# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

## 1. GENERAL

The Company is incorporated in Bermuda as an exempted company with limited liability and its shares are listed on The Stock Exchange of Hong Kong Limited ("Stock Exchange"). The address of the registered office and principal place of business of the Company are disclosed in the corporate information to the annual report.

The financial statements are presented in Hong Kong dollars, which is the same as the functional currency of the Company.

The Company acts as an investment holding company. The principal activities of the Group are the manufacture and trading of information storage media products and computer accessories and distribution of storage media products.

## 2. ADOPTION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS

In the current year, the Group has applied, for the first time, a number of new Hong Kong Financial Reporting Standards ("HKFRSs"), Hong Kong Accounting Standards ("HKASs") and Interpretations (hereinafter collectively referred as "new HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA") that are effective for accounting periods beginning on or after 1 January 2005. The adoption of the new HKFRSs has resulted in changes to the Group's accounting policies in the following areas that have an effect on how the result for the current year is prepared and presented:

## 2. ADOPTION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS *(continued)*

**Business Combinations**

In the current year, the Group has applied HKFRS 3 "Business Combinations", which is effective for business combinations for which the agreement date is on or after 1 January 2005. The principal effects of the application of HKFRS 3 to the Group are summarised below:

**Goodwill**

In previous years, goodwill arising on acquisitions prior to 1 January 2001 was held in reserves, and goodwill arising on acquisition after 1 January 2001 was capitalised and amortised over its estimated useful life. The Group has applied the relevant transitional provisions in HKFRS 3. Goodwill previously recognised in reserves of HK$26,910,000 has been transferred to the Group's retained profits as at 1 January 2005. With respect to goodwill previously capitalised on the balance sheet, the Group on 1 January 2005 eliminated the carrying amount of the related accumulated amortisation of HK$9,887,000 with a corresponding decrease in the cost of goodwill. The Group has discontinued amortising such goodwill from 1 January 2005 and such goodwill will be tested for impairment at least annually. Goodwill arising on acquisitions after 1 January 2005 is measured at cost less accumulated impairment losses (if any) after initial recognition. As a result of this change in accounting policy, no amortisation of goodwill has been charged in the current year. Comparative figures for 2004 have not been restated.

**Share-based Payments**

In the current year, the Group has applied HKFRS 2 "Share-based Payment" which requires an expense to be recognised where the Group buys goods or obtains services in exchange for shares or rights over shares, or in exchange for other assets equivalent in value to a given number of shares or rights over shares. The principal impact of HKFRS 2 on the Group is in relation to the expensing of the fair value of share options granted to directors and employees of the Company, determined at the date of grant of the share options, over the vesting period. Prior to the application of HKFRS 2, the Group did not recognise the financial effect of these share options until they were exercised. The Group has applied HKFRS 2 to share options granted on or after 1 January 2005. In relation to share options granted before 1 January 2005, the Group chooses not to apply HKFRS 2 with respect to share options granted on or before 7 November 2002 and vested before 1 January 2005. The Group has no share options that were granted after 7 November 2002 which had not yet vested before 1 January 2005.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2005

## 2. ADOPTION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS *(continued)*

**Financial Instruments**

In the current year, the Group has applied HKAS 39 "Financial Instruments: Recognition and Measurement". HKAS 39, which is effective for annual periods beginning on or after 1 January 2005, generally does not permit retrospective application. The principal effects resulting from the implementation of HKAS 39 are summarised below:

*Derecognition*

HKAS 39 provides more rigorous criteria for the derecognition of financial assets than the criteria applied in previous periods. Under HKAS 39, a financial asset is derecognised, when and only when, either the contractual rights to the asset's cash flows expire, or the asset is transferred and the transfer qualifies for derecognition in accordance with HKAS 39. The decision as to whether a transfer qualifies for derecognition is made by applying a combination of risks and rewards and control tests. The Group has applied the relevant transitional provisions and applied the revised accounting policy prospectively to transfers of financial assets from 1 January 2005 onwards. As a result, the Group's bills receivable discounted with full recourse which were derecognised prior to 1 January 2005 have not been restated. As at 31 December 2005, the Group's bills receivable discounted with full recourse have not been derecognised. Instead, the related borrowings of HK$80,898,000 have been recognised and included under bank and other borrowings, on the balance sheet date. This change in accounting policy has had no material effect on the results for the current year.

**Owner-occupied Leasehold Interest in Land**

In previous years, owner-occupied leasehold land and buildings were included in property, plant and equipment and measured using the revaluation model. In the current year, the Group has applied HKAS 17 "Leases". Under HKAS 17, the land and buildings elements of a lease of land and buildings are considered separately for the purposes of lease classification, unless the lease payments cannot be allocated reliably between the land and buildings elements, in which case, the entire lease is generally treated as a finance lease. Where the allocation between the land and buildings elements cannot be made reliably, the leasehold interests in land continue to be accounted for as property, plant and equipment.

## 2A. SUMMARY OF THE EFFECTS OF THE CHANGES IN ACCOUNTING POLICIES

The effects of the changes in the accounting policies described above on the results for the current and prior years are as follows:

| | **2005** **HK$'000** | 2004 HK$'000 |
|---|---|---|
| Non-amortisation of goodwill (decrease in administrative expenses) | **2,472** | – |
| Recognition of share-based payments as expense (increase in employee share-based compensation) | **(4,400)** | – |
| Increase in loss for the year | **(1,928)** | – |

The cumulative effects of the application of the new HKFRSs as at 1 January 2005 are summarised below:

| | **At 31 December 2004 (originally stated)** HK$'000 | **Effect of HKFRS 3** HK$'000 | **At 1 January 2005 (restated)** HK$'000 |
|---|---|---|---|
| Capital reserve | (25,047) | 26,910 | 1,863 |
| Retained profits | 179,240 | (26,910) | 152,330 |
| Total effects on equity | 154,193 | – | 154,193 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

## 2B. POTENTIAL IMPACT ARISING ON THE NEW OR REVISED ACCOUNTING STANDARDS NOT YET EFFECTIVE

The Group has not early applied the following new standards and interpretations that have been issued but are not yet effective:

| | |
|---|---|
| HKAS 1 (Amendment) | Capital disclosures[1] |
| HKAS 19 (Amendment) | Actuarial gains and losses, group plans and disclosures[2] |
| HKAS 21 (Amendment) | The effects of change in foreign exchange rate-net investment in a foreign operation[2] |
| HKAS 39 (Amendment) | Cash flow hedge accounting of forecast intragroup transactions[2] |
| HKAS 39 (Amendment) | The fair value option[2] |
| HKAS 39 & HKFRS 4 (Amendments) | Financial guarantee contracts[2] |
| HKFRS 6 | Exploration for and evaluation of mineral resources[2] |
| HKFRS 7 | Financial instruments: Disclosures[1] |
| HK(IFRIC) – INT 4 | Determining whether an arrangement contains a lease[2] |
| HK(IFRIC) – INT 5 | Rights to interests arising from decommissioning, restoration and environmental rehabilitation funds[2] |
| HK(IFRIC) – INT 6 | Liabilities arising from participating in a specific market – waste electrical and electronic equipment[3] |
| HK(IFRIC) – INT 7 | Applying the restatement approach under HKAS 29 Financial Reporting in Hyperinflationary Economies[4] |
| HK(IFRIC) – INT 8 | Scope of HKFRS 2[5] |
| HK(IFRIC) – INT 9 | Reassessment of embedded derivatives[6] |

1 Effective for annual periods beginning on or after 1 January 2007
2 Effective for annual periods beginning on or after 1 January 2006
3 Effective for annual periods beginning on or after 1 December 2005
4 Effective for annual periods beginning on or after 1 March 2006
5 Effective for annual periods beginning on or after 1 May 2006
6 Effective for annual periods beginning on or after 1 June 2006

The Group is in the process of determining whether these new and revised standards on interpretations will have any material impact on the financial statements of the Group.

## 3. PRINCIPAL ACCOUNTING POLICIES

The consolidated financial statements have been prepared under the historical cost basis except for the leasehold land and buildings which are measured at revalued amount.

The consolidated financial statements have been prepared in accordance with HKFRSs issued by the HKICPA. In addition, the consolidated financial statements include applicable disclosures required by the Rules Governing the Listing of Securities on the Stock Exchange and the Hong Kong Companies Ordinance.

**Basis of consolidation**

The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries.

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.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Group.

All significant intra-group transactions, balances, income and expenses are eliminated on consolidation.

**Goodwill**

*Goodwill arising on acquisition prior to 1 January 2005*

Goodwill arising on an acquisition of a subsidiary for which the agreement date is before 1 January 2005 represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets and liabilities of the relevant subsidiary at the date of acquisition.

Goodwill arising on acquisitions prior to 1 January 2001 has been transferred to the Group's retained profits as at 1 January 2005.

For previously capitalised goodwill arising on acquisitions after 1 January 2001, the Group has discontinued amortisation from 1 January 2005, and such goodwill is tested for impairment annually, and whenever there is an indication that the cash generating unit to which the goodwill relates may be impaired. Capitalised goodwill arising on an acquisition of a subsidiary is presented separately in the balance sheet.

## 3. PRINCIPAL ACCOUNTING POLICIES *(continued)*

**Goodwill** *(continued)*

*Goodwill arising on acquisitions on or after 1 January 2005*

Goodwill arising on an acquisition of a subsidiary for which the agreement date is on or after 1 January 2005 represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets, liabilities and contingent liabilities of the relevant subsidiary at the date of acquisition. Such goodwill is carried at cost less any accumulated impairment losses.

Capitalised goodwill arising on an acquisition of a subsidiary is presented separately in the balance sheet.

For the purpose of impairment testing, goodwill arising from an acquisition is allocated to each of the relevant cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the acquisition. A cash-generating unit to which goodwill has been allocated is tested for impairment annually, and whenever there is an indication that the unit may be impaired. For goodwill arising on an acquisition in a financial year, the cash-generating unit to which goodwill has been allocated is tested for impairment before the end of that financial year. When the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated to reduce the carrying amount of any goodwill allocated to the cash-generating unit first, and then to the other assets of the cash-generating unit pro rata on the basis of the carrying amount of each asset. Any impairment loss for goodwill is recognised directly in the income statement. An impairment loss for goodwill is not reversed in subsequent periods.

On subsequent disposal of a subsidiary, the attributable amount of goodwill capitalised is included in the determination of the amount of profit or loss on disposal.

## 3. PRINCIPAL ACCOUNTING POLICIES *(continued)*

**Revenue recognition**

Revenue is measured at the fair value of the consideration received or receivable and represents the net amount receivable for goods and services provided in the normal course of business, net of returns.

Sales of goods are recognised when goods are delivered and title has passed.

Service income is recognised when services are provided.

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts the estimated future cash receipts through the expected life of the financial assets to that asset's net carrying amount.

Operating lease rental income is recognised over the terms of relevant leases on a straight line basis.

**Property, plant and equipment**

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

Leasehold land and buildings held for use in the production or supply of goods or services, or for administrative purposes, are stated in the balance sheet at their revalued amount, being the fair value at the date of revaluation less any subsequent accumulated depreciation and impairment losses. Revaluations are performed with sufficient regularity such that the carrying amount does not differ materially from that which would be determined using fair values at the balance sheet date.

Any revaluation increase arising on revaluation of leasehold land and buildings is credited to the properties revaluation reserve, except to the extent that it reverses a revaluation decrease of the same asset previously recognised as an expense, in which case the increase is credited to the income statement to the extent of the decrease previously charged. A decrease in the net carrying amount arising on revaluation of an asset is dealt with as an expense to the extent that it exceeds the balance, if any, on the properties revaluation reserve relating to a previous revaluation of that asset. On the subsequent sale or retirement of a revalued asset, the attributable revaluation surplus is transferred to retained profits.

## 3. PRINCIPAL ACCOUNTING POLICIES *(continued)*

**Property, plant and equipment** *(continued)*

Depreciation is provided to write off the cost or fair value of property, plant and equipment other than plant and machinery used for the manufacture of compact disc products over their estimated useful lives and after taking into account their estimated residual value, using the straight line method.

Depreciation is provided to write off the cost of plant and machinery used for the manufacture of compact disc products to their estimated residual value based on the actual units of production as a proportion of its total anticipated units of production. The anticipated units of production are determined with reference to the production specifications obtained from the suppliers.

Assets held under finance leases are depreciated over their expected useful lives on the same basis as owned assets.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of an asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the income statement in the year in which the item is derecognised.

**Assets held under finance leases**

Leases are classified as finance leases when the terms of the lease transfer substantially all the risks and rewards of ownership of the assets concerned to the Group. Assets held under finance leases are capitalised at their fair values at the date of acquisition. The corresponding liability to the lessor, net of interest charges, is included in the balance sheet as a finance lease. Finance costs, which represent the difference between the total obligations and the fair value of the assets acquired, are charged to the income statement over the period of the relevant leases so as to produce a constant periodic rate of charge on the remaining balance of the obligations for each accounting period.

All other leases are classified as operating leases and the rental income and expenses are credited and charged to the income statement on a straight-line basis over the relevant lease terms respectively.

## 3. PRINCIPAL ACCOUNTING POLICIES *(continued)*

**Intangible assets**

On initial recognition, intangible assets acquired separately are recognised at cost. After initial recognition, intangible assets with finite useful lives are carried at costs less accumulated amortisation and any accumulated impairment losses. Amortisation for intangible assets with finite useful lives is provided on a straight-line basis over their estimated useful lives.

Gains or losses arising from derecognition of an intangible asset are measured at the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the income statement when the asset is derecognised.

*Development expenditure*

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, and carried at cost less subsequent accumulated amortisation and impairment losses.

Where no internally-generated intangible asset can be recognised, development expenditure is charged to profit or loss in the period in which it is incurred.

*Distribution rights*

Distribution rights represent payments made to independent third parties for the purpose of acquiring the rights for publication and distribution of data media products and are stated at cost less subsequent accumulated amortisation and impairment losses.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

## 3. PRINCIPAL ACCOUNTING POLICIES *(continued)*

**Intangible assets** *(continued)*

*Technical know-how*

Technical know-how represents payments made to independent third parties for the purpose of acquiring existing specialised knowledge required to produce a product that is not readily available to the Group and is stated at cost less subsequent accumulated amortisation and impairment losses.

*Impairment*

Intangible assets not yet available for use are tested for impairment annually by comparing their carrying amounts with their recoverable amounts, irrespective of whether there is any indication that they may be impaired. 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. An impairment loss is recognised as an expense immediately.

When 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.

Intangible assets with finite useful lives are tested for impairment when there is an indication that an asset may be impaired.

**Inventories**

Inventories are stated at the lower of cost and net realisable value. Cost is calculated using the first-in, first-out method.

## 3. PRINCIPAL ACCOUNTING POLICIES *(continued)*

**Impairment (other than goodwill and intangible assets that are not yet ready for use (see the accounting policies in respect of goodwill and intangible assets above))**

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 immediately unless the revalued asset is carried at a revalued amount under another standard, in which case the impairment loss is treated as revaluation decrease under that standard.

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 unless the revalued asset is carried at a revalued amount under another standard, in which case the reversal of the impairment loss is treated as a revaluation increase under that other standard.

**Foreign currencies**

In preparing the financial statements of each individual group entity, transactions in currencies other than the functional currency of that entity (foreign currencies) are recorded in its functional currency (i.e. the currency of the primary economic environment in which the entity operates) at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary items denominated in foreign currencies are retranslated at the rates prevailing at the balance sheet date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences arising on the settlement of monetary items, and on the translation of monetary items, are recognised in profit or loss in the period in which they arise. Exchange differences arising on the retranslation of non-monetary items carried at fair value are included in profit or loss for the period except for differences arising on the retranslation of non-monetary items in respect of which gains and losses are recognised directly in equity, in which cases, the exchange differences are also recognised directly in equity.

## 3. PRINCIPAL ACCOUNTING POLICIES *(continued)*

**Foreign currencies** *(continued)*

For the purposes of presenting the consolidated financial statements, the assets and liabilities of the Group's foreign operations are translated into the presentation currency of the Company (i.e. Hong Kong dollars) at the rate of exchange prevailing at the balance sheet date, and their income and expenses are translated at the average exchange rates for the year, unless exchange rates fluctuate significantly during the period, in which case, the exchange rates prevailing at the dates of transactions are used. Exchange differences arising, if any, are recognised as a separate component of equity (the translation reserve). Such exchange differences are recognised in profit or loss in the period in which the foreign operation is disposed of.

**Borrowing costs**

All borrowing costs are expensed as incurred.

**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 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. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised on differences between the carrying amounts 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 (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

## 3. PRINCIPAL ACCOUNTING POLICIES *(continued)*

**Taxation** *(continued)*

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

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 period when the liability is settled or the asset is realised using tax rates that have been enacted or substantively enacted by the balance sheet date. Deferred tax is charged or credited to profit or loss, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

**Retirement benefit scheme**

Payments to defined contribution retirement benefit plans are charged as an expense as they fall due.

**Financial instruments**

Financial assets and financial liabilities are recognised on the Group's balance sheet when a group entity becomes a party to the contractual provisions of the instrument. Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. All regular way purchases or sales of financial assets are recognised and derecognised on a trade date basis.

## 3. PRINCIPAL ACCOUNTING POLICIES *(continued)*

**Financial instruments** *(continued)*

*Debtors*

Debtors are measured at initial recognition at fair value, and are subsequently measured at amortised cost using the effective interest rate method less any identified impairment losses. The impairment losses for estimated irrecoverable amounts are recognised in profit or loss when there is objective evidence that the asset is impaired. Impairment losses made are measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the effective interest rate computed at initial recognition. Impairment losses are reversed in subsequent periods when an increase in the asset's recoverable amount can be related objectively to an event occurring after the impairment was recognised, subject to a restriction that the carrying amount of the asset at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

*Cash and cash equivalents*

Cash and cash equivalents comprise cash on hand and bank deposits and are subject to an insignificant risk of changes in value.

*Financial liabilities and equity*

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument. An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities.

*Trade and other payables, bank and other borrowings, and obligations under finance leases*

Trade and other payables, bank and other borrowings, and obligations under finance leases are initially measured at fair value and are subsequently measured at amortised cost, using the effective interest rate method.

*Equity instruments*

Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

## 3. PRINCIPAL ACCOUNTING POLICIES *(continued)*

**Financial instruments** *(continued)*

*Derecognition*

Financial assets are derecognised when the rights to receive cash flows from the assets expire or, the financial assets are transferred and the Group has transferred substantially all the risks and rewards of ownership of the financial assets. On derecognition of a financial asset, the difference between the asset's carrying amount and the sum of the consideration received and the cumulative gain or loss that had been recognised directly in equity is recognised in profit or loss.

For financial liabilities, they are removed from the Group's balance sheet (i.e. when the obligation specified in the relevant contract is discharged, cancelled or expires). The difference between the carrying amount of the financial liability derecognised and the consideration received or receivable is recognised in profit or loss.

**Share-based payment transactions**

*Share options granted to employees of the Company*

The fair value of services received determined by reference to the fair value of share options granted at the grant date is recognised as an expense in full at the grant date when the share options granted vest immediately, with a corresponding increase in equity (employee share-based compensation reserve).

At the time when the share options are exercised, the amount previously recognised in employee share-based compensation reserve will be transferred to share premium. When the share options are forfeited or are still not exercised at the expiry date, the amount previously recognised in share-based compensation reserve will be transferred to retained profits.

## 4. CRITICAL ACCOUNTING JUDGEMENT AND KEY SOURCES OF ESTIMATION UNCERTAINTY

The key assumptions concerning the future, and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

## 4. CRITICAL ACCOUNTING JUDGEMENT AND KEY SOURCES OF ESTIMATION UNCERTAINTY *(continued)*

**Critical accounting judgement**

*Amount receivable from a legal claim*

As explained to in note 31, debtors, deposits and prepayments at 31 December 2005 include an amount of HK$102.1 million (2004: HK$87.4 million) recoverable from a customer. The Group is pursuing a legal claim to recover the amount and subsequent to 31 December 2005 has recovered approximately HK$80.2 million. The directors believe that the remaining balance of approximately HK$21.9 million will be recovered as the outcome of the legal claim is in favour of the Group.

**Estimation uncertainty**

*Estimated impairment of goodwill*

Determining whether goodwill is impaired requires an estimation of the value in use of the cash-generating units to which goodwill has been allocated. The value in use calculation requires the Group to estimate the future cash flows expected to arise from the cash-generating unit and a suitable discount rate in order to calculate the present value. Where the actual future cash flows are less than expected, a material impairment loss may arise. At 31 December 2005, the carrying amounts of goodwill as separately presented in the balance sheet is HK$39,545,000.

*Estimated impairment of property, plant and equipment*

The Group assesses annually whether property, plant and equipment have any indication of impairment, in accordance with the relevant accounting policies. The recoverable amounts of property, plant and equipment have been determined based on value-in-use calculations or scrap value. These calculations and valuations require the use of judgment and estimates on future operating cash flows and discount rates adopted and estimated market value of the scraps.

## 4. CRITICAL ACCOUNTING JUDGEMENT AND KEY SOURCES OF ESTIMATION UNCERTAINTY *(continued)*

**Estimation uncertainty** *(continued)*

*Estimated allowances for bad and doubtful debts*

The Group makes allowances for bad and doubtful debts based on an assessment of the recoverability of debtors. Allowances are applied to debtors where events or changes in circumstances indicate that the balances may not be collectible. The identification of bad and doubtful debts requires the use of judgment and estimates. Where the expectation on the recoverability of debtors is different from the original estimate and the present value of estimated future cash flows discounted at the effective rate computed at initial recognition is less than the asset's carrying amount, such difference will impact the carrying value of debtors and allowances of bad and doubtful debts should be made in the periods in which such estimate has been changed.

*Estimated allowance for inventories*

The Group makes allowance for inventories based on an assessment of the net realisable value of inventories. Allowances are applied to inventories where events or changes in circumstances indicate that the net realisable value is lower than the cost of inventories. The identification of obsolete inventories requires the use of judgment and estimates on the conditions and usefulness of the inventories.

## 5. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's major financial instruments include debtors and deposits, trade and other payables, bank and other borrowings, and obligations under finance leases. Details of these financial instruments are disclosed in respective notes. The risks associated with these financial instruments and the policies on how to mitigate these risks are set out below. The management manages and monitors these exposures to ensure appropriate measures are implemented on a timely and effective manner.

**Liquidity risk**

The Group incurred a loss in the current year and was financed by significant bank and other borrowings and obligations under finance leases. The Group's operations are exposed to liquidity risk. Management monitors closely the liquidity position of the Group so as to meet all the financial obligations as and when they fall due. Management will consider to raise fund by ways of issuing debt and equity instruments of the Group.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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## 5. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(continued)*

**Cash flow interest rate risk**

The Group is exposed to cash flow interest rate risk on variable-rate bank borrowings and obligations under finance leases. Management monitors the related cash flow interest rate risk exposure closely and will consider hedging significant cash flow interest rate risk exposure should the need arise.

**Credit risk**

The Group's maximum exposure to credit risk in the event that counterparties fail to perform their obligations at 31 December 2005 in relation to each class of recognised financial assets is the carrying amounts of these assets as stated in the consolidated balance sheet.

The Group's credit risk is primarily attributable to its trade debtors. The Group is exposed to concentration of credit risk as a substantial portion of its trade debtors are due from a small number of customers. The Group manages its credit risk by closely monitoring the granting of credit period to its customers. The Group also reviews the recoverable amount of each individual trade debtor at each balance sheet date to ensure that adequate allowances are made for irrecoverable amounts. In this regard, the directors of the Company consider that the Group's credit risk is minimised.

The credit risk on bank deposits is limited because the counterparties are banks with high credit-ratings assigned by international credit-rating agencies or state-owned banks in the People's Republic of China ("PRC").

## 6. REVENUE

Revenue represents the aggregate of the amounts received and receivable for goods sold and services rendered, net of returns, by the Group to outside customers during the year and is analysed as follows:

| | **2005**<br>**HK$'000** | 2004<br>HK$'000 |
|---|---|---|
| Manufacture and trading of media products | **126,890** | 150,315 |
| Manufacture and trading of computer accessories | **98,786** | 76,753 |
| Distribution of media products | **104,069** | 130,011 |
| Others | **–** | 6,686 |
| | **329,745** | 363,765 |

## 7. BUSINESS AND GEOGRAPHICAL SEGMENTS

### Business segments

For management purposes, the Group is currently organised into four operating divisions – the manufacture and trading of media products and computer accessories, distribution of media products and others. These divisions are the basis on which the Group reports its primary segment information.

Segment information about these business segments is presented below.

| | Manufacture and trading of media products HK$'000 | Manufacture and trading of computer accessories HK$'000 | Distribution of media products HK$'000 | Others HK$'000 | Eliminations HK$'000 | Consolidated HK$'000 |
|---|---|---|---|---|---|---|
| **Year ended 31 December 2005** | | | | | | |
| Revenue | | | | | | |
| External sales | 147,118 | 98,786 | 104,069 | – | (20,228) | 329,745 |
| Inter-segment sales | (20,228) | – | – | – | 20,228 | – |
| Total | 126,890 | 98,786 | 104,069 | – | – | 329,745 |
| Inter-segment sales are charged at prevailing market rates. | | | | | | |
| Results | | | | | | |
| Segment results | (67,735) | 4,271 | (2,628) | (1,456) | – | (67,548) |
| Other income | | | | | | 11 |
| Unallocated corporate expenses | | | | | | (51,074) |
| Finance costs | | | | | | (15,401) |
| Loss before taxation | | | | | | (134,012) |
| Income tax expense | | | | | | (1,207) |
| Loss for the year | | | | | | (135,219) |

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

## 7. BUSINESS AND GEOGRAPHICAL SEGMENTS *(continued)*

**Business segments** *(continued)*

| | Manufacture and trading of media products HK$'000 | Manufacture and trading of computer accessories HK$'000 | Distribution of media products HK$'000 | Others HK$'000 | Consolidated HK$'000 |
|---|---|---|---|---|---|
| **At 31 December 2005** | | | | | |
| BALANCE SHEET | | | | | |
| ASSETS | | | | | |
| Segment assets | 159,977 | 104,815 | 93,714 | 13,235 | 371,741 |
| Unallocated corporate assets | | | | | 153,290 |
| Consolidated total assets | | | | | 525,031 |
| LIABILITIES | | | | | |
| Segment liabilities | 2,990 | 21,435 | 22,294 | 17,428 | 64,147 |
| Unallocated corporate liabilities | | | | | 252,475 |
| Consolidated total liabilities | | | | | 316,622 |
| OTHER INFORMATION | | | | | |
| Capital additions | 20,855 | 14,135 | 39 | – | 35,029 |
| Allowances for bad and doubtful debts | 8,525 | 12,632 | 10,811 | 1,004 | 32,972 |
| Impairment losses of property, plant and equipment | 82,647 | 3,735 | – | 452 | 86,834 |
| Depreciation of property, plant and equipment | 10,496 | 6,505 | 292 | 68 | 17,361 |
| Amortisation of other intangible assets | – | 3,249 | – | 1,311 | 4,560 |

## 7. BUSINESS AND GEOGRAPHICAL SEGMENTS *(continued)*

**Business segments** *(continued)*

| | Manufacture and trading of media products HK$'000 | Manufacture and trading of computer accessories HK$'000 | Distribution of media products HK$'000 | Others HK$'000 | Eliminations HK$'000 | Consolidated HK$'000 |
|---|---|---|---|---|---|---|
| Year ended 31 December 2004 | | | | | | |
| Revenue | | | | | | |
| External sales | 173,195 | 76,753 | 130,011 | 6,686 | (22,880) | 363,765 |
| Inter-segment sales | (22,880) | – | – | – | 22,880 | – |
| Total | 150,315 | 76,753 | 130,011 | 6,686 | – | 363,765 |
| Inter-segment sales are charged at prevailing market rates. | | | | | | |
| Results | | | | | | |
| Segment results | 23,523 | 24,786 | 23,184 | 2,176 | – | 73,669 |
| Other income | | | | | | 9 |
| Unallocated corporate expenses | | | | | | (43,374) |
| Finance costs | | | | | | (10,521) |
| Gain on disposal of a subsidiary | | | | | | 619 |
| Profit before taxation | | | | | | 20,402 |
| Income tax expense | | | | | | (285) |
| Profit for the year | | | | | | 20,117 |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2005

## 7. BUSINESS AND GEOGRAPHICAL SEGMENTS *(continued)*

**Business segments** *(continued)*

| | Manufacture and trading of media products HK$'000 | Manufacture and trading of computer accessories HK$'000 | Distribution of media products HK$'000 | Others HK$'000 | Consolidated HK$'000 |
|---|---|---|---|---|---|
| At 31 December 2004 | | | | | |
| BALANCE SHEET | | | | | |
| ASSETS | | | | | |
| Segment assets | 263,438 | 84,449 | 76,037 | 6,079 | 430,003 |
| Unallocated corporate assets | | | | | 140,247 |
| Consolidated total assets | | | | | 570,250 |
| LIABILITIES | | | | | |
| Segment liabilities | 26,079 | 8,795 | 10,536 | 2,583 | 47,993 |
| Unallocated corporate liabilities | | | | | 203,459 |
| Consolidated total liabilities | | | | | 251,452 |
| OTHER INFORMATION | | | | | |
| Capital additions | 3,478 | 27,487 | 5 | 246 | 31,216 |
| Allowances for bad and doubtful debts | 90 | 60 | – | – | 150 |
| Depreciation of property, plant and equipment | 11,460 | 3,495 | 57 | 811 | 15,823 |
| Amortisation of goodwill | – | – | 2,472 | – | 2,472 |
| Amortisation of other intangible assets | – | 584 | – | 655 | 1,239 |

## 7. BUSINESS AND GEOGRAPHICAL SEGMENTS *(continued)*

**Geographical segments**

The Group's operations are mainly located in Asia, Europe and North and South America.

The following table provides an analysis of the Group's sales by geographical market, irrespective of the origin of the goods/services:

| | **Revenue by geographical market** | |
|---|---|---|
| | **2005** | 2004 |
| | **HK$'000** | HK$'000 |
| Asia | | |
| – The PRC including Hong Kong | **156,299** | 214,394 |
| – Other regions in Asia | **59,468** | 77,329 |
| Europe | **46,677** | 53,083 |
| North and South America | **49,508** | 18,959 |
| Others | **17,793** | – |
| | **329,745** | 363,765 |

## 7. BUSINESS AND GEOGRAPHICAL SEGMENTS *(continued)*

**Geographical segments** *(continued)*

The following is an analysis of the carrying amount of segment assets, and additions to property, plant and equipment and intangible assets, analysed by geographical area in which the assets are located:

| | Carrying amount of segment assets | | Additions to property, plant and equipment and intangible assets | |
|---|---|---|---|---|
| | **2005** | 2004 | **2005** | 2004 |
| | **HK$'000** | HK$'000 | **HK$'000** | HK$'000 |
| Asia | | | | |
| – Hong Kong | **363,549** | 413,298 | **8,837** | 4,313 |
| – The PRC | **142,266** | 130,136 | **26,116** | 26,112 |
| – Other regions in Asia | **6,093** | 10,993 | **–** | – |
| Europe | **6,377** | 11,799 | **76** | 582 |
| North and South America | **6,746** | 4,024 | **–** | 209 |
| | **525,031** | 570,250 | **35,029** | 31,216 |

## 8. OTHER INCOME

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Commission income | **2,253** | 1,154 |
| Interest income | **296** | 142 |
| Operating lease rental income from plant and machinery | **1,290** | 1,080 |
| Gain on disposal of property, plant and equipment | **307** | – |
| Released from payment for assets purchased (note) | **–** | 3,510 |
| Others | **623** | 1,461 |
| | **4,769** | 7,347 |

Note: The amount in 2004 represented the release, by a supplier, of the Group's obligation to make payment for certain plant and equipment purchased from the supplier.

## 9. OTHER EXPENSES

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Impairment losses of property, plant and equipment (note i) | **86,834** | – |
| Allowances for bad and doubtful debts (note ii) | **32,972** | – |
| | **119,806** | – |

Notes:

(i) During the year ended 31 December 2005, the directors conducted a review on the Group's plant and machinery used for the manufacture of compact disc products and other fixed assets of the Group and determined that a number of those assets were impaired, due to the idleness of the assets which were neither used by the Group for its manufacture process nor leased out for rentals. Accordingly, impairment losses of HK$86,834,000 have been recognised in respect of these assets in current year. The recoverable amounts of the relevant assets have been determined on the basis of their sale value by reference to quotation on the second hand market of trading of similar plant and machinery.

(ii) During the year ended 31 December 2005, the directors have assessed the recoverability of the Group's debtors, deposits and prepayments and determined that allowances for bad and doubtful debts of approximately HK$32,972,000 be made in the current year financial statements. The allowances were made to those aged debtors who defaulted in payment to the Group. The allowance amount was estimated by the directors as the shortfall of the present value of estimated future cash flows of the relevant debts discounted at the effective rate computed at initial recognition over the carrying value of debtors.

## 10. FINANCE COSTS

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Interest on: | | |
| – Bank loans, overdrafts and other borrowings wholly repayable within five years | **11,319** | 7,106 |
| – Obligations under finance leases | **1,492** | 1,177 |
| Bank charges | **1,720** | 1,798 |
| Exchange loss | **870** | 440 |
| | **15,401** | 10,521 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

## 11. (LOSS) PROFIT BEFORE TAXATION

| | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|
| (Loss) profit before taxation has been arrived at after charging: | | |
| Amortisation of goodwill (included in administrative expenses) | – | 2,472 |
| Amortisation of other intangible assets (HK$1,311,000 (2004: HK$655,000) included in administrative expenses and HK$3,249,000 (2004: HK$584,000) included in cost of sales) | 4,560 | 1,239 |
| Auditors' remuneration | 2,450 | 750 |
| Depreciation on | | |
| – Owned assets | 13,636 | 12,928 |
| – Assets held under finance leases | 3,725 | 2,895 |
| | 17,361 | 15,823 |
| Loss on disposal of property, plant and equipment | – | 145 |
| Rental payments in respect of premises under operating leases | 6,338 | 6,442 |
| Employee share-based compensation | 4,400 | – |
| Other staff costs, including directors' remuneration | 43,973 | 41,728 |
| Retirement benefits scheme contributions, including those attributable to directors | 757 | 601 |
| Total staff costs | 49,130 | 42,329 |

## 12. DIRECTORS' EMOLUMENTS

The emoluments paid or payable to each of the 9 (2004: 6) directors of the Company were as follows:

**For the year ended 31 December 2005**

| | Ms. Ho Yin King, Helena HK$'000 | Mr. Ho Fai Keung, Jacky HK$'000 | Mr. Low Nyap Heng HK$'000 | Mr. Cheung Sze Ming HK$'000 (note a) | Ms. Lo Suk King HK$'000 (note a) | Mr. Lai Kam Hung HK$'000 (note b) | Dr. Li Sau Hung, Eddy HK$'000 | Mr. Leung Ka Kui, Johnny HK$'000 | Mr. Chan Kam Kwan, Jason HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|---|---|---|---|---|
| Fees | – | – | – | – | – | – | 200 | 200 | 200 | 600 |
| Other emoluments | | | | | | | | | | |
| Salaries and other benefits | 4,068 | 2,388 | 1,476 | 969 | 632 | – | – | – | – | 9,533 |
| Contributions to retirement benefits schemes | 12 | 12 | – | 8 | 8 | – | – | – | – | 40 |
| Share-based payments | 660 | 660 | 660 | 660 | – | – | 220 | 220 | 220 | 3,300 |
| Total emoluments | 4,740 | 3,060 | 2,136 | 1,637 | 640 | – | 420 | 420 | 420 | 13,473 |

For the year ended 31 December 2004

| | Ms. Ho Yin King, Helena HK$'000 | Mr. Ho Fai Keung, Jacky HK$'000 | Mr. Low Nyap Heng HK$'000 | Dr. Li Sau Hung, Eddy HK$'000 | Mr. Leung Ka Kui, Johnny HK$'000 | Mr. Chan Kam Kwan, Jason HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|---|---|
| Fees | – | – | – | 200 | 200 | 39 | 439 |
| Other emoluments | | | | | | | |
| Salaries and other benefits | 4,463 | 2,508 | 1,671 | – | – | – | 8,642 |
| Contributions to retirement benefits schemes | 12 | 12 | – | – | – | – | 24 |
| Total emoluments | 4,475 | 2,520 | 1,671 | 200 | 200 | 39 | 9,105 |

No directors waived any emoluments in the years ended 31 December 2005 and 2004.

## 12. DIRECTORS' EMOLUMENTS *(continued)*

Notes:

(a) Mr. Cheung Sze Ming and Ms. Lo Suk King were appointed as directors of the Company on 22 April 2005.

(b) Mr. Lai Kam Hung was appointed and resigned as a director of the Company on 22 April 2005 and 23 September 2005 respectively.

## 13. EMPLOYEES' EMOLUMENTS

Of the five individuals with the highest emoluments in the Group, four (2004: three) were directors of the Company as at 31 December 2005. The aggregate emoluments of the five highest paid individuals were as follows:

| | **2005**<br>**HK$'000** | 2004<br>HK$'000 |
|---|---|---|
| Salaries and other benefits | **10,645** | 11,258 |
| Contributions to retirement benefits scheme | **48** | 48 |
| Share-based payments | **2,640** | – |
| | **13,333** | 11,306 |

Their emoluments were within the following bands:

| | **2005**<br>**No. of**<br>**individuals** | 2004<br>No. of<br>individuals |
|---|---|---|
| HK$1,000,001 to HK$1,500,000 | 1 | 2 |
| HK$1,500,001 to HK$2,000,000 | 1 | 1 |
| HK$2,000,001 to HK$2,500,000 | 1 | 1 |
| HK$3,000,001 to HK$3,500,000 | 1 | – |
| HK$4,500,001 to HK$5,000,000 | 1 | 1 |
| | 5 | 5 |

## 13. EMPLOYEES' EMOLUMENTS *(continued)*

During the years ended 31 December 2005 and 2004, no emolument was paid to the directors and the five highest paid individuals as an inducement to join or upon joining the Group or as compensation for loss of office.

## 14. INCOME TAX EXPENSE

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| The taxation charge comprises: | | |
| Current tax | | |
| Hong Kong | **901** | – |
| Overseas | **224** | 170 |
| | **1,125** | 170 |
| Underprovision in respect of prior years | | |
| Hong Kong | **–** | 53 |
| Overseas | **82** | 62 |
| | **82** | 115 |
| | **1,207** | 285 |

Hong Kong Profits Tax is calculated at 17.5% (2004: 17.5%) of the estimated assessable profits for the year. Taxation arising in other jurisdictions is calculated at the rates prevailing in the relevant jurisdictions.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2005

## 14. INCOME TAX EXPENSE *(continued)*

The tax charge for the year can be reconciled to the (loss) profit before taxation per the income statement as follows:

| | 2005<br>HK$'000 | 2004<br>HK$'000 |
|---|---|---|
| (Loss) profit before taxation | **(134,012)** | 20,402 |
| Tax at the Hong Kong Profits Tax rates of 17.5% (2004: 17.5%) | **(23,452)** | 3,570 |
| Tax effect of expenses not deductible for tax purpose | **13,777** | 752 |
| Tax effect of income not taxable for tax purpose | **(1,300)** | (5,231) |
| Underprovision in respect of prior years | **82** | 115 |
| Tax effect of tax losses not recognised | **12,444** | 1,843 |
| Effect of different tax rates of subsidiaries operating in other jurisdictions | **(66)** | 27 |
| Others | **(278)** | (791) |
| Tax charge for the year | **1,207** | 285 |

## 15. (LOSS) EARNINGS PER SHARE

The calculation of the basic (loss) earnings per share is based on the following data:

| **(Loss) earnings** | **2005 HK$'000** | 2004 HK$'000 |
|---|---|---|
| (Loss) earnings for the purposes of basic (loss) earnings per share ((loss) profit for the year) | **(135,219)** | 20,117 |

| **Number of shares** | **2005** | 2004 (restated) |
|---|---|---|
| Weighted average number of ordinary shares for the purposes of basic (loss) earnings per share | **684,047,216** | 509,180,793 |

No diluted (loss) earnings per share has been presented as the exercise price of the Company's outstanding share options was higher than the average market price for both 2005 and 2004.

The weighted average number of ordinary shares for the purpose of basis (loss) earning per share has been adjusted retrospectively for the issue of ordinary shares by way of an open offer as referred to in note 25.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

## 16. PROPERTY, PLANT AND EQUIPMENT

| | Leasehold land and buildings HK$'000 | Plant and machinery HK$'000 | Furniture, fixtures and equipment HK$'000 | Moulds and stampers HK$'000 | Motor vehicles HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|---|
| COST OR VALUATION | | | | | | |
| At 1 January 2004 | 15,160 | 384,663 | 79,417 | 18,823 | 4,465 | 502,528 |
| Additions | – | 13,169 | 1,146 | – | 260 | 14,575 |
| Disposals | – | (1,132) | (15) | – | (81) | (1,228) |
| Disposal of a subsidiary | – | (807) | (149) | (537) | – | (1,493) |
| Adjusted on revaluation | (158) | – | – | – | – | (158) |
| At 31 December 2004 | 15,002 | 395,893 | 80,399 | 18,286 | 4,644 | 514,224 |
| Additions | – | 22,434 | 2,292 | – | 477 | 25,203 |
| Disposals | – | (3,880) | (187) | – | (551) | (4,618) |
| Adjusted on revaluation | (263) | – | – | – | – | (263) |
| **At 31 December 2005** | **14,739** | **414,447** | **82,504** | **18,286** | **4,570** | **534,546** |
| COMPRISING: | | | | | | |
| At cost | – | 414,447 | 82,504 | 18,286 | 4,570 | 519,807 |
| At valuation 2005 | 14,739 | – | – | – | – | 14,739 |
| | 14,739 | 414,447 | 82,504 | 18,286 | 4,570 | 534,546 |
| DEPRECIATION AND IMPAIRMENT LOSS | | | | | | |
| At 1 January 2004 | – | 230,856 | 50,764 | 16,177 | 2,988 | 300,785 |
| Provided for the year | 158 | 10,875 | 3,797 | 427 | 566 | 15,823 |
| Eliminated on disposals | – | (422) | (9) | – | (81) | (512) |
| Disposal of a subsidiary | – | (576) | (124) | (535) | – | (1,235) |
| Eliminated on revaluation | (158) | – | – | – | – | (158) |
| At 31 December 2004 | – | 240,733 | 54,428 | 16,069 | 3,473 | 314,703 |
| Provided for the year | 322 | 12,680 | 4,027 | 1 | 331 | 17,361 |
| Impairment loss recognised in the income statement (note 9(i)) | – | 79,279 | 7,525 | 1 | 29 | 86,834 |
| Eliminated on disposals | – | (3,224) | (172) | – | (551) | (3,947) |
| Eliminated on revaluation | (322) | – | – | – | – | (322) |
| **At 31 December 2005** | **–** | **329,468** | **65,808** | **16,071** | **3,283** | **414,629** |
| NET BOOK VALUES | | | | | | |
| **At 31 December 2005** | **14,739** | **84,979** | **16,696** | **2,215** | **1,288** | **119,917** |
| At 31 December 2004 | 15,002 | 155,160 | 25,971 | 2,217 | 1,171 | 199,521 |

## 16. PROPERTY, PLANT AND EQUIPMENT *(continued)*

The above items of property, plant and equipment are depreciated at the following rates per annum:

| | |
|---|---|
| Leasehold land and buildings | 2.5% or over the term of the leases if less than 40 years |
| Plant and machinery other than those for manufacturing of compact disc products | 10% – 20% |
| Furniture, fixtures and equipment | 20% |
| Moulds | 20% |
| Stampers | $33^1/_3$% |
| Motor vehicles | 30% |

Plant and machinery used for the manufacture of compact disc products are depreciated to their estimated residual value based on the actual units of production as a proportion of its total anticipated units of production. The anticipated units of production are determined with reference to the production specifications obtained from the suppliers.

The net book value of leasehold land and buildings comprises:

| | **2005 HK$'000** | 2004 HK$'000 |
|---|---|---|
| Land and buildings in Hong Kong under medium-term lease | **13,900** | 13,264 |
| Land and buildings outside Hong Kong under short-term lease | **839** | 1,738 |
| | **14,739** | 15,002 |

Notes:

(a) The leasehold land and buildings of the Group were revalued on 31 December 2005 on an open market value basis by Messrs. Great China Appraisal Limited and Messrs. Jointgoal Surveyors Limited. Both of them are firms of professional valuers and are not connected with the Group.

Market value is the estimated amount for which a property should be exchanged on the date of valuation between a willing buyer and a willing seller in an arm's length transaction. The valuation is made on assumption that the owner sells the property on the market without the benefit of cash rebate or any similar arrangement which could serve to affect the value of property.

If leasehold land and buildings had not been revalued, they would have been included in these financial statements at historical cost less accumulated depreciation and impairment losses of HK$9,903,000 (2004: HK$10,273,000).

(b) The net book value of property, plant and equipment includes an amount of HK$63,352,000 (2004: HK$44,225,000) in respect of assets held under finance leases.

(c) The Group had pledged its leasehold land and buildings with a net book value of HK$13,900,000 (2004: HK$13,264,000) to secure bank and other borrowings granted to the Group.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

## 17. GOODWILL

| | HK$'000 |
|---|---|
| COST | |
| At 1 January 2004 and 2005 | 49,432 |
| Elimination of accumulated amortisation upon the application of HKFRS 3 | (9,887) |
| **At 31 December 2005** | **39,545** |
| AMORTISATION | |
| At 1 January 2004 | 7,415 |
| Charged for the year | 2,472 |
| At 31 December 2004 | 9,887 |
| Elimination of accumulated amortisation upon the application of HKFRS 3 | (9,887) |
| At 31 December 2005 | – |
| NET BOOK VALUES | |
| **At 31 December 2005** | **39,545** |
| At 31 December 2004 | 39,545 |

Until 31 December 2004, goodwill had been amortised over its estimated useful life of 20 years.

For the purposes of impairment testing, goodwill acquired in a business combination has been allocated to the business segment of distribution of media. The Group tests goodwill annually for impairment, or more frequently if there are indications that goodwill might be impaired.

During the year ended 31 December 2005, management of the Group determines that there is no impairment of the goodwill. The recoverable amount of the cash generating unit relating to the goodwill has been determined based on a value in use calculation. That calculation uses cash flow projections based on financial budgets approved by management covering a 5-year period, and discount rate of 5%. Cash flows of cash generating unit beyond the 5-year period are extrapolated using a steady 10% growth rate as estimated by management by reference to relevant industry growth forecasts. Another key assumption for the value in use calculation is the budgeted gross margin, which is determined based on the unit's past performance and management's expectations for the market development. Management believes that any reasonably possible change in any of these assumptions would not cause the aggregate carrying amount of the cash generating unit to exceed the aggregate recoverable amount of the cash generating unit.

## 18. OTHER INTANGIBLE ASSETS

| | Development costs HK$'000 | Distribution rights HK$'000 | Technical know-how HK$'000 | Total HK$'000 |
|---|---|---|---|---|
| COST | | | | |
| At 1 January 2004 | 4,650 | 8,519 | – | 13,169 |
| Additions | 11,181 | – | 5,460 | 16,641 |
| At 31 December 2004 | 15,831 | 8,519 | 5,460 | 29,810 |
| Additions | 9,826 | – | – | 9,826 |
| **At 31 December 2005** | **25,657** | **8,519** | **5,460** | **39,636** |
| AMORTISATION AND IMPAIRMENT LOSS | | | | |
| At 1 January 2004 | – | – | – | – |
| Charge for the year | 129 | 655 | 455 | 1,239 |
| At 31 December 2004 | 129 | 655 | 455 | 1,239 |
| Charge for the year | 2,157 | 1,311 | 1,092 | 4,560 |
| **At 31 December 2005** | **2,286** | **1,966** | **1,547** | **5,799** |
| CARRYING AMOUNTS | | | | |
| **At 31 December 2005** | **23,371** | **6,553** | **3,913** | **33,837** |
| At 31 December 2004 | 15,702 | 7,864 | 5,005 | 28,571 |

Notes:

(a) Development costs are amortised on a straight line basis over ten years from the date of commencement of production of the relevant products.

(b) Distribution rights are amortised on a straight line basis over the remaining term of the distribution agreement.

(c) Technical know-how is amortised on a straight line basis over the terms of the technical know-how consultancy agreement of five years.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

## 19. INVENTORIES

| | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|
| Raw materials | **35,407** | 19,066 |
| Work in progress | **6,164** | 3,562 |
| Finished goods | **31,622** | 33,231 |
| | **73,193** | 55,859 |

## 20. DEBTORS, DEPOSITS AND PREPAYMENTS

| | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|
| Trade debtors | **122,680** | 77,103 |
| Other debtors, deposits and prepayments | **114,693** | 132,846 |
| | **237,373** | 209,949 |

The Group has a policy of allowing a credit period ranging from 30 to 90 days. The aged analysis of the trade debtors is as follows:

| | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|
| 1 to 3 months | **88,568** | 63,316 |
| 4 to 6 months | **12,500** | 5,050 |
| 7 to 9 months | **725** | 1,992 |
| 10 to 12 months | **3,745** | 125 |
| Over 1 year | **17,142** | 6,620 |
| | **122,680** | 77,103 |

## 20. DEBTORS, DEPOSITS AND PREPAYMENTS *(continued)*

At the balance sheet date, the Group's debtors, deposits and prepayments that are denominated in currencies other than the functional currencies of the relevant group entities are set out below:

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| United State dollars | **50,352** | 28,360 |
| Reminbi | **16,940** | 16,767 |
| Others | **369** | 385 |
| | **67,661** | 45,512 |

In the opinion of the directors, the carrying amounts of debtors approximates their fair values.

## 21. BANK DEPOSIT PLEDGED AND BANK BALANCES AND CASH

The bank deposit pledged represents bank balance pledged with a bank in the PRC as security for a guarantee issued by the bank to a court in the PRC in relation to a claim against a debtor of the Group amounting to HK$2,906,000. The deposit carries interest at 0.72% per annum (2004: 0.72% per annum). In the opinion of the directors, the carrying amount approximates its fair value.

Bank balances and cash at 31 December 2005 represent bank deposits and cash which carry at average market interest rate of 2.5% per annum. Bank balances and cash at 31 December 2004 comprised time deposits with banks of HK$10,190,000 carried fixed average interest rate of 1.85% per annum and other bank deposits and cash of HK$25,226,000 carried at average market interest rate of 1.6% per annum. In the opinion of the directors, the carrying amounts of bank balances and cash approximate their fair values.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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## 22. TRADE AND OTHER PAYABLES

| | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|
| Trade creditors | **41,139** | 25,320 |
| Other creditors and accruals | **36,879** | 25,559 |
| | **78,018** | 50,879 |

The aged analysis of the trade creditors is as follows:

| | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|
| 1 to 3 months | **33,297** | 18,511 |
| 4 to 6 months | **4,253** | 6,292 |
| 7 to 9 months | **472** | 183 |
| 10 to 12 months | **97** | 47 |
| Over 12 months | **3,020** | 287 |
| | **41,139** | 25,320 |

At the balance sheet date, the Group's trade and other payables that are denominated in currencies other than the functional currencies of the relevant group entities are set out below:

| | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|
| United State dollars | **29,302** | 13,962 |
| Reminbi | **504** | 531 |
| Others | **1,063** | 1,090 |
| | **30,869** | 15,583 |

In the opinion of the directors, the carrying amounts of trade and other payables approximates their fair values.

## 23. BANK AND OTHER BORROWINGS

| | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|
| Mortgage loan | **5,786** | 2,802 |
| Other bank loans | **44,574** | 63,117 |
| Bank import and export loans | **136,216** | 83,710 |
| Bank overdrafts | **15,724** | 22,129 |
| | **202,300** | 171,758 |
| Other loan | **6,630** | 6,630 |
| | **208,930** | 178,388 |
| Secured | **5,786** | 2,802 |
| Unsecured | **203,144** | 175,586 |
| | **208,930** | 178,388 |

| | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|
| Bank and other borrowings are repayable as follows: | | |
| On demand or within one year | **197,486** | 174,177 |
| More than one year, but not exceeding two years | **6,167** | 3,354 |
| More than two years, but not exceeding three years | **2,063** | 857 |
| More than three years, but not exceeding four yeas | **857** | – |
| More than four years, but not exceeding five years | **857** | – |
| More than five years | **1,500** | – |
| | **208,930** | 178,388 |
| Less: Amounts due within one year shown under current liabilities | **(197,486)** | (174,177) |
| Amounts due after one year | **11,444** | 4,211 |

## 23. BANK AND OTHER BORROWINGS *(continued)*

The Group's bank borrowings are principally on a floating rate basis which carry interest at prevailing market rates.

The ranges of effective annual interest rates for the year on the Group's borrowings are 1.9% to 9.1% (2004: 1.6% to 6.1%).

The other loan is unsecured, carries annual interest at 8% (2004: 7%) per annum and repayable within one year.

At the balance sheet date, the Group's borrowings that are denominated in currencies other than the functional currencies of the relevant group entities are set out below:

| | **2005**<br>**HK$'000** | 2004<br>HK$'000 |
|---|---|---|
| United State dollars | **8,986** | 9,984 |

In the opinion of the directors, the carrying amounts of bank and other borrowings approximate their fair value.

## 24. OBLIGATIONS UNDER FINANCE LEASES

| | Minimum lease payments | | Present value of minimum lease payments | |
|---|---|---|---|---|
| | **2005** | 2004 | **2005** | 2004 |
| | **HK$'000** | HK$'000 | **HK$'000** | HK$'000 |
| Amounts payable under finance leases | | | | |
| Within one year | **17,798** | 11,749 | **16,605** | 11,209 |
| In more than one year but not more than two years | **9,514** | 8,440 | **9,028** | 8,284 |
| In more than two years but not more than three years | **2,491** | 1,775 | **2,329** | 1,693 |
| | **29,803** | 21,964 | **27,962** | 21,186 |
| Less: Future finance charges | **(1,841)** | (778) | **N/A** | N/A |
| | **27,962** | 21,186 | **27,962** | 21,186 |
| Less: Amounts due within one year shown under current liabilities | | | **(16,605)** | (11,209) |
| Amounts due after one year | | | **11,357** | 9,977 |

## 24. OBLIGATIONS UNDER FINANCE LEASES *(continued)*

It is the Group's policy to lease certain of its plant and equipment under finance leases. The average lease term is 3 years. For the year ended 31 December 2005, the average effective annual borrowing rate ranged from 2.4% to 8.3% (2004: ranged from 2.5% to 5.5%). Interest rates are fixed at respective contract dates. All leases are on a fixed repayment basis and no arrangements have been entered into for contingent rental payments.

The Group's obligations under finance leases are secured by the lessor's charge over the leased assets.

The fair value of the Group's obligations under finance leases, determined based on the present value of the estimated future cash flows discounted using the prevailing market rate at the balance sheet date approximates to their carrying amount.

During the year, the Group entered into sixteen (2004: six) arrangements to obtain finance from the financers. Under these arrangements, the Group sold certain plant and machinery with a carrying amount of approximately HK$29.1 million (2004: HK$9.3 million) to the financers and obtained finance from the financers amounting to approximately HK$23.9 million (2004: HK$11.2 million). At the same time, the Group entered into lease agreements with the financers to lease back the plant and machinery for an average period of 36 (2004: 36) months; and at the end of those lease terms, the Group is entitled to either repurchase or continue to lease the plant and machinery at notional prices. Accordingly, the sale proceeds from the sale of these plant and machinery are treated as borrowings and classified as obligations under finance leases. The finance charges, which represent the differences between the total minimum lease payments and the obligations under finance leases, are charged to the income statement over the periods of the relevant leases so as to produce a constant periodic rate of charge on the remaining balance of the obligations for each accounting period.

## 25. SHARE CAPITAL

| | Number of shares | Amount |
|---|---|---|
| | | HK$'000 |
| Shares of HK$0.10 each | | |
| Authorised: | | |
| At 1 January 2004, 31 December 2004 and 2005 | 1,000,000,000 | 100,000 |
| Issued and fully paid: | | |
| At 1 January 2004 and 31 December 2004 | 458,308,545 | 45,830 |
| Issue of shares on 12 January 2005 (note) | 229,154,272 | 22,916 |
| **At 31 December 2005** | **687,462,817** | **68,746** |

Note: On 3 December 2004, the Company announced a proposal to raise not less than approximately HK$22.9 million, before expenses, by issuing not less than 229,154, 272 new shares but not more than 234,972,772 new shares by way of an open offer to its shareholders whose names appear on the register of members of the Company on 23 December 2004 at the subscription price of HK$0.10 per offer share on the basis of one offer share for every two existing shares held by the shareholders (the "Open Offer"). The Open Offer became unconditional on 10 January 2005 resulting in 229,154,272 offer shares having been issued on 12 January 2005.

## 26. SHARE OPTIONS

The Company operated share option schemes for the purpose of providing incentives to directors and eligible employees.

A share option scheme was adopted by the Company pursuant to a resolution passed on 8 November 1996 (the "Old Scheme"). Owing to the changes in the Listing Rules in relation to share option schemes, the board of directors considers it is appropriate to adopt a new share option scheme in replacement of the Old Scheme as the provision of the new share option scheme will be in line with such changes in the Listing Rules.

## 26. SHARE OPTIONS *(continued)*

Pursuant to a resolution of the annual general meeting passed on 12 June 2004, the Company adopted a new share option scheme (the "New Scheme") and the Old Scheme was terminated on the same date. Upon termination of the Old Scheme, no further options may be offered but in all other respects the provisions of the Old Scheme shall remain in force. The outstanding options under the Old Scheme shall continue to be subject to the provisions of the Old Scheme and the adoption of the New Scheme will not in any way affect the terms of the grant of such outstanding options.

**Old Scheme**

Under the Old Scheme, the board of directors of the Company may grant options to eligible employees, including directors (executive and non-executive) of the Company and its subsidiaries, to subscribe for shares in the Company.

The total number of shares in respect of which options may be granted under the Old Scheme is not permitted to exceed 10% of the issued shares of the Company from time to time excluding the aggregate number of shares of the Company which have been duly allotted and issued pursuant to the Old Scheme, without prior approval from the Company's shareholders. The number of shares in respect of which options may be granted to any individual in aggregate is not permitted to exceed 25% of the shares of the Company in issue and issuable.

Options granted must be take up within 30 days of the date of grant, upon payment of HK$1 per option. Options may be exercised at any time from the date of acceptance of the share option to the 10th anniversary of the date of acceptance of the option. The exercise price is determined by the directors, and will not be less than the higher of 80% of the average closing price of the shares for the 5 business days immediately preceding the date of grant and the nominal value of the Company's share. There is no minimum period for which an option must be held before it can be exercised.

All the outstanding options granted under the Old Scheme were cancelled on 30 December 2005.

## 26. SHARE OPTIONS *(continued)*

**New Scheme**

The New Scheme will expire in June 2014. Under the New Scheme, the board of directors of the Company may grant options to eligible employees and directors (including executive and non-executive) of the Company, its subsidiaries and associated companies to subscribe for shares in the Company.

The total number of shares which may be issued upon exercise of all options to be granted under the New Scheme and any other share option schemes shall not in aggregate exceed 10% of the total number of shares in issue as at the date of approval of the New Scheme, unless the Company obtains a fresh approval from its shareholders. Notwithstanding, this, the maximum number of shares which may be issued upon exercise of all outstanding options granted and yet to be exercised under the New Scheme and any other share option schemes shall not exceed 30% of the total number of shares in issue from time to time. The total number of shares issued and to be issued upon exercise of the options granted to any individual in any 12-month period shall not exceed 1% of the total number of shares in issue at any point in time, without prior approval from the Company's shareholders. Options granted to any individual who is a substantial shareholder of the Company or independent non-executive director or any of their respective associates in the 12-month period up to and including date of such grant in excess of 0.1% of the Company's share capital at the date of grant or with a value in excess of HK$5 million must be approved in advance by the Company's shareholders.

Options granted must be taken up within 28 days of the date of grant upon payment of HK$1 per grant of option. Options may generally be exercised at any time during the period after the option has been granted, such period to expire not later than 10 years after the date of the grant of the option. The subscription price for shares will not be less than the higher of (i) the closing price of the Company's shares on the date of options granted; (ii) the average closing price of the Company's shares for the 5 business days immediately preceding the date of options granted; and (iii) the nominal value of the Company's share. There is no minimum period for which an option must be held before it can be exercised.

During the year ended 31 December 2005, 45,829,766 options were granted by the Company under the New Scheme and no option under the Old Scheme was granted.

At the balance sheet date, the Company had 45,829,766 share options outstanding under the New Scheme, which represented approximately 6.67% of the Company's shares in issue at that date. The exercise in full of the remaining share options would, under the present capital structure of the Company, result in the issue of 45,829,766 additional ordinary shares of the Company and additional share capital of approximately HK$4.6 million and share premium of approximately HK$2.7 million (before issue expenses).

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## 26. SHARE OPTIONS *(continued)*

**New Scheme** *(continued)*

The following table discloses movements in the Company's share options during the year ended 31 December 2005:

| | Date of share option granted | Share option scheme category | Outstanding at 1.1.2004 and 1.1.2005 | Granted during the year | Cancelled during the year | Outstanding at 31.12.2005 | Subscription price | Exercise period |
|---|---|---|---|---|---|---|---|---|
| **Directors** | | | | | | | | |
| Ms. Ho Yin King, Helena | 24.12.1996 | 1997A | 3,750,000 | – | (3,750,000) | – | 1.0336 | 8.1.1997 – 7.1.2007 |
| | 25.1.2005 | 2005 | – | 6,872,628 | – | 6,872,628 | 0.1580 | 25.1.2005 – 24.1.2015 |
| Mr. Ho Fai Keung, Jacky | 24.12.1996 | 1997A | 2,537,000 | – | (2,537,000) | – | 1.0336 | 8.1.1997 – 7.1.2007 |
| | 25.1.2005 | 2005 | – | 6,872,628 | – | 6,872,628 | 0.1580 | 25.1.2005 – 24.1.2015 |
| Mr. Low Nyap Heng | 25.1.2005 | 2005 | – | 6,872,628 | – | 6,872,628 | 0.1580 | 25.1.2005 – 24.1.2015 |
| Mr. Cheung Sze Ming | 25.1.2005 | 2005 | – | 6,872,628 | – | 6,872,628 | 0.1580 | 25.1.2005 – 24.1.2015 |
| Dr. Li Sau Hung, Eddy | 25.1.2005 | 2005 | – | 2,291,542 | – | 2,291,542 | 0.1580 | 25.1.2005 – 24.1.2015 |
| Mr. Leung Ka Kui, Johnny | 25.1.2005 | 2005 | – | 2,291,542 | – | 2,291,542 | 0.1580 | 25.1.2005 – 24.1.2015 |
| Mr. Chan Kam Kwan, Jason | 25.1.2005 | 2005 | – | 2,291,542 | – | 2,291,542 | 0.1580 | 25.1.2005 – 24.1.2015 |
| Total for directors | | | 6,287,000 | 34,365,138 | (6,287,000) | 34,365,138 | | |
| Employees | 25.12.1996 | 1997B | 4,300,000 | – | (4,300,000) | – | 1.0336 | 24.1.1997 – 23.1.2007 |
| | 4.9.1999 | 1999 | 1,050,000 | – | (1,050,000) | – | 0.8832 | 4.9.1999 – 3.9.2009 |
| | 25.1.2005 | 2005 | – | 11,464,628 | – | 11,464,628 | 0.1580 | 25.1.2005 – 24.1.2015 |
| Total for employees | | | 5,350,000 | 11,464,628 | (5,350,000) | 11,464,628 | | |
| | | | 11,637,000 | 45,829,766 | (11,637,000) | 45,829,766 | | |

## 26. SHARE OPTIONS *(continued)*

**New Scheme** *(continued)*

| | Date of share option granted | Share option scheme category | Outstanding at 1.1.2004 and 1.1.2005 | Granted during the year | Cancelled during the year | Outstanding at 31.12.2005 | Percentage to total Company's shares in issue at end of the year |
|---|---|---|---|---|---|---|---|
| Total under Old Scheme | | | | | | | |
| – 1997A | | | 6,287,000 | – | (6,287,000) | – | N/A |
| – 1997B | | | 4,300,000 | – | (4,300,000) | – | N/A |
| – 1999 | | | 1,050,000 | – | (1,050,000) | – | N/A |
| | | | 11,637,000 | – | (11,637,000) | – | N/A |
| Total under New Scheme | | | | | | | |
| – 2005 | | | – | 45,829,766 | – | 45,829,766 | 6.67% |
| | | | 11,637,000 | 45,829,766 | (11,637,000) | 45,829,766 | |

Notes:

(i) The 1997A, 1997B and 1999 options were granted under the scheme adopted on 8 November 1996 and terminated on 12 June 2004 (the "Old Scheme"). The outstanding options granted under the Old Scheme were cancelled on 30 December 2005. The 2005 options were granted under scheme adopted on 12 June 2004 (the "New Scheme").

(ii) Other than that mentioned in note (i), no option was exercised, lapsed or cancelled during the years ended 31 December 2005 and 2004.

(iii) The closing price of the Company's shares immediately before 25 January 2005, the date of grant of 2005 options, was HK$0.1590.

The estimated fair value of each option granted on 25 January 2005 is approximately HK$0.096.

## 26. SHARE OPTIONS *(continued)*

**New Scheme** *(continued)*

The fair values were calculated using the Black-Scholes pricing model. The inputs into the model were as follows:

| | **2005** |
|---|---|
| Stock asset price | **HK$0.1580** |
| Exercise price | **HK$0.1580** |
| Expected volatility | **72%** |
| Expected life | **5 years** |
| Risk-free rate | **2.801%** |
| Expected dividend yield | **0%** |

Expected volatility was determined by using the historical volatility of the Company's share price over the previous ten years. The expected life used in the model has been adjusted, based on management best estimate, for the effects of non-transferability, exercise restrictions and behavioural considerations.

Because the Black-Scholes option pricing model requires the input of highly subjective assumptions, including the volatility of share price, changes in subjective input assumptions can materially affect the fair value estimate.

## 27. DISTRIBUTABLE RESERVES OF THE COMPANY

In the opinion of directors, the reserves of the Company which are available for distribution to shareholders at 31 December 2005 amounted to HK$128,412,000 (2004: HK$136,142,000), representing the aggregate of share premium of HK$111,575,000 (2004: HK$113,225,000), contributed surplus of HK$15,048,000 (2004: HK$15,048,000) and retained profits of HK$1,789,000 (2004: HK$7,869,000).

The contributed surplus of the Company represents the difference between the underlying net tangible assets of the subsidiaries acquired by the Company and the nominal value of the share capital issued by the Company at the time of the group reorganisation prior to the listing of the Company's shares in 1994. Under the Companies Act 1981 of Bermuda (as amended), the contributed surplus is available for distribution to shareholders. However, the Company cannot declare or pay a dividend, or make a distribution out of contributed surplus if (a) it is, or would after the payment be, unable to pay its liabilities as they become due; and (b) the realisable value of its assets would thereby be less than the aggregate of its liabilities and its issued share capital and share premium account.

## 28. DEFERRED TAXATION

The followings are the major deferred tax liabilities (assets) recognised and movements thereon during the current and prior years:

| | **Accelerated tax depreciation** | **Tax losses** | **Revaluation of properties** | **Total** |
|---|---|---|---|---|
| | HK$'000 | HK$'000 | HK$'000 | HK$'000 |
| At 1 January 2004 | 22,115 | (22,115) | 999 | 999 |
| (Credit) charge to income for the year | (19,900) | 19,900 | – | – |
| At 31 December 2004 | 2,215 | (2,215) | 999 | 999 |
| Charge (credit) to the income for the year | 9,890 | (9,890) | – | – |
| **At 31 December 2005** | **12,105** | **(12,105)** | **999** | **999** |

For the purpose of balance sheet presentation, certain deferred tax assets and liabilities have been offset. At 31 December 2005, the Group has unused tax losses of approximately HK$171,424,000 (2004: HK$43,684,000) available for offset against future profits. A deferred tax asset has been recognised in respect of HK$69,284,000 (2004: HK$12,652,000) of such losses. No deferred tax asset has been recognised in respect of the remaining HK$102,140,000 (2004: HK$31,032,000) due to the unpredictability of future profit streams. Included in unrecognised tax losses are losses of HK$17,824,000 (2004: HK$9,492,000) which will expire as follows:

| | **Tax losses** | |
|---|---|---|
| **Year of expiry** | **2005** | 2004 |
| | **HK$'000** | HK$'000 |
| 2006 | **1,477** | 1,477 |
| 2007 | **4,409** | 4,409 |
| 2008 | **1,233** | 1,233 |
| 2009 | **2,373** | 2,373 |
| 2010 | **8,332** | – |
| | **17,824** | 9,492 |

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

## 29. DISPOSAL OF A SUBSIDIARY

During the year ended 31 December 2004, the Group disposed of its subsidiary, Sunny Printing (International) Company Limited ("Sunny Printing"). The net assets of Sunny Printing at the date of disposal were as follows:

| | HK$'000 |
|---|---|
| NET ASSETS DISPOSED OF: | |
| Property, plant and equipment | 258 |
| Inventories | 316 |
| Debtors, deposits and prepayments | 3,563 |
| Bank balance and cash | 115 |
| Trade and other payables | (2,168) |
| Bank overdrafts | (1,140) |
| | 944 |
| Capital reserve realised on disposal | (1,463) |
| Gain on disposal of a subsidiary | 619 |
| Total cash consideration | 100 |
| Net cash inflow on disposal: | |
| Cash consideration received | 100 |
| Bank balances and cash disposed of | (115) |
| Bank overdrafts disposed of | 1,140 |
| | 1,125 |

The subsidiary disposed of in prior year contributed HK$5,596,000 to the Group's revenue and incurred a loss of HK$118,000 attributable to the Group for the year ended 31 December 2004.

## 30. MAJOR NON-CASH TRANSACTIONS

During the year ended 31 December 2004, the Group was released by a supplier of its obligation to make payment for assets purchased of HK$3,510,000 from the supplier.

## 31. AMOUNT RECEIVABLE FROM A LEGAL CLAIM

In 1997, a subsidiary of the Company (the "Subsidiary") entered into an agreement with a former customer, IBM Engineering Technology (Shanghai) Co. Ltd. ("IBMETC") under which the Subsidiary was required to set up a software manufacturing fulfillment plant in Shanghai, the PRC and IBMETC was obliged, among other things, to place annual minimum orders to the Subsidiary for the five years ended 31 December 2002. Should IBMETC fail to place the minimum orders, the Subsidiary is entitled to claim for the shortfall. During the two years ended 31 December 1999, the orders from IBMETC did not meet the minimum orders stipulated in the agreement and IBMETC had unilaterally terminated the agreement in March 2000. The Group took arbitration proceedings in 2000 to claim against IBMETC for the total shortfall under the agreement amounting to approximately US$54 million (approximately HK$420 million) or damages to be assessed.

The tribunal has issued a partial award on the issue of liability on 18 July 2003. Pursuant to the partial award, the tribunal ruled that IBMETC has wrongfully purported to terminate the agreement and acted in repudiatory breach of the agreement. It is therefore a matter for the quantum hearing to assess how much IBMETC has to pay to the Subsidiary in terms of damages.

The quantum hearing completed in March 2005, and the final award (the "Award") was published on 30 July 2005. Damages and interest of US$12,507,700 (approximately HK$97,560,000) and US$2,853,139 (approximately HK$22,254,000) respectively have been awarded by the tribunal in favour of the Subsidiary. The Award provided for payment of such sum (together with interest from the date of the Award at the prime rate of The Hongkong and Shanghai Banking Corporation Limited plus 0.5% compounded monthly until payment) to be made to the Subsidiary within 14 days upon receipt of the formal notice of Award by the parties' lawyers, which took place on 1 August 2005.

Following the publication of the Award made on 30 July 2005, the Subsidiary applied to the Shanghai First Intermediate People's Court (the "Shanghai Court") for enforcement of the Award against IBMETC. IBMETC subsequently applied to the Shanghai Court for non-enforcement of the Award, but the application was dismissed by the Shanghai Court on 7 April 2006. According to legal advice obtained by the Subsidiary in the PRC, the decision of the Shanghai Court on 7 April 2006 is final and conclusive and cannot be appealed. The Subsidiary therefore was at liberty to continue with its enforcement application against IBMETC. As part of the enforcement application, cash in IBMETC's bank accounts of approximately RMB60 million (approximately HK$58.2 million) was frozen and IBMETC was required to provide a bank guarantee to the Shanghai Court of approximately RMB70 million (approximately HK$67.9 million). The Subsidiary received the sum of RMB20,692,000 (approximately HK$20,071,000) and RMB62,026,000 (approximately HK$60,165,000) on 26 April 2006 and 16 May 2006 respectively as part of its recovery from IBMETC in the enforcement application.

## 31. AMOUNT RECEIVABLE FROM A LEGAL CLAIM *(continued)*

The tribunal has not yet made an award in respect of the costs of the arbitration proceedings amounted to HK$40.4 million (31 December 2004: HK$40.4 million).

As at 31 December 2005, total direct expenditure incurred for the claim amounted to HK$102.1 million (2004: HK$87.4 million). The directors are of the opinion that the above expenditure is fully recoverable from IBMETC. Therefore, the expenditures were recognised as other receivables and included under debtors, deposits and prepayments in the balance sheet. The direct expenditure incurred mainly comprised legal and professional fees, loss on disposal of an associate and other direct costs incurred in respect of the arbitration.

## 32. CONTINGENT LIABILITIES

As at 31 December 2004, bills discounted with recourse of the Group amounted to HK$29,839,000.

## 33. LEASE COMMITMENTS

**The Group as lessee**

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

| | **2005**<br>**HK$'000** | 2004<br>HK$'000 |
|---|---|---|
| Within one year | **5,590** | 5,748 |
| In the second to fifth year inclusive | **12,977** | 15,549 |
| Over five years | **2,061** | 4,738 |
| | **20,628** | 26,035 |

Operating lease payments represent rentals payable by the Group for certain of its office properties. Leases are negotiated for an average term of two (2004: three) years and rentals are fixed for an average of two (2004: three) years.

## 33. LEASE COMMITMENTS *(continued)*

**The Group as lessor**

All of the plant and machinery leased originally have committed lessees for an average of two (2004: two) years. Rentals are fixed throughout the lease period without any renewal option.

At the balance sheet date, the Group had contracted with lessees for the following future minimum lease payments:

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Within one year | **2,520** | 90 |
| In the second year | **2,310** | – |
| | **4,830** | 90 |

## 34. CAPITAL COMMITMENTS

The Group did not have any significant capital commitment at 31 December 2005.

At 31 December 2004, the Group had capital expenditure in respect of acquisition of property, plant and equipment contracted for but not provided in the financial statements amounting to HK$7,214,000.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

## 35. RETIREMENT AND BENEFITS PLANS

The Group has a Mandatory Provident Fund Scheme ("MPF Scheme") for all employees in Hong Kong. The MPF Scheme is registered with the Mandatory Provident Fund Scheme Authority under the Mandatory Provident Fund Schemes Ordinance. The assets of the MPF Scheme are held separately from those of the Group in funds under the control of an independent trustee. Under the rules of the MPF Scheme, the employer and its employees are each required to make contributions to the MPF Scheme at rates specified in the rules of the MPF Scheme. The only obligation of the Group with respect to MPF Scheme is to make the required contributions under the MPF Scheme.

The retirement benefits scheme contributions arising from the MPF Scheme charged to the income statement represent contributions payable to the funds by the Group at rates specified in the rules of the MPF Scheme.

The employees of the Company's subsidiaries in other jurisdictions are members of state-managed retirement benefits schemes operated by the government of the respective jurisdictions. The subsidiaries are required to contribute a specified percentage of their payroll costs to the retirement benefits schemes. The only obligations of the Group with respect of the retirement benefits schemes is to make the specified contributions.

During the year, the Group made retirement benefits scheme contributions amounting to HK$757,000 (2004: HK$601,000). At the balance sheet date, there are no forfeited contributions.

## 36. RELATED PARTY TRANSACTIONS

During the year, the Group paid rentals to Ms. Chan Siu Chu, mother of the directors of the Company, namely Ms. Ho Yin King, Helena and Mr. Ho Fai Keung, Jacky and mother-in-law of the director of the Company, Ms. Lo Suk King, amounting to HK$282,000 (2004: HK$282,000). The transaction was conducted on terms with reference to current market prices.

**Compensation of key management personnel**

The remuneration of directors and other members of key management during the year was as follows:

| | **2005**<br>**HK$'000** | 2004<br>HK$'000 |
|---|---|---|
| Short-term benefits | **13,251** | 11,745 |
| Share-based payments | **3,300** | – |
| | **16,551** | 11,745 |

## 37. POST BALANCE SHEET EVENTS

Subsequent to 31 December 2005, the Group has the following significant events:

**i) Issuance of HK$25 million unsecured notes and unlisted warrants**

Pursuant to the subscription agreements ("Subscription Agreements") entered into between a wholly-owned subsidiary of the Company (the "Issuer") and certain independent third parties (the "Subscribers") on 28 December 2005, the Issuer issued, and the Subscriber subscribed for, notes (the "Notes") in the aggregate principal of HK$25 million on 24 March 2006. The Notes are unsecured and carry interest at 10% per annum. As stipulated in the Subscription Agreements and the supplementary amendments to the Subscription Agreements, upon the receipt of the proceeds from the Award as refer to in note 31 by the Group but up to the aggregate principal amount of the Notes outstanding together with interest thereon from time to time, the Issuer shall within 30 days redeem the Notes.

On the same date, the Company issued unlisted warrants to the Subscribers (the "Warrants") conferring rights entitling the holders to subscribe for up to HK$17,872,920 in aggregate in cash for 137,484,000 new shares of HK$0.10 each of the Company at an initial subscription price of HK$0.13 per share, subject to adjustment. The Warrants are exercisable within a period of three years from 24 March 2006 to 23 March 2009.

**ii) Receipt of cash compensation from the legal claim**

The Group received the sum of approximately RMB20,692,000 (approximately HK$20,071,000) and RMB62,026,000 (approximately HK$60,165,000) on 26 April 2006 and 16 May 2006 respectively as part of its recovery from IBMETC in the enforcement application of the legal claim as referred to in note 31.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

## 38. PARTICULARS OF PRINCIPAL SUBSIDIARIES

Particulars of the principal subsidiaries as at 31 December 2005 are as follows:

| Name of subsidiary | Place/country of incorporation and operation (Note c) | Issued and paid up share capital/ registered capital | Percentage of issued share capital/ registered capital (Note a) | Principal activities |
|---|---|---|---|---|
| Afex International (HK) Limited | Hong Kong | 50,000 ordinary shares of HK$1 each | 100 | Trading of computer accessories |
| Cheson Magnetic Limited | Macau | MOP5,100,000 | 100 | Manufacture of floppy disks |
| Clearview Development Limited | British Virgin Islands | 10,000 ordinary shares of US$1 each | 100 | Investment holding |
| Feitian Magnetic Information-Technology (Shenzhen) Co., Ltd. | The PRC# | US$2,500,000 | 100 | Manufacture of floppy disks |
| Fortune Luck Development Ltd. | British Virgin Islands | 4 ordinary shares of US$1 each | 100 | Distribution of data media products |
| Great China Global Limited | British Virgin Islands | 1 ordinary share of US$1 each | 100 | Distribution of data media products |
| Havenport Management Limited | British Virgin Islands | 10,000 ordinary shares of US$1 each | 100 | Investment holding |

## 38. PARTICULARS OF PRINCIPAL SUBSIDIARIES *(continued)*

| Name of subsidiary | Place/country of incorporation and operation (Note c) | Issued and paid up share capital/ registered capital | Percentage of issued share capital/ registered capital (Note a) | Principal activities |
|---|---|---|---|---|
| Jackin Accessories Industrial Company Limited | British Virgin Islands | 1 ordinary share of US$1 each | 100 | Investment holding |
| Jackin Trading Company Limited | British Virgin Islands | 1 ordinary share of US$1 | 100 | Trading of data media products |
| Jackin Magnetic Company Limited | Hong Kong | 10 ordinary shares of HK$100 each and 10,000 non-voting deferred shares of HK$100 each (Note b) | 100 | Trading of floppy disks |
| Jackin Magnetic (United Kingdom) Company Limited | England | 3 ordinary shares of GBP 1 each | 100 | Trading of floppy disks |
| Jackin Manufacturing (Shenzhen) Limited | British Virgin Islands | 1 ordinary share of US$1 | 100 | Investment holding |
| Jackin Optical Marketing Company Limited | Hong Kong | 2 ordinary shares of HK$1 each | 100 | Trading of data media products |
| Jackin Total Fulfilment Services Limited | Hong Kong | 2 ordinary shares of HK$1 each | 100 | Inactive |

## 38. PARTICULARS OF PRINCIPAL SUBSIDIARIES *(continued)*

| Name of subsidiary | Place/country of incorporation and operation (Note c) | Issued and paid up share capital/ registered capital | Percentage of issued share capital/ registered capital (Note a) | Principal activities |
|---|---|---|---|---|
| Jackin U.S.A. Inc. | United States of America | 1 ordinary share of US$1 | 100 | Trading of data media products and computer accessories |
| Jackin Video Cassette Co. Limited | Hong Kong | 1,000 ordinary shares of HK$1 each and 1,000,000 non-voting deferred shares of HK$1 each (Note b) | 100 | Property holding |
| Jackin Video Cassette (Taiwan) Limited | Taiwan | 2,000,000 ordinary shares of NT$10 each | 99.9 | Property holding |
| Noble Team Holdings Limited | British Virgin Islands | 10,000 ordinary shares of US$1 each | 100 | Investment holding |
| Oakview International Limited | British Virgin Islands | 100 ordinary shares of US$1 each | 100 | Investment holding |
| Prince Diamond Co., Ltd. | British Virgin Islands | 2 ordinary shares of US$1 each | 100 | Investment holding |
| Tempair Developments Limited | British Virgin Islands | 10,000 ordinary shares of US$1 each | 100 | Investment holding |

## 38. PARTICULARS OF PRINCIPAL SUBSIDIARIES *(continued)*

| Name of subsidiary | Place/country of incorporation and operation (Note c) | Issued and paid up share capital/ registered capital | Percentage of issued share capital/ registered capital (Note a) | Principal activities |
|---|---|---|---|---|
| Ugent Holdings Limited | British Virgin Islands | 10,000 ordinary shares of US$1 each | 100 | Investment holding |
| 珠海利滿豐源打印耗材有限公司 | The PRC# | HK$5,000,000 | 100 | Manufacture of computer accessories |
| 深圳利滿豐源打印耗材有限公司 | The PRC# | HK$5,000,000 | 100 | Manufacture of computer accessories |

Notes:

(a) Except Oakview International Limited, which is directly owned by the Company, all other subsidiaries are indirectly held.

(b) The Company holds 100% of the issued ordinary share capital only. The deferred shares, which are not held by the Group, practically carry no rights to dividends or to receive notice of or to attend or vote at any general meeting of the respective companies or to participate in any distribution on winding up.

(c) Other than those subsidiaries incorporated in the British Virgin Islands, whose place of operations are basically in Hong Kong, the places of operations of all other subsidiaries are the same as their places of incorporation.

(d) The directors are of the opinion that a complete list of the particulars of all subsidiaries will be of excessive length and therefore the above list contains only the particulars of the subsidiaries which materially affect the results or assets of the Group.

(e) None of the subsidiaries had issued any debt securities at the end of the year.

# These subsidiaries are wholly foreign-owned enterprises established in the PRC.