 12,  
as to which date is March 28, 2000

PLC SYSTEMS INC.  
CONSOLIDATED BALANCE SHEETS  
December 31, 1999 and 1998

<TABLE>  
<CAPTION>

	1999 ----	1998 ----
(In thousands)		
<b>ASSETS</b>		
<S>	<C>	<C>
Current assets:		
Cash and cash equivalents	\$ 4,467	\$ 4,846
Accounts receivable, net	1,894	2,262
Lease receivables, net	642	-
Inventories, net	2,348	2,953
Prepaid expenses and other current assets	460	547
	-----	-----
Total current assets	9,811	10,608
Equipment, furniture and leasehold improvements, net	3,336	5,091
Lease receivables, net	1,782	-
Other assets	390	558
	-----	-----
Total assets	\$15,319	\$16,257
	=====	=====

**LIABILITIES AND STOCKHOLDERS' EQUITY**

Current liabilities:		
Accounts payable	\$ 1,338	\$ 986
Accrued clinical costs	769	1,016
Accrued compensation	653	989
Accrued expenses	630	1,199
Deferred revenue	138	195
Secured borrowings	824	240
Convertible debentures	-	934
	-----	-----
Total current liabilities	4,352	5,559
Capital lease obligations	-	37
Secured borrowings	2,082	-
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, no par value, 5,000 shares authorized, none issued and outstanding		
Common stock, no par value, unlimited shares authorized, 21,223 shares issued and outstanding in 1999, 50,000 shares authorized, and 19,740 shares issued and outstanding in 1998	84,380	79,521
Accumulated deficit	(74,691)	(68,136)
Accumulated other comprehensive loss	(804)	(724)
	-----	-----
	8,885	10,661
	-----	-----
Total liabilities and stockholders' equity	\$15,319	\$16,257
	=====	=====

</TABLE>

The accompanying notes are an integral part of the consolidated financial statements.

F - 3

PLC SYSTEMS INC.  
CONSOLIDATED STATEMENTS OF OPERATIONS  
For The Years Ended December 31, 1999, 1998 and 1997

<TABLE>  
<CAPTION>

	1999 -----	1998 -----	1997 -----
(In thousands, except per share data)			
<S>	<C>	<C>	<C>
Revenue:			
Product sales	\$ 8,400	\$ 3,088	\$ 5,687
Placement and service fees	3,236	2,605	3,254
	-----	-----	-----
Total revenues	11,636	5,693	8,941
Cost of revenues:			
Product sales	3,615	1,945	2,721
Placement and service fees	2,061	2,622	2,595
	-----	-----	-----
Total cost of revenues	5,676	4,567	5,316
	-----	-----	-----

Gross Profit	5,960	1,126	3,625
Operating expenses:			
Selling, general and administrative	10,054	13,718	13,049
Research and development	2,672	4,468	5,158
Total operating expenses	12,726	18,186	18,207
Loss from operations	(6,766)	(17,060)	(14,582)
Other income, net	211	457	178
Net loss	\$(6,555)	\$(16,603)	\$(14,404)
Net loss per share - Basic and Diluted	\$ (.32)	\$ (.86)	\$ (.84)
Shares used to compute net loss per share - Basic and Diluted	20,675	19,218	17,050

The accompanying notes are an integral part of the consolidated financial statements.

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PLC SYSTEMS INC.  
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY  
For The Years Ended December 31, 1999, 1998 and 1997

<TABLE>  
<CAPTION>

	Common Stock		Accumulated Deficit	Accumulated Other Comprehensive Loss	Total
	Shares	Amount			
			(In Thousands)		
<S>	<C>	<C>	<C>	<C>	<C>
Balance, December 31, 1996	16,513	\$ 54,030	\$(37,129)	\$ (434)	\$ 16,467
Exercise of stock options	435	1,909	-	-	1,909
Exercise of warrants	17	94	-	-	94
Conversion of debentures	1,403	14,465	-	-	14,465
Issuance of warrants	-	617	-	-	617
Comprehensive loss:					
Net loss	-	-	(14,404)	-	(14,404)
Foreign currency translation	-	-	-	(139)	(139)
Total comprehensive loss					(14,543)
Balance, December 31, 1997	18,368	71,115	(51,533)	(573)	19,009
Exercise of stock options	142	623	-	-	623
Conversion of 5% debentures due 2002	577	3,923	-	-	3,923
Conversion of debentures due 2003	653	3,810	-	-	3,810
Issuance of warrants	-	50	-	-	50
Comprehensive loss:					
Net loss	-	-	(16,603)	-	(16,603)
Foreign currency translation	-	-	-	(151)	(151)
Total comprehensive loss					(16,754)
Balance, December 31, 1998	19,740	\$ 79,521	\$(68,136)	\$ (724)	\$ 10,661
Exercise of stock options	4	17	-	-	17
Conversion of debentures due 2003	163	972	-	-	972
Issuance of common stock	1,316	3,786	-	-	3,786
Compensation expense	-	84	-	-	84
Comprehensive loss:					
Net loss	-	-	(6,555)	-	(6,555)
Foreign currency translation	-	-	-	(80)	(80)
Total comprehensive loss					(6,635)
Balance, December 31, 1999	21,223	\$ 84,380	\$(74,691)	\$ (804)	\$ 8,885

</TABLE>

The accompanying notes are an integral part of the consolidated financial statements.

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PLC SYSTEMS INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
For The Years Ended December 31, 1999, 1998 and 1997

<TABLE>  
<CAPTION>

	1999 ----	1998 ----	1997 ----
	(In thousands)		
<S>	<C>	<C>	<C>
Operating activities:			
Net loss	\$ (6,555)	\$ (16,603)	\$ (14,404)
Adjustments to reconcile net loss to net cash used for operating activities:			
Depreciation and amortization	2,378	3,170	2,007
Compensation on stock options	84	-	-
Change in assets and liabilities:			
Accounts receivable	313	(973)	1,389
Inventories	607	(475)	(136)
Prepaid expenses and other assets	234	89	(20)
Accounts payable	342	82	24
Deferred revenue	(57)	142	(77)
Accrued liabilities	(1,139)	304	1,163
Net cash used for operating activities	(3,793)	(14,264)	(10,054)
Investing activities:			
Purchase of fixed assets	(1,166)	(2,574)	(2,642)
Retirement of fixed assets at net book value	581	-	-
Purchase of marketable securities	-	(1,986)	(17,827)
Maturities of marketable securities	-	14,831	10,452
Net cash provided by (used for) investing activities	(585)	10,271	(10,017)
Financing activities:			
Net proceeds from sale of common stock	3,803	623	2,003
Secured borrowing	242	240	-
Principal payments on capital lease obligations	(66)	(79)	(25)
Issuance of 5% Convertible Debentures, net of issuance costs	-	-	18,779
Issuance of Convertible Debentures, net of issuance costs	-	4,659	-
Net cash provided by financing activities	3,979	5,443	20,757
Effect of exchange rate changes on cash and cash equivalents	20	(88)	(241)
Net increase (decrease) in cash and cash equivalents	(379)	1,362	445
Cash and cash equivalents at beginning of year	4,846	3,484	3,039
Cash and cash equivalents at end of year	\$ 4,467	\$ 4,846	\$ 3,484
	=====	=====	=====
Non-Cash Financing Activities:			
Conversion of Convertible Debentures and accrued interest into Common Stock	\$ 972	\$ 7,733	\$ 14,465
Ascribed warrant value	-	50	617
Capital leases	-	-	150

</TABLE>

The accompanying notes are an integral part of the consolidated financial statements.

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PLC SYSTEMS INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
December 31, 1999

1. NATURE OF BUSINESS

PLC Systems Inc. ("PLC" or the "Company") has developed a patented high-powered carbon dioxide laser system known as The Heart Laser System for use in the treatment of coronary artery disease in a surgical laser procedure, pioneered by the Company and its clinical investigators, known as transmyocardial revascularization ("TMR"). TMR is a new laser based treatment for relieving debilitating pain in patients suffering from severe coronary artery disease ("CAD"). The Company's CO2 laser is used by a cardiovascular surgeon to create between 20 and 40 tiny channels in the heart wall of a patient suffering from severe CAD. Each TMR procedure requires a sterile, single use, TMR kit containing assorted TMR handpieces, drapes and other disposable items.

2. SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION

The consolidated financial statements include the accounts of PLC Systems Inc. (PLC or the "Company") and its five wholly owned subsidiaries, PLC

Medical Systems, Inc., PLC Sistemas Medicos GmbH, PLC Medical Systems AG, PLC Medical Systems Asia/Pacific Pte Ltd, and PLC Medical Systems Australia Pty Ltd. All intercompany accounts and transactions have been eliminated. Certain prior year amounts may have been reclassified to conform to the current year's presentation.

These consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (GAAP). Had the statements been prepared in accordance with Canadian GAAP, certain transactions in 1998 would have been accounted for differently. Under Canadian GAAP, the Convertible Debentures, net of issuance costs, would be classified as equity since the Company has the right to settle the principal and interest amounts due on the debentures by issuing common stock.

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Accordingly, if the accompanying financial statements had been prepared under Canadian GAAP at December 31, 1998, common stock would be \$934,000 greater due to the inclusion of the Convertible Debentures and accrued expenses would be reduced by \$33,000 in 1998 due to the elimination of accrued interest on the debt. In addition, the accumulated deficit would be reduced by \$252,000 in 1998 as a result of the elimination of interest and other debt issuance expenses included in the accompanying statement of operations for the year ended December 31, 1998 as required under U.S. GAAP. In 1999, the financial statements presented are in accordance with both U.S. GAAP and Canadian GAAP.

#### CASH AND MARKETABLE SECURITIES

Investments with a maturity of three months or less at the date of purchase are considered to be cash equivalents and those with maturities greater than three months are considered to be marketable securities. Marketable securities are stated at cost, which approximates fair value. Cash equivalents and marketable securities, which are classified as available-for-sale securities, consist primarily of time deposits, bankers acceptances and obligations of U.S. government and agencies.

#### INVENTORIES

Inventory is stated at the lower of cost or market value.

#### EQUIPMENT, FURNITURE AND LEASEHOLD IMPROVEMENTS

Equipment, fixtures and leasehold improvements are stated on the basis of cost. Depreciation is computed principally on the straight-line method for financial reporting purposes and on accelerated methods for income tax purposes.

Depreciation and amortization are based on the following useful lives:

<TABLE>

<CAPTION>

<S>

	<C>
Equipment	3-5 years
Equipment under placement contracts	Life of contract
Office furniture and fixtures	5 years
Equipment under capital lease	5 years
Leasehold improvements	Life of lease

</TABLE>

The Company reviews and evaluates long-lived assets for impairment on a regular basis. In management's opinion, long-lived assets are not impaired as of the balance sheet dates presented. The amounts capitalized have future value to the Company.

#### REVENUE RECOGNITION

The Company sells its principal product, The Heart Laser System, and related disposable surgical kits to hospital customers both directly and through distributors. Revenues from the sale of disposable kits are recorded as product sales at the time of shipment. Revenues from the sale or lease of The Heart Laser System, which result in substantially all the risks and benefits of ownership of The Heart Laser System being transferred to the customer, are recorded as product at the time of ownership transfer. In sales transactions this typically occurs at time of shipment. In lease transactions this typically occurs upon lease commencement, at which time the Company records revenue equal to the present value of the guaranteed minimum lease payments.

The Company also installs The Heart Laser System at hospitals under placement agreements which do not transfer substantial ownership of the equipment to the customer. Revenues from these transactions are recognized over the life of the placement agreement in accordance with the specific terms of the contract.

Revenues from service and maintenance contracts are recognized ratably over the life of the contract.

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#### FOREIGN CURRENCY TRANSLATION

Assets and liabilities are translated into U.S. dollars at current exchange rates, while income and expense items are translated at average rates of exchange prevailing during the year. Exchange gains and losses arising from translation are accumulated as a separate component of stockholders' equity. Gains and losses from foreign currency transactions are recorded in the accompanying statements of operations and are not material.

#### NET LOSS PER SHARE

Basic earnings per share is computed based only on the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed using the weighted average number of common shares outstanding during the period, plus the dilutive effect of future issues of common stock relating to stock option programs and convertible debt financing. In calculating diluted earnings per share, the dilutive effect of stock options is computed using the average market price for the period unless their inclusion would be antidilutive.

#### STOCK BASED COMPENSATION

The Company grants stock options for a fixed number of shares to employees and certain other individuals with exercise prices equal to the fair value of the shares at the dates of grant. The Company has adopted the disclosure only provisions of Statement of Financial Accounting Standards No. 123, ACCOUNTING FOR STOCK-BASED COMPENSATION ("FAS 123") and will continue to account for its stock option plans in accordance with the provisions of APB 25 ACCOUNTING FOR STOCK ISSUED TO EMPLOYEES.

#### USE OF ESTIMATES

The preparation of financial statements in accordance with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The Company has provided a valuation allowance for all deferred tax assets due to the inability to assume the realization of such tax benefits in the foreseeable future.

#### 1. INVENTORIES

Inventories consist of the following at December 31 (in thousands):

<TABLE>  
<CAPTION>

	1999	1998
	----	----
<S>	<C>	<C>
Raw materials	\$1,044	\$1,035
Work in process	439	145
Finished goods	865	1,773
	-----	-----
	\$2,348	\$2,953
	=====	=====

</TABLE>

#### 2. EQUIPMENT, FURNITURE AND LEASEHOLD IMPROVEMENTS

Equipment, furniture and leasehold improvements consist of the following at December 31 (in thousands):

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<TABLE>  
<CAPTION>

	1999	1998
	----	----
<S>	<C>	<C>
Equipment	\$ 2,614	\$ 2,461
Equipment under placement contracts	6,354	6,617
Office furniture and fixtures	881	929
Equipment under capital lease	429	429
Leasehold improvements	591	587
	-----	-----
	10,869	11,023
Less accumulated depreciation and amortization	7,533	5,932
	-----	-----
	\$ 3,336	\$ 5,091
	=====	=====

</TABLE>

Depreciation expense was \$2,340,000, \$3,116,000 and \$1,894,000, respectively, for the years ended December 31, 1999, 1998 and 1997.

#### 5. LEGAL PROCEEDINGS

In September 1996, CardioGenesis filed a civil lawsuit in the United States District Court for the Northern District of California asking the court

to declare the Company's synchronization patent (U.S. Patent No. 5,125,926) invalid and unenforceable, or, alternatively, to find that CardioGenesis' TMR and PMR lasers do not infringe this patent. The Company filed a counterclaim alleging that all of CardioGenesis' TMR and PMR lasers infringe U.S. Patent No. 5,125,926. In January 1997, CardioGenesis filed an opposition in the European Patent Office to have the Company's German synchronization patent declared invalid. In April 1997, the Company filed an infringement lawsuit against CardioGenesis and one of its distributors in the Munich District Court alleging that CardioGenesis' TMR and PMR lasers infringe the Company's German synchronization patent. The PLC patents at issue in these lawsuits cover the Company's synchronization technology, which the Company believes is a critical factor in increasing the safety of TMR and PMR procedures.

In January 1999, the Company settled its outstanding patent infringement litigation with CardioGenesis, who subsequently merged with Eclipse Surgical Technologies, Inc. Under the settlement, CardioGenesis agreed that U.S. Patent No. 5,125,926 and related international patents of the Company are valid and enforceable. PLC granted CardioGenesis a non-exclusive worldwide license to the patents in exchange for payment of a license fee and ongoing royalties over the life of the patents (at least 10 years unless the patents are all held invalid in future lawsuits).

As part of the settlement, CardioGenesis agreed to pay the Company:

- a minimum of \$2.5 million over the next 42 months; and
- license fees and ongoing royalties on sales of all covered products for at least 10 years (unless the patents are all held invalid in future lawsuits).

In July 1997, a U.S. Food and Drug Administration ("FDA") advisory panel recommended against approval of the Company's application to market The Heart Laser System in the United States. Following this recommendation, the Company was named as defendant in 21 purported class action lawsuits filed between August 1997 and November 1997 in the United States District Court for the District of Massachusetts. The lawsuits seek an unspecified amount of damages in connection with alleged violations of the federal securities laws based on the Company's failure to obtain a favorable FDA panel recommendation in 1997. Nineteen of these complaints have been consolidated by the court into a single action for pretrial purposes (hereafter referred to as the "federal suit"). Two of these suits were voluntarily dismissed. The Company moved to dismiss all claims in the federal suit. On March 26, 1999, the court issued an order dismissing some, but not all, of the claims in the federal suit. The parties filed cross motions for reconsideration and on October 12, 1999, the court dismissed additional, but not all remaining claims in the federal suit. The Company has also been named as a defendant in a lawsuit filed in Massachusetts Superior Court in September 1998 (hereafter referred to as the "state suit") seeking over \$2 million in damages for alleged negligent misrepresentations and fraud arising from the Company's failure to obtain a favorable FDA recommendation in 1997. The Company cannot make a meaningful estimate of the amount or range of loss that could result from an unfavorable outcome of these

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lawsuits, but an unfavorable outcome could have a material adverse effect on the Company's business, financial position and results of operations. The Company believes that it has meritorious defenses to these litigation matters and continues to vigorously defend itself in these matters.

In August 1997, the Company received from the United States Securities and Exchange Commission (the "Commission") an informal request for information relating to the decision by the FDA Advisory Panel not to recommend approval of The Heart Laser System in July 1997. The Company has responded and has not received any further communication from the Commission regarding this matter since June 1998.

In February 1996, PLC Medical Systems, Inc. filed suit against Eclipse Surgical Technologies, Inc. ("Eclipse") in the United States District Court for the District of Massachusetts alleging copyright infringement and unfair and deceptive trade practices based on Eclipse's misappropriation and copying of one of PLC's confidential clinical study protocols. The Company settled this suit in April 1999 on confidential terms. The settlement of the lawsuit did not have a material impact on the Company's financial statements.

In November 1998, a hospital in France, Centre Medico Chirurgical Foch ("Foch Hospital"), sued the Company's Portuguese subsidiary, PLC Sistemas Medicos Internacionais Lda., and a third party, Johnson & Johnson Leasing GmbH, in Paris, France alleging breach of contract. In October 1997, the French Ministry of Health suspended commercial use of TMR devices in France. Foch Hospital is seeking reimbursement of lease payments made for The Heart Laser System. The Company intends to vigorously defend itself in this matter. A hearing on the merits of the case has been held, however no decision has been rendered and a meaningful estimate of the loss that could result from this matter can not be made. However, the Company does not believe that the loss, if any, would have a material adverse impact on the Company's financial condition.

#### 6. ISSUANCE OF CONVERTIBLE DEBENTURES

In April 1998, the Company obtained a \$10 million financing commitment

from three institutional investors. Pursuant to the terms of the financing, the Company received approximately \$5 million in April 1998 from the issuance of non-interest bearing, five-year convertible debentures. In 1998, \$4,000,000 of the convertible debentures outstanding converted into 653,063 shares of the Company's Common Stock. In January 1999, the remaining \$1,000,000 of the convertible debentures outstanding converted into 163,264 shares of the Company's Common Stock. The remaining \$5 million of the commitment expired on December 31, 1998.

In connection with the April 1998 financing, the Company issued redeemable warrants to purchase 4,864 shares of its Common Stock at \$19.53 per share. If the average closing sale price of its Common Stock for any consecutive thirty trading day period commencing April 23, 1999 exceeds the exercise price by more than 50%, the Company has the right, exercisable at any time upon 30 days notice to the holder, to redeem the warrants at a price of \$.10 per warrant. The warrants expire on April 23, 2003. The detachable warrants were valued at \$50,000 (using the Black-Scholes formula), classified as a component of equity, and disclosed separately in the Consolidated Statement of Stockholders' Equity.

## 7. STOCKHOLDERS' EQUITY

The Company's 1992 Stock Option Plan ("1992 Plan"), the 1993 Stock Option Plan ("1993 Plan") and the 1995 Stock Option Plan ("1995 Plan") allow for the granting of options aggregating 2,505,000 shares of common stock. All of the Plans consist of both incentive stock options and non-qualified options. Incentive stock options are issuable only to employees of the Company, while non-qualified options may be issued to non-employee directors, consultants, and others, as well as to employees. The options granted under all the Plans generally become

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exercisable ratably over one to three years from the date of grant, or based on the attainment of specific performance criteria, and expire ten years from the date of grant.

The Company's 1993 Formula Stock Option Plan (the "Formula Plan") provides for the grant of non-qualified options to non-employee directors to purchase up to 250,000 shares of common stock. The Plan is administered by the Board of Directors. Annually, the Company grants 10,000 options to each of its non-employee directors. A director must attend at least 60% of all Board meetings, as well as committee meetings, to receive the grant. The options vest over one year on a quarterly basis and expire ten years from the date of grant. The exercise price is the fair market value of the Company's common stock on the last business day preceding the date of grant. As of December 31, 1999, the options are fully exercisable and expire ten years from the date of grant.

The Company's 1997 Executive Stock Option Plan ("1997 Executive Plan") provides for the grant of non-qualified options to officers and directors of the Company to purchase up to 1,000,000 shares of common stock. The

options vest over time and/or the attainment of specific performance criteria.

The per share exercise price of the common stock subject to an incentive stock option may not be less than the fair market value of the common stock on the date the option is granted. The Company must grant non-qualified options at an exercise price of at least 85% of the fair market value of the common stock on the date the option is granted.

During 1998, the Board of Directors (together with its Compensation and Executive Committees) adopted the following incentive compensation programs:

a.) In January 1998, the outstanding options of all employees (except executive officers and directors) having a higher exercise price were repriced to \$8.88 per share. As a result, the exercise price of options to purchase 526,784 shares of Common Stock was reduced to \$8.88 per share.

b.) In August, 1998, the outstanding options of all directors and executive employees having a higher exercise price were repriced to \$7.75 per share. As a result, the exercise price of options to purchase 1,373,500 shares of Common Stock was reduced to \$7.75 per share.

c.) In September 1998, a new Senior Management Investment Program ("SMIP") was adopted to promote investment in the Company's stock by directors and members of the Company's senior management team. Under the SMIP, individuals who purchased additional shares of the Company's stock between September 15, 1998 and December 15, 1998 (the "Participants") received options to purchase an additional 1.5 shares of Common Stock at an exercise price equal to the Participant's share purchase price (the "Share Purchase Price"). In addition, Participants received ten "option credits" for each share of Common Stock purchased between September 15, 1998 and December 15, 1998. Participants could use each "option credit" to: (i) reduce the exercise price of an outstanding option (vested or unvested) to purchase one share of Common Stock to the Participant's Share Purchase Price; or (ii) extend the expiration date of any outstanding option (vested or unvested) for an additional three years; or (iii) acquire new vested options with an exercise price equal to the Participant's Share Purchase Price (at a rate of 6.67 option credits for each new option to purchase one share of Common Stock). Under this program, the Company granted options to purchase an additional 331,575 shares of Common Stock at exercise

prices ranging from \$3.875 to \$6.625 per share . Furthermore, the Company has reduced the exercise prices of options to purchase 1,243,500 shares of Common Stock to new exercise prices ranging from \$4.6875 to \$5.5625.

d.) In December 1998, the outstanding options held by employees not eligible to participate in the SMIP having a higher exercise price were repriced to \$4.875 per share. As a result, the exercise price of options to purchase 332,316 shares of Common Stock were repriced to \$4.875 per share.

The following is a summary of option activity under all Plans (in thousands, except per option data):

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<TABLE>  
<CAPTION>

	1999 ----	1998 ----	1997 ----
<S>	<C>	<C>	<C>
Outstanding at beginning of year	2,788	2,187	1,914
Granted	1,204	823	938
Exercised	(4)	(142)	(435)
Canceled	(1,282)	(80)	(230)
	-----	-----	-----
Outstanding at end of year	2,706	2,788	2,187
	=====	=====	=====
Exercisable at end of year	1,681	1,711	878
Available for grant at end of year	152	71	463
	-----	-----	-----
Weighted - average exercise price:			
Outstanding at beginning of year	\$4.88	\$8.75	\$8.18
Granted	\$2.53	\$5.39	\$13.56
Canceled	\$5.46	\$9.09	\$11.50
Exercised	\$3.91	\$4.39	\$4.39
Outstanding at end of year	\$3.84	\$5.16	\$10.84
Exercisable at end of year	\$4.47	\$4.88	\$8.75
Weighted - average fair value of Options granted during the year	\$1.44	\$3.33	\$8.20

</TABLE>

<TABLE>  
<CAPTION>

	Range of Exercise Prices		
	\$2.00 - \$5.00 -----	\$5.01 - \$8.88 -----	\$2.00 - \$8.88 -----
<S>	<C>	<C>	<C>
Options Outstanding:			
Number (in thousands)	2,184	522	2,706
Weighted-Average Remaining Contractual Life	7.71	7.43	7.66
Weighted-Average Exercise Price	\$3.32	\$6.03	\$3.84
Options Exercisable:			
Number (in thousands)	1,210	471	1,681
Weighted-Average Exercise Price	\$3.91	\$5.89	\$4.47

</TABLE>

Pursuant to the requirements of FAS 123, the following are the pro forma net loss and net loss per share for 1999, 1998 and 1997, as if the compensation cost for the option plans had been determined based on the fair value at the grant date for grants in 1999, 1998 and 1997, consistent with the provisions of FAS 123.

<TABLE>  
<CAPTION>

	1999 -----	1998 -----	1997 ----
<S>	<C>	<C>	<C>
Proforma net loss (in thousands)	\$(5,163)	\$(22,438)	\$(16,523)
Proforma net loss per share	\$ (.25)	\$ (1.17)	\$ (.97)

</TABLE>

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The fair value of options issued at the date of grant were estimated

using the Black-Scholes model with following weighted average assumptions:

	1999	1998	1997
Expected life (years)	2	2	2
Interest rate	5.87%	5.53%	6.01%
Volatility	1.052	.761	1.141

The effects on pro forma disclosures of applying FAS 123 are not likely to be representative of the effects on pro forma disclosures of future years.

As of December 31, 1999, the Company had the following outstanding warrants to purchase common stock: 69,875 shares at \$27.81 per share expiring July 22, 2002; 80,125 shares at \$15.78 per share expiring August 14, 2002; and 4,864 shares at \$19.53 per share expiring April 23, 2003.

At December 31, 1999, there were 3,023,026 shares of authorized but unissued common stock reserved for issuance under all stock option plans and stock warrants.

In March 1999, the Company obtained a provisional equity financing commitment of up to \$8 million from a major institutional investor. In 1999, the Company had sold 649,474 shares of common stock under this commitment, resulting in proceeds to the Company (net of all issuance costs payable upon closing) of approximately \$1,900,000. This commitment expired on July 16, 1999. In July 1999, the Company also sold 666,666 shares of common stock to another investor resulting in net proceeds to the Company of approximately \$1,900,000.

The Company has 5,000,000 authorized shares of preferred stock. The Board of Directors is authorized to fix designations, relative rights, preferences and limitations in the preferred stock at time of issuance.

The Company has never declared nor paid dividends on any of its capital stock and does not expect to do so in the foreseeable future.

#### 8. LEASE RECEIVABLES

The Company has entered into third-party financing arrangements to provide an array of lease financing alternatives to hospitals interested in acquiring The Heart Laser System. The lease financing alternatives available complement the Company's traditional placement and sales strategies.

Under these arrangements, the Company receives payment from the leasing company equal to the present value of guaranteed minimum procedure payments due from the customer after customer acceptance of The Heart Laser System. In transactions where the Company has transferred substantially all of the risks and rewards of ownership to the customer and the customer has accepted The Heart Laser System, the Company recognizes revenue, which is reported as a component of product sales. The Company recognizes a lease receivable equal to the present value of the guaranteed minimum lease payments until such time as the Company can legally isolate the lease receivables. The payment received from the leasing company is recognized as a secured borrowing. Interest income and interest expense related to the lease receivables and secured borrowing, respectively, is recognized over time using the effective interest method. Equal amounts of interest income and interest expense are included as a component of other income, net, in the Consolidated Statement of Operations.

#### 9. LEASE COMMITMENTS

The Company occupies its worldwide facilities under operating lease agreements, which expire through March 2002. The Company has the option to renew the U.S. facilities lease for up to six years. In addition to the

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minimum lease payments, the agreement requires payment of the Company's pro-rata share of property taxes and building operating expenses. The Company also leases certain equipment.

As of December 31, 1999, future minimum lease payments are as follows (in thousands):

Year	Future Minimum Lease Payments
2000	\$327
2001	213
2002	12
	====
	\$552
	====

</TABLE>

Total rent expense was \$424,000 in 1999, \$375,000 in 1998 and \$458,000 in 1997.

10. INCOME TAXES

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's deferred tax assets as of December 31 are as follows (in thousands):

	1999 ----	1998 ----
<S>	<C>	<C>
Net U.S. operating loss carryforwards	\$16,279	\$13,791
Net foreign operating loss carryforwards	1,775	2,263
Intercompany profit	189	313
Accrued clinical costs	307	406
Research & development credits	761	679
Inventory and warranty reserves	484	497
Alternative minimum tax credit	63	63
Accrued salaries	200	195
Deferred revenue	55	173
Other	(62)	4
	-----	-----
Total deferred tax assets	20,051	18,384
Valuation allowance	(20,051)	(18,384)
	-----	-----
Net deferred tax assets	\$ -	\$ -
	=====	=====

</TABLE>

The valuation allowance increased by approximately \$1,700,000 primarily due to additional net operating loss carryforwards. The Company recorded the valuation allowance due to the uncertainty of the realizability of the related net deferred tax asset of \$20,051,000.

Loss before taxes consisted of the following (in thousands):

	1999 ----	1998 ----	1997 ----
<S>	<C>	<C>	<C>
Domestic	\$ (5,027)	\$ (14,137)	\$ (11,340)
Foreign	(1,528)	(2,472)	(3,064)
	-----	-----	-----
	\$ (6,555)	\$ (16,603)	\$ (14,404)
	=====	=====	=====

</TABLE>

Income taxes (benefit) computed at the federal statutory rate differ from amounts provided as follows (in thousands):

F - 15

	1999 ----	1998 ----	1997 ----
<S>	<C>	<C>	<C>
Statutory income tax benefit	\$ (2,229)	\$ (5,645)	\$ (4,898)
Utilization of loss carryforwards	(290)	(85)	-
Unbenefited U.S. losses	1,709	4,807	3,856
Unbenefited foreign losses	810	923	1,042
	-----	-----	-----
Benefit for income taxes	\$ -	\$ -	\$ -
	=====	=====	=====

</TABLE>

At December 31, 1999 the Company had U.S. net operating loss carryforwards available to reduce future taxable income of approximately \$40.8 million, which expire at various dates through 2013. In addition, the Company had foreign net operating loss carryforwards of approximately \$4.4 million.

In 1999, certain subsidiaries were liquidated. The foreign net operating loss carryforwards were reduced for amounts that will not be utilized as a result of the liquidations.

11. SEGMENT INFORMATION

The Company operates in one industry segment - the development, manufacture and sales of medical lasers and related products. Net sales to unaffiliated customers (by origin) are summarized below (in thousands).

<TABLE>

<CAPTION>

	North America	Europe	Other	Eliminations	Total
<S>	<C>	<C>	<C>	<C>	<C>
1999					
Net sales to unaffiliated customers	\$10,196	\$1,440	\$ -	\$ -	\$ 11,636
Long-lived assets	\$ 391	\$ -	\$ -	\$ -	\$ 391
1998					
Net sales to unaffiliated Customers					
	\$ 3,992	\$1,615	\$ 86	\$ -	\$ 5,693
Long-lived assets	\$ 558	\$ -	\$ -	\$ -	\$ 558
1997					
Net sales to unaffiliated Customers	\$ 4,092	\$4,683	\$166	\$ -	\$ 8,941
Long-lived assets	\$ 701	\$ -	\$ -	\$ -	\$ 701

</TABLE>

No one customer accounted for more than 10% of the Company's revenues for the year ended December 31, 1999 or 1998. Approximately 20% of the Company's revenues for the year ended December 31, 1997 came from one customer, Imatron Japan. The Company believes that its exposure to concentrations of credit risk is not significant based on experiences with these customers. In addition, letters of credit or payment in advance are required in credit risk situations. The Company does not believe its future revenues to be dependent on those generated from any single customer.

## 12. SUBSEQUENT EVENT

On March 28, 2000, the Company closed an equity financing with two institutional investors at \$2.00 per share. In conjunction with this offer, the Company sold 2,683,000 shares of common stock, resulting in proceeds to the Company (net of all issuance costs) of approximately \$5,000,000 and issued the placement agent a three year warrant for 61,326 shares of common stock at \$3.15 per share. The Company may seek additional financing through the issuance and sale of debt or equity securities, bank financing, joint ventures or by other means. The availability of such financing and the reasonableness of any related terms in comparison to market conditions cannot be assured.

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## Schedule II

### PLC SYSTEMS INC. Valuation and Qualifying Accounts

<TABLE>

<CAPTION>

Description	Column A	Column B	Column C	Column D	Column E
	-----	-----	-----	-----	-----
		Balance at Beginning of Period	Additions	Deductions	Balance at End of Period
<S>	<C>	<C>	<C>	<C>	<C>
For the Year Ended December 31, 1999					
Allowance for Doubtful Accounts		\$228,000	\$190,000	\$ 0	\$418,000
For the Year Ended December 31, 1998					
Allowance for Doubtful Accounts		\$140,000	\$100,000	\$12,000	\$228,000
For the Year Ended December 31, 1997					
Allowance for Doubtful Accounts		\$ 28,000	\$112,000	\$ 0	\$140,000

</TABLE>

### PLC SYSTEMS INC. QUARTERLY DATA (UNAUDITED)

<TABLE>

<CAPTION>

	March 31	June 30	September 30	December 31	Total
<S>	<C>	<C>	<C>	<C>	<C>
1999					
Total revenue	\$ 2,846	\$ 3,492	\$ 2,542	\$2,756	\$11,636
Gross profit	1,484	1,720	1,232	1,524	5,960
Loss from operations	(2,206)	(1,830)	(1,443)	(1,287)	(6,766)
Net loss	(2,199)	(1,705)	(1,395)	(1,256)	(6,555)
Net loss per share, basic and diluted	(.11)	(.08)	(.07)	(.06)	(.32)

1998

Total revenue	\$ 945	\$ 680	\$ 1,615	\$2,453	\$5,693
Gross profit (loss)	257	(351)	320	900	1,126
Loss from operations	(4,087)	(5,569)	(4,032)	(3,372)	(17,060)
Net loss	(3,936)	(5,402)	(4,006)	(3,259)	(16,603)
Net loss per share, basic and diluted	(.21)	(.28)	(.21)	(.17)	(.86)

</TABLE>

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EXHIBIT INDEX

Exhibit Number	Description of Document
-----	-----
3.1	Certificate of Incorporation, incorporated by reference to the Registrant's registration statement on Form S-1 (SEC File No. 33-48340) and amendments thereto, as previously filed with the Securities and Exchange Commission.
3.2*	Articles of Continuance, pursuant to the Yukon Business Corporations Act.
3.3*	By-Law No. 1, a By-Law relating generally to the transaction of the business and affairs of PLC Systems, Inc.
4.1	Form of Common Stock Certificate, incorporated by reference to the Registrant's registration statement on Form S-1 (SEC File No. 33-48340) and amendments thereto, as previously filed with the Securities and Exchange Commission.
10.1	1992 Stock Option Plan, incorporated by reference to the Registrant's registration statement on Form S-1 (SEC File No. 33-48340) and amendments thereto, as previously filed with the Securities and Exchange Commission.
10.2	1993 Stock Option Plan, incorporated by reference to the Registrant's registration statement on Form S-1 (SEC File No. 33-58258) and amendments thereto, as previously filed with the Securities and Exchange Commission.
10.3	1993 Formula Stock Option Plan, incorporated by reference to the Registrant's registration statement on Form S-1 (SEC File No. 33-58258) and amendments thereto, as previously filed with the Securities and Exchange Commission.
10.4	Revised Form of Key Employee Agreement for Dr. Robert I. Rudko, incorporated by reference to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1994 (SEC File No. 1-11388), as previously filed with the Securities and Exchange Commission.
10.5	1995 Stock Option Plan, incorporated by reference to the Registrant's Registration Statement on Form S-8 (SEC File No. 33-95168), as previously filed with the Securities and Exchange Commission.
10.6	Convertible Debenture Agreement, incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 1997 (SEC File No. 1-11388), as previously filed with the Securities and Exchange Commission.
10.7	First Amendment to Convertible Debenture Agreement, incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 1997 (SEC File No. 1-11388), as previously filed with the Securities and Exchange Commission.
10.8	Second Amendment to Convertible Debenture Agreement, incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 1997 (SEC File No. 1-11388), as previously filed with the Securities and Exchange Commission.
10.9	Form of Convertible Debenture, incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 1997 (SEC File No. 1-11388), as previously filed with the Securities and Exchange Commission.
10.10	Form of Redeemable Warrant, incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 1997 (SEC File No. 1-11388), as previously filed with the Securities and Exchange Commission.
10.11	Registration Rights Agreement, incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 1997 (SEC File No. 1-11388), as previously filed with the Securities and Exchange Commission.
10.12	Form of Key Employment Agreement for William C. Dow, incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 1997 (SEC File No. 1-11388), as previously filed with the Securities and Exchange Commission.

- 10.13 1997 Executive Stock Option Plan, incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 1997 (SEC File No. 1-11388), as previously filed with the Securities and Exchange Commission.
- 10.14 Convertible Debenture Purchase Agreement dated as of April 23, 1998 between Southbrook International Investment, Ltd., Brown Simpson Strategic Growth Fund, L.P. and Brown Simpson Strategic Growth Fund, Ltd. and the Registrant, incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the Quarter ended March 31, 1998 (File No. 1-11388), as previously filed with the Securities and Exchange Commission.
- 10.15 Form of Convertible Debenture, incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the Quarter ended March 31, 1998 (File No. 1-11388), as previously filed with the Securities and Exchange Commission.
- 10.16 Form of Redeemable Warrant, incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the Quarter ended March 31, 1998 (File No. 1-11388), as previously filed with the Securities and Exchange Commission.
- 10.17 Registration Rights Agreement dated as of April 23, 1998 between Southbrook International Investment, Ltd., Brown Simpson Strategic Growth Fund, L.P. and Brown Simpson Strategic Growth Fund, Ltd. and the Registrant, incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the Quarter ended March 31, 1998 (File No. 1-11388), as previously filed with the Securities and Exchange Commission.
- 10.18 Key Employee Agreement of Robert Svihart, incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the Quarter ended June 30, 1998 (File No. 1-11388), as previously filed with the Securities and Exchange Commission.
- 10.19 Form of Common Stock Purchase Agreement, incorporated by reference to the Registrant's Current Report on Form 8-K dated March 12, 1999 (File No. 1-11388), as previously filed with the Securities and Exchange Commission.
- 21.1 \* Subsidiaries of the Registrant.  
23.1 \* Consent of Ernst & Young LLP.  
27.1 \* Financial Data Schedule.

\* Filed with this Annual Report on Form 10-K for the fiscal year ended December 31, 1999.

YUKON BUSINESS CORPORATIONS ACT

(SECTION 190)

FORM 3-01

ARTICLES OF CONTINUANCE

1. NAME OF CORPORATION:  
PLC SYSTEMS INC.

2. THE CLASSES AND ANY MAXIMUM NUMBER OF SHARES THAT THE CORPORATION IS  
AUTHORIZED TO ISSUE:

The Corporation is authorized to issue an unlimited number of common shares  
and an unlimited number of preferred shares, issuable in series, having the  
special rights and restrictions set forth in Appendix "1" hereto.

3. RESTRICTIONS, IF ANY, ON SHARE TRANSFERS:

None.

4. NUMBER (OR MINIMUM OR MAXIMUM NUMBER) OF DIRECTORS:

Minimum of 3                      Maximum of 20

5. RESTRICTIONS, IF ANY, ON BUSINESS THE CORPORATION MAY CARRY ON:

The Corporation is restricted from carrying on the business of a railway,  
steamship, air transport, canal, telegraph or irrigation company.

6. IF CHANGE OF NAME EFFECTED, PREVIOUS NAME:

Not application.

7. DETAILS OF INCORPORATION:

The Corporation was incorporated on March 3, 1987 under the name "Videx  
Communication Systems Inc." by registration of memorandum pursuant to the  
Company Act (British Columbia) under Certificate of Incorporation No. 322734.  
The Corporation changed its name on May 20, 1987 to PLC Systems Inc.

8. OTHER PROVISIONS, IF ANY:

See attached Appendix "2" hereto.

9. DATE March 4, 1999    SIGNATURE /s/ Jennifer T. Miller    TITLE Secretary

ARTICLES OF CONTINUANCE OF

PLC SYSTEMS INC.

(THE "CORPORATION")

The following special rights and restrictions shall be attached to the preferred shares ("preferred shares"):

- (i) The preferred shares as a class shall have attached thereto the special rights and restrictions specified in this Appendix "1";
- (ii) Preferred shares may at any time and from time to time be issued in one or more series. The directors may from time to time by resolution passed before the issue of any preferred shares of any particular series, alter the Articles of the Company to fix the number of preferred shares of any particular series, alter the Articles of the Company to fix the number of preferred shares in, and to determine the designation of the preferred shares of, that series and alter the Articles to create, define and attach special rights and restrictions to the preferred shares of that series including, but without in any way limiting or restricting the generality of the foregoing: the rate or amount of dividends, whether cumulative, non-cumulative or partially cumulative; the dates, places and currencies of payment thereof, the consideration for, and the terms and conditions of, any purchase for cancellation or redemption thereof, including redemption after a fixed term or at a premium; conversion or exchange rights or rights of retraction (provided that any such conversion or exchange rights or rights of retraction shall be in accordance with the provisions existing at the time of creation of such series relating to conversion, exchange, or retraction as prescribed by the policies of the American Stock Exchange or any other stock exchange on which the shares of the Company are then listed); the terms and conditions of any share purchase plan or sinking fund; and voting rights and restrictions, but no special right or restriction so created, defined or attached shall contravene the provisions of subclauses (iii) and (iv) of this Appendix "1";
- (iii) Holders of preferred shares shall be entitled, on the distribution of assets of the Company or on the liquidation, dissolution or winding-up of the Company, whether voluntary or involuntary, or on any other distribution of assets of the Company among its shareholders for the purpose of winding-up its affairs, to receive before any distribution to be made to holders of common shares or any other shares of the Company ranking junior to the preferred shares with respect to repayment of capital, the amount due to such holders of preferred shares in accordance with the Articles with respect to each preferred share held by them, together with all accrued and unpaid cumulative dividends, (if any and if preferential) thereon, and all declared and unpaid non-cumulative dividends (if any and if preferential) thereon. After payment to holders of preferred shares of the amounts so payable to them, such holders shall not be entitled to share in any further distribution of the property or assets of the Company except as specifically provided in the special rights and restrictions attached to any particular series of the preferred shares; and
- (iv) Except for such voting rights as may be attached to any series of the preferred shares by the directors, holders of preferred shares shall not be entitled as such to vote at, any general meeting of shareholders of the Company. Holders of preferred shares shall be given notice of and be invited to attend meetings of voting shareholders of the Company.

APPENDIX "2"

ATTACHED TO AND FORMING PART OF FORM 3-01

ARTICLES OF CONTINUANCE OF  
PLC SYSTEMS INC.  
(THE "CORPORATION")

- (1) The Directors of the Corporation may, between annual general meetings of the Corporation, appoint one or more additional directors to serve until the next annual general meeting but the number of additional

directors shall not at any time exceed one third of the number of directors who held office at the expiration of the last annual general meeting, and in no event shall the total number of directors exceed the maximum number of directors fixed pursuant to paragraph 4 of the Articles of Continuance.

- (2) Meetings of Shareholders shall be held in the Cities of Boston, in the State of Massachusetts, New York, in the State of New York, Vancouver in the Province of British Columbia or such other place or places as the directors in their absolute discretion may determine from time to time.
- (3) At each annual general meeting of the Company, the Company shall elect directors to the Board of Directors as may be required to fill any positions vacated by reason of the expiration of the term of office of one or more of the directors. A director may be elected for a term of office of one or more years of office as may be specified in the resolution by which he is elected. In this part, "year or office" means the period of time commencing on the date of an annual general meeting of the Company and ending on the date of the annual general meeting held in the next subsequent calendar year. If in any calendar year the Company does not hold an annual general meeting, the directors whose terms of office would have expired in such calendar year shall be deemed to have been elected as directors on the last date on which the annual general meeting could have been held in such calendar year pursuant to the Yukon Business Corporations Act and each director so deemed elected may hold office until the next annual general meeting is held and other directors are elected. The shareholders may, by special resolution, vary the term of office of any director.

BY-LAW NO. 1  
A BY-LAW RELATING GENERALLY TO THE TRANSACTION OF  
THE BUSINESS AND AFFAIRS OF  
PLC SYSTEMS INC.  
(THE "CORPORATION")

CONTENTS:

1. Interpretation
2. Business of the Corporation
3. Borrowing and Securities
4. Directors
5. Committees
6. Officers
7. Protection of Directors, Officers and Others
8. Shares
9. Dividends and Rights
10. Meetings of Shareholders
11. Division and Departments
12. Notices

BE IT ENACTED as a By-Law of the Corporation as follows:

SECTION ONE

INTERPRETATION

1.01 DEFINITIONS - in the By-Laws of the Corporation, unless the context otherwise requires:

"ACT" means the BUSINESS CORPORATIONS ACT, and any statute that may be substituted therefore, as from time to time amended; marginal references to sections of the Act herein are not made for the purpose of modifying or affecting the meaning of any provision of this By-Law in any way but are inserted only for the purpose of directing attention to provisions of the Act which may be regarded as relevant;

"APPOINT" includes "ELECT" and vice versa;

"ARTICLES" means the Articles attached to the Certificate of Continuance dated the 12th day of March, 1999 of the Corporation as from time to time amended or restated;

"BOARD" means the Board of Directors of the Corporation;

"BY-LAWS" means this By-Law and all other By-Laws of the Corporation from time to time in force and effect relating to transaction of business and affairs of the Corporation in addition hereto, or in amendment hereof or in substitution for all or any part of this ByLaw;

"CORPORATION" means the Corporation incorporated by Certificate of Continuance

under the Act and named: PLC SYSTEMS INC.

"MEETING OF SHAREHOLDERS" includes an annual meeting of Shareholders and a Special Meeting of Shareholders; "Special Meeting of Shareholders" includes both a meeting of any class or classes acting separately from any other class or classes and also a meeting, other than an annual meeting, of all Shareholders entitled to vote at any annual meeting of Shareholders;

"NON-BUSINESS DAY" means Saturday, Sunday and any other day that is a holiday as defined in the INTERPRETATION ACT (CANADA) or the INTERPRETATION ACT (YUKON);

"PROHIBITED CORPORATE SHAREHOLDER" means a corporation prohibited from holding shares in itself or its holding body corporate or a subsidiary corporation prohibited from holding shares in its parent corporation pursuant to the Act and not exempted from such prohibited shareholdings by Virtue of the Act;

"RECORDED ADDRESS" means in the case of a Shareholder his address as recorded in the securities register, and in the case of joint Shareholders the address appearing in the securities register in respect of such joint holdings determined under Section 8.09; and in the case of a Director, Officer, auditor or member of a Committee of Directors, his latest address as recorded in the records of the Corporation; save as aforesaid, words and expressions defined in the Act have the

Same meaning when used herein; and words importing the singular number include the plural and vice versa; words importing gender include the masculine, feminine and neuter genders; and words importing persons include individuals, bodies corporate, partnerships, trusts and unincorporated organizations.

## SECTION TWO

### BUSINESS OF THE CORPORATION

2.01 REGISTERED OFFICE - Until changed in accordance with the Act, the registered office of the Corporation shall be at the City of Whitehorse, in the Yukon Territory, and at such location therein as the Board may from time to time determine.

2.02 CORPORATE SEAL - Until changed by the Board, the corporate seal of the Corporation and any facsimiles thereof adopted by the Board for use in jurisdictions outside the Yukon Territory shall be in the form approved by the Directors.

2.03 FINANCIAL YEAR - The financial year of the Corporation shall end on the day in each year that is established by the Board.

2.04 EXECUTION OF INSTRUMENTS - Deeds, transfers, assignments, contracts, obligations, certificates and other instruments required by law or otherwise by these By-Laws or any resolution of the Board or Shareholders of the Corporation to be executed under corporate seal may be signed on behalf of the Corporation by any one or more persons each of which is either a Director of the Corporation or a person who holds the office of Chief Executive Officer, Chairman of the Board, President, Managing Director, Vice-President, Secretary, Treasurer, Assistant Secretary, Assistant Treasurer or any other office created by by-law or by resolution of the Board. Notwithstanding the foregoing, the Board may from time to time direct the manner in which and the person or persons by whom any particular instrument or class of instruments may or shall be signed or sealed. Any one Officer may affix the corporate seal to any instrument requiring the same.

2.05 BANKING ARRANGEMENTS - The banking business of the Corporation including, without limitation, the borrowing of money and the giving of security therefore, shall be transacted with such banks, trust companies or other bodies corporate or organizations as may from time to time be designated by or under the authority of the Board. Such banking business or any part thereof shall be transacted under such agreements, instructions and delegations of powers as the Board may from time to time by resolution prescribe or authorize.

2.06 VOTING RIGHTS IN OTHER BODIES CORPORATE - Any one of the Officers of the Corporation may execute and deliver proxies and arrange for the issuance of voting certificates or other evidence of the right to exercise the voting rights

attaching to any securities held by the Corporation. Such instruments, certificates or other evidence shall be in favor of such person or persons as may be determined by the Officers executing such proxies or arranging for the issuance of voting certificates or such other evidence of the right to exercise such voting rights.

In addition the Board may from time to time direct the manner in which and the person or persons by whom any particular voting rights or class of voting rights may or shall be exercised.

**2.07 WITHHOLDING INFORMATION FROM SHAREHOLDERS** - Subject to the provisions of the Act, no Shareholder shall be entitled to discovery of any information respecting any details or conduct of the Corporation's business which, in the opinion of the Board, would not be in the best interests of the Shareholders or the Corporation to communicate to the public. The Board may from time to time determine whether and to what extent and at what time and place and under what conditions or regulations the accounts, records and documents of the Corporation or any of them shall be open to the inspection of Shareholders and no Shareholder shall have any right of inspecting any account, record or document of the Corporation except as conferred by the Act or authorized by the Board or by resolution passed at a general meeting of Shareholders,

**2.08 MECHANICAL REPRODUCTION OF SIGNATURES** - The signature of any officer of the Corporation may, if authorized by the Board, be printed, lithographed, engraved or otherwise mechanically reproduced upon all instruments executed or issued by the Corporation or any officer thereof; and any instrument on which the signature of any such person is so reproduced, shall subject to Section 2.04 hereof be deemed to have been manually signed by such person whose signature is so reproduced and shall be as valid to all intents and purposes as if such instrument had been signed manually, and notwithstanding that the person whose signature is so reproduced may have ceased to hold office at the date of the delivery or issue of such instrument. The term "instrument" as used in this Section shall include deeds, mortgages, hypothecs, charges, conveyances, transfers and assignments of property, real or personal, agreements, releases, receipts and discharges for the payment of money or other obligations, certificates of the Corporation's shares, share warrants of the Corporation, bonds, debentures and other debt obligations of the Corporation, and all paper writings.

### SECTION THREE

#### BORROWING AND SECURITIES

**3.01 BORROWING POWER** - Without limiting the borrowing powers of the Corporation as set forth in the Act, the Board is authorized from time to time:

- (a) to borrow money upon the credit of the Corporation in such amounts and on such terms as may be deemed expedient by obtaining loans or advances or by way of overdraft or otherwise;
- (b) to issue, re-issue, sell or pledge bonds, debentures, notes or other evidence of indebtedness or guarantees of the Corporation, whether secured or unsecured for such sums and at such prices as may be deemed expedient;
- (c) subject to the Act, to issue guarantees on behalf of the Corporation to secure the performance of the obligations of any person; and
- (d) to charge, mortgage, hypothecate, pledge or otherwise create a security interest in all or any currently owned or subsequently acquired real or personal, movable or immovable, property and undertaking of the Corporation, including book debts, rights, powers and franchises for the purpose of securing any such bonds, debentures, notes or other evidences of indebtedness or guarantee or any other present or future indebtedness or liability of the Corporation.

Nothing in this section limits or restricts the borrowing of money by the Corporation on bills of exchange or promissory notes made, drawn, accepted or endorsed by or on behalf of the Corporation.

3.02 DELEGATION OF BORROWING POWER - The Board may from time to time delegate to such one or more of the Directors and Officers of the Corporation as may be designated by the Board all or any of the powers conferred on the Board by Section 3.01 to such extent and in such manner as the Board shall determine at the time of each such delegation.

3.03 EXECUTION OF DEBT OBLIGATION DOCUMENTS - If the Board so authorizes, or if any instrument under which any bonds, debentures or other debt obligations of the Corporation are issued so provides, any bonds, debentures and other debt obligations of the Corporation, instead of being manually signed by the Directors or Officers authorized in that behalf, may have the facsimile signatures of such Directors or Officers printed or otherwise mechanically reproduced thereon and in either case, shall be as valid as if signed manually, but no such bond, debenture or other debt obligation, shall be issued unless it is manually signed, countersigned or certified by or on behalf of a trust company or other transfer agent or registrar duly authorized by the Board or the instrument under which such bonds, debentures or other debt obligations are issued so to do. Notwithstanding that any persons whose facsimile signature is so used shall have ceased to hold the office that he is stated on such bond, debenture or other debt obligation to hold at the date of the actual issue thereof, the bond debenture or other debt obligation shall be valid and binding on the Corporation.

#### SECTION FOUR

##### DIRECTORS

4.01 NUMBER OF DIRECTORS AND QUORUM - Until changed in accordance with the Act, the Board shall consist of not fewer than three (3) and not more than twenty (20) Directors. Subject to Section 4.07 and subject also to the Articles and the Act, the quorum for the transaction of business at any meeting of the Board shall consist of a majority of the Directors or such lesser number of Directors as the Board may from time to time determine. A Director interested is to be counted in a quorum notwithstanding his interest.

4.02 QUALIFICATION - No person shall be qualified for election as a Director if he is less than Nineteen (19) years of age; if he is of unsound mind and has been so found by a Court in Canada or elsewhere; if he is not an individual; or if he has the status of a bankrupt. A Director need not be a Shareholder.

4.03 ELECTION AND TERM - Each Director named in the Notice of Directors filed at the time of continuance shall hold office from the date of the Certificate of Continuance until the expiration of the term of office applicable to that Director at the date of the Certificate of Continuance. At each annual general meeting of the Corporation, the Corporation shall elect directors to the Board as may be required to fill any positions vacated by reason of the expiration of the term of office of one or more of the Directors. A Director may be elected for a term of office of one or more years of office as may be specified in the resolution by which he is elected. In this part, "year or office" means the period of time commencing on the date of an annual general meeting of the Corporation and ending on the date of the annual general meeting held in the next subsequent calendar year. If in any calendar year the Corporation does not hold an annual general meeting, the Directors whose terms of office would have expired in such calendar year shall be deemed to have been elected as Directors on the last date on which the annual general meeting could have been held in such calendar year pursuant to the Act and each Director so deemed elected may hold office until the next annual general meeting is held and other Directors are elected. The shareholders may, by special resolution, vary the term of office of any Director. The number of Directors to be elected at any such meeting shall be the number of Directors in office prior to the meeting unless the Directors or the Shareholders otherwise determine. The election shall be by ordinary resolution of the Shareholders. If an election of Directors is not held at the proper time, the incumbent Directors shall continue in office until their successors are elected.

4.04 REMOVAL OF DIRECTORS - Subject to the provisions of the Act, the Shareholders may by ordinary resolution passed at a special meeting remove any Director from office and the vacancy created by such removal may be filled at the same meeting failing which it may be filled by the Directors.

4.05 VACATION OF OFFICE - A Director ceases to hold office when: he dies; he is removed from office by the Shareholders; he ceases to be qualified for election as a Director, or his written resignation is sent or delivered to the Corporation, or if a time is specified in such resignation, at the time so specified, whichever is later.

#### 4.06 VACANCIES

(a) Subject to the Act and the Articles, a quorum of the Board may fill a vacancy in the Board, except a vacancy resulting from an increase in the minimum number of Directors or from a failure of the Shareholders to elect the minimum number of Directors. In the absence of a quorum of the Board, or if the vacancy has arisen from a failure of the Shareholders to elect the minimum number of Directors, the Board shall forthwith call a special meeting of the Shareholders to fill the vacancy. If the Board fails to call such meeting or if there are no such Directors then in office, any Shareholder may call the meeting; and

(b) The Directors of the Corporation may, between annual general meetings of the Corporation, appoint one or more additional Directors to serve until the next annual general meeting but the number of additional Directors shall not at any time exceed one

third of the number of Directors who held office at the expiration of the last annual general meeting, and in no event shall the total number of Directors exceed the maximum number of Directors fixed pursuant to paragraph 4 of the Articles of Continuance. Any Director so appointed shall hold office only until the next following annual general meeting of the Corporation but shall be eligible for election at such meeting and, so long as he is an additional Director prior to such meeting, the number of Directors for election at such meeting shall be increased accordingly.

4.07 ACTION BY THE BOARD - The Board shall manage the business and affairs of the Corporation. The powers of the Board may be exercised by resolution passed at a meeting at which a quorum is present or by resolution in writing, whether by document, telegram, teletype or any method of transmitting legibly recorded messages or other means, signed by all the Directors entitled to vote on that resolution at a meeting of the Board and any resolution in writing so signed shall be as valid as if it had been passed at a meeting of Directors or a Committee of Directors and shall be held to relate to any date therein stated to be the effective date thereof, and a copy of every such resolution in writing shall be kept with the minutes of the proceedings of Directors or Committee of Directors. Where there is a vacancy in the Board, the remaining Directors may exercise all the powers of the Board so long as a quorum remains in office. Where the Corporation has only one Director, that Director may constitute a meeting. An act of a Director is valid notwithstanding any irregularity in his election or appointment or a defect in his qualifications.

4.08 MEETINGS BY TELEPHONE -If all of the Directors consent, a Director may participate in a meeting of the Board or of a Committee of Directors by means of telephone or such other communications facilities as permit all persons participating in the meeting to hear each other, and a Director participating in such a meeting by such means is deemed to be present at the meeting. Any such consent shall be effective whether given before or after the meeting to which it relates and may be given with respect to all meetings of the Board and of Committees of Directors held while a Director holds office.

4.09 PLACE OF MEETING -Meetings of the Board may be held at any place in or outside Canada.

4.10 CALLING OF MEETINGS -Meetings of the Board shall be held from time to time and at such place as the Board may determine. In addition, each of the Chairman of the Board, the Managing Directors, the President or any two Directors may convene or direct the convening of a meeting of the Board.

4.11 NOTICE OF MEETING -Except as otherwise provided in Section 4.12, notice of the time and place of each meeting of the Board shall be given in the manner provided in Section 12.01 to each Director not less than forty-eight (48) hours

before the time when he meeting is to be held. A notice of a meeting of Directors need not specify the purpose of or the business to be transacted at the meeting except where Section 115(3) of the Act requires such purpose or business to be specified, including any proposal to:

- (a) submit to the Shareholders any question or matter requiring approval of the Shareholders;
- (b) fill a vacancy among the Directors or in the office of auditor,
- (c) issue securities;
- (d) declare dividends;
- (e) purchase, redeem, or otherwise acquire shares of the Corporation;
- (f) pay a commission for the sale of shares;
- (g) approve a management proxy circular;
- (h) approve any annual financial statements; or
- (i) adopt, amend or repeal By-Laws.

A Director may in any manner waive notice of or otherwise consent to a meeting of the Board either before or after the convening of the meeting.

4.12 REGULAR MEETINGS - The Board may by resolution appoint a day or days in any month or months for regular meetings of the Board at a place and hour to be named in the resolution. No notice shall be required for any such regular meeting.

4.13 FIRST MEETING OF NEW BOARD - Provided a quorum of Directors is present, each newly elected Board may without notice hold its first meeting immediately following the meeting of Shareholders at which such Board or portion thereof is elected.

4.14 ADJOURNED MEETING - Notice of an adjourned meeting of the Board is not required if the time and place of the adjourned meeting is announced at the original meeting.

4.15 CHAIRMAN - The Chairman of any meeting of the Board shall be the first mentioned of such of the following Officers as have been appointed and who is a Director and is present at the meeting: Chairman of the Board, Managing Director, President, or a Vice-President who is a Director. If no such Officer is present, the Directors present shall choose one of their number to be Chairman.

4.16 VOTES TO GOVERN - At all meetings of the Board every question shall be decided by a majority of the votes cast on the question. In cases of an equality of votes the Chairman of the meeting shall not be entitled to a second or casting vote.

4.17 CONFLICT OF INTEREST - A Director or Officer who is a party to, or who is a Director or Officer of or has a material interest in any person who is a party to, a material contract or proposed material contract with the Corporation shall disclose the nature and extent of his interest at the time and in the manner provided by the Act. Any such contract or proposed

contract shall be referred to the Board or Shareholders for approval even if such contract is one that in the ordinary course of the Corporation's business would not require approval by the Board or Shareholders, and a Director interested in a contract so referred to the Board shall not vote on any resolution to approve the same except as provided by the Act.

4.18 REMUNERATION AND EXPENSES - The Directors shall be paid such remuneration for their services as the Board may from time to time determine. The Directors shall also be entitled to be reimbursed for travelling and other expenses properly incurred by them in attending meetings of the Board or any committee

thereof. Nothing herein contained shall preclude any Director from serving the Corporation in any other capacity and receiving remuneration therefore.

4.19 ALTERNATE DIRECTOR - Any director (herein called the "Appointor") may from time to time by written notice to the Corporation appoint any person (herein called the "Appointee") to be his alternate director provided that the directors approve of such appointment by resolution. Such approval shall not be required if a director is appointed alternate director for another director. A person (including a director) may be appointed as an alternate director by more than one director.

- (a) The Appointee while he holds office as an alternate director shall be entitled and authorized:
  - (i) if expressly so specified by the Appointor in the instrument appointing the Appointee, to receive notice of meetings of the directors, and notice of meetings of all committees of which the Appointor is a member;
  - (ii) to attend and vote as a director at meetings of the directors in the absence of the Appointor;
  - (iii) to attend and vote at meetings of all committees of which the Appointor is a member, in the absence of the Appointor,
  - (iv) execute consents to resolutions in writing of the directors and such committees, in substitution for the Appointor; and
  - (v) if expressly so authorized by the Appointor in the instrument appointing the Appointee, to execute all documents, instruments and writings under the sea[ of the Corporation or otherwise which the Appointor is authorized to execute on behalf of the Corporation, in substitution for the Appointor,

and for the purposes thereof the Appointee shall be deemed to be a director. He shall not be deemed to be the agent of the Appointor.

- (b) The Appointee shall have a separate vote on behalf of each director for whom he is an alternate director. If the Appointee is also a director, the Appointee shall be counted separately in determining the quorum of a meeting and shall have a separate vote on behalf of each director for whom he is an alternate director in addition to being so

counted and voting in his own right as a director.

- (c) The Appointee shall not be entitled to be remunerated as an alternate director otherwise than out of the remuneration of the Appointor.
- (d) No person shall act as an alternate director unless he qualifies under the Act to act as a director of the Corporation and has consented in writing to his appointment.
- (e) An Appointee's appointment as an alternate director shall terminate if:
  - (i) the Appointor gives written notice revoking the Appointee's appointment; or
  - (ii) the Appointee resigns; or
  - (iii) The Appointor ceases for any reason to be a director, or
  - (iv) the Appointee ceases to be qualified under the Act to act as a director, or
  - (v) the term of the Appointee's appointment, if any, expires.
- (f) Any Appointor may make or revoke an appointment of an Appointee by notice in writing delivered to, mailed to or transmitted by telegram, cable or telecopier to the registered office of the Corporation, delivery, postage or transmission charges prepaid.

SECTION FIVE

COMMITTEES

5.01 COMMITTEE OF DIRECTORS

- (a) The Board may appoint one or more Committees of Directors, however designated, and delegate to such committee any of the powers of the Board except those which, under the Act, a Committee of Directors has no authority to exercise.
- (b) The Directors may by resolution appoint an Executive Committee to consist of such member or members of their body as they think fit, which Committee shall have, and may exercise during the intervals between the meetings of the Board, all the powers vested in the Board except the power to fill vacancies in the Board, the power to change the membership of, or fill vacancies in, said Committee or any other committee of the Board and such other powers, if any, as may be specified in the resolution. The said Committee shall keep regular minutes of its transactions and shall cause them to be recorded in books kept for that purpose, and shall report the same to the Board of Directors at such times as the Board of Directors may from time to time require. The Board shall have the power at any time to revoke or override the authority given to or acts done by the Executive Committee except as to acts done before such revocation or overriding and to terminate

the appointment or change the membership of such Committee and to fill vacancies in it. The Executive Committee may make rules for the conduct of its business and may appoint such assistants as it may deem necessary. A majority of the members of said Committee shall constitute a quorum thereof.

- (c) The Directors may from time to time by resolution constitute, dissolve or reconstitute standing committees and other committees consisting of such persons as the Board may determine. Every committee constituted by the Board shall have the powers, authorities and discretions delegated to it by the Board (which shall not include the power to fill vacancies in the Board and the power to change the membership of or fill vacancies in any committee constituted by the Board or the power to appoint or remove officers appointed by the Board) and shall conform to the regulations which may from time to time be imposed upon it by the Board.
- (d) The Executive Committee and any other committee may meet and adjourn as it thinks proper. Questions arising at any meeting shall be determined by a majority of votes of the members of the committee present, and in case of an equality of votes the chairman shall not have a second or casting vote. A resolution approved in writing by all the members of the Executive Committee or any other committee shall be as valid and effective as if it had been passed at a meeting of such Committee duly called and constituted. Such resolution may be in two or more counterparts which together shall be deemed to constitute one resolution in writing. Such resolution shall be filed with the minutes of the proceedings of the committee and shall be effective on the date stated thereon or on the latest date stated in any counterpart.

5.02 TRANSACTION OF BUSINESS - Subject to the provisions of Section 5.01, the powers of a Committee of Directors may be exercised by a meeting at which a quorum is present or by resolution in writing signed by all the members of such committee who would have been entitled to vote on that resolution at a meeting of the committee. Meetings of such committee may be held at any place in or outside Canada.

5.03 AUDIT COMMITTEE - When required by the Act the Board shall, and at any other time the Board may, elect annually from among its number an audit committee to be composed of not fewer than three (3) directors of whom a majority shall not be Officers or employees of the Corporation or its affiliates. The audit committee shall have the powers and duties provided in the Act.

5.04 PROCEDURE - Unless otherwise determined by the Board, each Committee of Directors shall have the power to fix its quorum at not less than a majority of its members, to elect its Chairman and to regulate its procedure.

## SECTION SIX

### OFFICERS

6.01 APPOINTMENT - The Board may from time to time appoint a President, one or more Vice-Presidents (to which title may be added words indicating seniority or function), a Secretary; a Treasurer and such other Officers as the Board may determine, including one or more assistants to any of the Officers so appointed (herein referred to as "Officers"). The Board may specify the duties of and, in accordance with this By-Law and subject to the provisions of the Act, delegate to such Officers powers to manage the business and affairs of the Corporation. Subject to Sections 6.02 and 6.03, an Officer may but need not be a Director and one person may hold more than one office.

6.02 CHAIRMAN OF THE BOARD - The Board may from time to time also appoint a Chairman of the Board who shall be a Director. The Chairman of the Board shall, when present, preside at all meetings of the Board, Committees of Directors and at all meetings of Shareholders. In addition, the Board may assign to him any of the powers and duties that may by the provisions of this by-law be assigned to the Managing Director or to the President; and he shall have such other powers and duties as the board may specify.

6.03 MANAGING DIRECTOR - The Board may from time to time appoint a Managing Director who shall be a Director. If appointed, he shall be the Chief Executive Officer and, subject to the authority of the Board, shall have general supervision of the business and affairs of the Corporation; and he shall, subject to the provisions of the Act, have such other powers and duties as the Board may specify. During the absence or disability of the President, or if no President has been appointed, the Managing Director shall also have the powers and duties of the President's office.

6.04 PRESIDENT - The Board, from time to time, may elect from among its number, a President. The President, in the absence or non-appointment of the Chairman of the Board, shall preside at meetings of the Board and at all meetings of the Shareholders. He shall have general and active management of the business and affairs of the Corporation, and without limitation to the foregoing:

- (i) he shall have general supervision and direction of all the other officers of the Corporation;
- (ii) he shall submit the annual report of the Board, if any, and the annual balance sheets and financial statements of the business and affairs and reports on the financial position of the Corporation as required by the statutes to the annual general meeting and from time to time shall report to the Board on all matters within his knowledge which the interest of the Corporation requires to be brought to their attention.
- (iii) he shall be ex-officio a member of all standing committees.

6.05 VICE-PRESIDENT - A Vice-President shall have such powers and duties as the Board may specify.

6.06 SECRETARY - The Secretary shall attend and be the Secretary of all meetings of the Board, Shareholders and Committees of the Board and shall enter or cause to be entered in records kept for that purpose minutes of all proceedings thereat; he shall give or cause to be given, as and when instructed, all notices to Shareholders, Directors, Officers, the auditor and members of the Committees of Directors; he shall be the custodian of the stamp or mechanical device generally used for affixing the corporate seal of the Corporation and of all books, papers, records, documents and instruments belonging to the Corporation, except when some other Officer or agent has been appointed for that purpose; and he shall have such other powers and duties as the Board may specify.

6.07 TREASURER - The Treasurer shall keep proper accounting records in

compliance with the Act and shall be responsible for the deposit of money, the safekeeping of securities and the disbursement of the funds of the Corporation; he shall render to the Board whenever required an account of all his transactions as Treasurer and of the financial position of the Corporation; and he shall have such other powers and duties as the Board may specify.

6.08 POWERS AND DUTIES OF OTHER OFFICERS - The powers and duties of all other Officers shall be such as the terms of their engagement call for or as the Board or the Chief Executive Officer may specify. Any of the powers and duties of an Officer to whom an assistant has been appointed may be exercised and performed by such assistant, unless the Board otherwise directs.

6.09 VARIATION OF POWERS AND DUTIES - The Board may from time to time and subject to the provisions of the Act, vary, add to or limit the powers and duties of any Officer.

6.10 TERM OF OFFICE - The Board, in its discretion, may remove any Officer of the Corporation, without prejudice to such Officer's rights under any employment contract, otherwise each Officer appointed by the Board shall hold office until the earlier of the date his resignation becomes effective, the date his successor is appointed or he shall cease to be qualified for that office.

6.11 TERMS OF EMPLOYMENT AND REMUNERATION - The terms of employment and the remuneration of Officers appointed by the Board shall be settled by it from time to time.

6.12 CONFLICT OF INTEREST - An Officer shall disclose his interest in any material contract or proposed material contract with the Corporation in accordance with Section 4.17.

6.13 AGENTS AND ATTORNEYS - The Board shall have power from time to time to appoint agents or attorneys for the Corporation in or outside of Canada with such powers of management or otherwise (including the power to sub-delegate) as may be thought fit.

6.14 FIDELITY BONDS - The Board may require such Officers, employees and agents of the Corporation as the Board deems advisable to furnish bonds for the faithful discharge of their powers and duties, in such form and with such surety as the Board may from time to time determine.

## SECTION SEVEN

### PROTECTION OF DIRECTORS, OFFICERS AND OTHERS

7.01 LIMITATION OF LIABILITY - No Director shall be liable for the acts, receipts, neglects or defaults of any other Director or Officer or employee, or for joining in any receipt or other act for conformity, or for any loss, damage or expense happening to the Corporation through the insufficiency or deficiency of title to any property acquired for or on behalf of the Corporation, or for the insufficiency or deficiency of any security in or upon which any of the moneys of the Corporation shall be invested, or for any loss or damage arising from the bankruptcy, insolvency or tortious acts of any person with whom any of the moneys, securities or effects of the Corporation shall be deposited, or for any loss occasioned by any error of judgement or oversight on his part, or for any other loss, damage or misfortune whatever which shall happen in the execution of the duties of his office or in relation thereto, unless the same are occasioned by his own wilful neglect or default; provided that nothing herein shall relieve any Director or Officer from the duty to act in accordance with the Act and the regulations thereunder or from liability for any breach thereof.

7.02 INDEMNITY - Subject to the limitations contained in the Act, and to the extent he is otherwise fairly and reasonably entitled thereto, the Corporation shall indemnify a Director or Officer, a former Director or Officer, or a person who acts or acted at the Corporation's request as a Director or Officer of a body corporate of which the Corporation is or was a Shareholder or creditor (or a person who undertakes or has undertaken any liability on behalf of the Corporation or any such body corporate) and his heirs and legal representatives, against all costs, charges and expenses, including an amount paid to settle an action or satisfy a judgement, reasonably incurred by him in respect of any civil, criminal or administrative action or proceeding to which he is made a

party by reason of being or having been a Director or Officer of the Corporation or such body corporate, if

- (a) he acted honestly and in good faith with a view to the best interests of the Corporation; and
- (b) in the case of a criminal or administrative action or proceeding that is enforced by a monetary penalty, he had reasonable grounds for believing that his conduct was lawful.

7.03 INSURANCE - Subject to the limitations contained in the Act, the Corporation may purchase and maintain such insurance for the benefit of its Directors and Officers as the Board may from time to time determine.

7.04 DIRECTORS MAY RELY - Directors may rely upon the accuracy of any statement of fact represented by an Officer of the Corporation to be correct or upon statements in a written report of the auditor of the Corporation and shall not be responsible or held liable for any loss or damage resulting from the paying of any dividends or otherwise acting in good faith upon any such statement.

## SECTION EIGHT

### SHARES

8.01 ALLOTMENT AND ISSUE - The Board may from time to time allot, or grant options to purchase the whole or any part of the authorized and unissued shares of the Corporation at such times and to such persons and for such consideration as the Board shall determine, provided that no share shall be issued until it is fully paid as prescribed by the Act. Subject to the Articles, no holder of any class of share of the capital of the Corporation shall be entitled as of right to subscribe for, purchase or receive any part of any new or additional issue of shares of any class, whether now or hereafter authorized or any bonds, debentures or other securities convertible into shares of any class.

8.02 COMMISSIONS - The Board may from time to time authorize the Corporation to pay a reasonable commission to any person in consideration of his purchasing or agreeing to purchase shares of the Corporation, whether from the Corporation or from any other person, or procuring or agreeing to procure purchasers for any such shares.

### 8.03 REGISTRATION OF TRANSFER

- (a) Subject to the provisions of the Act, no transfer of shares shall be registered in a securities register except upon presentation of the Certificate representing such shares with a transfer endorsed thereon or delivered therewith duly executed by the registered holder or by his attorney or successor duly appointed, together with such reasonable assurance or evidence of signature, identification and authority to transfer as the Board may from time to time prescribe, upon payment of all applicable taxes and any fees prescribed by the Board, upon compliance with such restrictions on transfer, if any, as are authorized by the Articles, and upon satisfaction of any lien referred to in Section 8.05.
- (b) The signature of the registered owner of any shares, or of his duly authorized attorney, upon an authorized instrument of transfer shall constitute a complete and sufficient authority to the Corporation, its Directors, Officers and agents to register, in the name of the transferee as named in the instrument of transfer, the number of shares specified therein or, if no number is specified, all the shares of the registered owner represented by share certificates deposited with the instrument of transfer. If no transferee is named in the instrument of transfer, the instrument of transfer shall constitute a complete and sufficient authority to the corporation, its Directors, Officers and agents to register, in the name of the person in whose behalf any certificate for the shares to be transferred is deposited with the Corporation for the purpose of having the transfer registered, the number of shares specified in the instrument of transfer or, if no number is specified, all the shares represented by all share certificates deposited with the instrument of transfer.

(c) Neither the Corporation nor any Director, Officer or agent thereof shall be bound to inquire into the title of the person named in the form of transfer as transferee, or, if no person is named therein as transferee, of the person on whose behalf the certificate is

deposited with the Corporation for the purpose of having the transfer registered or be liable to any claim by such registered owner or by any intermediate owner or holder of the certificate or of any of the shares represented thereby or any interest therein for registering the transfer, and the transfer, when registered, shall confer upon the person in whose name the shares have been registered a valid title to such shares.

(d) Every instrument of transfer shall be executed by the transferor and left at the registered office of the Corporation or at the office of its transfer agent or branch transfer agent or registrar for registration together with the share certificate for the shares to be transferred and such other evidence if any, as the Directors or the transfer agent or branch transfer agent or registrar or branch registrar may require to prove the title of the transferor or his right to transfer the shares and the right of the transferee to have the transfer registered. All instruments of transfer where the transfer is registered shall be retained by the Corporation or its transfer agent or branch transfer agent or registrar or branch registrar and any instrument of transfer, where the transfer is not registered, shall be returned to the person depositing the same together with the share certificate which accompanied the same when tendered for registration.

(e) There shall be paid to the Corporation in respect of the registration of any transfer such sum, if any, as the Directors may from time to time determine.

**8.04 TRANSFER AGENTS AND REGISTRARS** - The Board may from time to time appoint a registrar to maintain the securities register and a transfer agent to maintain the register of transfers and may also appoint one or more branch registrars to maintain branch securities registers and one or more branch transfer agents to maintain branch registers of transfer, but one person may be appointed both registrar and transfer agent. The Board may at any time terminate any such appointment.

**8.05 PURCHASE AND REDEMPTION OF SHARES** - Subject to the provisions of the Act and the Articles, a Corporation may purchase or otherwise acquire shares issued by it and may purchase or redeem any redeemable shares issued by it at prices not exceeding the redemption of those shares stated in the Articles or calculated according to a formula stated in the Articles.

**8.06 NON-RECOGNITION OF TRUSTS** - Subject to the provisions of the Act, the Corporation shall treat as absolute owner of the share the person in whose name the share is registered in the securities register as if that person had full legal capacity and authority to exercise all rights of ownership, irrespective of any indication to the contrary through knowledge or notice or description in the Corporation's records or on the share certificate.

**8.07 SHARE CERTIFICATES** - Every holder of one or more shares of the Corporation shall be entitled, at his option, to a share certificate, or to a non-transferable written acknowledgement of his right to obtain a share certificate, stating the number and list or series of shares held by him as shown on the securities register. Share Certificates and acknowledgements of a Shareholder's right to a share certificate, respectively, shall be in such form as the Board shall from time to time approve. Any share certificate shall be signed in accordance with Section 2.04 and need not

be under the corporate seal; provided that, unless the Board otherwise determines, certificates representing shares in respect of which a transfer agent and/or registrar has been appointed shall not be valid unless countersigned by or on behalf of such transfer agent and/or registrar. The signature of one of the signing Officers or, in the case of share certificates which are not valid unless countersigned by or on behalf of a transfer agent and/or registrar, the signature of one of the Officers, may be printed or

mechanically reproduced in facsimile upon share certificates and every such facsimile signature shall for all purposes be deemed to be the signature of the Officer whose signature it reproduces and shall be binding upon the Corporation. A share certificate executed as aforesaid shall be valid notwithstanding that one or both of the Officers whose facsimile signature appears thereon no longer holds office at the date of issue of the Certificate.

8.08 REPLACEMENT OF SHARE CERTIFICATES - The Board or any Officer or agent designated by the Board may in its or his discretion direct the issue of a new share certificate in lieu of and upon cancellation of a share certificate that has been mutilated or in substitution for a share certificate claimed to have been lost, destroyed or wrongfully taken or which does not comply as to form with the requirements from time to time of the Act in this regard, on payment of such fee as the Board may direct and on such terms as to indemnity; reimbursement of expenses and evidence of loss and of title as the Board may from time to time prescribe, whether generally or in any particular case.

8.09 JOINT SHAREHOLDERS - If two or more persons are registered as joint holders of any share, the Corporation shall not be bound to issue more than one certificate in respect thereof, and delivery of such certificate to one of such persons shall be sufficient delivery to all of them. Any one of such persons may give effectual receipts for the certificate issued in respect thereof or for any dividend, bonus, return of capital or other money payable or warrant issuable in respect of such share. Joint Shareholders may collectively designate in writing an address as their recorded address for service of notice and payment of dividends but in default of such designation the address of the first named joint Shareholder shall be deemed to be the recorded address aforesaid.

8.10 DECEASED SHAREHOLDERS - In the event of the death of a holder, or of one of the joint holders, of any share, the Corporation shall not be required to make any entry in the securities register in respect thereof or to make payment of any dividends thereon except upon production of all such documents as may be required by law and upon compliance with the reasonable requirements of the Corporation and its transfer agents.

## SECTION NINE

### DIVIDENDS AND RIGHTS

9.01 DIVIDENDS - Subject to the provisions of the Act, the Board may from time to time declare dividends payable to the Shareholders according to their respective rights and interest in the Corporation. Dividends may be paid in money or property or by issuing fully paid shares of the Corporation.

9.02 DIVIDEND CHEQUES - A dividend payable in cash shall be paid by cheque drawn on the

Corporation's bankers or one of them to the order of each registered holder of shares of the class or series in respect of which it has been declared and mailed by prepaid ordinary mail to such registered holder at his recorded address, unless such holder otherwise directs. In the case of joint holders the cheque shall, unless such joint holders otherwise direct, be made payable to the order of all of such joint holders and mailed to them at their recorded address. The mailing of such cheque as aforesaid, unless the same is not paid on due presentation, shall satisfy and discharge the liability for the dividend to the extent of the sum represented thereby plus the amount of any tax which the Corporation is required to and does withhold.

9.03 NON-RECEIPT OF CHEQUES - In the event of non-receipt of any dividend cheque by the person to whom it is sent as aforesaid, the Corporation shall issue to such person a replacement cheque for a like amount on such terms as to indemnity, reimbursement of expenses and evidence of non-receipt and of title as the Board may from time to time prescribe, whether generally or in any particular case.

9.04 RECORD DATE FOR DIVIDENDS AND RIGHTS - The Board may fix in advance a date, preceding by not more than Fifty (50) days the date for the payment of any dividend or the date for the issue of any warrant or other evidence of right to subscribe for securities of the Corporation, as a record date for the determination of the persons entitled to receive payment of such dividend or to exercise the right to subscribe for such securities, provided that, where the

Corporation is a distributing Corporation for purposes of the Act, notice of any such record date is given not less than seven (7) days before such record date by newspaper advertisement and otherwise in the manner provided in the Act. Where no record date is fixed in advance as aforesaid, the record date for the determination of the persons entitled to receive payment of any dividend or to exercise the right to subscribe for securities of the Corporation shall be at the close of business on the day on which the resolution relating to such dividend or right to subscribe is passed by the Board.

9.05 UNCLAIMED DIVIDENDS - Any dividend unclaimed after a period of six (6) years from the date on which the same has been declared to be payable shall be forfeited and shall revert to the Corporation.

## SECTION TEN

### MEETINGS OF SHAREHOLDERS

10.01 ANNUAL MEETINGS - The annual meeting of Shareholders shall be held at such time in each year and, subject to the Act, the Articles and to Section 10.04, at such place as the Board may from time to time determine, for the purpose of considering the financial statements and reports required by the Act to be placed before the annual meeting, electing Directors, appointing auditors and for the transaction of such other business as may properly be brought before the meeting.

10.02 SPECIAL MEETINGS - The Board shall have power to call a special meeting of Shareholders at any time.

10.03 SPECIAL BUSINESS - All business transacted at a special meeting of Shareholders and all business transacted at an annual meeting of Shareholders, except consideration of the financial statements, auditors reports, election of directors and reappointment of the incumbent auditors, is deemed to be special business.

10.04 PLACE OF MEETING - Subject to the Articles, meetings of Shareholders may be held in the Cities of Boston, in the State of Massachusetts, New York, in the State of New York, Vancouver in the Province of British Columbia or such other place or places as the Directors in their absolute discretion may determine from time to time.

10.05 NOTICE OF MEETING - Notice of the time and place of each meeting of Shareholders shall be given in the manner provided in Section 12.01 not less than twenty-one (21) nor more than fifty (50) days before the date of the meeting to each Director, to the auditor and to each Shareholder who at the close of business on the record date, if any, for notice is entered in the securities register as the holder of one or more shares carrying the right to vote at the meeting. Notice of a meeting of Shareholders called for any purpose other than consideration of the financial statements and auditor's report, election of Directors and re-appointment of the incumbent auditor shall state the nature of such business in sufficient detail to permit the Shareholder to form a reasoned judgement thereon and shall state the text of any special resolution to be submitted to the meeting. A Shareholder and any other person entitled to attend a meeting of Shareholders may in any manner waive notice of or otherwise consent to a meeting of Shareholders.

10.06 LIST OF SHAREHOLDERS ENTITLED TO NOTICE - For every meeting of Shareholders, at any time that the Corporation has more than fifteen (15) Shareholders entitled to vote at a meeting of Shareholders, the Corporation shall prepare a list of Shareholders entitled to receive notice of the meeting, arranged in alphabetical order and showing the number of shares entitled to vote at the meeting held by each Shareholder. If a record date for the meeting is fixed pursuant to Section 10.07, the Shareholders listed shall be those registered or constructively registered pursuant to the Act at the close of business of the record date, such list to be prepared on a day not later than ten (10) days after such record date. If no record date is fixed, the list of Shareholders shall be prepared no later than at the close of business on the day immediately preceding the day on which notice of the meeting is given, or where no such notice is given, the day on which the meeting is held. The list shall be available for examination by any Shareholder during usual business hours at the records office of the Corporation or at the place where the central securities register is kept and at the place where the meeting is held.

10.07 RECORD DATE FOR NOTICE - The Board may fix in advance a record date, preceding the date of any meeting of Shareholders by not more than fifty (50) days and not less than twenty-one (21) days for the determination of the Shareholders entitled to notice of the meeting, provided that notice of any such record date is given, not less than seven (7) days before such record date, by newspaper advertisement in the manner provided in the Act. If no record date is so fixed, the record date for the determination of the Shareholders entitled to notice of the meeting shall be the close of business on the day immediately preceding the day on which the notice is given, or if no

notice is given, the day on which the meeting is held.

10.08 MEETINGS WITHOUT NOTICE - A meeting of Shareholders may be held without notice at any time and place permitted by the Act:

- (a) if all the Shareholders entitled to vote thereat are present in person or represented by proxy or if those not present or represented by proxy waive notice of or otherwise consented to such meeting being held, and
- (b) if the auditor and the Directors are present or waived notice of or otherwise consent to such meeting being held.

At such meeting any business may be transacted which the Corporation at a meeting of Shareholders may transact. If the meeting is held at a place outside the Yukon Territory, Shareholders not present or represented by proxy, but who have waived notice of or otherwise consented to such meeting, shall also be deemed to have consented to the meeting being held at such place.

10.09 MEETINGS BY TELEPHONE - If all the Shareholders consent, a Shareholder may participate in a meeting of Shareholders by means of telephone or such other communications facilities as permit all persons participating in the meeting to hear each other, and a Shareholder participating in such a meeting by such consent shall be effective whether given before or after the meeting to which it relates.

10.10 CHAIRMAN, SECRETARY AND SCRUTINEERS - The Chairman of any meeting of Shareholders shall be the first mentioned of such of the following Officers as having been appointed and who is present at the meeting: Chairman of the Board, President, Managing Director, or a Vice-President. If no such Officer is present within fifteen (15) minutes from the time fixed for holding the meeting, the persons present and entitled to vote shall choose one of their number to be Chairman. If the Secretary of the Corporation is absent, the Chairman shall appoint some person, who need not be a Shareholder, to act as Secretary of the meeting. If desired, one or more scrutineers, who need not be Shareholders, may be appointed by a resolution or by the Chairman with the consent of the meeting.

10.11 PERSONS ENTITLED TO BE PRESENT - The only persons entitled to be present at a meeting of Shareholders shall be those entitled to vote thereat, the Directors and auditor of the Corporation and others who, although not entitled to vote, are entitled or required under any provision of the Act or the Articles or By-Laws to be present at the meeting. Any other person may be admitted only on the invitation of the Chairman of the meeting or with the consent of the meeting.

10.12 QUORUM - Save as herein otherwise provided, a quorum shall be two shareholders or proxyholders present, holding not less than ten percent (10%) of the outstanding shares of the Corporation entitled to vote at the meeting. If there is only one shareholder, the quorum is one person present and being, or representing by proxy, such shareholder. The Directors, the Secretary or, in his absence, an assistant Secretary, and the solicitor of the Corporation shall be

entitled to attend at any general meeting but no such person shall be counted in the quorum or be entitled to vote at any general meeting unless he is a shareholder or proxyholder entitled to vote thereat. If a quorum is present at the opening of any meeting of Shareholders, the Shareholders present or represented by proxy may proceed with the business of the meeting notwithstanding that a quorum is not present throughout the meeting. No business, other than the election of a Chairman of the meeting and the

adjournment of the meeting shall be transacted at any general meeting unless the quorum requisite was present at the commencement of the meeting. If within one-half hour from the time appointed for a meeting a quorum is not present, the meeting if convened by requisition of the Shareholders, shall be dissolved; but in any other case it shall stand adjourned to the same day in the next week at the same time and place. If at such adjourned meeting a quorum is not present within one-half hour from the time appointed, the Shareholders present in person or by proxy shall be a quorum.

10.13 RIGHT TO VOTE - RECORD DATE FOR VOTING - Subject to the provisions of the Act as to authorized representative of any other body corporate, at any meeting of Shareholders in respect of which the Corporation has prepared the list referred to in Section 10.06, every person who is named in such list shall be entitled to vote the shares shown thereon opposite his name except, where the Corporation has fixed a record date in respect of such meeting pursuant to Section 10.07, to the extent that such person has transferred any of his shares after such record date and the transferee, upon producing properly endorsed Certificates evidencing such shares or otherwise establishing that he owns such shares, demands not later than ten (10) days before the meeting that his name be included in such list, in which event the transferee alone shall be entitled to vote the transferred shares at the meeting. Where no record date for notice has been fixed and no notice of meeting given, or in the absence of a list prepared as aforesaid in respect of a meeting of Shareholders, every person shall be entitled to vote at the meeting who at the time is entered in the securities register as the holder of one or more shares carrying the right to vote at such meeting.

#### 10.14 PROXIES

(a) Every Shareholder entitled to vote at a meeting of Shareholders, may appoint a proxyholder, or one or more alternate proxyholders, who need not be Shareholders, to attend and act at the meeting in the manner and to the extent authorized and With the authority conferred by the proxy. A proxy shall be in writing executed by the Shareholder or his attorney and shall conform with the requirements of the Act. An instrument of proxy shall be valid only at the meeting in respect of which it is given or any adjournment thereof.

(b) Any corporation, other than a Prohibited Corporate Shareholder, which is a Shareholder of the Corporation may by resolution of its Directors or other governing body authorize such person as it thinks fit to act as its representative at any meeting. The person so authorized shall be entitled to exercise in respect of and at such meeting the same powers on behalf of the corporation which he represents as that corporation could exercise if it were an individual member of the Corporation personally present, including, without limitation, the right, unless restricted by such resolution, to appoint a proxyholder to

represent such corporation, and shall, If present at the meeting, be counted for the purpose of forming a quorum and be deemed to be a member present at the meeting. Evidence of the appointment of any such representative may be sent to the Corporation by written instrument, telegram, telex, facsimile or any method of transmitting legibly recorded messages.

(c) Every ballot case upon a poll and every proxy appointing a proxyholder who cast a ballot upon a poll shall be retained by the Secretary for the period and be subject to the inspection as the Act may provide.

10.15 TIME FOR DEPOSIT OF PROXIES - The Board may specify in a notice calling a meeting of Shareholders a time, preceding the time of such meeting by not more than forty-eight (48) hours exclusive of non-business days, before which time proxies to be used at such meeting must be deposited. A proxy shall be acted upon only if, prior to -the time so specified, it shall have been deposited by written instrument, telegram, telex, facsimile or any method of transmitting legibly recorded messages with the Corporation or an agent thereof specified in such notice or, if no such time is specified in such notice, unless it has been received by the Secretary of the Corporation or by the Chairman of the meeting or any adjournment thereof prior to the time of voting.

10.16 JOINT SHAREHOLDERS - If two or more persons hold shares jointly, any one

of them present in person or represented by proxy at a meeting of Shareholders may, in the absence of the other or others, vote the shares but if two or more of those persons are present in person or represented by proxy and vote, they shall vote as one on the shares jointly held by them and in the absence of agreement between those so voting the person named first in the Register shall vote the shares.

10.17 VOTES TO GOVERN - At any meeting of Shareholders every question shall, unless otherwise required by the Articles or By-Laws or by law, be determined by the majority of the votes cast on the question. In case of an equality of votes either upon a show of hands or upon a poll, the Chairman of the meeting shall be entitled to a second or casting vote in addition to vote or votes to which he may be entitled as a shareholder.

10.18 MOTION - No resolution proposed at a meeting need be seconded. The Chairman may propose or second a motion.

10.19 SHOW OF HANDS - Subject to the provisions of the Act any question at a meeting of Shareholders shall be decided by a show of hands unless a ballot thereon is required or demanded as hereinafter provided. Upon a show of hands, every person who is present and entitled to vote shall have one vote. Whenever a vote by show of hands shall have been taken upon a question, unless a ballot thereon is so required or demanded, a declaration by the Chairman of the meeting that the vote upon the question has been carded or carried by a particular majority or not carried, an entry to that effect in the minutes of the meeting shall be conclusive evidence of the fact without proof of the number or proportion of the votes recorded in favor of or against any resolution or other proceeding in respect of the said question, and the result of the vote so taken shall be the decision of the Shareholders upon the said question.

#### 10.20 BALLOTS

- (a) On any question proposed for consideration at a meeting of Shareholders, and whether or not a show of hands has been taken thereof, any Shareholder or proxyholder entitled to vote at the meeting may require or demand a ballot. A ballot so required or demanded shall be taken in such manner as the Chairman shall direct. A requirement or demand for a ballot may be withdrawn at any time prior to the taking of the ballot. If a ballot is taken each person present shall be entitled in respect of the shares which he is entitled to vote at the meeting upon the question, to that number of votes provided by the Act or the Articles, and the result of the ballot so taken shall be the decision of the Shareholders upon the said question.
- (b) No ballot may be demanded on the election of a Chairman. A ballot demanded on a question of adjournment shall be taken forthwith. A ballot demanded on any other question shall be taken as soon as, in the opinion of the chairman, is reasonably convenient, but in no event later than seven (7) days after the meeting and at such time and place and in such manner as the chairman of the meeting directs. The result of the ballot shall be deemed to be the resolution of and passed at the meeting at which the ballot was demanded. Any business other than that upon which the ballot has been demanded may be proceeded with pending the taking of the ballot. In any dispute as to the admission or rejection of a vote the decision of the chairman made in good faith shall be final and conclusive.

10.21 ADJOURNMENT - If a meeting of Shareholders is adjourned for less than thirty (30) days, it shall not be necessary to give notice of the adjourned meeting, other than by announcement at the earliest meeting that it is adjourned. If a meeting of Shareholders is adjourned by one or more adjournments for an aggregate of thirty (30) days or more, notice of the adjourned meeting shall be given as for an original meeting. At any such adjourned meeting no business shall be transacted other than business left unfinished at the meeting from which the adjournment took place.

10.22 RESOLUTION IN WRITING - A resolution in writing signed by all the Shareholders entitled to vote on that resolution at a meeting of Shareholders is as valid as if it had been passed at a meeting of the Shareholders, and shall be held to relate to any date therein stated to be the effective date thereof.

10.23 ONLY ONE SHAREHOLDER - Where the Corporation has only one Shareholder or only one holder of any class or series of shares, the Shareholder present in person or by proxy constitutes a meeting.

10.24 ONLY TWO SHAREHOLDERS - Where the Corporation has only two Shareholders a quorum for transaction of business at any meeting of Shareholders shall be one (1) person present in person, being a Shareholder entitled to vote thereat, or a duly appointed proxy of said Shareholder, holding not less than ten percent (10%) of the outstanding shares of the Corporation entitled to vote at the meeting.

## SECTION ELEVEN

### DIVISIONS AND DEPARTMENTS

11.01 CREATION AND CONSOLIDATION OF DIVISIONS - The Board may cause the business and operations of the Corporation or any part thereof to be divided or to be segregated into one or more divisions upon such basis, including without limitation, character or type of operation, geographical territory, product manufactured or service rendered, as the Board may consider appropriate in each case. The Board may also cause the business and operations of any such division to be further divided into sub-units and the business and operations of any such divisions or sub-units to be consolidated upon such basis as the Board may consider appropriate in each case.

11.02 NAME OF DIVISION - Subject to the Act any division or its sub-units may be designated by such name as the Board may from time to time determine and may transact business, enter into contracts, sign cheques and other documents of any kind and do all acts and things under such name, provided that the Corporation shall set out its name in legible characters in all contracts, invoices, negotiable instruments and orders for goods or services issued or made by or on behalf of the Corporation. Any such contract, cheque or documents shall be binding upon the Corporation as if it had been entered into or signed in the name of the Corporation.

11.03 OFFICERS OF DIVISION - From time to time the Board or if authorized by the Board, the Chief Executive Officer, may appoint one or more Officers for any division, prescribe their powers and duties and settle their terms of employment and remuneration. The Board or, if authorized by the Board, the Chief Executive Officer, may remove at its or his pleasure any Officers so appointed, without prejudice to such Officer's right under any employment contract. Officers of divisions or their sub-units shall not, as such, be Officers of the Corporation.

## SECTION TWELVE

### NOTICES

12.01 METHOD OF GIVING NOTICES - Any notice (which term includes any communication or document) to be given (which term includes sent, delivered or served) pursuant to the Act, the regulations thereunder, the Articles, the By-Laws or otherwise to a Shareholder, Director, Officer, auditor or member of a Committee of Directors shall be sufficiently given if delivered personally to the person to whom it is to be given or if delivered to his recorded address by any means of prepaid transmitted or recorded communication. A notice so delivered shall be deemed to have been given when it is delivered personally or to the recorded address as aforesaid; a notice so mailed shall be deemed to have been received by him on the business day following the day the notice is posted; and a notice so sent by any means of transmitted or recorded communication shall be deemed to have been given when dispatched or delivered to the appropriate communication corporation or agency or its representative for dispatch. Subject to the Act, a notice of meeting of Shareholders shall be deemed to have been sent to the

Shareholder on the business day following the day on which it is deposited in the mail. The Secretary may change or cause to be changed the recorded address of any Shareholder, Director, Officer, auditor or member of a Committee of Directors in accordance with any information believed by him to be reliable.

12.02 NOTICE TO JOINT SHAREHOLDERS - if two or more persons are registered as

joint holders of any share, any notice shall be addressed to all of such joint holders but notice given to any one or more of such persons at the recorded address for such joint shareholders shall be sufficient notice to all of them.

12.03 COMPUTATION OF TIME - In computing the date when notice must be given under any provision requiring a specified number of days notice of any meeting or other event, the date of giving the notice shall be excluded and the date of the meeting or other event in respect of which the notice is being given shall be included.

12.04 UNDELIVERED NOTICES - any notice given to a Shareholder pursuant to Section 12.01 is returned on three (3) consecutive occasions because he cannot be found or served or is unknown at his recorded address, the Corporation shall not be required to give any further notices to such Shareholder until he informs the Corporation in writing of his new recorded address.

12.05 PROOF OF SERVICE - A certificate of the Secretary or other duly authorized Officer of the Corporation in office at the time of the making of the certificate, or of any agent of the Corporation as to the facts in relation to the mailing or delivery or sending of any notice to any Shareholder, Director, the auditors, or conclusive evidence thereof and shall be binding on every Shareholder, Director, the auditors or any Officer of the Corporation as the case may be.

12.06 OMISSIONS AND ERRORS - The accidental omission to give any notice to any Shareholder, Director, Officer, auditor or member of a Committee of Directors or the non-receipt of any notice by any such person or any error in any notice not affecting the substance thereof shall not invalidate any action taken at any meeting held pursuant to such notice or otherwise founded thereon.

12.07 PERSONS ENTITLED BY DEATH OR OPERATION OF LAW - Every person who by operation of law, transfer, death of a Shareholder or any other means whatsoever, shall become entitled to any share, shall be bound by every notice in respect of such share which shall have been duly given to the Shareholder from whom he derives his title prior to such person's name and address being entered on the securities register (whether such notice was given before or after the happening of the event upon which he became so entitled) and prior to his furnishing to the Corporation the proof of authority or evidence of his entitlement prescribed by the Act.

12.08 WAIVER OF NOTICE -Any Shareholder (or his duly appointed proxyholder), Director, Officer, auditor or member of a Committee of Directors may at any time waive the sending of any notice, or waive or abridge the time for any notice, required to be given to him under any provision of the Act, the regulations thereunder, the Articles, the By-Laws or otherwise and such waiver or abridgement shall cure any default in the giving or the time of such notice, as the case

may be. Any such waiver or abridgement shall be in writing except a waiver of notice of a meeting of Shareholders or of the Board which may be given in any manner.

PLC SYSTEMS INC.

SUBSIDIARIES OF REGISTRANT

- 1.) *PLC Medical Systems, Inc., a Delaware Corporation*
- 2.) *PLC Sistemas Medicos Internacionais GmbH, a German Corporation*
- 3.) *PLC Medical Systems AG, a Swiss Corporation*
- 4.) *PLC Medical Systems Asia/Pacific Pte Ltd, a Singapore Corporation*
- 5.) *PLC Medical Systems Australia Pty Ltd, an Australian Corporation*

CONSENT OF INDEPENDENT AUDITORS

We consent to the incorporation by reference in this Annual Report (Form 10-K) of PLC Systems Inc. of our report dated February 18, 2000, except for Note 12, as to which date is March 28, 2000, included in the 1999 Annual Report to Shareholders of PLC Systems Inc.

Our audits also included the financial statement schedule of PLC Systems Inc. listed in Item 14(a). This schedule is the responsibility of the Company's management. Our responsibility is to express an opinion on this schedule based on our audits. In our opinion, the financial statement schedule referred to above, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

We consent to the incorporation by reference in the Registration Statements (Form S-3 Nos. 33-98744, 333-34315, 333-53649, 333-68923 and 333-80045 and Form S-8 Nos. 33-95168 and 333-51547) of PLC Systems Inc. of our report dated February 18, 2000, except for Note 12, as to which date is March 28, 2000 with respect to the consolidated financial statements and schedule of PLC Systems Inc. included in this Annual Report (Form 10-K) for the year ended December 31, 1999.

/s/ Ernst & Young LLP

Ernst & Young LLP

Boston, Massachusetts  
March 28, 2000

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THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM CONDENSED BALANCED SHEET AND CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.

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