



Notes to the Consolidated Financial Statements

For the year ended 31 December 2004

1. GROUP RESTRUCTURING AND BASIS OF PRESENTATION OF FINANCIAL STATEMENTS

The Company was incorporated in the Cayman Islands under the Companies Law as an exempted company with limited liability on 5 January 2004.

Pursuant to a group reorganisation (the "Reorganisation") in preparation for the listing of the Company's shares, the Company became the holding company of the Group on 27 October 2004. Details of the Reorganisation are set out in the prospectus issued by the Company on 8 November 2004. Its shares were listed on The Stock Exchange of Hong Kong Limited on 18 November 2004 (the "Listing Date").

The Group resulting from the Reorganisation is regarded as a continuing entity. Accordingly, the financial statements of the Group have been prepared using the principle of merger accounting in accordance with Statement of Standard Accounting Practice 27 "Accounting for Group Reconstructions" issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA").

The Company is an investment holding company. The principal activities of its subsidiaries are set out in note 14.

2. POTENTIAL IMPACT ARISING FROM THE RECENTLY ISSUED ACCOUNTING STANDARDS

In 2004, the HKICPA issued a number of new and revised Hong Kong Accounting Standards and Hong Kong Financial Reporting Standards (herein collectively referred to as the "New HKFRSs") which are effective for accounting periods beginning on or after 1 January 2005. The Group has not early adopted these New HKFRSs in the financial statements for the year ended 31 December 2004.

The Group has commenced considering the potential impact of these New HKFRSs but is not yet in a position to determine whether these New HKFRSs would have a significant impact on how its results of operations and financial position are prepared and presented. These New HKFRSs may result in changes in future as to how the results and financial position are prepared and presented.

3. SIGNIFICANT ACCOUNTING POLICIES

The financial statements have been prepared under the historical cost convention as modified for the revaluation of certain investments in securities and have been prepared in accordance with accounting principles generally accepted in Hong Kong. The principal accounting policies adopted are set out below:

BASIS OF CONSOLIDATION

The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries made up to 31 December each year. The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

All significant intercompany transactions and balances between group enterprises are eliminated on consolidation.

INVESTMENTS IN SUBSIDIARIES

Investments in subsidiaries are included in the Company's balance sheet at cost less any identified impairment loss.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

INTEREST IN AN ASSOCIATE

The consolidated income statement includes the Group's share of the post-acquisition results of its associate for the year. In the consolidated balance sheet, interest in an associate is stated at the Group's share of the net assets of the associate less any identified impairment loss.

INVESTMENT IN SECURITIES

Investment in securities is recognised on a trade date basis and is initially measured at cost.

At subsequent reporting dates, debt securities that the Group has the expressed intention and ability to hold to maturity (held-to-maturity debt securities) are measured at amortised cost, less any impairment loss recognised to reflect irrecoverable amounts. The annual amortisation of any discount or premium on the acquisition of a held-to-maturity security is aggregated with other investment income receivable over the terms of the instrument so that the revenue recognised in each period represents a constant yield on the investment.

Investments other than held-to-maturity debt securities are classified as investment securities and other investments.

Investment securities, which are securities held for an identified long-term strategic purpose, are measured at subsequent reporting dates at cost, as reduced by any impairment loss that is other than temporary.

Other investments are measured at fair value, with unrealised gains and losses included in net profit or loss for the year.

REVENUE RECOGNITION

Income from sale of hardware and third party software is recognised when goods are delivered or accepted by the customers, whenever is later. Income from sale of self-developed software and provision of system integration services is recognised based on the percentage of completion method.

Maintenance and training income is recognised when services are provided.

Interest income is accrued on a time basis, by reference to the principal outstanding and at the interest rate applicable.

Value-added tax refund income is recognised upon the relevant conditions were fulfilled.

RESEARCH AND DEVELOPMENT EXPENDITURE

Expenditure on research activities is recognised as an expense in the year in which it is incurred.

An internally-generated intangible asset arising from development expenditure is recognised only if it is anticipated that the development costs incurred on a clearly-defined project will be recovered through future commercial activity. The resultant asset is amortised on a straight-line basis over its useful life with a maximum of two years.

Where no internally-generated intangible asset can be recognised, development expenditure is recognised as an expense in the year in which it is incurred.



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3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are stated at cost less accumulated depreciation and accumulated impairment losses.

Depreciation is provided to write off the cost of property, plant and equipment over their estimated useful lives and after taking into account their estimated residual value, using the straight-line method, at the following rates per annum:

Leasehold improvements	Over the term of the lease
Furniture and fixtures	19%
Computers and equipment	19%
Motor vehicles	12%

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the income statement.

IMPAIRMENT

At each balance sheet date, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. Impairment losses are recognised as an expense incurred.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised as income immediately.

INVENTORIES

Inventories are stated at the lower of cost and net realisable value. Cost is calculated using weighted average method.

GOVERNMENT GRANTS

Government grants are recognised as income when there is reasonable assurance that the conditions attaching to such grants are complied with and the rights to receive payment have been established.

TAXATION

Income tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years, and it further excludes items that are never taxable or deductible.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

TAXATION (Continued)

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences, and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the year when the liability is settled or the asset is realised. Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

FOREIGN CURRENCIES

Transactions in currencies other than Renminbi ("RMB") are initially recorded at the rates of exchange ruling on the dates of the transactions. Monetary assets and liabilities denominated in currencies other than RMB are retranslated at the rates ruling on the balance sheet date. Profits and losses arising on exchange are dealt with in the income statement.

On consolidation, the assets and liabilities of the Group's overseas operations are translated at exchange rates prevailing on the balance sheet date. Income and expense items are translated at the average exchange rates for the year. Exchange differences arising, if any, are classified as equity and transferred to the Group's translation reserve. Such translation differences are recognised as income or as expenses in the year in which the operation is disposed of.

OPERATING LEASES

Rentals under operating leases are charged to the income statement on a straight line basis over the relevant lease term.

RETIREMENT BENEFIT COSTS

Payments to defined contribution retirement benefits scheme are charged as an expense as they fall due.

4. TURNOVER AND SEGMENT INFORMATION

The Group is principally engaged in the development and provision of operational support system products and solutions in the People's Republic of China (the "PRC").

Turnover, which is stated net of value-added tax and other sales tax and returns, represents amounts received and receivable for sale of hardware and software and service income from provision of system integration and maintenance, training and other services.



Notes to the Consolidated Financial Statements

For the year ended 31 December 2004

4. TURNOVER AND SEGMENT INFORMATION (Continued)

BUSINESS SEGMENTS

The Group is currently organised into four revenue streams - sale of self-developed software, sale of third party software and hardware in relation to system integration, system integration and maintenance, training and other services. These revenue streams are the basis on which the Group reports its primary segment information.

Segment information about these businesses is presented below:

For the year ended 31 December 2004

	Sale of self- developed software RMB	Sale of third party software and hardware in relation to system integration business RMB	System integration RMB	Maintenance, training and other services RMB	Consolidated RMB
TURNOVER					
External sales	38,634,766	55,542,709	7,247,375	6,801,226	108,226,076
RESULT					
Segment result	27,327,762	9,944,962	4,756,059	4,585,107	46,613,890
Unallocated other operating income					147,878
Unallocated corporate expenses					(17,051,923)
Profit from operations					29,709,845
Share of result of an associate					(59,224)
Gain on disposal of interest in an associate					333,494
Profit before taxation					29,984,115
Taxation					(1,460,452)
Net profit for the year					28,523,663

4. TURNOVER AND SEGMENT INFORMATION (Continued)

As at 31 December 2004

BALANCE SHEET

	Sale of self-developed software RMB	Sale of third party software and hardware in relation to system integration business RMB	System integration RMB	Maintenance, training and other services RMB	Consolidated RMB
ASSETS					
Segment assets	24,798,868	12,219,063	6,092,327	3,560,390	46,670,648
Unallocated corporate assets					105,620,279
Consolidated total assets					<u>152,290,927</u>
LIABILITIES					
Segment liabilities	442,432	12,761,909	437,420	74,874	13,716,635
Unallocated corporate liabilities					15,052,605
Consolidated total liabilities					<u>28,769,240</u>

OTHER INFORMATION

	Sale of self-developed software RMB	Sale of third party software and hardware in relation to system integration business RMB	System integration RMB	Maintenance, training and other services RMB	Consolidated RMB
Amortisation of intangible assets	718,078	—	—	—	718,078
Write-off of inventories	—	162,393	—	—	162,393



Notes to the Consolidated Financial Statements

For the year ended 31 December 2004

4. TURNOVER AND SEGMENT INFORMATION (Continued)

For the year ended 31 December 2003

	Sale of self-developed software RMB	Sale of third party software and hardware in relation to system integration business RMB	System integration RMB	Maintenance, training and other services RMB	Consolidated RMB
TURNOVER					
External sales	<u>32,476,513</u>	<u>48,019,432</u>	<u>4,439,574</u>	<u>7,261,755</u>	<u>92,197,274</u>
RESULT					
Segment result	<u>21,941,792</u>	<u>9,303,297</u>	<u>3,198,472</u>	<u>6,391,004</u>	40,834,565
Unallocated other operating income					333,873
Unallocated corporate expenses					<u>(13,762,547)</u>
Profit from operations					27,405,891
Interest on bank borrowings wholly repayable within five years					(154,292)
Share of result of an associate					<u>(234,270)</u>
Profit before taxation					27,017,329
Taxation					<u>(1,670,791)</u>
Net profit for the year					<u>25,346,538</u>

4. TURNOVER AND SEGMENT INFORMATION (Continued)

As at 31 December 2003

BALANCE SHEET

	Sale of self-developed software RMB	Sale of third party software and hardware in relation to system integration business RMB	System integration RMB	Maintenance, training and other services RMB	Consolidated RMB
ASSETS					
Segment assets	15,122,667	23,590,001	2,741,633	1,411,580	42,865,881
Unallocated corporate assets					89,615,408
Consolidated total assets					<u>132,481,289</u>
LIABILITIES					
Segment liabilities	3,681,022	10,133,010	1,201,084	465,220	15,480,336
Unallocated corporate liabilities					64,991,639
Consolidated total liabilities					<u>80,471,975</u>

OTHER INFORMATION

	Sale of self-developed software RMB	Sale of third party software and hardware in relation to system integration business RMB	System integration RMB	Maintenance, training and other services RMB	Consolidated RMB
Amortisation of intangible assets	640,468	—	—	—	640,468
Write-off of inventories	—	56,536	—	—	56,536



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For the year ended 31 December 2004

5. OTHER OPERATING INCOME

	2004	2003
	RMB	RMB
Value-added tax refund income (Note a)	4,104,995	5,438,417
Government grants (Note b)	892,500	552,500
Interest income	147,878	333,873
Sundry income	—	20,000
	<u>5,145,373</u>	<u>6,344,790</u>

Notes:

- a. In accordance with the Notice on Certain Issues of Tax Policies to Encourage the Development of Software and Integrated Circuits Industries (關於鼓勵軟件生產和集成電路產業發展有關稅收政策問題的通知) jointly issued by the Ministry of Finance, the State of General Administration of Taxation and the State of General Administration of Customs, an ordinary taxpayer shall be refunded, after subscribing 17% value-added tax on the income from sale of internally-developed and produced software products, an amount of 14% value-added tax on such income with effect from 24 June 2000 to 31 December 2010. On 24 January 2000, the Beijing Municipal Science and Technology Commission issued the Software Enterprise Verification Certificate(軟件企業認定證書) to Beijing Zhizhen Node Technology Development Co., Ltd.北京直真節點技術開發有限公司("ZZNode (Beijing)") and on 20 February 2002, the Shanghai Information Office issued the Software Enterprise Verification Certificate (軟件企業認定證書) to Shanghai Zhizhen Node Technology Development Co., Ltd. 上海直真節點技術開發有限公司("ZZNode (Shanghai)"). Both ZZNode (Beijing) and ZZNode (Shanghai) were therefore entitled to receive 14% tax refund from sale of internally-developed software products after the Software Products Taxation Review and tax refund notice(稅收收入退款書)were approved. This tax refund was recognised as income in the period upon the relevant conditions were fulfilled.
- b. The Group is principally engaged in software technology development industry and it is entitled to receive government grants after the Group has obtained approvals from 中國科學技術部科技型中小企業技術創新基金管理中心 (The Small and Middle-Sized Enterprise Technology Innovation Fund Management Center under the Ministry of Technology and Science of the PRC) and 昌平縣區財政所(The Bureau of Finance of the Changping District People's Government) for encouraging software technology development in the PRC.

6. PROFIT FROM OPERATIONS

Profit from operations has been arrived at after charging or crediting:

	2004	2003
	RMB	RMB
Directors' emoluments (Note 7)	1,923,250	1,405,354
Other staff costs (Note)	16,335,988	12,514,142
Retirement benefits scheme contributions excluding directors	874,331	518,658
	<hr/>	<hr/>
Total staff costs	19,133,569	14,438,154
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Auditors' remuneration	583,000	100,000
Allowance for bad and doubtful debts	141,349	—
Depreciation of property, plant and equipment	1,924,512	1,797,748
(Gain) loss on disposal of property, plant and equipment	(223)	41,740
Operating lease rentals in respect of rented premises	3,426,605	3,171,667
Research and development expenditure	10,156,490	8,659,435
Add: Amortisation of intangible assets	718,078	640,468
Less: amount capitalised	(2,554,532)	(1,077,195)
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	8,320,036	8,222,708
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Write-off of inventories	162,393	56,536
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Note: Amount included staff costs of RMB8,320,036 (2003: RMB7,582,240) categorised as research and development expenditure for the year ended 31 December 2004.



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7. DIRECTORS' EMOLUMENTS

	2004	2003
	RMB	RMB
Fees		
Non-executive directors	4,873	—
Independent non-executive directors	36,588	—
	<u>41,461</u>	<u>—</u>
Other emoluments (executive directors):		
Salaries and other benefits	1,647,567	1,264,628
Retirement benefits scheme contributions	52,046	21,327
Performance-related incentive payments	182,176	119,399
	<u>1,881,789</u>	<u>1,405,354</u>
	<u>1,923,250</u>	<u>1,405,354</u>

The emoluments of the directors were within the following bands:

	2004	2003
	Number of directors	Number of directors
HK\$Nil to HK\$1,000,000 (equivalent to RMB Nil to approximately RMB1,060,000)	<u>8</u>	<u>4</u>

8. EMPLOYEES' EMOLUMENTS

During the year, the five highest paid individuals included 4 (2003: 4) directors, details of whose emoluments are set out above. The emoluments of the remaining highest paid individual were as follows:

	2004	2003
	RMB	RMB
Salaries and other benefits	290,076	244,334
Performance-related incentive payments	17,040	100,000
Retirement benefits scheme contributions	11,960	4,325
	<u>319,076</u>	<u>348,659</u>

During the year, no emolument was paid by the Group to the directors or the five highest paid individuals (including directors and employee) as an inducement to join or upon joining the Group or as compensation for loss of office. None of the directors has waived any emoluments during the year.

9. TAXATION

No provision for Hong Kong Profits Tax has been made in the consolidated income statements for the two years ended 31 December 2004 as the Group's income neither arises in, nor is derived from Hong Kong.

ZZNode (Beijing) and ZZNode (Shanghai) are recognised as advanced technology enterprises and software enterprise respectively according to the Changping District Tax Notices [1999] No. 176 and [2003] No. 310 of 北京市新技術產業開發試驗暫行條例 (Provisional Regulation on Test Plot of New Technical Industry and Development in Beijing Municipality) approved by Local Tax Bureau of Changping District of Beijing Municipality and the Shanghai State Tax Notice 滬國稅浦政[2002] No. 70 of 《關於鼓勵軟件產業和集成電路產業發展有關稅收政策問題的通知》(Circular of the Ministry of Finance, the State Administration of Taxation and General Administration Custom on the Tax Policies for Further Encouraging the Development of Software and Integrated Circuit Industries) approved by State Tax Bureau and Local Tax Bureau of Pudong New District of Shanghai Municipality, respectively. ZZNode (Beijing) is exempted from the PRC Enterprise Income Tax for the three years ended 31 December 2002 and is entitled to a 50% tax reduction for the three years ending 31 December 2005. ZZNode (Shanghai) is exempted from the PRC Enterprise Income Tax for the two years ended 31 December 2003 and entitled to a 50% tax reduction for the three years ending 31 December 2006.

For the years ended 31 December 2003 and 2004, the tax charge represents the current tax expense for the year.

For the year ended 31 December 2003 and 2004, ZZNode (Beijing) and ZZNode (Shanghai) enjoyed a reduced income tax rate of 7.5% in accordance with the relevant rules promulgated by the Beijing municipal government and Shanghai municipal government respectively.



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9. TAXATION (Continued)

The charge for the year can be reconciled to the profit before taxation per the consolidated income statement as follows:

	2004		2003	
	RMB	%	RMB	%
Profit before taxation	<u>29,984,115</u>		<u>27,017,329</u>	
Tax at the domestic income tax rate of 15% (2003: 15%)	4,497,617	15.0	4,052,599	15.0
Tax effect of expenses not deductible for tax purposes	209,856	0.7	311,677	1.1
Tax effect of income not taxable for tax purpose	(621,614)	(2.1)	(872,531)	(3.2)
Tax effect of expenses with additional tax preferential deductions	(1,408,415)	(4.7)	—	—
Tax effect of income not taxable under tax holidays	<u>(1,216,992)</u>	<u>(4.0)</u>	<u>(1,820,954)</u>	<u>(6.7)</u>
Tax expense and effective tax rate for the year	<u>1,460,452</u>	<u>4.9</u>	<u>1,670,791</u>	<u>6.2</u>

There was no significant unprovided deferred taxation for the year or at the balance sheet date.

10. DIVIDEND

	NOTES	2004 RMB	2003 RMB
Proposed final — HK1.7 cents (approximately RMB1.8 cents) (2003: Nil) per ordinary share	(a)	7,200,000	—
Paid by a subsidiary	(b)	—	29,000,000
		<u>7,200,000</u>	<u>29,000,000</u>

Notes:

- (a) At the meeting held on 19 April 2005, the directors recommended a final dividend of HK1.7 cents (approximately RMB1.8 cents) per share for the year ended 31 December 2004. This proposed final dividend is not reflected as a dividend payable in the accounts, but will be reflected as an appropriation of retained earnings for the year ending 31 December 2005.
- (b) The dividend for the year ended 31 December 2003 was paid by a subsidiary to its then shareholders prior to the Reorganisation.

11. EARNINGS PER SHARE

The calculation of basic earnings per share is based on the Group's net profit for the year of RMB28,523,663 (2003: RMB25,346,538) and on the weighted average number of ordinary shares of approximately 312,021,858 (2003: 300,000,000) in issue and issuable on the assumption that the capitalisation issue of 300,000,000 shares of the Company had been effective on 1 January 2003.

No diluted earnings per share has been presented as there were no potential ordinary shares outstanding during the year ended 31 December 2003 and 2004.



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12. PROPERTY, PLANT AND EQUIPMENT

	Leasehold improvements	Furniture and fixtures	Computers and equipment	Motor vehicles	Total
	RMB	RMB	RMB	RMB	RMB
THE GROUP					
COST					
At 1 January 2004	2,391,535	75,464	5,532,448	896,962	8,896,409
Additions	—	—	1,352,297	—	1,352,297
Disposals	—	—	(130,543)	—	(130,543)
At 31 December 2004	<u>2,391,535</u>	<u>75,464</u>	<u>6,754,202</u>	<u>896,962</u>	<u>10,118,163</u>
DEPRECIATION					
At 1 January 2004	1,712,622	55,916	1,903,017	72,181	3,743,736
Provided for the year	678,913	12,803	1,126,237	106,559	1,924,512
Disposals	—	—	(4,124)	—	(4,124)
At 31 December 2004	<u>2,391,535</u>	<u>68,719</u>	<u>3,025,130</u>	<u>178,740</u>	<u>5,664,124</u>
NET BOOK VALUES					
At 31 December 2004	<u>—</u>	<u>6,745</u>	<u>3,729,072</u>	<u>718,222</u>	<u>4,454,039</u>
At 31 December 2003	<u>678,913</u>	<u>19,548</u>	<u>3,629,431</u>	<u>824,781</u>	<u>5,152,673</u>

13. INTANGIBLE ASSETS

	Development costs RMB
THE GROUP	
COST	
At 1 January 2004	3,100,867
Additions	2,554,532
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At 31 December 2004	5,655,399
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AMORTISATION	
At 1 January 2004	1,518,609
Charge for the year	718,078
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At 31 December 2004	2,236,687
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NET BOOK VALUES	
At 31 December 2004	3,418,712
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At 31 December 2003	1,582,258
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Development costs are amortised using the straight-line method over their estimated useful life of two years.

14. INVESTMENTS IN SUBSIDIARIES

THE COMPANY

	2004 RMB
Unlisted equity investments, at cost	74,569,800
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14. INVESTMENTS IN SUBSIDIARIES

Details of the Company's subsidiaries as at 31 December, 2004 are as follows:

Name of company	Place of incorporation/ establishment	Issued and fully paid share capital/ registered capital	Proportions of nominal value of share capital/ registered capital held by the Company	Principal activities
<i>Direct subsidiary</i>				
Modern Age Investments Limited ("Modern Age")	British Virgin Inlands ("BVI")	US\$4,600,000	100%	Investment holding
<i>Indirect subsidiaries</i>				
ZZNode (Beijing)	The PRC	RMB6,250,000	100%	Provision of telecommunications and Internet technologies related services and products
ZZNode (Shanghai)	The PRC	RMB1,000,000	90%	Provision of telecommunications and Internet technologies related services and products
Great Process Limited ("Great Process")	BVI	HK\$100	100%	Inactive

ZZNode (Beijing) is a wholly foreign owned enterprise and ZZNode (Shanghai) is a private limited company.

None of the subsidiaries had any debt securities outstanding as at the end of the year or at any time during the year.

15. INTEREST IN AN ASSOCIATE

	THE GROUP	
	2004	2003
	RMB	RMB
Share of net assets	—	275,730

The Group held 51% equity interest in Hangzhou Aeteco Tech Company, Ltd. 杭州天地靈通科技有限公司 (“Hangzhou Aeteco”), which was established on 19 November 2003 in the PRC with a registered capital of RMB1,000,000. Hangzhou Aeteco was principally engaged in the provision of software development and video networking integration. The Company’s directors considered that the Group was not in a position to exercise control over Hangzhou Aeteco and therefore classified it as an associate of the Company.

On 2 February, 2004 a sale and purchase agreement was entered into by the Group and Shanghai Zhizhen Video-Communications Science-Tech Co., Ltd. (“Zhizhen Video (Shanghai)”), a former shareholder of ZZNode (Beijing), to dispose of the entire 51% interest in Hangzhou Aeteco at a consideration of RMB550,000. The transfer of interest in Hangzhou Aeteco was completed on 23 February 2004.

16. OTHER INVESTMENT

	THE GROUP	
	2004	2003
	RMB	RMB
Unlisted investments	5,600,000	5,600,000

Name of investee company	Place of registration and operation	Issued and fully paid registered capital	Proportion of nominal value of registered capital	Principal activities
Capital Engineering & Research Incorporation Limited 中冶京誠工程技術有限公司	The PRC	RMB80,000,000	7%	Provision of technology advancement and consultancy services



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17. INVENTORIES

	THE GROUP	
	2004	2003
	RMB	RMB
Work-in-progress	1,232,047	978,196
Spare parts	385,659	326,152
	<u>1,617,706</u>	<u>1,304,348</u>
Less: Allowance	(215,070)	(215,070)
	<u>1,402,636</u>	<u>1,089,278</u>

Included above are spare parts of RMB60,661 (2003: RMB46,037) which are carried at net realisable value. All work-in-progress are stated at cost.

18. TRADE RECEIVABLES AND NOTES RECEIVABLE

The Group allows an average credit period of 90 days to its customers. The following is an ageing analysis of trade receivables:

	THE GROUP	
	2004	2003
	RMB	RMB
0-90 days	18,616,706	29,730,028
91-180 days	912,985	185,025
181-270 days	13,797,440	—
271-360 days	1,273,917	3,462,547
1-2 years	2,841,535	309,671
	<u>37,442,583</u>	<u>33,687,271</u>

All notes receivable are due within 180 days.

19. AMOUNTS DUE FROM/TO RELATED PARTIES

THE GROUP

	2004	2003
	RMB	RMB
Amounts due from former shareholders		
Bright Pearl Holdings Limited ("Bright Pearl")	—	19,896,864
New Wingo Investments Limited ("New Wingo")	—	9,147,216
Grand Advance Investments Limited ("Grand Advance")	—	5,007,600
	<u>—</u>	<u>34,051,680</u>
Amounts due to former shareholders of a subsidiary		
Beijing Jiabeilin Technology Co., Limited	—	15,160,000
Guangzhou Shulian Information Investment Company	—	5,922,856
Shanghai Zhizhen Video-Communications Science-Tech Co., Ltd.	—	7,540,000
	<u>—</u>	<u>28,622,856</u>
Amounts due from a related party		
Beijing Peng Cheng Xun Dong Technology Co., Ltd. ("Peng Cheng Xun Dong") (Note)	<u>3,559,739</u>	<u>—</u>

The amounts due from/to related parties were unsecured, non-interest bearing and repayable on demand.

Note: A director of ZZNode (Beijing) is also a director of Peng Cheng Xun Dong. The maximum outstanding debit for the year ended 31 December 2004 is amounted to RMB17,604,261, which is due within 90 days.

20. AMOUNT DUE FROM A SUBSIDIARY

THE COMPANY

The amount due from a subsidiary was unsecured, non-interest bearing and repayable on demand.

21. TRADE PAYABLES

THE GROUP

All trade payables are due within 90 days.



Notes to the Consolidated Financial Statements

For the year ended 31 December 2004

22. SHARE CAPITAL

THE GROUP AND THE COMPANY

	Notes	Number of ordinary shares of HK\$0.10 each	Nominal value of ordinary shares HK\$	Equivalent nominal value of ordinary shares RMB
Authorised:				
On incorporation		3,800,000	380,000	402,800
Increase in authorised share capital	(c)	996,200,000	99,620,000	105,597,200
At 31 December 2004		<u>1,000,000,000</u>	<u>100,000,000</u>	<u>106,000,000</u>
Issued:				
Allotted	(a)	1	—	—
Further allotment	(a)	99	—	—
On reorganisation to acquire Modern Age	(b)	999,900	99,990	105,989
Shares to be issued pursuant to the public offer and placing	(d)	100,000,000	10,000,000	10,600,000
Shares to be issued pursuant to the capitalisation issue of share premium	(e)	299,000,000	29,900,010	31,694,011
		<u>400,000,000</u>	<u>40,000,000</u>	<u>42,400,000</u>

The Company was incorporated in the Cayman Islands on 5 January 2004 with an initial authorised share capital of HK\$380,000 divided into 3,800,000 shares of HK\$0.1 each. In relation to the listing of the Company's shares, the following changes in the issued share capital of the Company took place during the year ended 31 December 2004:

- (a) On 5 January 2004, one share of the Company was allotted and issued nil paid to Codan Trust Company (Cayman) Limited as subscriber, which was subsequently transferred to Bright Pearl.

A further aggregate 99 shares were allotted and issued nil paid by the Company of which 26 shares to New Wingo, 20 shares to Grand Advance and 53 shares to Bright Pearl.

The 100 nil paid shares were subsequently credited as fully paid up.

- (b) On 27 October 2004, New Wingo, Grand Advance and Bright Pearl transferred their respective equity interests in Modern Age (which, together, constitute the entire issued share capital of Modern Age) to the Company in consideration of the Company allotting and issuing, credited as fully paid, 259,974 new shares to New Wingo, 199,980 new shares to Grand Advance and 539,946 new shares to Bright Pearl.

22. SHARE CAPITAL (Continued)

- (c) On 31 October 2004, the authorised share capital of the Company was increased to HK\$100,000,000 divided into 1,000,000,000 shares of HK\$0.10 each.
- (d) On 18 November 2004, 100,000,000 shares were issued to the public by way of the public offer and placing (the "Share Offer") for cash of HK\$0.55 per share, raising a total amount of HK\$55,000,000. The excess over the par value of the shares issued was credited to the share premium account.
- (e) Immediately after the Share Offer, 299,000,000 shares of HK\$0.10 each were allotted, issued at par and credited as fully paid to the shareholders of the Company in proportion to their respective shareholdings in the Company prior to the Share Offer, by the capitalisation of HK\$29,900,010 (together with 100 shares issued in note (a)) from the share premium of the Company.

As at 31 December 2003, the share capital of the Group represented Modern Age's paid-in capital of RMB4,339,920 and called capital of RMB34,051,680, totalling RMB38,391,600.

23. SHARE OPTION SCHEME

Pursuant to a share option scheme approved by a resolution of the shareholders of the Company on 31 October 2004 (the "Share Option Scheme"), the Company may grant options to any employees (whether full time or part time), executives or officers of the Company or any of its subsidiaries (including the executive Directors, non-executive Director and independent non-executive Directors of the Company and/or any of its subsidiaries), consultants, agents or legal and financial advisers to the Company or its subsidiaries as incentives and rewards for their contributions to the Group, to subscribe for shares in the Company with a payment of HK\$1.0 upon each grant of options offered and the options granted must be taken up within 30 days from the date of grant. The exercise price of the share option will be determined at the higher of the average of closing prices of shares as stated in the Stock Exchange's daily quotations sheet for the five business days immediately preceding the date of grant of the option; the closing price of the Company's shares as stated in the Stock Exchange's daily quotations sheet on the date of grant; and the nominal value of the shares.

The share options are exercisable at any time during a period of not more than 10 years from the date of grant, subject to the terms and conditions of the Share Option Scheme and any conditions of grant as may be stipulated by the board of directors.

The maximum number of shares in respect of which options may be issued upon exercise of all outstanding options granted and yet to be exercised under the Share Option Scheme and any other schemes shall not exceed 30% of the number of shares of the Company in issue from time to time. The total number of shares which may be issued upon exercise of all options to be granted under the Scheme and any other schemes must not, in aggregate, exceed 10% of the number of shares of the Company in issue as at the date of approval of the Share Option Scheme unless further shareholders' approval has been obtained pursuant to the conditions set out in the Share Option Scheme. No person shall be granted an option which, if all the options granted to the person (including both exercised and outstanding options) in any 12-month period up to the date of grant are exercised in full, would result in such person's maximum entitlement exceeding 1% of the number of issued shares of the Company.

No option has been granted by the Company under the Share Option Scheme since its adoption.



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For the year ended 31 December 2004

24. RESERVES

	Share premium	Special reserve	Statutory surplus reserve	Statutory public welfare fund	Discretionary reserve	Exchange fluctuation reserve	Accumulated profits	Total
	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB
	Note (a)	Note (b)	Note (c)	Note (d)	Note (e)			
THE GROUP								
At 1 January 2003	—	—	3,125,000	2,108,264	13,621,296	—	21,166,616	40,021,176
Arising on combination	—	(22,750,000)	—	—	—	—	—	(22,750,000)
Net profit for the year	—	—	—	—	—	—	25,346,538	25,346,538
Transfer	—	—	—	1,362,535	—	—	(1,362,535)	—
Dividend	—	—	—	—	(13,125,476)	—	(15,874,524)	(29,000,000)
At 31 December 2003	—	(22,750,000)	3,125,000	3,470,799	495,820	—	29,276,095	13,617,714
Arising from								
Reorganisation	—	38,285,611	—	—	—	—	—	38,285,611
Shares issued pursuant to Share Offer	47,700,000	—	—	—	—	—	—	47,700,000
Shares issued by capitalisation of the share premium	(31,694,011)	—	—	—	—	—	—	(31,694,011)
Share issue expenses	(15,369,989)	—	—	—	—	—	—	(15,369,989)
Currency translation differences	—	—	—	—	—	58,699	—	58,699
Transfer	—	—	3,014,673	—	—	—	(3,014,673)	—
Net profit for the year	—	—	—	—	—	—	28,523,663	28,523,663
At 31 December 2004	636,000	15,535,611	6,139,673	3,470,799	495,820	58,699	54,785,085	81,121,687

24. RESERVES (Continued)

	Share premium	Contributed surplus	Accumulated loss	Total
	RMB	RMB Note (f)	RMB	RMB
THE COMPANY				
Arising from Reorganisation	—	74,463,811	—	74,463,811
Shares issued pursuant to Share Offer	47,700,000	—	—	47,700,000
Shares issued by capitalisation of the share premium	(31,694,011)	—	—	(31,694,011)
Share issue expenses	(15,369,989)	—	—	(15,369,989)
Net loss for the year	—	—	(624,642)	(624,642)
	<hr/>	<hr/>	<hr/>	<hr/>
At 31 December 2004	636,000	74,463,811	(624,642)	74,475,169
	<hr/>	<hr/>	<hr/>	<hr/>

- (a) Under the Companies Law of the Cayman Islands, share premium is distributable to shareholders, subject to the condition that, immediately following the date on which the distribution or dividend is proposed to be made, the Company shall be able to pay off its debts as they fall due in the ordinary course of business.
- (b) Special reserve represents the difference between the nominal value of the ordinary shares issued by the Company and the aggregate of the share capital and share premium or net assets of the subsidiaries acquired by the Company through exchange of shares.



Notes to the Consolidated Financial Statements

For the year ended 31 December 2004

24. RESERVES (Continued)

- (c) As stipulated by the relevant laws and regulations in the PRC, the Company's subsidiaries in the PRC are required to provide appropriation of 10% of their profit after taxation each year calculated in accordance with the accounting principles and financial regulations applicable to companies established in the PRC ("PRC GAAP") to the statutory surplus reserve until the balance reaches 50% of the registered capital. According to the provision of the Articles of Association of the Company's subsidiaries in the PRC, in normal circumstances, the statutory surplus reserve shall only be used for making up losses, capitalisation into registered capital and expansion of production and operation. For the capitalisation of statutory surplus reserve into registered capital, the remaining amount of such reserve shall not be less than 25% of the registered capital.

On 14 January 2004, ZZNode (Beijing) was transformed from a private limited company to a foreign-owned enterprise. According to relevant laws and regulations in the PRC, it is required to appropriate 10% of its profit after taxation each year under PRC GAAP to the reserve fund until the balance reaches 50% of its registered capital. The reserve fund can be used to offset accumulated losses and to increase capital upon approval from the relevant authorities.

- (d) Pursuant to the PRC Company Law, the Company's subsidiaries in the PRC shall make allocation from their profit after taxation under PRC GAAP at the rate of 5% to the statutory public welfare fund. The statutory public welfare fund can only be utilised on capital items for employees' collective welfare.

Subsequent to the transformation of ZZNode (Beijing) to a foreign-owned enterprise on 14 January 2004, appropriation to statutory public welfare fund is no longer required.

- (e) Discretionary reserve is a distributable reserve and is appropriated from accumulated profits in accordance with shareholders' approval. The discretionary reserve can be used for capitalisation into registered capital.
- (f) Contributed surplus of the Company represents the excess of the combined net assets of the subsidiaries acquired, over the nominal value of the ordinary shares of the Company in exchange thereof.

In the opinion of the directors, as at 31 December 2004, the Company's reserve available for distribution to shareholders consisted of share premium and contributed surplus of HK\$75,099,811.

25. OPERATING LEASE COMMITMENTS

At the balance sheet date, the Group had commitments for future minimum lease payments under non-cancellable operating leases in respect of rented office premises that fall due as follows:

	THE GROUP	
	2004	2003
	RMB	RMB
Within one year	2,013,000	2,913,000
In the second to fifth year inclusive	644,000	1,329,000
	<u>2,657,000</u>	<u>4,242,000</u>

Leases are negotiated for an average term of two years and rentals are fixed for an average of two years.

26. RETIREMENT BENEFITS SCHEME

The Group participates in a retirement benefits scheme established by the local PRC Social Insurance Industry Management Centre in the favour of the qualifying employees in the PRC. The assets of the scheme are held separately from the assets of the Group. Under the scheme, contributions made by the Group are calculated on the basis of 19% to 20% of the enrolled employees' salaries.

The amounts of such contributions charged to the consolidated income statement were:

	2004	2003
	RMB	RMB
Retirement benefits scheme contributions	<u>926,377</u>	<u>539,985</u>

At the balance sheet date, the Group and the Company had no significant forfeited contributions available to reduce the contribution payable by the Group in the future years.



Notes to the Consolidated Financial Statements

For the year ended 31 December 2004

27. RELATED PARTY TRANSACTIONS

Other than as disclosed the amounts due from/to related companies as disclosed in note 19, the Group entered into the following related party transaction during the year:

	NOTE	2004 RMB	2003 RMB
Name of related company			
Peng Cheng Xun Dong			
Nature of transaction			
Sale of hardware and provision of system integration services	(a)	<u>15,089,202</u>	<u>—</u>

Note:

(a) The transactions were transacted at terms agreed by both parties.