

SECURITIES AND EXCHANGE COMMISSION

FORM 10-K

Annual report pursuant to section 13 and 15(d)

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FILER

**AVT CORP**

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SIC: **7372** Prepackaged software

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SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

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FORM 10-K  
For annual and transition reports  
pursuant to sections 13 or 15(d) of the  
Securities Exchange Act of 1934.

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE  
ACT OF 1934

For the fiscal year ended: December 31, 1998

OR

TRANSACTION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 0-25186

AVT Corporation  
(Exact name of registrant as specified in its charter)

Washington 91-1190085  
(State or other jurisdiction of (IRS employer  
incorporation or organization) identification no.)

11410 N.E. 122nd Way 98034  
Kirkland, WA. (Zip code)  
(Address of principal executive offices)

Registrant's telephone number, including area code: (425) 820-6000

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, \$.01 par value per share  
-----  
(Title of class)

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 preceeding 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 \_\_\_\_

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. [ ]

Aggregate market value of voting stock held by non-affiliates of the registrant as of March 5, 1999 was \$320,322,612 (based upon the closing sale price of \$27.50 per share on the Nasdaq National Market on such date).

Number of shares of Common Stock outstanding as of March 5, 1999 was 13,092,674.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's Proxy Statement for the 1999 Annual Meeting of Shareholders to be held May 11, 1999 are incorporated by reference in response to Part III, Items 10-13 (Directors and Executive Officers of the Registrant)

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PART 1

Item 1. BUSINESS

The Company is a leading provider of software-based computer-telephony solutions for medium-sized enterprises. The Company provides flexible, cost-effective products that address the voice messaging, call center, fax server and production fax markets, and distributes these products primarily through independent distributors and value-added resellers. The Company's products run on off-the-shelf hardware, support Windows NT and OS/2, and interface with a wide variety of telephony and computer equipment.

Industry Background

Businesses are increasingly using information technology to improve customer service, increase employee productivity, decrease costs and more efficiently disseminate information. As the amount of information exchanged between organizations increases, and the diversity of the delivery formats and combinations used by organizations to exchange this information becomes more complex, there is a growing need for organizations to find new ways to manage information in a more timely and cost-effective manner.

In response to the growth in voice communications, organizations are increasingly using voice messaging, call centers with automated intelligent routing and IVR (interactive voice response) systems that provide voice-prompted access to data. These computer-telephony solutions allow employees to more effectively manage communications, significantly improve call center efficiency, and allow easy access by telephone to large amounts of information that resides on computer databases.

The growth in data communications presents additional opportunities for accessing and sending information. For example, organizations are deploying LAN-based fax servers to store, forward and broadcast their growing volume of facsimile traffic in an efficient manner. Electronic messaging over LANs, the Internet and corporate intranets has emerged as another way to access data and disseminate information. This rapid increase in multiple forms of voice and data communication has further accentuated the need for organizations to optimize their information management capabilities and integrate voice and data communications.

Large corporations have been the first to implement systems that provide enhanced voice and data integration. These large systems typically have been based on proprietary hardware and software and are not cost-effective for medium-sized organizations or smaller offices of large organizations. However, to remain competitive these medium-sized entities require systems with the same functionality to provide a comparable level of interaction with customers and

vendors and to reduce operating costs. These organizations do not typically have the resources or the number of users required to purchase, customize and maintain proprietary solutions. Rather, they require cost-effective computer-telephony solutions that provide open standards-based interfaces to a broad range of voice and data equipment, flexibility to add new functionality and scaleable capacity to add new users, and that operate on readily available hardware.

#### The AVT Solution

The Company is a leading provider of software-based computer-telephony solutions for medium-sized enterprises. These solutions are designed to enhance individual and work group productivity, improve customer service, reduce business operating costs and simplify information access and dissemination. The Company's products provide enhanced voice and data integration through applications such as unified voice and data messaging, call center management, IVR and document distribution. The Company's products run on off-the-shelf server hardware, support Windows NT and OS/2, and interface with a wide variety of telephony and computer equipment.

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#### Strategy

The Company's mission is to provide cost-effective, innovative computer-telephony software products that operate on industry-standard computer platforms, and market those products throughout the world. Key components of the Company's strategy include:

**Provide Complete Software-based Computer-telephony Solutions.** The Company is focused on providing a comprehensive and affordable set of software-based computer-telephony solutions designed to enhance productivity, improve customer service, reduce business operating costs and simplify access to data and dissemination of information. The Company's products provide enhanced voice and data integration through applications such as unified voice and data messaging, call center management, IVR and document distribution.

**Focus on Medium-sized Enterprise Market.** The Company currently targets enterprises with 100 to 2,000 employees, including divisions and subsidiaries of Fortune 1000 companies. The Company's strategy is to continue to invest in new product development and marketing initiatives to gain market share and further meet the computer-telephony needs of medium-sized enterprises.

**Leverage Telephony and Data Expertise.** The Company has established a knowledge base in the development of call processing, voice processing and call switching applications, as well as LAN, Internet and corporate intranet software applications. The Company believes that its expertise in these areas enables it to efficiently bring to market innovative software products that unify and exchange information on and between the telephone and computer. While the Company's product lines all provide computer-telephony functionality, the Company tailors its products to take advantage of the distinct telephony-oriented and computer-oriented distribution channels. The Company intends to leverage its expertise to continue to develop channel-specific products and to introduce new products that further integrate its telephony and computer capabilities.

**Capitalize on Installed Base.** The Company intends to capitalize on its installed base by offering add-on modules, software upgrades and new products, all of which provide increased capacity and functionality. Moreover, the Company believes the migration of many of its customers to the Windows NT operating system will present it with a significant opportunity to sell Windows NT product upgrades.

**Utilize Capabilities of Multiple Distribution Channels.** The Company targets medium-sized enterprises primarily through telephony-oriented distributors and computer-oriented value-added resellers. The Company believes that some enterprises will evaluate computer-telephony solutions from a telephony perspective while others will focus on data-centric solutions. The use of multiple distribution channels that target many of the same potential customers increases the likelihood that the Company's products will be sold to a particular customer. The Company intends to broaden its distribution channels by expanding its direct sales efforts and by continuing to enter into distribution agreements with private label OEMs and other strategic partners, such as the agreement with Ericsson Enterprise Networks AB.

**Grow Through Strategic Acquisitions.** The Company believes that growth through strategic acquisitions of complementary technologies, products and distribution channels offers the potential for significant competitive advantage. The Company's open-systems technology facilitates the rapid integration of and linkage to other complementary open-systems technologies. The Company believes it is therefore able to accelerate introduction of new technologies to the market through acquisition, and to respond rapidly to industry changes and opportunities.



to dealers who obtain their own hardware, or sold fully integrated on Company-provided PC hardware platforms. Software kits consist of software, documentation, a hardware security key, voice cards and fax cards. Fully integrated systems include all the components supplied in the software kits, plus fully integrated and tested PCs, disk drive storage devices of various sizes and configurations, modems, monitors and keyboards. While CallXpress was developed with a telephony orientation, it is designed to link with computer-oriented solutions through its standard LAN-connection and software-modular packaging.

CallXpress application modules consist of software programs that operate in an integrated, multi-tasking environment and are not dependent on secondary hardware processors. Modules may be purchased either at the time of initial installation or as subsequent add-ons. CallXpress software modules are divided into three application categories: call processing, unified messaging, and call center productivity.

#### Call Processing Applications

Automated Attendant/Voice Mail. The Automated Attendant/Voice Mail module answers calls on the first ring and invites the caller to enter an extension number, wait on the line for a receptionist or leave a voice mail message. The Audiotext feature of the Automated Attendant/Voice Mail module acts as a "spoken bulletin board."

Digital Networking. With the Digital Networking module, a company with multiple locations can link its offices together, thereby allowing subscribers at each location to send and receive voice and fax messages to and from any other office in the network using the Internet or corporate intranet.

#### Unified Messaging Applications

Desktop Message Manager. Desktop Message Manager provides a visual interface to the subscriber's unified mailbox, letting the subscriber know who sent a message, the type of message sent, when it arrived, whether it is urgent and its length. The module will play back voice mail messages on the subscriber's telephone or voice-enabled PC, as well as display fax messages on the computer screen. A related module provides the subscriber with a visual interface to manage his or her CallXpress unified mailbox from Microsoft Outlook.

E-Mail Access. E-Mail Access provides a subscriber with the option to hear electronic mail text messages through text-to-speech capabilities or convert them into faxes through text-to-fax capabilities. E-Mail Access integrates with Lotus cc:Mail, Lotus Notes, Microsoft Mail and Microsoft Exchange.

Fax Mail. The Fax Mail module provides store and forward capabilities for fax documents identical to those provided for voice messages. The Company's Fax Server supported under CallXpress for Windows NT extends the capabilities of Fax Mail to include the full feature set, performance and capacity of the RightFAX fax server.

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#### Call Center Productivity Applications

Automated Agent. Automated Agent is an interactive voice response module that enables complete application solutions to be designed for specific business functions such as catalog ordering and college registration. Automated Agent can be connected to the corporate database through a variety of host computer and LAN-based interfaces.

Fax Response. The Fax Response module provides documents such as order acknowledgments or printouts of customer accounts requested by callers through the Automated Agent module.

Desktop Call Manager. Desktop Call Manager provides intelligent, real-time management of incoming calls, allowing the subscriber or member of a workgroup to take the call, take a message, or redirect the call. Incoming calls are identified by Caller ID, prompting the system to display the caller's identity on the subscriber's PC. Desktop Call Manager can be a very cost-effective application for smaller, informal call centers where an ACD (automated call distribution) system cannot be cost-justified.

Faxtext. The Faxtext module provides callers 24-hour access to requested information such as product literature, specification sheets, rate sheets, technical bulletins or other types of information a company may want to quickly and easily communicate via fax.

#### PhoneXpress

PhoneXpress is designed to meet the requirements of small- to medium-sized enterprises that require full-featured automated attendant and voice mail functions. PhoneXpress is based on the same core technology as CallXpress3, but

does not provide the application interfaces to support all the advanced computer-telephony applications of unified messaging and call center productivity. PhoneXpress is designed to support from 4 to 16 ports and can be configured with faxtext and networking capability to provide a cost-effective branch voice processing system for enterprise-wide networks. PhoneXpress, like CallXpress messaging products, is available as a software kit or as a completely integrated system.

#### Call Center Products

##### AgentXpress for Windows NT

AgentXpress for Windows NT is the Company's first product resulting from the acquisition of selected assets and liabilities of Telcom Technologies in early 1997. AgentXpress for Windows NT, launched in the second quarter of 1997, brings a high-performance ACD offering to the Company's advanced computer-telephony application product line targeted at the call center. AgentXpress is an open systems-based platform, supporting up to 144 incoming trunk lines, including analog T1 or ISDN connections, and up to 96 agents utilizing either analog or digital display phone sets. Designed for the medium-sized call center, the system contains a variety of features and functions at a price point below comparable proprietary systems. Up to 16 AgentXpress systems can be networked together to form a distributed call center environment capable of supporting up to 1,536 agents and 2,300 incoming calls at any one time.

AgentXpress is sold as a complete turnkey system with fully integrated and tested PCs, disk drive storage devices of various sizes and configurations, voice cards, trunk cards, modems, monitors, keyboards and digital display phones.

##### Enhanced Agent

Enhanced Agent is a set of computer-telephony interfaces and applications designed to extend the capabilities of AgentXpress to support integration with CallXpress and RightFAX computer-telephony servers. Features provided by Enhanced Agent include seamless transfers of callers to voice mail, the use of IVR scripting for sophisticated caller interrogation, the ability for agents to transmit fax-based information to callers while on the line, and the simultaneous delivery through screen pops of computer-based caller information to the agent assigned the call.

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#### Enhanced Fax Products

The RightFAX high-performance, LAN-based fax servers are designed for businesses with high fax traffic, with many fax users, or that require secure and confidential fax management. The RightFAX products consist of server software, fax cards and desktop clients. Desktop clients can fax documents directly from any Windows application on their LAN-connected PC. All fax processing is performed on the server, thereby eliminating the need for a fax modem or telephone line connected directly to each user's PC. In addition, because the fax processing is performed on the server, the user's application sends the information to be faxed to the server, where all the conversions to fax format and outbound calling and transmission are managed. RightFAX products are sold in software kit form with or without fax cards.

Like the Company's telephony-oriented products, RightFAX provides a mailbox to receive incoming faxes, which can be routed to the user's mailbox in a variety of ways, including OCR (optical character recognition) of a cover page. The fax is digitally stored and can be viewed on a PC connected to the LAN or from any web browser on a PC connected to the Internet. Faxes can then be printed on any printer connected to the LAN or the user's PC, forwarded to other users on the RightFAX server, or re-faxed to any other fax machine in the world. Since the fax has been stored digitally, there is no further degradation due to multiple scannings through standalone fax machines.

RightFAX runs on the Windows NT operating system. The newly announced RightFAX Enterprise product offers more advanced features, including least-cost routing, Internet and corporate intranet capabilities and load-sharing features for multiple server environments. RightFAX servers can be configured from 1 to 32 simultaneous inbound/outbound fax channels, supporting analog or digital T1 connectivity. Capacity is added by installing voice/fax cards and by purchasing port licenses. RightFAX servers are compatible with all major network operating systems and are sold as either software licenses or software kits (including fax cards).

CommercePath offers a high-volume, production-oriented line of servers that attach to mainframe, midrange or network "host" computers and enable fax and other forms of electronic transmission for applications on specific host computers. Sold most often into high-volume business-to-business electronic commerce environments, these servers are used to convert, transmit or receive thousands of production documents such as purchase orders, order

acknowledgments, invoices or statements per hour.

CommercePath software is licensed for either Unix or Windows NT environments starting with a base set of software known as the CommercePath environment. Functions are purchased in individual module sets. These modules include Hostfax, Responsefax, EDI-Interpoint, Internetlink and a set of desktop applications know as Workstation. Capacity is added by installing voice/fax cards and by purchasing port licenses.

CommercePath servers support up to 48 simultaneous inbound/outbound channels per server, and analog or digital T1 connectivity, plus simultaneous attachments to multiple hosts and printers. Each system is scaleable to transmit/receive faxes at a rate of up to 2,800 pages per hour. CommercePath servers are sold as complete turnkey systems with fully integrated and tested PCs, disk drive storage devices of various sizes and configurations, voice and fax cards, modems, monitors and keyboards.

#### Distribution

The Company sells its products primarily through an indirect channel of resellers and distributors, as well as through direct sales and OEM and private label agreements. The Company believes that some enterprises will evaluate computer-telephony solutions from a telephony perspective while others will be more data-focused. The use of multiple distribution channels that access many of the same potential customers increases the likelihood that the Company's products will be sold to a particular customer. The Company has built large telephony-oriented and computer-oriented distribution channels in the United States and is developing its international distribution channels. In 1997, the Company took a significant step toward expanding its international distribution channels by forming a strategic relationship with Ericsson Enterprise Networks AB ("Ericsson"). See "--OEM/Strategic Accounts." No single customer represented 10% or more of the Company's net sales during 1997 or 1998. See "Risk Factors--Dependence on Indirect Distribution."

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#### Telephony-Oriented Distribution

The Company currently derives a substantial percentage of its U.S. telephony-oriented sales revenues from over 400 wholesale dealers and distributors comprised of customer premise telephone equipment dealers and voice processing specialists. This channel consists primarily of national telephone equipment dealers and regionally focused organizations and is serviced by 18 employees. The Company continues to selectively recruit additional dealers, focusing on those capable of marketing and servicing advanced computer-telephony application products.

Dealers are required to attend Company-sponsored training sessions on system usage, installation, maintenance and customer support. Advanced training is also available from the Company on an ongoing basis. All dealers are subject to agreements with the Company covering matters such as payment terms, protection of proprietary rights and nonexclusivity of sales territories, but these agreements generally do not restrict the dealer's ability to carry competitive products.

#### Computer-Oriented Distribution

In the United States, the Company's computer-oriented sales force sells most of the Company's computer-oriented products through an indirect channel of value-added resellers, independent software vendors, and professional services companies specializing in custom systems development. These computer-oriented resellers are small- to medium-sized regionally-focused organizations. In addition, the Company markets its computer-oriented products directly to end-user customers through trade shows and journal advertisements. As of December 31, 1998, the computer-oriented sales force consisted of 67 employees.

#### OEM/Strategic Accounts

To broaden its access to certain markets, the Company has entered into distribution and private label/OEM agreements with Dictaphone Corporation and Fujitsu Business Communications Systems Inc. to sell private label versions of the Company's CallXpress3 and PhoneXpress products, and has an arrangement with Cardiff Software, Inc. to sell a private label version of its RightFAX products. The Company expects to pursue additional OEM and private label agreements in the future. As of December 31, 1998 the Company had 11 employees focused on OEM and strategic accounts. In December 1997, the Company entered into an OEM agreement with Ericsson. The agreement provides for the integration of the Company's CallXpress for Windows NT application into certain Ericsson systems that will be distributed and marketed by Ericsson worldwide. The agreement also provides for certain joint product development initiatives.

#### International Distribution



The international market for computer-telephony products is not as developed as the market in the United States. The Company believes that over the next few years the market for both telephony-oriented and computer-oriented computer-telephony products will grow faster internationally than in the United States. To address this opportunity, the Company is developing broad coverage of international markets through a variety of dealer, distributor, and strategic relationships. To date, the majority of the Company's international sales have been in English-speaking countries: Canada, Australia, the United Kingdom, South Africa and New Zealand. The Company expects its accelerated distribution development and product localization efforts of the past few years will result in a higher growth rate in non-English-speaking countries than in English-speaking countries. The Company is actively recruiting new dealers and distributors in international markets. The Company has sales offices in Canada, the United Kingdom, Germany, Hong Kong and Dubai. Although the Company's sales to date have generally been denominated in U.S. dollars, the Company expects that in the future an increasing portion of its international sales will be made in local currencies. See "Risk Factors--Risks of International Markets" and Note 1 to the Consolidated Financial Statements.

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#### Product Support

The Company's dealers and distributors are primarily responsible for supporting end-users of the Company's products. The Company provides telephone-based technical support to its dealers and distributors. Telephone support service hours to dealers have been expanded to more effectively service non-U.S. customers. The Company has also expanded its technical training offerings of both telephony-oriented and computer-oriented products to its dealers. The Company provides limited warranties on its RightFAX products and certain hardware components distributed in conjunction with its products.

The majority of product support is provided by the Company within three months of product shipment, and the estimated cost of such support is recognized as product revenues are recorded. The Company generally charges its customers separately for post-sale updates and upgrades.

#### Product Development

The Company has established a knowledge base in the development of call processing, voice processing and call switching applications, as well as in the development of LAN and Internet software applications. The Company believes that its expertise in these areas enable it to efficiently bring to market innovative software products that unify and exchange information on and between the telephone and computer.

The Company maintains four product development centers: CallXpress and PhoneXpress products are developed in Kirkland, Washington; AgentXpress products in Montclair, California; RightFAX products in Tucson, Arizona; and CommercePath products in Portland, Oregon. In total, the Company employed, as of December 31, 1998, 118 engineers, technicians and quality assurance specialists in its development centers. While development efforts in the past have been separate, the convergence of technologies is allowing the Company to collaborate and leverage development efforts among these groups. An example of such collaborative efforts is the incorporation of the RightFAX fax server into the CallXpress for Windows NT products. The Company expects these cross-development efforts to increase in the future.

The Company internally develops its core technology, but believes that it is more cost-effective to license from third parties certain components of its products, such as database software, screen viewers, voice and fax cards and network connectors. Whenever practical, the Company will license and integrate such technology into its product offerings in order to decrease the cost of development and shorten the time to market. In addition, the Company also believes that the acquisition of new technology and new product offerings is consistent with its strategic initiatives and will continue to pursue such opportunities as they become available.

The Company believes that, for its product offerings to continue to achieve acceptance, it will be necessary to continue to develop enhanced versions of its computer-telephony applications. Over the past year the Company has released major new versions of its products which operate in the Windows NT environment. The Company expects to continue to expend significant research and development efforts in developing new technology, but does not expect to introduce as many new product lines in future years as the Company did in 1997. See "Risk Factors--Rapidly Changing Technology and Customer Needs."

Additionally, with international markets expected to grow at a faster rate than the North American market over the next several years, the Company intends to continue to develop versions of its products that have been localized for foreign markets. Localization includes converting client screens, documentation, and voice-prompt sets into foreign languages. The Company anticipates expending significant research and development resources to develop localized versions of

### Proprietary Rights

AVT relies on a combination of patents, copyright, trademark and trade secret laws, nondisclosure and other agreements and technical measures to protect its proprietary technology. The Company has received a patent in the area of unified messaging. There can be no assurance that the Company's efforts to protect its proprietary rights will be successful. AVT has periodically received letters from third parties asserting patent rights. Following analysis, the Company generally has not believed it necessary to license any of the patent rights referred to in such letters. In those cases in which the Company has determined a license of patent rights was necessary, it has entered into a license agreement. The Company believes that any necessary licenses or other rights under patents to products or features could be obtained on conditions that would not have a material adverse effect on its financial condition, although there can be no assurance in this regard. See "Risk Factors--Limited Intellectual Property Protection; Potential Infringements."

The Company licenses certain portions of its technology from third parties under written agreements, some of which contain provisions for ongoing royalty payments. As of December 31, 1998, the Company had license agreements with Octel Corporation, Syntellect Inc., Intelligent Environments, Inc., International Business Machines Corporation and Metasoft Systems, Inc.

### Competition

The computer-telephony market is highly competitive and the Company believes that the competitive pressures it faces are likely to intensify, particularly as new offerings based on the Windows NT operating system emerge. System features, product pricing, ease of use and installation, sales engineering and marketing support, and product reliability are the primary bases of competition. The Company believes that it competes favorably with respect to these factors in its target markets. See "Risk Factors--Competition."

The Company's principal competitors in the telephony-oriented market for voice messaging and unified messaging systems are independent suppliers, including the Octel Messaging Division of Lucent Technologies, Inc., Centigram Communications Corporation, Active Voice Corporation, Voysys Corporation and Callware Technologies, Inc. The Company's principal competitors in the call center systems market are manufacturers such as Aspect Telecommunications Corporation and Rockwell International Corporation. PBX and key telephone systems manufacturers such as Lucent Technologies, Inc., Northern Telecom Ltd., Siemens Business Communication Systems, Inc., Executone Information Systems, Inc., Panasonic Communications and Systems Co., NEC America, Inc. and Toshiba America Information Systems, Inc. also compete with the Company by offering integrated voice messaging systems, unified messaging systems and ACD systems of their own design or under various OEM agreements.

In the market for LAN-based facsimile systems, the Company's principal competitors are Omtool, Ltd., Optus Software, Inc., Esker S.A. and Computer Associates International, Inc. The Company's fax server products also compete with vendors offering a range of alternative facsimile solutions, including operating systems containing facsimile and document transmission features, low-end fax modem products, desktop fax software, single-platform facsimile software products and customized proprietary software solutions. In the market for production facsimile systems, the Company's principal competitors are Biscom, Inc., Esker S.A. and Topcall International AG.

### Manufacturing

The Company's manufacturing operations consist primarily of diskette duplication, documentation fulfillment, final assembly and quality control testing of materials, subassemblies and systems. Some limited hardware fabrication is performed by third parties for the Company on certain telephone switch integration modules, for which the Company has designed a proprietary device to emulate a particular manufacturer's telephone station set, and for certain internal "switching" components and digital hand sets used in the Company's ACD products. The Company is dependent on third-party manufacturers and vendors for certain critical hardware components such as PC chassis, keyboards, disk drives, monitors, memory modules and other miscellaneous components.

The Company's products incorporate a number of commercially available application cards, fax cards, voice cards and circuit boards that enable integration with certain telephone switches. The Company currently purchases voice cards from Dialogic, Natural Microsystems Corp. and Mitel Corp. The Company purchases fax cards from Brooktrout and Dialogic. See "Risk Factors--

Employees

As of December 31, 1998, the Company had 323 full-time employees, including 44 in administration, 19 in manufacturing, 74 in engineering and product development, and 186 in sales, marketing and technical support. The Company's employees enter into agreements containing confidentiality restrictions. The Company has never had a work stoppage and no employees are represented by a labor organization. The Company considers its employee relations to be good.

Item 2. PROPERTIES

The Company's headquarters and its telephony-oriented administrative, engineering, manufacturing and marketing operations are located in approximately 60,000 square feet of space in Kirkland, Washington under a lease that expires in January 2003. The Company also conducts telephony-oriented operations in approximately 6,600 square feet of leased space in Montclair, California. The Company's computer-oriented operations are primarily located in approximately 19,500 square feet of leased space in Tucson, Arizona and approximately 10,900 square feet of leased space in Portland, Oregon.

The Company believes that these facilities are adequate to meet its current needs and that suitable additional or alternative space will be available, as needed, in the future on commercially reasonable terms.

Item 3. LEGAL PROCEEDINGS

In May 1998, CallWare brought suit against AVT in federal court in Salt Lake City, Utah, alleging various claims relating to purported false advertising by AVT. (CallWare Technologies, Inc. v. Applied Voice Technology, Inc., Case No. 2:98CV 0329K.) CallWare has claimed \$20 million in monetary damages, and an additional \$60 million in punitive damages. The suit is in the discovery phase, and an initial pretrial conference was held on January 14, 1999 and a trial date of January 10, 2000 has been set. AVT believes that CallWare's claims are without merit and is vigorously defending the lawsuit.

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

There were no matters submitted to a vote of security holders during the fourth quarter of 1998.

PART II

Item 5. MARKET FOR REGISTRATION'S COMMON EQUITY AND RELATED SHAREHOLDER MATTERS

The information required by this Item is incorporated by reference to information contained in Note 9 to the Consolidated Financial Statements: Quarterly Financial Data and Market Information (unaudited).

Item 6. SELECTED CONSOLIDATED FINANCIAL DATA

<TABLE>  
<CAPTION>

	Year Ended December 31,				
	1994	1995	1996	1997	1998
	<C>	<C>	<C>	<C>	<C>
	(in thousands, except per share data)				
Statement of Income Data:					
Net sales.....	\$28,761	\$31,284	\$44,127	\$58,091	\$81,126
Cost of sales.....	12,391	13,364	16,895	21,066	28,098
Gross profit.....	16,370	17,920	27,232	37,025	53,028
Operating expenses:					
Research and development.....	2,671	2,732	4,149	6,719	8,082
Selling, general and administrative.....	8,357	8,458	14,509	19,212	27,663
Non-recurring charges (1).....	--	--	4,140	11,025	287
Total operating expenses.....	11,028	11,190	22,798	36,956	36,032
Operating income.....	5,342	6,730	4,434	69	16,996
Other income, net.....	294	1,116	919	1,070	1,145
Income before income tax expense.....	5,636	7,846	5,353	1,139	18,141
Income tax expense.....	1,398	2,512	3,419	410	6,531
Net income.....	\$ 4,238	\$ 5,334	\$ 1,934	\$ 729	\$11,610

Diluted earnings per common share(2).....	\$0.52	\$0.48	\$0.17	\$0.06	\$0.88
Net income excluding nonrecurring items(3).....	\$ 4,238	\$ 5,334	\$ 6,074	\$ 7,785	\$11,793
Diluted earnings per common share excluding nonrecurring Items (2) (3).....	\$0.52	\$0.48	\$0.52	\$0.62	\$0.90
Weighted average common and common equivalent shares outstanding(2).....	8,142	11,222	11,748	12,598	13,165

</TABLE>

<TABLE>

<CAPTION>

	December 31,				
	1994	1995	1996	1997	1998
	(in thousands)				
<S>	<C>	<C>	<C>	<C>	<C>
Balance Sheet Data:					
Cash, cash equivalents and short-term investments.....	\$22,685	\$24,446	\$27,679	\$22,233	\$39,049
Working capital.....	\$24,294	\$29,670	\$30,870	\$27,926	\$48,873
Total assets.....	\$28,944	\$36,932	\$46,127	\$54,410	\$76,107
Long-term debt, less current portion.....	\$ --	\$ 899	\$ 313	\$ --	\$ --
Total shareholders' equity.....	\$24,998	\$32,889	\$38,883	\$43,010	\$63,395

</TABLE>

- (1) Reflects nonrecurring charges of \$287,000 related to the withdrawal of the follow-on stock offering in February 1998 as well as \$4,140,000, \$3,898,000 and \$7,127,000 for the write-off of purchased, in-process research and development associated with the acquisition of RightFAX in January 1996, Telcom Technologies in January 1997 and CommercePath in October 1997, respectively.
- (2) Computed on the basis described in Note 1 to the Consolidated Financial Statements.
- (3) Excludes the after-tax effect of the nonrecurring charges in 1996, 1997 and 1998 referred to above.

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

Overview

The Company is a leading provider of software-based computer-telephony solutions for medium-sized enterprises. These solutions are designed to enhance individual and work group productivity, improve customer service, reduce business operating costs and simplify access to data and dissemination of information. The Company's products provide enhanced voice and data integration through applications such as unified voice and data messaging, call center management, IVR and document distribution. The Company's key products are multi-application computer-telephony platforms that run on off-the-shelf hardware, support Windows NT and OS/2, and interface with a wide variety of telephony and computer equipment. The Company also offers add-on modules and software upgrades that provide increased capacity and functionality.

The Company sells its products primarily through an indirect channel of resellers and distributors, as well as through direct sales and OEM and private label agreements. The Company expanded its product offerings significantly in 1997 by releasing Windows NT-based products in each of its main product categories. The Company's product lines serve the needs of two areas of the computer telephony market - the telephony oriented buyer and the data oriented buyer of enterprise software and systems. The Company's telephony-oriented products include: CallXpress for Windows NT and CallXpress3, the Company's premier multi-application, high capacity computer-telephony product lines; PhoneXpress, a full-featured voice messaging system for small to medium-sized enterprises; AgentXpress for Windows NT, a high-performance Windows NT-based automated call center (ACD) system for medium-sized call centers; the recently released Automated Agent for Windows NT, an IVR capability for CallXpress for Windows NT; and Enhanced Agent, a set of interfaces and applications designed to extend the capabilities of AgentXpress. The Company's data-oriented products include RightFAX and RightFAX Enterprise, the Company's LAN-based fax server lines for Windows NT, and CommercePath's line of production document delivery systems for Windows NT and Unix. At this time the Company's data-oriented products are focused on the enterprise fax market. The Company significantly expanded its product offering in the past 24 months by releasing Windows NT-based products in each of its main product areas.

Since January 1996, the Company has made three strategic acquisitions, each of which was accounted for as a purchase. The Company acquired RightFAX, a developer of LAN-based fax server software, in January 1996. In January 1997, the Company acquired selected assets and liabilities of Telcom Technologies, a developer of NT-based open-architecture ACD systems. In October 1997, the Company acquired CommercePath, a developer of high-volume production-oriented fax servers. In connection with the RightFAX, Telcom Technologies and

CommercePath acquisitions, the Company recorded nonrecurring charges of \$4.1 million, \$3.9 million and \$7.1 million, respectively, in January 1996, January 1997 and October 1997 for the write-off of purchased, in-process research and development, and recorded additional amounts of goodwill that are being amortized over future years. See "--Liquidity and Capital Resources" and Note 8 to the Consolidated Financial Statements.

Results of Operations

The following table sets forth, for the periods indicated, the percentage of net sales represented by certain items in the Company's consolidated statements of income.

<TABLE>  
<CAPTION>

	Year Ended December 31,		
	1996	1997	1998
<S>	<C>	<C>	<C>
Net sales.....	100.0%	100.0%	100.0%
Cost of sales.....	38.3	36.3	34.6
Gross profit.....	61.7	63.7	65.4
Operating expenses:			
Research and development.....	9.4	11.6	10.0
Selling, general and administrative.....	32.9	33.1	34.1
Non-recurring charges.....	9.4	18.9	0.3
Total operating expenses.....	51.7	63.6	44.4
Operating income.....	10.0	0.1	21.0
Other income, net.....	2.1	1.9	1.4
Income before income tax expense.....	12.1	2.0	22.4
Income tax expense.....	7.7	0.7	8.1
Net income.....	4.4%	1.3%	14.3%

</TABLE>

Net Sales

The Company derives net sales primarily from initial sales of software kits and licenses and fully integrated systems, as well as follow-on sales of add-on software modules and product upgrades. Sales to dealers and distributors are recognized when the products are shipped. The sales mix among the Company's product categories and between software kits and fully integrated systems affects both net sales and gross margin. Because of their hardware components, fully integrated systems generate higher revenue per unit and lower margins than comparable software kits. Advanced CTI application systems generally are sold at a higher unit price and with a higher gross margin than basic messaging systems due to the additional software modules purchased and the higher mix of software kits and software licenses as compared to fully integrated systems. Over the past three years, sales have shifted toward higher-margin advanced CTI products and software kits from lower-margin CTI-ready systems and basic messaging products, but there can be no assurance that this trend will continue. See "Risk Factors--Fluctuations in Quarterly Operating Results; Limited Backlog" and "--Declining Average Sales Prices."

Years ended December 31, 1998 and 1997. Net sales increased 40% to \$81.1 million in 1998 from \$58.1 million in 1997. This increase resulted primarily from increased sales of enhanced fax products and a full year of sales from our CommercePath business unit, which on a combined basis increased 92% in 1998, and represented 57% of net sales, as compared to 42% of net sales in 1997. Sales of advanced messaging and call center systems continued to strengthen during 1998 and constituted 35% of total product sales in 1998. The lower-margin basic messaging market continued to be affected by price pressures from competitive offerings. Basic messaging sales declined 33% in 1998 from 1997, and represented 8% of net sales in 1998 compared to 16% of net sales in 1997. International sales for 1998 increased 23% from 1997, and represented 18% of net sales.

Years ended December 31, 1997 and 1996. Net sales increased 32% to \$58.1 million in 1997 from \$44.1 million in 1996. The increase resulted primarily from sales of enhanced fax products, which increased 79% in 1997, and represented 42% of net sales, as compared to 31% of net sales in 1996. The Company introduced new, Windows NT-based, advanced CTI-oriented product lines in the first half of 1997 and included CommercePath's results of operations beginning in November 1997. The lower-margin basic messaging market continued to be affected by price pressures from competitive offerings. Basic messaging sales declined 18% in 1997 from 1996, and represented 16% of net sales in 1997 compared to 26% of net sales in 1996.

#### Gross Profit

Years ended December 31, 1998 and 1997. Gross profit as a percentage of net sales increased to 65.4% in 1998, as compared to 63.7% in 1997, due primarily to the favorable sales mix of enterprise fax products and advanced CTI applications and the declining sales of basic messaging systems.

Years ended December 31, 1997 and 1996. Gross profit as a percentage of net sales improved to 63.7% in 1997, as compared to 61.7% in 1996, due primarily to the favorable sales mix of advanced CTI applications as compared to basic messaging systems. Gross profit on basic messaging system sales in 1997 continued to be negatively affected by price erosion and a higher ratio of fully integrated systems as compared to advanced CTI application systems.

#### Research and Development

Years ended December 31, 1998 and 1997. Research and development expenses increased 20% to \$8.0 million in 1998 from \$6.7 million in 1997, due primarily to increased personnel costs relating to acceleration of certain development projects, and a full year of research and development expenses associated with CommercePath. As a percentage of net sales, research and development expenses represented 10% in 1998, as compared to 11.6% in 1997.

Years ended December 31, 1997 and 1996. Research and development expenses increased 62% to \$6.7 million in 1997 from \$4.1 million in 1996, due primarily to increased personnel costs relating to acceleration of certain development projects, the inclusion of the recently formed call center development group, which was acquired from Telcom Technologies, and research and development expenses associated with CommercePath. As a percentage of net sales, research and development expenses represented 11.6% in 1997, as compared to 9.4% in 1996.

#### Selling, General and Administrative

Years ended December 31, 1998 and 1997. Selling, general and administrative expenses increased 44% to \$27.7 million in 1998 from \$19.2 million in 1997, due primarily to the inclusion of CommercePath expenses for the entire year as well as increased personnel-related costs of domestic and international development of both the telephony-oriented and computer-oriented distribution channels. Selling, general and administrative expenses for 1998 included amortization of \$1.1 million of goodwill relating to acquisitions compared to \$0.7 million in 1997. Selling, general and administrative expenses represented 34.1% of net sales in 1998, as compared to 33.1% in 1997.

Years ended December 31, 1997 and 1996. Selling, general and administrative expenses increased 32% to \$19.2 million in 1997 from \$14.5 million in 1996, due primarily to increased personnel-related costs of domestic and international development of both the telephony-oriented and computer-oriented distribution channels, the new product launches of CallXpress for Windows NT and AgentXpress for Windows NT, and the inclusion of CommercePath expenses for the last two months of 1997. Selling, general and administrative expenses for 1997 included amortization of \$0.7 million of goodwill relating to acquisitions. Selling, general and administrative expenses represented 33.1% of net sales in 1997, as compared to 32.9% in 1996.

#### Non-recurring Charges

In February, 1998 the Company withdrew a follow-on stock offering originally filed in October 1997 and wrote-off the costs of \$287,000 in connection with the canceled offering. In connection with the acquisitions of Telcom Technologies and CommercePath, the Company recognized nonrecurring charges of \$3.9 million and \$7.1 million in the first and fourth quarters of 1997, respectively, for the write-off of purchased, in-process research and development. The Company recognized a nonrecurring charge of \$4.1 million in the first quarter of 1996 for the write-off of purchased, in-process research and development associated with the acquisition of RightFAX.

#### Other Income, Net

For the years ended December 31, 1998 and 1997, other income remained constant at \$1.1 million. Other income increased to \$1.1 million in 1997 from \$0.9 million in 1996 due to increased cash and investment balances.

#### Income Tax Expense

The effective income tax rate in 1998, 1997 and 1996 was 36%, excluding

acquisition-related charges. The acquisitions of Telcom Technologies and CommercePath in 1997 were taxable transactions, and, therefore, the resulting excess of purchase price over net tangible assets acquired is deductible for income tax purposes. By contrast, the excess of the purchase price over net tangible assets acquired associated with the acquisition of RightFAX in 1996 is not tax deductible. Primarily as a result of the differing tax treatment of these acquisitions, the Company recognized an income tax expense of \$6.5 million in 1998 and \$0.4 million in 1997, as compared to an income tax expense of \$3.4 million in 1996.

#### Net Income and Net Income Per Share

Years ended December 31, 1998 and 1997. The Company recognized net income in 1998 of \$11.6 million as compared to \$0.7 million in 1997. Excluding the nonrecurring charges related to the cancellation of the follow-on stock offering in 1998, net income would have increased to \$11.8 million compared to the 1997 net income excluding non-recurring charges of \$7.8 million. Diluted net income per share, excluding the nonrecurring charges, increased to \$.90 per share in 1998 from \$.62 per share in 1997.

Years ended December 31, 1997 and 1996. The Company recognized net income in 1997 of \$0.7 million as compared to \$1.9 million in 1996. Excluding the nonrecurring charges related to the RightFAX, Telcom Technologies and CommercePath transactions discussed above, net income for 1997 would have increased 28% to \$7.8 million, from \$6.1 million in 1996. Diluted net income per share, excluding the nonrecurring charges, increased to \$.62 per share in 1997 from \$.52 per share in 1996.

#### Liquidity and Capital Resources

Cash and cash equivalents and short-term investments increased to \$39.0 million at December 31, 1998 from \$22.2 million at December 31, 1997 and from \$27.7 million at December 31, 1996, due primarily from operations. Cash flow generated from operating activities was \$15.7 million, \$10.3 million and \$8.2 million in the years ended December 31, 1998, 1997 and 1996, respectively. The increases resulted primarily from profitable operations.

The Company is exposed to market risk related to changes in interest rates and foreign currency exchange rates, each of which could adversely affect the value of the Company's investments. The Company does not currently use derivative financial instruments.

The Company maintains a short-term investment portfolio consisting of interest bearing securities with an average maturity of less than one year. These securities are classified as "available for sale" securities. The interest bearing securities are subject to interest rate risk and will fall in value if market interest rates increase. If market interest rates were

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to increase immediately and uniformly by 10% from levels at December 31, 1998, the fair value of the portfolio would decline by an immaterial amount. Because the Company has the ability to hold its fixed income investments until maturity, it does not expect its operating results or cash flows to be affected to any significant degree by a sudden change in market interest rates on its securities portfolio.

The Company has assets and liabilities denominated in certain foreign currencies related to the Company's international sales operations. The Company has not hedged its translation risk on these currencies as the Company has the ability to hold its foreign-currency denominated assets indefinitely and does not expect that a sudden or significant change in foreign exchange rates would have a material impact on future net income or cash flows.

In February 1995, the Company prepaid the remaining balance due under a royalty agreement associated with a 1989 business combination. See Note 6 to the Consolidated Financial Statements. The cash disbursement, which amounted to \$1.8 million, was recorded as an intangible asset and has been amortized over the remaining term of the original royalty agreement, approximately six years. In addition, the Company amended a license agreement in September 1995, prepaying its remaining royalty obligation by issuing a note in the amount of \$1.9 million payable in 12 equal quarterly installments of \$161,417 each, including imputed interest at 8.75% per annum. The Company amended an additional license agreement in July 1996, prepaying its remaining royalty obligation by issuing a non-interest-bearing note for \$450,000 that was fully paid prior to December 31, 1996. For each of these license agreement amendments, the related intangible asset is being amortized on a straight-line basis over the average remaining lives of the patents, which are approximately 12 years in the case of the license amended in September 1995 and approximately seven years in the case of the license amended in July 1996.

In January 1996, the Company acquired RightFAX for \$4.2 million in cash plus 326,000 shares of Common Stock. The business combination was accounted for as a purchase. Approximately \$4.1 million of the purchase price was recognized as a nonrecurring charge in the first quarter of 1996, representing the value of purchased, in-process research and development. The remaining intangible assets are being amortized over seven years from the date of acquisition. As a result of the earn out and guaranteed value of the stock issued in the acquisition of RightFAX, the Company made payments in January 1998 and 1997 of \$668,000 and \$1,408,000, respectively, and also issued 52,000 and 190,000 additional shares of common stock. In January 1999, the Company paid the final amounts on the earn out of \$250,000 and 9,800 shares of common stock. This earn out resulted in additional goodwill being recorded in December 1998, 1997 and 1996 of \$0.5 million, \$1.3 million and \$2.0 million, respectively.

In January 1997, the Company acquired selected assets and liabilities of Telcom Technologies. The purchase price for the acquisition was \$3.5 million in cash, plus warrants to purchase 200,000 shares of Common Stock exercisable at \$6.68 per share, which may be exercised any time prior to January 3, 2002. The Company accounted for the business combination as a purchase and recognized a nonrecurring charge of \$3.9 million in the first quarter of 1997, representing the value of the purchased, in-process research and development.

In October 1997, the Company acquired all the outstanding capital stock of CommercePath from Forest City Trading Group, Inc. for \$10.4 million in cash. In connection with the acquisition, the Company also granted options to purchase 240,000 shares of Common Stock, at an exercise price of \$14.05 per share, to two of CommercePath's executive officers. The Company accounted for the acquisition as a purchase and recorded a nonrecurring charge of \$7.1 million for the write-off of purchased, in-process research and development. In addition, the Company recorded \$1.8 million of goodwill that will be amortized over seven years. See Note 8 to the Consolidated Financial Statements.

At December 31, 1998, the Company had a \$4.0 million unsecured revolving line of credit, none of which was outstanding. The Company's line of credit expires in May 1999 and contains certain financial covenants and restrictions as to various matters. The Company is currently in compliance with all such covenants and restrictions. Borrowings under the line of credit bear interest at the bank's prime rate or its interbank offering rate plus 1.50%, at the Company's option.

The Company invested \$2.1 million, \$1.1 million and \$0.9 million in equipment and leasehold improvements in the years ended December 31, 1998, 1997 and 1996, respectively. Equipment purchases in such years consisted primarily of computer hardware and software.

The Company expects that its current cash, cash flow from operations and available bank line of credit, will provide sufficient working capital for operations for the foreseeable future.

#### Impact of the Year 2000 Issue

The "Year 2000 Issue" is pervasive and complex as virtually every computer operation will be affected in some way by the rollover of the two-digit year value to 00. Systems that do not properly recognize date sensitive information when the year changes to 2000, or interact with systems or components that fail to do so, could generate erroneous data or otherwise fail to function properly, or at all. There is speculation that a significant amount of litigation will arise out of Year 2000 compliance issues, and the Company is aware of a growing number of lawsuits against other software vendors. Because of the unprecedented nature of such litigation, it is uncertain whether or to what extent the Company may be affected by it.

The Company has developed a plan to ensure its internal systems and products are Year 2000 compliant, and to mitigate its risks in the event that its vendors or other third-parties with whom it has material relationships are not Year 2000 compliant on a timely basis. The Company has potential exposure relating to the Year 2000 issue in four areas: (1) the Company's internal software and hardware systems, including non-information technology systems; (2) suppliers of hardware and software the Company resells as part of its products; (3) internally developed software the Company sells; and (4) other third-parties with whom the Company has material relationships. The following information explains how the Company is addressing each of these potential risk areas:

1. With respect to internal software and hardware systems, the Company reviewed all its material systems to determine which systems were not Year 2000 compliant. The Company is currently in the process of completing all necessary upgrades, modifications and conversions to its programs and equipment to ensure they will continue to be effective in the year 2000, and expects to complete this process not later than June 30, 1999. All of such upgrades have been or are being done as part of a normal upgrade cycle and accordingly no additional costs are being



incurred as a result of Year 2000 issues. The Company expects that the only expense it will incur to make its internal software and hardware systems Year 2000 compliant is approximately \$5,000 to update an alarm system.

2. The Company has tested and will continue to test computer components, including fax and voice cards and software it purchases from third parties, for Year 2000 compliance. The Company has verified that all such components and software currently in use are Year 2000 compliant. The Company, however, has identified alternate sources for critical components in the event that a supplier's business is disrupted by the advent of the year 2000.
3. Since June 1998, all of the Company's products available for sale to customers have been Year 2000 compliant. The Company has offered free or reduced cost upgrades to certain purchasers of the Company's products that were not Year 2000 compliant when sold. The cost of developing and providing such upgrades was approximately \$100,000. The Company does not intend to offer upgrades for certain of its older products.
4. The Company has begun a process to contact third parties with which it has material relationships, including its vendors, distributors, banks, and transfer agent, to attempt to determine their preparedness with respect to Year 2000 issues and to analyze the risks to the Company in the event any such third parties experience significant business interruptions as a result of Year 2000 noncompliance. The Company expects to complete this review process by March 31, 1999.

The Company believes that it is taking the necessary steps regarding Year 2000 compliance with respect to matters within its control to ensure that the Year 2000 issue will not materially impact the Company. However, the Company may be materially adversely affected if important distributors or customers of the Company experience significant disruptions in their systems or business due to the advent of the Year 2000. In addition, the costs of the Year 2000 project and the date on which the Company plans to complete Year 2000 modifications are based on management's best estimates, which were derived utilizing numerous assumptions of future events including the continued availability of certain resources, third

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party modification plans and other factors. There can be no guarantee that these assumptions will prove to be correct and actual results could differ materially from those expected. The Company intends to develop a contingency plan to address unexpected Year 2000 issues by June 30, 1999.

#### Certain Trends and Uncertainties

When used in this discussion, the words "believes," "anticipates" and similar expressions are intended to identify forward-looking statements. Such statements are subject to certain risks and uncertainties that could cause actual results to differ materially from those projected. Factors which could affect the Company's financial results are described below under "Risk Factors" and in Item 1 (Business) of this Annual Report on Form 10-K. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. The Company undertakes no obligation to publicly release the results of any revisions to these forward-looking statements that may be made to reflect events or circumstances after the date hereof or to reflect the occurrences of unanticipated events.

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#### RISK FACTORS

Fluctuations in Quarterly Operating Results; Limited Backlog. The Company's quarterly results of operations are subject to significant fluctuations due to a variety of factors, including the timing of customer orders, changes in the Company's mix of products and distribution channels, the announcement or introduction of new products by the Company or its competitors, pricing pressures and general economic conditions. For example, mix shifts between fully integrated systems and software kits result in fluctuations in gross margins because fully integrated systems generate higher revenue per unit but have lower margins due to their hardware component. The Company's results of operations also may fluctuate as a result of seasonal factors. Specifically, due to typical year-end dealer sales patterns and end-user buying patterns, net sales in the Company's first quarter, without taking into account the effect of acquisitions, have in the past declined from the fourth quarter of the previous year. Because substantially all of the Company's revenues in each quarter result from orders received in that quarter, the Company has historically operated with little or no backlog. The Company establishes its expenditure levels for product development and other operating expenses based on its expected revenues, and expenses are relatively fixed in the short term. As a result, variations in the

timing of sales can cause significant variations in quarterly results of operations. Accordingly, the Company's results of operations for any period are not necessarily indicative of results for any future period.

**Dependence on Indirect Distribution.** A substantial majority of the Company's net sales depends on a network of independent telephone equipment dealers and computer-oriented value-added resellers. There is intense competition for the attention of these independent dealers and resellers from both the Company's competitors and from providers of other products normally distributed through these channels. In addition, many of these dealers and resellers do not have the financial resources to withstand a downturn in their businesses. The lack of active effort or interest on the part of these dealers and resellers in selling the Company's products, the loss of a major dealer or reseller, or any other event or condition negatively affecting the distribution network could have a material adverse effect on the Company's business, results of operations and financial condition. There can be no assurance that the Company will be able to maintain or expand its network of dealers and resellers in the future or that such dealers and resellers will maintain or expand their present level of efforts to sell the Company's products. See "Business--Distribution."

**Risks Associated With Recent and Future Acquisitions.** Since January 1996, the Company has made three strategic acquisitions. The Company's management frequently evaluates potential acquisitions of products, technologies and businesses. Acquisitions by the Company may result in the diversion of management's attention from the day-to-day operations of the Company's business and may include numerous other risks, including difficulties in the integration of operations, products and personnel. The failure of efforts to integrate future acquisitions could have a material adverse effect on the Company's business, results of operations and financial condition. In addition, acquisitions by the Company have the potential to result in dilutive issuances of equity securities, the incurrence of debt, write-offs of purchased, in-process research and development and amortization expenses related to goodwill and other intangible assets.

**Rapidly Changing Technology and Customer Needs.** The market for the Company's products is subject to rapid technological change, changes in customer requirements and frequent new product and feature introductions. Customer needs and expectations will require the Company to continue to identify, develop and market new products and features that satisfy those needs and keep pace with technological developments, including evolving industry standards and competitive offerings. Such activities will require the Company to make substantial expenditures on product development. In addition, the Company has devoted significant expenditures to technologies that it anticipates will become widely adopted, such as Windows NT and the Internet. There can be no assurance that new products or product enhancements developed by the Company will achieve market acceptance or that the Company will successfully develop new products or product enhancements on a timely basis. Any failure by the Company to anticipate or respond adequately to technological developments, customer requirements or evolving industry standards, or any significant delays in product development or introduction, could have a material adverse effect on AVT's business, results of operations and financial condition. See "Business--Product Development."

**Competition.** The computer-telephony market is highly competitive and the Company believes that the competitive pressures it faces are likely to intensify, particularly as new offerings based on the Windows NT operating system emerge. The Company's principal competitors in the telephony-oriented market for messaging systems are independent suppliers, including the Octel Messaging Division of Lucent Technologies, Inc., Mitel Corporation, Active Voice Corporation,

Voysys Corporation and Callware Technologies, Inc. The Company's principal competitors in the call center systems market are manufacturers such as Aspect Telecommunications Corporation and Rockwell International Corporation. In addition to these independent suppliers of computer-telephony solutions, private branch exchange ("PBX") and key telephone systems manufacturers such as Lucent Technologies, Inc., Northern Telecom Ltd., Siemens Business Communication Systems, Inc., Executone Information Systems, Inc., Panasonic Communications and Systems Co., NEC America, Inc. and Toshiba America Information Systems, Inc. also compete with the Company by offering integrated voice messaging systems, unified messaging systems and automatic call distribution ("ACD") systems of their own design or under various OEM agreements.

In the market for LAN-based facsimile systems, the Company's principal competitors are Omtool, Ltd., Optus Software, Inc., Esker, S.A. and Computer Associates International, Inc. The Company's fax server products also compete with vendors offering a range of alternative facsimile solutions, including operating systems containing facsimile and document transmission features, low-end fax modem products, desktop fax software, single-platform facsimile software products and customized proprietary software solutions. In the market for production facsimile systems, the Company's principal competitors are Biscom, Inc., Esker, S.A. and Topcall International AG.

The Company believes that further acceptance of open systems architectures and the development of industry standards in the call processing market will eliminate some of the technical barriers to entry, allowing additional competitors to enter the market. Many of the Company's existing competitors have substantially greater technical, financial and marketing resources, as well as larger customer and installed bases and greater name recognition, than the Company. Further, some of the Company's competitors are able to achieve marketing advantages by bundling their call processing equipment or competitive facsimile solutions as part of their broader product offerings. The Company expects its competitors to continue to offer improved product technologies and capabilities, the availability of which could cause a significant decline in sales of the Company's existing products. There can be no assurance that the Company will be able to compete successfully or that such competition will not have a material adverse effect on the Company's business, results of operations or financial condition. See "Business--Competition."

**Declining Average Sales Prices.** The Company has experienced declining average sales prices in its basic voice messaging products as a result of competitive pressures and in the future may experience declining prices in some of its other product lines. Declining average sales prices of the Company's more significant product lines could lead to a decline in the Company's overall gross margins. To offset and forestall declining average sales prices, the Company believes that it must continue to develop product enhancements and new products with advanced features that are likely to generate higher-margin incremental revenue. If the Company is unable to develop new products and enhancements in a timely manner or if such products do not achieve significant customer acceptance, the Company's business, results of operations and financial condition could be materially adversely affected. See "--Competition".

**Limited Intellectual Property Protection; Potential Infringements.** The Company's success depends in part on its ability to protect its proprietary technology. The Company has received a patent in the area of unified messaging, but there can be no assurance that the claims in the patent will not be successfully challenged or circumvented by competitors, or that the patent will provide competitive advantages for the Company's products. In addition, the Company relies on a combination of copyright, trademark and trade secret laws, nondisclosure and other agreements and technical measures to protect its proprietary technology. There can be no assurance that the Company will be able to obtain any meaningful patent protection for its technology in the future, or that the measures taken by the Company will be adequate to prevent or deter misappropriation of its technology or the development of technologies having similar performance characteristics. The Company's use of open systems architecture in the design of its products may make it easier for competitors to misappropriate or replicate the Company's designs and developments. The computer-telephony software industry has historically been characterized by numerous allegations of patent infringement among competitors, and considerable related litigation. The Company has received claims of patent infringement from several parties and likely will receive additional claims in the future. Although none of these claims has led to litigation to date, the Company's investigation into some of these claims has been limited by, among other things, lack of sufficient information regarding the claims. These claims may yet result in the Company's incurring substantial legal expenses and being required to obtain licenses, pay damages for infringement, or cease offering products that infringe such patents. There can be no assurance that a license under patents or other intellectual property that the Company is allegedly infringing would be available to the Company on reasonable terms, if at all. The inability of the Company to obtain necessary licenses or other rights or to protect its proprietary

technology could have a material adverse effect on the Company's business, results of operations and financial condition. See "Business--Proprietary Rights."

**Risks of International Markets.** The Company's future growth depends in part on continued expansion of its international sales, which accounted for approximately 18%, 21% and 18% of net sales in the years ended December 31, 1996, 1997 and 1998, respectively. This expansion requires significant management attention and financial resources, and has resulted in a significant portion of the Company's revenues being subject to the risks associated with international sales. Such risks include necessary product adaptations to local languages and telephone system technology, changes in regulatory requirements, special standards requirements, exposure to exchange rate fluctuations, tariffs and other trade barriers, difficulties in staffing and managing international operations, potentially adverse tax consequences, and uncertainties arising from local business practices and cultural considerations. Although substantially all of the Company's international sales currently are denominated in U.S. dollars, as the Company continues to expand its international operations, it expects its non-dollar-denominated sales and its exposure to gains and losses on international currency transactions to increase. The Company does not currently engage in transactions to hedge against the risk of currency fluctuations.

Because most sales are U.S.-dollar denominated, exchange rate fluctuations may make the Company's products noncompetitive in certain markets. Furthermore, continued growth in international markets for the Company's products depends in part on the pace at which various foreign countries are upgrading their telephone systems. There can be no assurance that these factors will not have a material adverse effect on the Company's business, results of operations or financial condition. See "Business--Distribution--International Distribution."

**Dependence on Key Personnel; Management of Growth.** The Company's success depends on its ability to attract and retain key personnel involved in engineering, research and development, marketing, sales, finance and administration. In particular, the Company depends to a significant degree on the efforts of its senior management team. The Company does not maintain material key person life insurance. The competition for skilled personnel is intense and the loss of the services of key persons in any functional area could have a material adverse effect on AVT's current operations and on new product development efforts. There can be no assurance that the Company will be able to hire or retain sufficient qualified staff to meet its goals. The Company's success also depends on the ability of its officers and key employees to manage growth successfully and to continue to successfully develop product enhancements and new products. The growth in the Company's business has placed, and is expected to continue to place, significant demands on the Company's management and operations. To manage its growth, the Company must continue to implement and improve its operational, financial and management information systems and expand, train and manage its employees. The Company's failure to manage growth effectively could have a material adverse effect on the Company's business, results of operations or financial condition.

**Dependence on Suppliers.** The Company uses standard computer hardware for its products. While most components utilized by the Company are readily available, voice processing circuit boards ("voice cards") and facsimile processing circuit boards ("fax cards") are available in quantity only from three domestic suppliers of voice cards and two domestic suppliers of fax cards. The Company has historically relied almost exclusively on Dialogic Corporation ("Dialogic") for its voice cards, and on Dialogic and Brooktrout Technologies, Inc. ("Brooktrout") for its fax cards, primarily because of volume price discounts and the cost and effort required to develop software for an alternate voice or fax card. If the Company were to experience significant delays, interruptions or reductions in its supply of voice or fax cards, or unfavorable changes to price and delivery terms, the Company's business, results of operations and financial condition would be materially adversely affected. See "Business--Manufacturing."

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**Possible Volatility of Stock Price.** The market price of the Company's Common Stock has been, and is likely to continue to be, volatile. Factors such as new product announcements or changes in product pricing policies by the Company or its competitors, quarterly fluctuations in the Company's operating results, announcements of technical innovations, announcements relating to strategic relationships or acquisitions, changes in earnings estimates by securities analysts and general conditions in the computer-telephony market, among other factors, may have a significant effect on the market price of the Company's Common Stock. The market prices of securities issued by many companies, particularly in high-technology industries, experience volatility for reasons unrelated to the operating performance of the specific companies. These broad market fluctuations may adversely affect the market price of the Company's Common Stock.

#### Item 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The information required by this item is incorporated by reference from the section labeled "Liquidity and Capital Resources" in Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations" of this Annual Report on Form 10-K.

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#### Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

##### AVT CORPORATION

##### CONSOLIDATED BALANCE SHEETS

<TABLE>  
<CAPTION>

	December 31,	
	1997	1998
ASSETS		(in thousands)
<S>	<C>	<C>

Current assets:		
Cash and cash equivalents.....	\$ 7,965	\$10,824
Short-term investments.....	14,268	28,225
Accounts receivable, less allowance of \$787,000 and \$766,000.....	10,098	14,153
Inventories.....	4,908	5,560
Deferred and prepaid income taxes.....	1,119	1,430
Prepaid expenses and other.....	968	1,393
	-----	-----
Total current assets.....	39,326	61,585
Equipment and leasehold improvements, net.....	2,364	3,263
Intangibles, net.....	8,815	7,677
Deferred income taxes.....	3,905	3,582
	-----	-----
	\$54,410	\$76,107
	=====	=====

LIABILITIES AND SHAREHOLDERS' EQUITY

Current liabilities:		
Accounts payable.....	\$ 2,352	\$ 3,669
Other current liabilities.....	6,114	8,669
Note payable--current portion.....	313	-
Income taxes payable.....	2,621	374
	-----	-----
Total current liabilities.....	11,400	12,712
	-----	-----
Commitments.....		
Shareholders' equity:		
Preferred stock, par value \$.01 per share, 2,000,000 shares authorized; none outstanding.....	--	--
Common stock, par value \$.01 per share, 60,000,000 shares authorized; 11,522,558 and 12,623,255 outstanding.....	115	126
Additional paid-in capital.....	31,604	40,368
Retained earnings.....	11,291	22,901
	-----	-----
Total shareholders' equity.....	43,010	63,395
	-----	-----
	\$54,410	\$76,107
	=====	=====

</TABLE>

See the accompanying notes to these consolidated financial statements.

AVT CORPORATION  
CONSOLIDATED STATEMENTS OF INCOME

<TABLE>

<CAPTION>

	Year Ended December 31,		
	1996	1997	1998
	-----	-----	-----
	(in thousands, except per share data)		
	<C>	<C>	<C>
Net sales.....	\$44,127	\$58,091	\$81,126
Cost of sales.....	16,895	21,066	28,098
	-----	-----	-----
Gross profit.....	27,232	37,025	53,028
	-----	-----	-----
Operating expenses:			
Research and development.....	4,149	6,719	8,082
Selling, general and administrative.....	14,509	19,212	27,663
Non-recurring charges.....	4,140	11,025	287
	-----	-----	-----
Total operating expenses.....	22,798	36,956	36,032
	-----	-----	-----
Operating income.....	4,434	69	16,996
	-----	-----	-----
Other income:			
Interest income.....	909	808	1,056
Other.....	10	262	89
	-----	-----	-----
Other income.....	919	1,070	1,145
	-----	-----	-----
Income before income tax expense.....	5,353	1,139	18,141
Income tax expense.....	3,419	410	6,531
	-----	-----	-----
Net income.....	\$ 1,934	\$ 729	\$11,610
	=====	=====	=====
Basic earnings per common share.....	\$0.18	\$0.06	\$0.96

Weighted average common shares outstanding.....	10,752	11,364	12,115
Diluted earnings per common share.....	\$0.17	\$0.06	\$0.88
Weighted average common and common equivalent shares outstanding.....	11,748	12,598	13,165

See the accompanying notes to these consolidated financial statements.

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AVT CORPORATION

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

Years Ended December 31, 1996, 1997 and 1998

<TABLE>  
<CAPTION>

	Common Stock		Additional	Deferred	Retained	Total
	Shares	Amount	paid-in	compensation	earnings	shareholders'
	-----		capital			equity
	-----		-----	-----	-----	-----
	(in thousands, except share data)					
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Balance at December 31, 1995.....	10,288,080	\$103	\$24,170	\$ (34)	\$ 8,650	\$32,889
Unrealized loss on investments.....	--	--	--	--	(22)	(22)
Exercise of stock options.....	236,748	2	616	--	--	618
Stock compensation expense.....	--	--	--	34	--	34
Stock issued in acquisition.....	326,598	3	3,427	--	--	3,430
Net income.....	--	--	--	--	1,934	1,934
	-----	-----	-----	-----	-----	-----
Balance at December 31, 1996.....	10,851,426	108	28,213	--	10,562	38,883
Stock issued in acquisition.....	191,032	2	666	--	--	668
Warrants issued in acquisition.....	--	--	700	--	--	700
Exercise of stock options.....	480,100	5	1,463	--	--	1,468
Tax benefit of stock options exercised.....	--	--	562	--	--	562
Net income.....	--	--	--	--	729	729
	-----	-----	-----	-----	-----	-----
Balance at December 31, 1997.....	11,522,558	115	31,604	--	11,291	43,010
Stock issued in acquisition.....	52,200	1	249	--	--	250
Exercise of stock options.....	1,048,497	10	3,866	--	--	3,876
Tax benefit of stock options exercised.....	--	--	4,649	--	--	4,649
Net income.....	--	--	--	--	11,610	11,610
	-----	-----	-----	-----	-----	-----
Balance at December 31, 1998.....	12,623,255	\$126	\$40,368	\$ --	\$22,901	\$63,395
	=====	=====	=====	=====	=====	=====

</TABLE>

See the accompanying notes to these consolidated financial statements.

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AVT CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

<TABLE>  
<CAPTION>

	Year Ended December 31,		
	-----	-----	-----
	1996	1997	1998
	-----	-----	-----
<S>	<C>	<C>	<C>
	(in thousands)		
Cash flows from operating activities:			
Net income.....	\$ 1,934	\$ 729	\$ 11,610
	-----	-----	-----
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization.....	1,395	2,083	2,908
Non-recurring charges.....	4,140	11,025	287
Stock compensation expense.....	34	--	--
Deferred income taxes.....	(137)	(3,406)	228
Changes in current assets and liabilities:			
Accounts receivable.....	5	(1,944)	(4,055)
Inventories.....	(551)	(1,239)	(652)
Prepaid expenses and other assets.....	(237)	(340)	(712)
Accounts payable.....	241	16	1,317

Accrued compensation and benefits.....	514	(52)	2,283
Income taxes payable.....	546	2,278	2,183
Other accrued liabilities.....	271	1,124	272
	-----	-----	-----
Total adjustments.....	6,221	9,545	4,059
	-----	-----	-----
Net cash provided by operating activities.....	8,155	10,274	15,669
	-----	-----	-----
Cash flows from investing activities:			
Purchase of equipment and leasehold improvements.....	(930)	(1,112)	(2,136)
Cash paid in acquisition, net of cash acquired.....	(3,318)	(15,426)	--
Purchase of short-term investments.....	(3,309)	--	(13,957)
Net proceeds from the sale of investments.....	--	1,216	--
Other intangibles and long-term assets.....	--	(64)	(280)
	-----	-----	-----
Net cash used in investing activities.....	(7,557)	(15,386)	(16,373)
	-----	-----	-----
Cash flows from financing activities:			
Repayment of long-term debt.....	(983)	(586)	(313)
Proceeds from exercise of common stock options.....	331	1,468	3,876
	-----	-----	-----
Net cash provided by (used in) financing activities.....	(652)	882	3,563
	-----	-----	-----
Net decrease in cash.....	(54)	(4,230)	2,859
Cash and cash equivalents at beginning of period.....	12,249	12,195	7,965
	-----	-----	-----
Cash and cash equivalents at end of period.....	\$12,195	\$ 7,965	\$ 10,824
	=====	=====	=====
Cash paid for interest.....	\$ 129	\$ 57	\$ 15

</TABLE>

See the accompanying notes to these consolidated financial statements.

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AVT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Nature of Business and Summary of Significant Accounting Policies

Nature of Business

AVT Corporation (the Company), a Washington corporation, provides software-based computer-telephony products for medium-sized enterprises. The Company's products address the voice messaging, call center, fax server and production fax markets and are distributed primarily through independent distributors and value-added resellers. The consolidated financial statements include the accounts of all subsidiaries, all of which are wholly owned, from the date of acquisition, including RightFAX, Inc., as of January 2, 1996, and CommercePath, Inc., as of October 22, 1997. All intercompany accounts have been eliminated.

Cash and Cash Equivalents

The Company's policy is to invest cash in excess of operating requirements in income-producing investments. For purposes of the consolidated statements of cash flows, the Company considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents. Cash and cash equivalents include all cash balances and highly liquid investments in a money market fund. Investments are recorded at cost, which approximates market prices.

Inventories

Inventories consist primarily of computer assemblies, components and related equipment, and are stated at the lower of cost (first-in, first-out) or market (net realizable value).

Equipment and Leasehold Improvements

Equipment and leasehold improvements are stated at cost and are depreciated on the straight-line method over the estimated useful lives of the assets, which range from three to five years. Equipment and leasehold improvements consist of the following:

<TABLE>

<CAPTION>

December 31,

-----  
1997                      1998  
-----

<u>&lt;S&gt;</u>	<u>&lt;C&gt;</u>	<u>&lt;C&gt;</u>
	(in thousands)	
Computers and other equipment.....	\$ 5,758	\$ 7,505
Leasehold improvements.....	427	606
Furniture and fixtures.....	584	794
	-----	-----
	6,769	8,905
Less accumulated depreciation.....	(4,405)	(5,642)
	-----	-----
Equipment and leasehold improvements, net.....	\$ 2,364	\$ 3,263
	=====	=====

</TABLE>

APPLIED VOICE TECHNOLOGY, INC  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

Intangibles

Goodwill is being amortized using the straight-line method over its estimated useful life of seven years. License agreements are amortized using the straight-line method over the remaining lives of the related patents, which range from approximately 6 to 12 years.

<TABLE>  
<CAPTION>

	December 31,	
	1997	1998
	-----	
	(in thousands)	
<u>&lt;S&gt;</u>	<u>&lt;C&gt;</u>	<u>&lt;C&gt;</u>
Goodwill on CommercePath acquisition.....	\$ 1,793	\$ 1,829
Goodwill on RightFAX acquisition.....	5,406	5,906
License agreements.....	4,516	4,516
	-----	-----
	11,715	12,251
Less accumulated amortization.....	(2,900)	(4,574)
	-----	-----
Intangibles, net.....	\$ 8,815	\$ 7,677
	=====	=====

</TABLE>

Other Current Liabilities

<TABLE>  
<CAPTION>

	December 31,	
	1997	1998
	-----	
	(in thousands)	
<u>&lt;S&gt;</u>	<u>&lt;C&gt;</u>	<u>&lt;C&gt;</u>
Accrued compensation and benefits.....	\$1,485	\$3,768
Acquisition costs.....	1,336	250
Deferred maintenance revenue.....	1,891	2,210
Other.....	1,402	2,441
	-----	-----
Other current liabilities.....	\$6,114	\$8,669
	=====	=====

</TABLE>

Use of Estimates

The preparation of the Company's consolidated financial statements, in conformity 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. Certain prior period balances have been reclassified to conform with the current period presentation.

Revenue Recognition

Revenues from sales to dealers are recognized when the products are shipped. When the Company has an installation obligation, revenues are recognized when product installation is complete. Revenues for software maintenance contracts are recognized over the maintenance periods, generally one year. Revenues from extended warranty agreements are recognized over the lives of the related service contracts on the straight-line method. The Company accrues estimated costs of technical support to customers as related revenues are recognized.



Research and development costs are expensed as incurred. The Company has not capitalized any software development costs, as technological feasibility is not generally established until substantially all development is complete.

AVT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

Earnings Per Share

Basic earnings per common share were computed by dividing net income by the weighted average number of shares of common stock outstanding during the year. Diluted earnings per common share were computed by dividing net income by the sum of the weighted average number of shares of common stock outstanding during the year plus the net additional shares that would have been issued had all dilutive options been exercised less shares that would be repurchased with the proceeds from such exercise. Dilutive options are those that have an exercise price which is less than the average stock price during the year.

The computation of diluted earnings per common share is as follows:

<TABLE>  
<CAPTION>

	Year Ended December 31,		
	1996	1997	1998
	(in thousands, <C>)	except per share amounts <C>	<C>
<S>			
Diluted earnings per common share:			
Net income.....	\$ 1,934	\$ 729	\$11,610
Weighted average common shares outstanding.....	10,752	11,364	12,115
Plus: dilutive options assumed exercised.....	1,592	2,790	2,364
Less: shares assumed repurchased with proceeds from exercise.....	(786)	(1,624)	(1,314)
Plus: other common stock equivalents.....	190	68	-
Weighted average common and common equivalent shares outstanding.....	11,748	12,598	13,165
Diluted earnings per common share.....	\$0.17	\$0.06	\$0.88

</TABLE>

Concentration of Credit Risk; Export Sales

The Company achieves broad U.S. market coverage for its products primarily through a nationwide network of telephony-oriented dealers and computer-oriented value-added resellers. For the years ended December 31, 1998, 1997 and 1996, no customer represented 10% or greater of the Company's net sales. The Company performs ongoing credit evaluations of its customers' financial conditions and, generally, no collateral is required.

The Company's export sales were as follows:

<TABLE>  
<CAPTION>

	Year Ended December 31,		
	1996	1997	1998
	(in thousands)		
<S>	<C>	<C>	<C>
Canada.....	\$2,660	\$ 3,395	\$ 3,914
Other.....	5,338	8,757	11,044
	\$7,998	\$12,152	\$14,958

</TABLE>

AVT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

Segment Reporting

The Company adopted Statement of Accounting Standard No. 131 "Disclosures about Segments of an Enterprise and Related Information " (SFAS No. 131) during 1998. SFAS 131 requires companies to disclose certain information about operating segments. Based on the criteria within SFAS No. 131, the Company has determined that it has one reportable segment, computer telephony products.

Sales of the Company's product by categories and amount are as follows:

<TABLE>  
<CAPTION>

	Year Ended December 31,		
	1996	1997	1998
	(in thousands)		
<S>	<C>	<C>	<C>
Enhanced fax products.....	\$13,580	\$24,253	\$46,532
Advanced messaging and call center products.....	18,911	24,276	28,159
Basic messaging products.....	11,636	9,562	6,435
	-----	-----	-----
	\$44,127	\$58,091	\$81,126
	=====	=====	=====

</TABLE>

2. Income Taxes

Income taxes are provided for in the consolidated statements of income using the asset and liability method. The difference between the provision for income taxes and the statutory tax rate applied to income before income tax expense is due to certain expenses not being deductible for tax purposes and research and experimentation credits.

The following is a reconciliation from the U.S. statutory rate to the effective tax rate:

<TABLE>  
<CAPTION>

	Year Ended December 31,					
	1996		1997		1998	
	Amount	%	Amount	%	Amount	%
<S>	<C>	<C>	<C>	<C>	<C>	<C>
	(dollars in thousands)					
Tax at statutory rate.....	\$1,820	34.0%	\$ 387	34.0%	\$6,168	34.0%
Research and experimentation credit.....	(69)	(1.3)	(105)	(9.2)	(150)	(1.0)
Write-off of purchased, in-process research and development.....	1,408	26.3	--	--	--	--
Nondeductible goodwill amortization.....	101	1.9	230	20.2	319	1.8
Nontaxable interest income.....	(217)	(4.0)	(235)	(20.6)	(227)	(1.3)
State taxes and other.....	376	7.0	133	11.6	421	2.5
	-----	-----	-----	-----	-----	-----
Income tax expense.....	\$3,419	63.9%	\$ 410	36.0%	\$6,531	36.0%
	=====	=====	=====	=====	=====	=====

</TABLE>

AVT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

Income tax expense and cash paid for income taxes are as follows:

<TABLE>  
<CAPTION>

	Year Ended December 31,		
	1996	1997	1998
	(in thousands)		
<S>	<C>	<C>	<C>
Current.....	\$3,556	\$ 4,378	\$6,303
Deferred.....	(137)	(3,968)	228
	-----	-----	-----
Total income tax expense.....	\$3,419	\$ 410	\$6,531
	=====	=====	=====
Cash paid for income taxes.....	\$3,010	\$ 1,539	\$4,101
	=====	=====	=====

</TABLE>

Deferred taxes result from temporary differences relating to items that are expensed for financial reporting, but are not currently deductible for income tax purposes.

Significant components of the Company's deferred tax asset as of December 31, 1997 and 1998 are as follows:

	December 31,	
	1997	1998
	(in thousands)	
<S>	<C>	<C>
Deferred tax assets:		
Accounts receivable allowances.....	\$ 283	\$ 276
Inventories.....	75	85
Depreciation and amortization.....	64	-
Accrued compensation and benefits.....	171	192
Purchased research and development.....	3,841	3,549
Deferred Revenue.....	-	468
Other.....	590	442
	-----	-----
Deferred tax assets and prepaid income taxes.....	\$5,024	\$5,012
	=====	=====

</TABLE>

### 3. Shareholders' Equity

On April 23, 1998, the Company announced that its Board of Directors approved a two-for-one stock split of the Common Stock effected in the form of a stock dividend. Shareholders received an additional share of common stock for every share held on the record date of May 4, 1998. The additional shares were payable on May 11, 1998. Accordingly, the accompanying financial statements have been restated to reflect this stock split.

On April 20, 1998, the Company's Board of Directors approved an increase of the authorized shares of Common Stock, from 30 million to 60 million and an increase of the authorized shares of Preferred Stock from one million to two million, in order to reflect the stock split. Shareholder approval of these increases was not required.

The Company has stock option plans under which employees, directors, officers and other agents may be granted options to purchase common stock. The Company has reserved approximately 5,700,000 shares of common stock for issuance pursuant to these plans upon exercise of outstanding options and upon exercise of options to be granted in the future. Options generally vest over three to four years and expire 10 years from the date of grant. The options are exercisable at prices determined at the discretion of the Board of Directors. The Company accounts for these plans under Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," under which no compensation cost has been recognized and is based on the difference between the exercise price and fair market value at the date of grant, if any. Had compensation cost for stock option grants made in 1996, 1997 and 1998 been determined using the fair value method consistent with Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based

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Compensation" (SFAS 123), the Company's net income and earnings per share would have been reduced to the following pro forma amounts:

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#### AVT CORPORATION

##### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

		Year Ended December 31,		
		1996	1997	1998
		( in thousands except per share data)		
<S>	<C>	<C>	<C>	<C>
Net Income:	As Reported.....	\$1,934	\$ 729	\$11,610
	Pro Forma.....	\$ 793	\$ (441)	\$ 9,374

Basic EPS:	As Reported.....	\$ 0.18	\$ 0.06	\$ 0.96
	Pro Forma.....	\$ 0.08	\$ (0.04)	\$ 0.77
Diluted EPS:	As Reported.....	\$ 0.17	\$ 0.06	\$ 0.88
	Pro Forma.....	\$ 0.07	\$ (0.04)	\$ 0.74

</TABLE>

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions used for grants during the year ended December 31, 1998: risk-free interest rates of 6.25%; expected lives of five years; expected volatility of 44%; and \$0 dividends. For 1997 the assumptions were: risk-free interest rates of 6.85%; expected lives of five years; expected volatility of 49%; and \$0 dividends. For 1996 the following assumptions were used: risk-free interest rates of 6.25%; expected lives of five years; expected volatility of 45%; and \$0 dividends.

#### Stock Option Plans

A summary of the status of the Company's stock option plans at December 31, 1996, 1997 and 1998, and the changes during the years then ended, is presented in the table and narrative below:

<TABLE>  
<CAPTION>

	1996		1997		1998	
	Shares	Wtd. Avg. Ex. Price	Shares	Wtd. Avg. Ex. Price	Shares	Wtd. Avg. Ex. Price
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Outstanding at beginning of period.....	1,476,568	\$1.48	2,900,730	\$ 4.44	2,840,210	\$ 5.71
Granted.....	1,783,800	\$6.63	483,600	\$10.86	852,978	\$18.82
Exercised.....	(236,748)	\$1.41	(480,102)	\$ 3.06	(1,018,344)	\$ 3.55
Canceled.....	(122,890)	\$6.51	(64,018)	\$ 6.95	(67,319)	\$14.19
Outstanding at end of period.....	2,900,730	\$4.44	2,840,210	\$ 5.71	2,607,525	\$10.62
Exercisable at end of period.....	1,196,472	\$1.38	1,472,694	\$ 3.46	1,333,282	\$ 6.17
Weighted average fair value of options granted.....		\$2.89		\$ 5.51		\$ 9.06

</TABLE>

Options outstanding have exercise prices ranging from \$0.50 to \$23.25 per share, with weighted average remaining contractual lives of 7.2, 6.9 and 7.3 years at December 31, 1996, 1997 and 1998, respectively. At December 31, 1998, 1,879,325 shares of the Company's common stock were available for future grant under the Company's stock option plans. Information relating to stock options outstanding and stock options exercisable at December 31, 1998 is as follows:

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#### AVT CORPORATION

##### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

<TABLE>  
<CAPTION>

Range of Exercise Prices	Options Outstanding			Options Exercisable		
	Shares	Wtd. Avg. Remaining Contractual Life	Wtd. Avg. Ex. Price	Shares	Wtd. Avg. Ex. Price	
<S>	<C>	<C>	<C>	<C>	<C>	
\$ 0.50 - \$8.25.....	1,505,292	6	\$ 5.50	1,218,875	\$ 5.52	
\$ 8.26 - \$16.50.....	574,487	9	\$14.08	114,307	\$13.07	
\$16.51 - \$23.25.....	527,748	9	\$20.91	100	\$22.50	
	2,607,525	7	\$10.63	1,333,282	\$ 6.17	
	=====	=	=====	=====	=====	

</TABLE>

#### Warrants

At December 31, 1998, there were outstanding warrants to purchase 174,560 shares of the Company's common stock at \$6.68 per share. The warrants were issued in connection with the Telcom Technologies Inc. acquisition discussed in Note 8 below.

#### 4. Line of Credit

At December 31, 1998, the Company had a \$4.0 million unsecured revolving line of credit, none of which was used during the years ended December 31, 1997 and 1998. The Company's line of credit expires in May 1999, and contains certain financial covenants and restrictions as to various matters, including the Company's ability to pay cash dividends without the bank's prior approval. The Company is currently in compliance with such financial covenants and restrictions. Borrowings under the line of credit bear interest at the bank's prime rate or, at the Company's option, its interbank offering rate plus 1.50%. At December 31, 1998, the bank's prime rate was 7.75%, and its interbank offering rate was 5.1%.

#### 5. Short-Term Investments

The Company has classified its investments as "available-for-sale" and recorded these investments at estimated fair value, with unrealized gains and losses, when material, reported as a component of shareholders' equity.

Interest income is recorded using an effective interest rate, with the associated premium or discount amortized to interest income over the term of the investment. The cost of securities sold is based upon the specific identification method. Available-for-sale securities as of December 31, 1997 and 1998 consisted of municipal notes and bonds whose amortized cost approximates estimated fair value. As of December 31, 1997 and 1998 average maturity for these investments was four and eight months respectively.

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### AVT CORPORATION

#### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

#### 6. Commitments and Contingencies

##### Leases

The Company leases its office space under noncancelable operating leases. Rent expense under the noncancelable leases amounted to \$654,000 in 1996, \$1,048,000 in 1997 and \$1,290,000 in 1998. Future minimum lease payments under noncancelable operating leases are as follows (in thousands):

<TABLE>

<S>	<C>
1999.....	\$1,403
2000.....	1,378
2001.....	1,251
2002.....	806
2003.....	67
	-----
	\$4,905
	=====

</TABLE>

##### Retirement Savings Plan

The Company offers a 401(k) profit-sharing plan to substantially all of its employees. Company contributions are determined annually and are at the discretion of the Board of Directors. Contributions made to the plan were \$54,000 in 1996, \$165,000 in 1997 and \$235,000 in 1998.

##### License Agreements

In connection with the acquisition of a business in 1989, the Company agreed to make royalty payments from future sales of the Company's products, up to a maximum of \$2,800,000 in total, payable up to \$70,000 per quarter, before adjustment for increases in the consumer price index. In February 1995, the Company made a prepayment of \$1,808,000 to satisfy this royalty commitment. This intangible is being amortized over the remainder of the original agreement's term (67 months). Amounts charged to expense under this agreement were \$324,000 in each of 1996, 1997 and 1998.

In addition to the agreement mentioned above, the Company has two nonexclusive licenses to sell products using patented technology. In exchange for the licenses, the Company has made quarterly payments equal to 6% of net revenues from sales of components utilized in the Company's products that use the licensed technology.

In September 1995, the Company renegotiated its royalty obligation for one of these licenses by issuing a note in the amount of \$1,937,000, payable in 12 equal quarterly installments of \$161,417 each, with the first installment paid upon the signing of the agreement. The Company accrued interest expense at an imputed rate of 8.75% per annum. This note was satisfied at December 31, 1998.

The Company recorded an intangible for this prepayment in the amount of \$1,725,000. The intangible is being amortized on a straight-line basis over the remaining average lives of the related patents (approximately 12 years).

In July 1996, the Company renegotiated its royalty obligation for the second license by issuing a note in the amount of \$450,000, payable over two quarters, with the first installment paid upon the signing of the agreement. The Company accrued interest expense at an imputed rate of 8.5% per annum. This note was satisfied at December 31, 1996. The Company recorded an intangible for this prepayment in the amount of \$446,000. The intangible is being amortized on a straight-line basis over the remaining average lives of the related patents (approximately seven years). Amounts charged to expense for the two nonexclusive licenses were \$212,000 in each of 1996, 1997 and 1998.

AVT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

Legal Proceedings

In May 1998, CallWare brought suit against AVT in federal court in Salt Lake City, Utah, alleging various claims relating to purported false advertising by AVT. (CallWare Technologies, Inc. v. Applied Voice Technology, Inc., Case No. 2:98CV 0329K.) CallWare has claimed \$20 million in monetary damages, and an additional \$60 million in punitive damages. The suit is in the discovery phase, and an initial pretrial conference was held on January 14, 1999 and a trial date of January 10, 2000 has been set. AVT believes that CallWare's claims are without merit and is vigorously defending the lawsuit.

7. Supplemental Information--Valuation and Qualifying Accounts

<TABLE>  
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Description	Balance at Beginning of period	Charged to costs and expenses	Charged to other accounts	Deductions(1)	Balance at end of period
(in thousands)					
Allowance for doubtful accounts:					
<S>	<C>	<C>	<C>	<C>	<C>
December 31, 1996.....	\$483	248	--	125	\$606
December 31, 1997.....	\$606	208	97	124	\$787
December 31, 1998.....	\$787	218	--	239	\$766

</TABLE>

(1) Amounts include write-offs of accounts receivable deemed uncollectable.

8. Businesses Acquired

On January 3, 1997, the Company acquired selected assets and liabilities of Telcom Technologies Inc., a developer of NT-based open-architecture automatic call distribution systems. The purchase price for the acquisition was \$3.5 million in cash, plus warrants to purchase 200,000 shares of the Company's common stock at \$6.68 per share, which may be exercised at any time prior to January 3, 2002. The Company accounted for the business combination as a purchase and recognized a nonrecurring charge of \$3.9 million in the first quarter of 1997, representing the value of the purchased, in-process research and development.

On October 22, 1997, the Company acquired all the outstanding capital stock of CommercePath, Inc. (CommercePath) from Forest City Trading Group, Inc. for \$10.4 million in cash. The Company accounted for the business combination as a purchase and recorded a nonrecurring charge of \$7.1 million in the fourth quarter of 1997, representing the value of the purchased, in-process research and development, and recorded \$1.8 million of goodwill that it will amortize over seven years.

The pro forma unaudited consolidated operating results of the Company for the years ended December 31, 1996 and 1997, assuming the acquisition of CommercePath had been made as of January 1, 1996 and 1997, respectively, are summarized below:

<TABLE>  
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1996		1997	
Actual	Pro Forma (unaudited)	Actual	Pro Forma (unaudited)
-----	-----	-----	-----

<S>	<C>	<C>	<C>	<C>
	(in thousands, except per share data)			
Net sales.....	\$44,127	\$50,401	\$58,091	\$63,468
Net income.....	\$ 1,934	\$ 1,811	\$ 729	\$ 226
Diluted earnings per share.....	\$ 0.17	\$ 0.16	\$ 0.06	\$ 0.02

</TABLE>

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AVT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

These pro forma results have been prepared for comparative purposes only and include certain adjustments such as additional amortization resulting from allocating a portion of the purchase price to goodwill. They do not purport to be indicative of the results of operations which actually would have resulted had the combination been in effect on January 1, 1996 or January 1, 1997, as the case may be, or future results of operations of the consolidated entity.

9. Quarterly Financial Data and Market Information (unaudited)

<TABLE>

<CAPTION>

	Quarter Ended							
	March 31, 1997	June 30, 1997	Sept. 30, 1997	Dec. 31, 1997	March 31, 1998	June 30, 1998	Sept. 30, 1998	Dec. 31, 1998
	(in thousands except per share data)							
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Net sales.....	\$12,062	\$13,660	\$14,781	\$17,588	\$17,166	\$19,439	\$20,834	\$23,687
Cost of sales.....	4,590	4,958	5,475	6,043	6,344	6,969	6,937	7,848
Gross profit.....	7,472	8,702	9,306	11,545	10,822	12,470	13,897	15,839
Operating expenses:								
Research and development.....	1,498	1,571	1,678	1,972	1,927	2,001	2,073	2,081
Selling, general and administrative.....	4,183	4,640	4,599	5,790	5,846	6,555	7,329	7,933
Non-recurring charges.....	3,898	--	--	7,127	287	--	--	--
Total operating expenses.....	9,579	6,211	6,277	14,889	8,060	8,556	9,402	10,014
Operating income (loss).....	(2,107)	2,491	3,029	(3,344)	2,762	3,914	4,495	5,825
Other income, net.....	240	278	265	287	235	320	241	348
Income (loss) before income tax expense.....	(1,867)	2,769	3,294	(3,057)	2,997	4,234	4,736	6,173
Income tax expense (benefit).....	(672)	997	1,185	(1,100)	1,079	1,524	1,705	2,223
Net income (loss).....	\$(1,195)	\$ 1,772	\$ 2,109	\$(1,957)	\$ 1,918	\$ 2,710	\$ 3,031	\$ 3,950
Diluted earnings (loss) per common share (1).....	\$ (0.11)	\$ 0.14	\$ 0.17	\$ (0.17)	\$ 0.15	\$ 0.20	\$ 0.22	\$ 0.29
Net income excluding nonrecurring Items.....	\$ 1,300	\$ 1,772	\$ 2,109	\$ 2,604	\$ 2,102	\$ 2,710	\$ 3,031	\$ 3,950
Diluted earnings per common share excluding nonrecurring items(1).....	\$ 0.12	\$ 0.14	\$ 0.17	\$ 0.20	\$ 0.16	\$ 0.20	\$ 0.22	\$ 0.29
Weighted average common and common equivalent shares outstanding.....	11,208	12,254	12,686	11,520	13,108	13,401	13,640	13,615
Stock price range (2)								
High.....	10.06	9.69	15.06	16.25	20.31	23.50	25.75	29.69
Low.....	5.88	5.69	8.69	9.50	13.38	17.13	19.63	12.19

</TABLE>

- (1) Earnings per common share is computed independently for each of the quarters presented. Therefore, the sum of the quarterly net income per share amounts will not necessarily equal the total for the year.
- (2) The Company's common stock is traded on the Nasdaq National Market under the symbol "AVTC." As of December 31, 1998, there were approximately 70 shareholders of record of the Company's common stock. The Company has not paid any cash dividends on its common stock.

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REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

We have audited the accompanying consolidated balance sheets of AVT Corporation (a Washington corporation) and its subsidiaries as of December 31, 1997 and 1998, and the related consolidated statements of income, shareholders' equity and cash flows for each of the three years in the period ended December 31, 1998. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. 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 financial statements referred to above present fairly, in all material respects, the financial position of AVT Corporation and its subsidiaries as of December 31, 1997 and 1998, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 1998, in conformity with generally accepted accounting principles.

ARTHUR ANDERSEN LLP

Seattle, Washington,  
January 28, 1999

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

None.

PART III

Item 10-13. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

The information required by Part III (Item 10-13) is incorporated by reference to information in the Company's definitive proxy statements which will be filed pursuant to Regulation 14a within 120 days of December 31, 1998.

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PART IV

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

A. LIST OF DOCUMENTS FILED AS A PART OF THIS REPORT

1. Index financial statements

<TABLE>

<CAPTION>

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<C>

- . Consolidated Balance Sheets--December 31, 1998 and 1997
- . Consolidated Statements of Income--Years ended December 31, 1998, 1997 and 1996
- . Consolidated Statements of Shareholders' Equity--Years ended December 31, 1998, 1997 and 1996
- . Consolidated Statements of Cash Flows--Years ended December 31, 1998, 1997 and 1996
- . Notes to Consolidated Financial Statements
- . Report of Independent Public Accountants

2. Index to Financial Statement Schedules

- . See Note 8 of Notes to Consolidated Financial Statements--Valuation and Qualifying--Accounts

3. Index to Exhibits

Exhibit No. Description

Exhibit No.	Description
3.1	Restated Articles of Incorporation of AVT Corporation (A) (Exhibit 3.1)
3.2	Amended and Restated Bylaws of AVT Corporation (A) (Exhibit 3.2)
4.1	Form of Warrant, dated January 3, 1997, issued by Applied Voice Technology, Inc. to shareholders of Telcom Technologies, Inc. (E) (Exhibit 4.1)
+10.1	1994 Nonemployee Directors Stock Option Plan (A) (Exhibit 10.1)
+10.2	Restated 1989 Stock Option Plan (F)
+10.3	1986 Incentive Stock Option Plan (A) (Exhibits 10.3)
+10.4	Management Incentive Compensation Plan (A) (Exhibit 10.4)



+10.5	Employment Agreement dated May 1, 1993 between Applied Voice Technology, Inc. and Richard J. LaPorte (A) (Exhibit 10.5)
+10.6	Form of Indemnification Agreement between Applied Voice Technology and each of its directors and officers (A) (Exhibit 10.6)
10.7	Loan Agreement and Promissory Note dated May 16, 1997 between U.S. Bank of Washington and Applied Voice Technology, Inc.(G) (Exhibit 10.7)
10.8	Lease Agreement dated June 30, 1989 between Riggs National Bank of Washington D.C. and Applied Voice Technology, Inc. as amended (A) (Exhibit 10.11)
10.9	Second Amendment to Lease Agreement dated February 1, 1995 between Riggs National Bank of Washington D.C. and Applied Voice Technology, Inc. (D) (Exhibit 10.11)
10.10	Third Amendment to Lease Agreement dated May 28, 1997 between Riggs National Bank of Washington D.C. and Applied Voice Technology, Inc. (G) (Exhibit 10.10)
10.11	Lease Agreement dated May 28, 1997 between Riggs National Bank of Washington D.C. and Applied Voice Technology, Inc. (G) (Exhibit 10.11)
#10.12	Amended Patent License Agreement dated September 29, 1995 between Syntellect Technology Corp. and Applied Voice, Technology Inc. (B) (Exhibit 10.1)
10.13	Master Software Manufacturing License Agreement dated June 11, 1992 between Intelligent Environments Inc. and Applied Voice Technology, Inc. as amended (A) (Exhibit 10.16)
10.14	Agreement and Plan of Merger among Applied Voice Technology, Inc., Cracchiolo & Feder, Inc., the shareholders of Cracchiolo & Feder, Inc. and CFI Acquisition Corp., dated as of January 2, 1996. (C) (Exhibit 10.1)
10.15	Registration Rights Agreement among Applied Voice Technology, Inc., Joseph J. Cracchiolo and Bradley H. Feder, dated as of January 2, 1996 (C) (Exhibit 10.2)
21.1	Subsidiaries of Applied Voice Technology, Inc.(G) (Exhibit 21.1)
23.1	Consent of Arthur Andersen, LLP.
27.1	Financial Data Schedule for Year End 12/31/1998

</TABLE>

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- (A) Previously filed with, and incorporated herein by reference to, designated exhibits to Registration Statement on Form S-1 of Applied Voice Technology, Inc. File No. 33-85452.
- (B) Previously filed with, and incorporated by reference to, designated exhibit to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 1995.
- (C) Previously filed with, and incorporated by reference to, designated exhibit to the Company's Current Report on Form 8-K dated January 2, 1996.
- (D) Previously filed with, and incorporated by reference to, designated exhibit to the Company's 1995 Annual Report on Form 10-K.
- (E) Previously filed with, and incorporated by reference to, designated exhibit to the Company's Current Report on Form 8-K dated January 3, 1997.
- (F) Previously filed with, and incorporated by reference to, appendix A to the Company's definitive Proxy Statement dated April 16, 1996.
- (G) Previously filed with, and incorporated by reference to, designated exhibit to the Company's 1997 Annual Report on Form 10-K.
- + Management contract or compensatory plan or arrangement.
- # Confidential treatment requested for a portion of this agreement.

B. Reports on Form 8-K

The Company did not file any reports on Form 8-K during the quarter ended December 31, 1998.

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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 the undersigned, thereunto duly authorized, in the City of Kirkland, State of Washington, on the 22nd day of March, 1999.

AVT CORPORATION

By: /s/ Richard J. LaPorte

-----  
Richard J. LaPorte  
President and Chief Executive Officer

Pursuant to the requirements of the Securities Act of 1934, this Report has been signed by the following persons in the capacities indicated below on the 22nd day of March, 1999.

<TABLE>

<CAPTION>

Signature	Title
<S>	<C>

/s/ Richard J. LaPorte ----- Richard J. LaPorte	President, Chief Executive Officer and Director (Principal Executive Officer)
/s/ Roger A. Fukai ----- Roger A. Fukai	Executive Vice President of Finance and Administration and Chief Financial Officer (Principal Financial and Accounting Officer)
/s/ James S. Campbell ----- James S. Campbell	Director
/s/ Robert L. Lovely ----- Robert L. Lovely	Director
/s/ William L. True ----- William L. True	Director
/s/ Robert F. Gilb ----- Robert F. Gilb	Director

</TABLE>

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EXHIBIT INDEX

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<CAPTION>	
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- (E) Previously filed with, and incorporated by reference to, designated exhibit to the Company's Current Report on Form 8-K dated January 3, 1997.
- (F) Previously filed with, and incorporated by reference to, appendix A to the

Company's definitive Proxy Statement dated April 16, 1996.

(G) Previously filed with, and incorporated by reference to, designated exhibit to the Company's 1997 Annual Report on Form 10-K.

+ Management contract or compensatory plan or arrangement.

# Confidential treatment requested for a portion of this agreement.

CONSENT OF INDEPENDENT PUBLIC ACCOUNTANTS

As independent public accountants, we hereby consent to the incorporation of our reports included in this Form 10-K, into the Company's previously filed Form S-8 Registration Statements, File Nos. 33-92438, 333-85452, 333-38557, 333-42279 and 333-71623.

/s/ Arthur Andersen LLP

Seattle, Washington,  
March 22, 1999

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