Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

1. GENERAL

The Company is a public limited company incorporated in the Cayman Islands under the Companies Law as an exempted company with limited liability on 5 January 2004. Its shares are listed on The Stock Exchange of Hong Kong Limited (the "Stock Exchange"). The addresses of the registered office and principal place of business of the Company in Hong Kong are disclosed in the "Corporate Information" section to the annual report.

Pursuant to a special resolution of the board of directors of the Company, the name of the Company has been changed from ZZNode Holdings Company Limited to ZZNode Technologies Company Limited effective 17 May 2006.

The consolidated financial statements are presented in Renminbi, which is the same as the functional currency of the Company.

The Company is an investment holding company. The principal activities of its subsidiaries are set out in note 32.

2. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS/CHANGE IN ACCOUNTING POLICIES

In the current year, the Group has applied, for the first time, a number of new standard, amendments and interpretations ("new HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA"), which are either effective for accounting periods beginning on or after 1 December 2005 or 1 January 2006. The adoption of the new HKFRSs had no material effect on how the results and financial position for the current or prior accounting periods have been prepared and presented. Accordingly, no prior period adjustment is required.

The Group has not early applied the following new standards, amendment or interpretations that have been issued but are not yet effective. The directors of the Company anticipate that the application of these standards, amendment or interpretations will have no material impact on the results and the financial position of the Group.

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

2. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS/CHANGE IN ACCOUNTING POLICIES *(CONTINUED)*

HKAS 1 (Amendment)	Capital Disclosures[1]
HKFRS 7	Financial Instruments: Disclosures[1]
HKFRS 8	Operating Segments[2]
HK(IFRIC)-Int 7	Applying the Restatement Approach under HKAS 29 Financial Reporting in Hyperinflationary Economies[3]
HK(IFRIC)-Int 8	Scope of HKFRS 2[4]
HK(IFRIC)-Int 9	Reassessment of Embedded Derivatives[5]
HK(IFRIC)-Int 10	Interim Financial Reporting and Impairment[6]
HK(IFRIC)-Int 11	HKFRS 2 – Group and Treasury Share Transactions[7]
HK(IFRIC)-Int 12	Service Concession Arrangements[8]

[1] Effective for annual periods beginning on or after 1 January 2007
[2] Effective for annual periods beginning on or after 1 January 2009
[3] Effective for annual periods beginning on or after 1 March 2006
[4] Effective for annual periods beginning on or after 1 May 2006
[5] Effective for annual periods beginning on or after 1 June 2006
[6] Effective for annual periods beginning on or after 1 November 2006
[7] Effective for annual periods beginning on or after 1 March 2007
[8] Effective for annual periods beginning on or after 1 January 2008

3. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared on the historical cost basis and in accordance with Hong Kong Financial Reporting Standards 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 of Hong Kong Limited and the Hong Kong Companies Ordinance.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries). Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

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.

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

3. SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

Basis of consolidation *(Continued)*

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

Minority interests in the net assets of consolidated subsidiaries are presented separately from the Group's equity therein. Minority interests in the net assets consist of the amount of those interests at the date of the original business combination and the minority share of changes in equity since the date of the combination. Losses applicable to the minority in excess of the minority interest in the subsidiary's equity are allocated against the interests of the Group except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses.

Investments in associates

An associate is an entity over which the Group has significant influence and that is neither a subsidiary nor an interest in a joint venture. Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies.

The results and assets and liabilities of associates are incorporated in these financial statements using the equity method of accounting. Under the equity method, investments in associates are carried in the consolidated balance sheet at cost as adjusted for post-acquisition changes in the Group's share of the profit or loss and of changes in equity of the associate, less any identified impairment loss. When the Group's share of losses of an associate equals or exceeds its interest in that associate, the Group discontinues recognising its share of further losses. An additional share of losses is provided for and a liability is recognised only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of that associate.

Any excess of the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities over the cost of acquisition, after reassessment, is recognised immediately in profit or loss.

Where a group entity transacts with an associate of the Group, profits and losses are eliminated to the extent of the Group's interest in the relevant associate.

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods and services provided in the normal course of business, net of discounts and sales related taxes.

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

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

3. SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

Revenue recognition *(Continued)*

Maintenance and training income is recognised when services are provided.

Interest income from a financial asset 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 asset to that asset's net carrying amount.

Dividend income from investments is recognised when the shareholders' rights to receive payment have been established.

Property, plant and equipment

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

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

Leasehold land and buildings	5%
Leasehold improvements	Over the term of the leases
Furniture and fixtures	20%
Computers and equipment	20%
Motor vehicles	12.5%

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 the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the consolidated income statement in the year in which the item is derecognised.

Operating leases

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Rentals payable under operating leases are charged to profit or loss on a straight-line basis over the terms of the relevant leases. Benefits received and receivable as an incentive to enter into an operating lease are recognised as a reduction of rental expense over the lease term on a straight-line basis.

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

3. SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

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 exchanges prevailing on the dates of the transactions. At each balance sheet date, monetary items denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. 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.

Government grants

Government grants are recognised as income over the periods necessary to match them with the related costs. Grants related to expense items are recognised in the same period as those expenses are charged in the consolidated income statement and are reported separately as other income.

Retirement benefit costs

Payments to the state-managed retirement benefits schemes are charged as expenses as the employees render the services entitling them to the contributions.

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 consolidated 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 consolidated financial statements and the corresponding tax base 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.

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

3. SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

Taxation *(Continued)*

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, 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 profits 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. 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.

Intangible assets

Intangible assets acquired separately

Intangible assets acquired separately and 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 consolidated income statement when the asset is derecognised.

Research and development expenditure

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

An internally-generated intangible asset arising from development expenditure is recognised only if it is anticipated that the development costs incurred on a clearly-defined project will be recovered through future commercial activity. The resultant asset is amortised on a straight-line basis over its useful life, and carried at cost less any subsequent accumulated amortisation and any accumulated impairment losses.

The amount initially recognised for internally-generated intangible asset is the sum of the expenditure incurred from the date when the intangible asset first meets the recognition criteria. 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.

Subsequent to initial recognition, internally-generated intangible asset is reported at cost less accumulated amortisation and accumulated impairment losses, on the same basis as intangible assets acquired separately.

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

3. SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

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. A reversal of impairment loss is recognised as income immediately.

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 weighted average method.

Financial instruments

Financial assets and financial liabilities are recognised on the 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. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in profit or loss. All regular way purchases or sales of financial assets are recognised and derecognised on a trade date basis. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace.

Financial assets

The Group's financial assets are mainly classified as loans and receivables. The accounting policy adopted in respect of loans and receivables is set out below.

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

3. SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

Financial instruments *(Continued)*

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. At each balance sheet date subsequent to initial recognition, loans and receivables (including trade receivables, note receivables, other receivables, amount due from a related party, bank deposits and bank balances and cash) are carried at amortised cost using the effective interest method, less any identified impairment losses. An impairment loss is recognised in profit or loss when there is objective evidence that the asset is impaired, and is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate. 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.

Financial liabilities and equity

Financial liabilities and equity instruments issued by a group entity 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. The Group's financial liabilities are classified as other financial liabilities. The accounting policies adopted in respect of financial liabilities and equity instruments are set out below.

Other financial liabilities

Other financial liabilities (including trade payables, note payables, other payables and note receivables discounted with recourse) are subsequently measured at amortised cost, using the effective interest method.

Equity instruments

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

Consideration paid to reacquire the Company's own equity instruments is deducted from equity. No gain or loss is recognised in profit or loss.

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.

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

3. SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

Financial instruments *(Continued)*

Financial liabilities are derecognised 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 paid or payable is recognised in profit or loss.

Share-based payment transactions

Equity-settled share-based payment transactions

The fair value of services received determined by reference to the fair value of share options granted at the grant date is expensed on a straight-line basis over the vesting period, with a corresponding increase in share option reserve.

At each balance sheet date, the Group revises its estimates of the number of options that are expected to ultimately vest. The impact of the revision of the original estimates, if any, is recognised in profit or loss over the remaining vesting period, with a corresponding adjustment to share option reserve.

At the time when the share options are exercised, the amount previously recognised in share option reserve will be transferred to share premium. When the share options are forfeited after the vesting date or are still not exercised at the expiry date, the amount previously recognised in share option reserve will continue to be held in share option reserve.

4. KEY SOURCES OF ESTIMATION UNCERTAINTY

The key assumption concerning the future, and other key sources of estimation uncertainty at the balance sheet dates, 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.

Allowance of trade receivables

When there is objective evidence of an impairment loss, the amount of the impairment loss is measured as the difference between the carrying amount of the assets and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). Where the actual future cash flows are less than expected, a material impairment loss may arise.

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

5. FINANCIAL INSTRUMENTS

5a. Financial risk management objectives and polices

The Group's major financial instruments include trade receivables, note receivables, other receivables, amount due from a related company, bank deposits, bank balances and cash, trade payables, note payables, advances from customers, accrued charges, other payables and bank borrowings. 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. Management manages and monitors these exposures to ensure appropriate measures are implemented on a timely and effective manner.

Currency risk

Certain bank balances of the Group are denominated in foreign currencies as disclosed in note 22. The Group currently does not have a foreign currency hedging policy. However, management monitors foreign exchange exposure and will consider hedging significant foreign currency exposure should the need arise.

Credit risk

As at 31 December 2006, the Group's maximum exposure to credit risk which will cause a financial loss to the Group due to failure to discharge an obligation by the counterparties is mainly arising from the carrying amount of the respective recognised financial assets as stated in the consolidated balance sheet.

In order to minimise the credit risk, management has credit approvals and other monitoring procedures to ensure that follow-up action is taken to recover overdue debts. In addition, the Group reviews the recoverable amount of each individual trade debt at each balance sheet date to ensure that adequate impairment losses are made for irrecoverable amounts. In this regard, the directors of the Company consider that the Group's credit risk is reduced.

The credit risk on liquid funds is limited because the counterparties are banks with high credit ratings.

The Group has its credit risk concentrated in a few customers. As at 31 December 2006, approximately 62% of the Group's trade receivables are receivables from its major customers. The Group's will continue to diversify and expand its customer base to mitigate this risk.

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

5. FINANCIAL INSTRUMENTS *(CONTINUED)*

5b. Fair value

The fair value of other financial assets and financial liabilities (excluding derivative instruments) are determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions.

The directors consider that the fair values of financial assets and financial liabilities recorded at amortised cost in the consolidated financial statements approximate to their corresponding carrying amounts.

6. REVENUE

Revenue represents the net amounts received and receivable for sales of hardware and software and service income from provision of system integration, maintenance, training and other services. An analysis of the Group's revenue for the year is as follows:

	2006	2005
	RMB	*RMB*
Sales of self-developed software	**36,983,360**	33,054,203
Sales of third party software and hardware	**73,299,551**	60,427,720
System integration services	**1,188,000**	1,327,009
Maintenance, training and other services	**13,915,129**	2,505,586
	125,386,040	97,314,518

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

7. BUSINESS AND GEOGRAPHICAL SEGMENTS

Business segments

The Group is principally engaged in the development and provision of telecommunications operational support system products and solutions in the PRC. Sales of self-developed software, and third party software and hardware are delivered mainly as part of the system integration solutions provided by the Group.

Segment information about these businesses is presented below:

For the year ended 31 December 2006

	Sales of self-developed software	Sales of third party software and hardware	System integration services	Maintenance, training and other services	Consolidated
	RMB	*RMB*	*RMB*	*RMB*	*RMB*
REVENUE					
External sales	36,983,360	73,299,551	1,188,000	13,915,129	125,386,040
RESULT					
Segment result	17,711,545	10,032,736	423,327	10,217,035	38,384,643
Unallocated corporate expenses					(26,435,029)
Unallocated other income					1,081,413
Share of result of an associate					(1,582,693)
Gain on disposal of available-for-sale investment					1,000,000
Profit before tax					12,448,334
Income tax expense					(90,745)
Profit for the year					12,357,589

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

7. BUSINESS AND GEOGRAPHICAL SEGMENTS *(CONTINUED)*

Business segments *(Continued)*

At 31 December 2006

BALANCE SHEET

	Sales of self-developed software	Sales of third party software and hardware	System integration services	Maintenance, training and other services	Consolidated
	RMB	*RMB*	*RMB*	*RMB*	*RMB*
ASSETS					
Segment assets	52,983,388	28,347,170	394,833	6,324,642	88,050,033
Unallocated corporate assets					85,771,132
Interest in an associate					5,954,982
Consolidated total assets					179,776,147
LIABILITIES					
Segment liabilities	616,933	14,683,625	–	82,298	15,382,856
Unallocated corporate liabilities					27,757,738
Consolidated total liabilities					43,140,594

OTHER INFORMATION

	Sales of self-developed software	Sales of third party software and hardware	System integration services	Maintenance, training and other services	Consolidated
	RMB	*RMB*	*RMB*	*RMB*	*RMB*
Amortisation of intangible assets	3,498,032	–	–	–	3,498,032
Reversal of impairment loss on trade receivables	(448,736)	(65,678)	–	–	(514,414)

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

7. BUSINESS AND GEOGRAPHICAL SEGMENTS *(CONTINUED)*

Business segments *(Continued)*

For the year ended 31 December 2005

	Sales of self–developed software *RMB*	Sales of third party software and hardware *RMB*	System integration services *RMB*	Maintenance, training and other services *RMB*	Consolidated *RMB*
REVENUE					
External sales	33,054,203	60,427,720	1,327,009	2,505,586	97,314,518
RESULT					
Segment results	13,304,161	11,991,643	162,721	1,963,269	27,421,794
Unallocated corporate expenses					(19,813,847)
Unallocated other income					2,937,639
Share of result of an associate					(562,325)
Profit before tax					9,983,261
Income tax expense					(727,739)
Profit for the year					9,255,522

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

7. BUSINESS AND GEOGRAPHICAL SEGMENTS *(CONTINUED)*

Business segments *(Continued)*

At 31 December 2005

BALANCE SHEET

	Sales of self–developed software *RMB*	Sales of third party software and hardware *RMB*	System integration services *RMB*	Maintenance, training and other services *RMB*	Consolidated *RMB*
ASSETS					
Segment assets	36,073,095	14,419,078	861,324	120,512	51,474,009
Unallocated corporate assets					99,715,400
Interest in an associate					7,537,675
Consolidated total assets					158,727,084
LIABILITIES					
Segment liabilities	964,241	19,347,795	22,802	178,558	20,513,396
Unallocated corporate liabilities					11,368,125
Consolidated total liabilities					31,881,521

OTHER INFORMATION

	Sales of self–developed software *RMB*	Sales of third party software and hardware *RMB*	System integration services *RMB*	Maintenance, training and other services *RMB*	Consolidated *RMB*
Amortisation of intangible assets	913,685	–	–	–	913,685
Allowance for inventories	–	102,191	–	–	102,191
Reversal of impairment loss on trade receivables	(175,517)	(475,072)	–	–	(650,589)

Geographical segments

As all the operations, assets and liabilities are situated in the PRC, no geographical segment has been prepared.

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

8. OTHER INCOME

	2006	2005
	RMB	*RMB*
Value-added tax refund income (note a)	**7,596,650**	4,036,096
Interest income	**1,070,344**	564,753
Government grants (note b)	**770,834**	252,300
Tax refund for reinvestment in ZZNode (Beijing) (note c)	**–**	692,886
Dividend income from unlisted available-for-sale investment	**–**	1,680,000
Others	**11,069**	–
	9,448,897	7,226,035

Notes:

(a) In accordance with the Notice on Certain Issues of Tax Policies to Encourage the Development of Software and Integrated Circuits Industries (關於鼓勵軟件生產和集成電路產業發展有關稅收政策問題的通知) jointly issued by the Ministry of Finance, the State of General Administration of Taxation and the State of General Administration of Customs, an ordinary taxpayer shall be refunded, after subscribing 17% value-added tax on the income from sales of self-developed software products, an amount of 14% value-added tax on such income for the period from 24 June 2000 to 31 December 2010. On 24 January 2000, the Beijing Municipal Science and Technology Commission issued a Software Enterprise Verification Certificate (軟件企業認定證書) to Beijing Zhizhen Node Technology Development Co., Ltd. 北京直真節點技術開發有限公司("ZZNode (Beijing)") and on 20 February 2002, the Shanghai Information Office issued a Software Enterprise Verification Certificate (軟件企業認定證書) to Shanghai Zhizhen Node Technology Development Co., Ltd. 上海直真節點技術開發有限公司 ("ZZNode (Shanghai)"). Both ZZNode (Beijing) and ZZNode (Shanghai) are therefore entitled to receive refund of 14% of value-added tax paid from sales of self-developed software products after the tax refund notice (稅收收入退款書) has been approved. This tax refund was recognised as other income in the period upon the relevant conditions were fulfilled.

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

8. OTHER INCOME *(CONTINUED)*

Notes:

(b) In 2006 the Group received government grants of RMB657,834 from 北京市昌平區人民政府 in respect of its contribution in terms of tax paid to the local district. There was no specific condition attached to the grants and, therefore, the Group recognised the grants upon receipt of the notice. In addition, the Group received government grants of RMB113,000 (2005: RMB102,300) from 北京市高新技術成果轉化服務中心in respect of its software development in the PRC. The amount was recognised as other income as the conditions attached to the grants have been fulfilled.

In 2005, the Group received government grants of RMB150,000 from 北京市財政局 in respect of its software development in the PRC. The amount was recognised to income as the conditions attached to the grant had been fulfilled.

(c) In 2005 the Company increased its investment in the registered capital of ZZNode (Beijing) to RMB27,441,194 by transferring RMB9,812,400 from retained earnings to registered capital. As a result, ZZNode (Beijing) was entitled to a refund which was calculated based on the prevailing tax rate on the amount capitalised.

9. INCOME TAX EXPENSE

	2006	2005
	RMB	*RMB*
The charge comprises:		
PRC Enterprise Income Tax	–	101,550
Deferred tax (note 27)	**90,745**	626,189
	90,745	727,739

No provision for PRC Enterprise Income tax has been made in the financial statements as the Group incurred tax losses for the year.

ZZNode (Beijing) is recognised as an advanced technology and software enterprise according to the Changping District Tax Notices [1999] No. 176 and [2003] No. 310 of Provisional Regulation on Test Plot of New Technology Industry and Development in Beijing Municipality (北京市新技術產業開發試驗暫行條例) approved by the Local Tax Bureau of Changping District of Beijing Municipality. It is exempted from the PRC Enterprise Income Tax for the three years ended 31 December 2002 and is entitled to a 50% tax reduction for the three years ended 31 December 2005. The tax reduction treatment was further extended for three years up to the year ending 31 December 2008 at a tax rate of 10% according to the Changping District Tax Notice [2006] No. 0085 of《關於對北京直真節點技術開發有限公司申請享受先進技術的企業所得稅減免稅問題的批復》.

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

9. INCOME TAX EXPENSE *(CONTINUED)*

ZZNode (Shanghai) is also recognised as an advanced technology and software enterprise according to the Shanghai State Tax Notice 滬國稅浦政 [2002] No. 70 of (Circular of the Ministry of Finance, the State Administration of Taxation and General Administration of Customs on the Tax Policies for Further Encouraging the Development of Software and Integrated Circuit Industries)《關於鼓勵軟件產業和集成電路產業發展有關稅收政策問題的通知》approved by the State Tax Bureau and Local Tax Bureau of Pudong New District of Shanghai Municipality. It is exempted from the PRC Enterprise Income Tax for the two years ended 31 December 2005 and entitled to a 50% tax reduction for the three years ended 31 December 2006.

Income tax expense for the year can be reconciled to the profit before tax per the consolidated income statement as follows:

	2006	2005
	RMB	*RMB*
Profit before tax	**12,448,334**	9,983,261
Tax at the domestic income tax rate of 15% (2005: 15%)	**1,867,250**	1,497,489
Tax effect of share of result of an associate	**237,404**	84,349
Tax effect of expenses not deductible for tax purpose	**1,749,006**	409,906
Tax effect of income not taxable for tax purpose	**(1,139,498)**	(605,414)
Tax effect of expenses with additional tax preferential deductions	**(2,210,330)**	(1,444,573)
Tax effect of income not taxable under tax holidays	**(373,757)**	(56,591)
Tax effect of tax losses not recognised	**–**	842,573
Utilisation of tax losses previously not recognised	**(39,330)**	–
Income tax expense for the year	**90,745**	727,739

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10. PROFIT FOR THE YEAR

Profit for the year has been arrived at after charging (crediting):

	2006	2005
	RMB	*RMB*
Directors' emoluments (note 11)	**4,130,467**	2,879,352
Other staff costs	**23,098,991**	14,529,374
Retirement benefits scheme contributions excluding directors' emoluments	**2,599,475**	1,229,589
Total staff costs	**29,828,933**	18,638,315
Auditors' remuneration	**974,559**	729,400
Reversal of impairment loss on trade receivables	**(514,414)**	(650,589)
Allowance for inventories	**–**	102,191
Share-based payment expenses	**2,254,901**	1,268,354
Cost of inventories recognised as expenses	**83,272,759**	61,331,654
Depreciation of property, plant and equipment	**2,172,867**	1,774,726
Loss on disposal of property, plant and equipment	**35,024**	5,000
Net exchange loss	**404,235**	557,892
Operating lease rentals in respect of rented premises	**3,400,204**	2,981,584
Research and development expenditure	**12,399,522**	17,356,649
Less: amount capitalised	**(3,382,534)**	(4,887,612)
	9,016,988	12,469,037

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For the year ended 31 December 2006

11. DIRECTORS' EMOLUMENTS

The emoluments paid or payable to each of the eight directors were as follows:

		Other emoluments			
	Fees	Salaries and other benefits	Retirement benefits scheme contributions	Share-based payments	Total emoluments
	RMB	*RMB*	*RMB*	*RMB*	*RMB*
Wang Feixue	–	521,000	19,016	727,348	1,267,364
Jin Jianlin	–	761,760	17,301	727,348	1,506,409
Yuan Juan	–	400,000	19,016	272,756	691,772
Hu Rong	–	254,520	19,016	90,916	364,452
Zhang Suyang	–	–	–	–	–
Hung Randy King Kuen	100,470	–	–	–	100,470
Chen Xiaohong	100,000	–	–	–	100,000
He Xingui	100,000	–	–	–	100,000
Total for 2006	300,470	1,937,280	74,349	1,818,368	4,130,467

The emoluments paid or payable to each of the eight directors were as follows:

		Other emoluments		
	Fees	Salaries and other benefits	Retirement benefit scheme contributions	Total emoluments
	RMB	*RMB*	*RMB*	*RMB*
Wang Feixue	–	835,777	16,364	852,141
Jin Jianlin	–	803,077	15,733	818,810
Yuan Juan	–	509,176	16,364	525,540
Hu Rong	–	362,296	16,364	378,660
Zhang Suyang	–	–	–	–
Hung Randy King Kuen	104,201	–	–	104,201
Chen Xiaohong	100,000	–	–	100,000
He Xingui	100,000	–	–	100,000
Total for 2005	304,201	2,510,326	64,825	2,879,352

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12. EMPLOYEES' EMOLUMENTS

Of the five individuals with the highest emoluments in the Group, four (2005: four) were directors of the Company whose emoluments are included in note 11 above. The emoluments of the remaining one (2005: one) individual were as follows:

	2006	2005
	RMB	*RMB*
Salaries and other benefits	**193,011**	240,888
Retirement benefits scheme contributions	**19,016**	7,294
Performance-related incentive payments	**40,000**	–
Share based payments	**98,493**	–
	350,520	248,182

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

13. DIVIDEND

	2006	2005
	RMB	*RMB*
2004 final dividend – HK1.7 cents per share (approximately RMB1.8 cents)	**–**	7,200,000
2006 interim dividend – HK0.7 cents per share (approximately RMB0.7 cents)	**2,813,160**	–

14. EARNINGS PER SHARE

The calculation of the basic earnings per share is based on the profit for the year of RMB12,357,589 (2005: RMB9,255,522) and weighted average number of ordinary shares of 399,958,904 (2005: number of ordinary shares of 400,000,000).

No diluted earnings per share has been presented as the average market price of ordinary shares exceeds the exercise price of the options for the year and there were no other potential ordinary shares outstanding during 2006.

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15. PROPERTY, PLANT AND EQUIPMENT

	Leasehold land and buildings	Leasehold improvements	Furniture and fixtures	Computers and equipment	Motor vehicles	Total
	RMB	*RMB*	*RMB*	*RMB*	*RMB*	*RMB*
COST						
At 1 January 2005	–	2,391,535	75,464	6,754,202	896,962	10,118,163
Additions	12,189,762	1,157,465	–	745,437	–	14,092,664
Disposals	–	–	–	(29,890)	–	(29,890)
At 31 December 2005	12,189,762	3,549,000	75,464	7,469,749	896,962	24,180,937
Additions	–	69,000	–	738,278	233,907	1,041,185
Disposals	–	–	–	(841,257)	–	(841,257)
At 31 December 2006	12,189,762	3,618,000	75,464	7,366,770	1,130,869	24,380,865
DEPRECIATION						
At 1 January 2005	–	2,391,535	68,719	3,025,130	178,740	5,664,124
Provided for the year	341,314	115,747	1,959	1,209,147	106,559	1,774,726
Disposals	–	–	–	(23,190)	–	(23,190)
At 31 December 2005	341,314	2,507,282	70,678	4,211,087	285,299	7,415,660
Provided for the year	585,109	259,093	809	1,195,824	132,032	2,172,867
Disposals	–	–	–	(784,754)	–	(784,754)
At 31 December 2006	926,423	2,766,375	71,487	4,622,157	417,331	8,803,773
CARRYING VALUES						
At 31 December 2006	11,263,339	851,625	3,977	2,744,613	713,538	15,577,092
At 31 Dec 2005	11,848,448	1,041,718	4,786	3,258,662	611,663	16,765,277

Leasehold land and buildings purchased in 2005 are held under a medium lease in the PRC. The allocation between the land and building elements cannot be made reliably, the leasehold interest in land is therefore accounted for as property, plant and equipment.

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

16. INTANGIBLE ASSETS

	Software Purchased *RMB*	Software development *RMB*	Total *RMB*
COST			
At 1 January 2005	–	5,655,399	5,655,399
Additions	–	4,887,612	4,887,612
At 31 December 2005	–	10,543,011	10,543,011
Additions	1,500,000	3,382,534	4,882,534
At 31 December 2006	1,500,000	13,925,545	15,425,545
AMORTISATION			
At 1 January 2005	–	2,236,687	2,236,687
Charge for the year	–	913,685	913,685
At 31 December 2005	–	3,150,372	3,150,372
Charge for the year	125,000	3,373,032	3,498,032
At 31 December 2006	125,000	6,523,404	6,648,404
CARRYING VALUES			
At 31 December 2006	1,375,000	7,402,141	8,777,141
At 31 December 2005	–	7,392,639	7,392,639

Software purchased is acquired from independent third party and software development is related to internally-generated software expenditure. The above intangible assets are amortised on a straight-line basis over their estimated useful lives of two years after they are available for use.

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17. INTEREST IN AN ASSOCIATE

	2006	2005
	RMB	*RMB*
Cost of investment in an associate		
Unlisted	**8,100,000**	8,100,000
Share of post-acquisition losses	**(2,145,018)**	(562,325)
	5,954,982	7,537,675

At 31 December 2006, the Group held 27% equity interest in Shanghai Beimanyuanmai Information Technology Company Ltd. 上海貝曼元脉信息技術有限公司 which was established and operated in the PRC. The principal activities of the associate are design, production and development of telecommunications terminal equipment.

The summarised financial information in respect of the associate is set out below:

	2006	2005
	RMB	*RMB*
Total assets	**48,867,954**	62,730,178
Total liabilities	**(26,812,466)**	(34,812,863)
Net assets	**22,055,488**	27,917,315
Group's share of net assets of the associate	**5,954,982**	7,537,675
Revenue	**52,549,548**	30,533,039
Loss for the year	**(5,861,827)**	(2,082,685)
Group's share of result of the associate for the year	**(1,582,693)**	(562,325)

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18. NON-CURRENT BANK DEPOSITS

Included in bank deposits are two certificates of deposits the terms of which are as follows:

A bank deposit certificate of US$300,000 issued in 2005, which will mature on 4 April 2007 and bears interest at 2.88% per annum. At each half year interval, the bank has the right to redeem the certificate at face value plus accrued interest.

A bank deposit certificate of US$300,000 issued in 2006, which will mature on 28 March 2007 and bears accelerating interest from 3.85% to 4.45% per annum. At each three month interval, the bank has the right to redeem the certificate at face value plus accrued interest.

The remaining deposits carry fixed interest rates ranging from 1.62% to 2.52% per annum. The directors consider that the fair values of the Group's bank deposits approximate to their corresponding carrying amounts.

19. INVENTORIES

	2006	2005
	RMB	*RMB*
Finished goods	**3,716,779**	2,439,224
Spare parts	**171,876**	395,320
	3,888,655	2,834,544
Less: Allowance	**–**	(317,261)
	3,888,655	2,517,283

20. TRADE RECEIVABLES AND NOTE RECEIVABLES

	2006	2005
	RMB	*RMB*
Trade receivables	**49,802,000**	37,669,488
Less: accumulated impairment loss	**(481,767)**	(996,181)
	49,320,233	36,673,307
Note receivables (note 25)	**16,963,953**	–
	66,284,186	36,673,307

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

20. TRADE RECEIVABLES AND NOTE RECEIVABLES *(CONTINUED)*

The Group allows an average credit period of 90 days to its trade customers. The following is an aged analysis of trade receivables net of accumulated impairment loss at the balance sheet date:

	2006	2005
	RMB	*RMB*
0-90 days	**46,327,027**	23,307,543
91-180 days	**5,258,837**	198,060
181-270 days	**8,776,758**	4,976,937
271-360 days	**2,508,149**	1,560,907
More than 1 year	**3,413,415**	6,629,860
	66,284,186	36,673,307

21. AMOUNT DUE FROM A RELATED PARTY

	2006	2005
	RMB	*RMB*
Beijing Jia Bei Lin Technology Co., Ltd. (“Jia Bei Lin”)	**950,000**	–

The amount is unsecured, non-interest bearing and repayable on demand.

Jia Bei Lin is a company in which Wang Feixue and Jin Jianlin have beneficiary interests. The maximum amount outstanding during the year ended 31 December 2006 is RMB950,000.

22. BANK BALANCES AND CASH

The savings accounts included in bank balances carry interest at 0.72% per annum.

Included in bank deposits and bank deposits are the following amounts denominated in a currency other than the functionary currency of the Group:

	2006	2005
	RMB	*RMB*
Hong Kong dollars	**887,489**	8,861,135
United State dollars	**4,925,765**	5,781,908

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

23. AVAILABLE-FOR-SALE INVESTMENT CLASSIFIED AS HELD FOR SALE

Available-for-sale investment classified as held for sale at 31 December 2005 represented 7% unlisted equity interest in Capital Engineering & Research Incorporation Limited (中冶京誠工程技術有限公司) ("CERI"), which was disposed of during the year.

24. TRADE PAYABLES AND NOTE PAYABLES

	2006	2005
	RMB	*RMB*
Trade payables	**14,032,190**	12,453,371
Note payables	**640,000**	6,300,054
	14,672,190	18,753,425

The following is an aged analysis of trade payables and note payables at the balance sheet date:

	2006	2005
	RMB	*RMB*
0-90 days	**5,949,323**	18,299,202
More than 90 days	**8,722,867**	454,223
	14,672,190	18,753,425

25. NOTE RECEIVABLES DISCOUNTED WITH RECOURSE

They bear interest rates ranging from 2.76% to 3.24% per annum and will mature during the period from January 2007 to April 2007. Upon maturity, the customers will reimburse the Company the interest charge in full.

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

26. SHARE CAPITAL

	Number of shares		Share capital		Equivalent nominal value of ordinary shares	
	2006	2005	**2006**	2005	**2006**	2005
			HK$	*HK$*	***RMB***	*RMB*
Ordinary shares of HK$0.1 each						
Authorised:						
At beginning and end of the year	**1,000,000,000**	1,000,000,000	100,000,000	100,000,000	**106,000,000**	106,000,000
Issued:						
At beginning of the year	**400,000,000**	400,000,000	**40,000,000**	40,000,000	**42,400,000**	42,400,000
Shares repurchased and cancelled	**(5,000,000)**	–	**(500,000)**	–	**(502,335)**	–
At end of the year	**395,000,000**	400,000,000	**39,500,000**	40,000,000	**41,897,665**	42,400,000

During the year, the Company repurchased its own shares through the Stock Exchange as follows:

Month of repurchase	**Number of repurchased shares**	**Price per share**	**Aggregate consideration paid**
		HK$	*HK$*
December 2006	5,000,000	0.4	2,000,000

The above shares were cancelled upon repurchase.

None of the Company's subsidiaries purchased, sold or redeemed any of the Company's shares during 2006 and 2005.

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27. DEFERRED TAX LIABILITIES

The following are the major deferred tax liabilities and assets recognised during the current year:

	Deferred software development expenditure	**Impairment loss on trade receivables**	**Allowance for inventories**	**Total**
	RMB	*RMB*	*RMB*	*RMB*
Charge (credit) to income for the year and balance at 31 December 2005	739,264	(81,349)	(31,726)	626,189
Charge to income for the year	950	58,069	31,726	90,745
At 31 December 2006	740,214	(23,280)	–	716,934

ZZNode (Beijing) is recognised as an advanced technology enterprise and has obtained approval which entitles to a reduced income tax rate of 10% for the three years ending 31 December 2008. The deferred tax liabilities are calculated based on the tax rate of 10% that the liabilities are expected to capitalise.

At the balance sheet date, the Group has unused tax losses of approximately RMB157,000 (2005: approximately RMB420,000) relating to ZZNode (Shanghai) available for offset against future profits. No deferred tax asset has been recognised in respect of such losses due to the unpredictability of future profit streams. All of the tax losses will expired in 2007.

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28. SHARE-BASED PAYMENTS

Equity-settled share options schemes:

(a) Share option scheme

Pursuant to a share option scheme approved by a resolution of the shareholders of the Company on 31 October 2004 (the "Share Option Scheme"), the Company may grant options to the directors or employees of the Company or its subsidiaries who meet the relevant criteria set out in the Share Option Scheme (the "Participants") as incentives and rewards for their contributions to the Group, to subscribe for shares in the Company with a payment of HK$1.00 upon each grant of options offered and the options granted must be taken up within 30 days from the date of grant. The exercise price of the share option will be determined at the higher of the average of closing prices of the shares as stated in the Stock Exchange's daily quotation sheet for the five business days immediately preceding the date of grant of the options, the closing price of the shares as stated in the Stock Exchange's daily quotation sheet on the date of grant and the nominal value of the shares.

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

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

At 31 December 2006, the number of options granted under the Share Option Scheme was 10,000,000 (2005: nil), representing 2.53 per cent (2005: Nil) of the shares of the Company in issue at that date.

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

28. SHARE-BASED PAYMENTS *(CONTINUED)*

(a) Share option scheme *(Continued)*

The following table discloses movements of the options issued under the Share Option Scheme held by the Eligible Participants during the year:

		Number of share options			
	Option category	**At 1.1.2006**	**Granted during the year**	**Forfeited during the year**	**At 31.12.2006**
Directors	2006	–	10,000,000	–	10,000,000

Details of specific categories of options are as follows:

	Date of grant	**Exercise period**	**Exercise price**
2006	20.1.2006	20.1.2007 – 20.1.2011	HK$0.48

The estimated fair value per share option is RMB0.18. The fair value of the options issued under the Share Option Scheme was calculated using the Black-Scholes Model. The inputs into the model were as follows:

	Date of grant 20.1.2006
Share price	HK$0.48
Exercise price	HK$0.48
Expected volatility	50.75%
Expected life (year)	3
Risk-free rate	3.9%
Expected dividend yield	0%

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

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28. SHARE-BASED PAYMENTS *(CONTINUED)*

(a) Share option scheme *(Continued)*

The Group recognised the total expense of RMB1,818,368 for the year ended 31 December 2006 (2005: Nil) in relation to the above share options granted by the Company.

The Black-Scholes option pricing model has been used to estimate the fair value of the options. The variables and assumptions used in computing the fair value of the share options are based on the directors' best estimate. The value of an option varies with different variables of certain subjective assumptions.

(b) Share incentive scheme

The Share Incentive Scheme was established by three shareholders of the Company as a trust into which they transferred in 18,000,000 shares of the Company (the "Transferred Shares"), representing 4.5% of the enlarged issued share capital of the Company after the listing of the Company to be held on trust by the trustee of the trust pursuant to the Trust Deed dated 27 October, 2004.

The consideration given to each of the shareholders for the Transferred Shares were HK$518,136, HK$582,177 and HK$707,687, respectively, which was determined with reference to the consolidated net asset value of ZZNode (Beijing) and ZZNode (Shanghai) of approximately RMB40.4 million as at 31 December, 2003. The trustee has entered into a loan agreement with an independent third party to obtain the necessary funding for acquiring the Transferred Shares.

The trustee of the trust is Silver Well Investment Limited ("Silver Well"), a company incorporated in the British Virgin Islands. Silver Well is wholly-owned by Mr. Jin Jianlin, an executive director.

The purpose of the Share Incentive Scheme is to issue options to selected employees, officers, consultants, agents and advisers of the Group who meet the relevant eligibility criteria set out in the Share Incentive Scheme (the "Eligible Participants"). The employee participants must have been employed by a member of the Group prior to the listing of the Company in November 2004.

The three shareholders of the Company believe that the trust arrangement and the Share Incentive Scheme are both in the interests of the Company and the potential investors of the Company since their operation will not dilute the Company's earnings per share or the interests of potential investors in the Company. In summary, the Share Incentive Scheme does not involve new shares to be issued by the Company.

The trust shall vest on the day occurring 80 days after the date of the Trust Deed, the date on which the Company ceases to have any Eligible Participants if the Company is wound-up, or such other date as the trustee may declare.

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28. SHARE-BASED PAYMENTS *(CONTINUED)*

(b) Share incentive scheme *(Continued)*

The Share Incentive Scheme shall remain in full force and effect for so long as is necessary to give effect to the issue and exercise of options granted in accordance with its terms.

The exercise price per share under the Share Inventive Scheme is HK$0.20 and each tranche of option has a term of five years from the first exercise date, after which any unexercised portion of an option shall lapse.

Each option is exercisable by an Eligible Participants who accepts the offer of a grant of share options (the "Grantee") during the option period applicable to the relevant Eligible Participant giving a written notice of exercise to acquire shares to the trustee in accordance with the terms of the Share Incentive Scheme.

The first date on which the Grantee may exercise a portion of their options will be the first business day occurring immediately after 12 months from the listing date of the Company.

Each option will be exercisable pursuant to the following vesting schedule:

(i) to acquire up to 20% of the shares the subject of the option, rounded down to the nearest whole number at any time within the period of five business days on or prior to 31 March, 30 June, 30 September and 31 December of each calendar year between the first exercise date and the last exercise date;

(ii) to acquire up to 40% of the shares the subject of the option (to the extent that such proportion of shares has not already been acquired), rounded down to the nearest whole number at any time within the period of five business days on or prior to 31 March, 30 June, 30 September and 31 December of each calendar year between the date which is the first anniversary after the first exercise date and the last exercise date;

(iii) to acquire up to 60% of the shares the subject of the option (to the extent that such proportion of shares has not already been acquired), rounded down to the nearest whole number at any time within the period of five business days on or prior to 31 March, 30 June, 30 September and 31 December of each calendar year between the date which is the second anniversary of the first exercise date and the last exercise date;

(iv) to acquire up to 80% of the shares the subject of the option (to the extent that such proportion of shares has not already been acquired), rounded down to the nearest whole number at any time within the period of five business days on or prior to 31 March, 30 June, 30 September and 31 December of each calendar year between the date which is the third anniversary of the first exercise date and the last exercise date;

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28. SHARE-BASED PAYMENTS *(CONTINUED)*

(b) Share incentive scheme *(Continued)*

(v) to acquire up to 100% of the shares the subject of the option (to the extent that such proportion of shares has not already been acquired), rounded down to the nearest whole number at any time within the period of five business days on or prior to 31 March, 30 June, 30 September and 31 December of each calendar year between the date which is the fourth anniversary of the first exercise date and the last exercise date;

At 31 December 2006, the number of options granted under the Share Incentive Scheme was 10,401,400 (2005: 12,363,400), representing 2.63 per cent (2005: 3.09 per cent) of the shares of the Company in issue at that date.

The following table discloses movements of the options issued under the Share Incentive Scheme held by the Eligible Participants during the year:

		Number of share options							
	Option category	At 1.1.2005	Granted during the year	Forfeited during the year	At 31.12.2005 and 1.1.2006	Granted during the year	Exercised during the year	Forfeited during the year	At 31.12.2006
Employees	2004	12,652,400	–	(2,369,000)	10,283,400	–	(168,000)	(2,784,000)	7,331,400
Consultants	2004	1,080,000	–	–	1,080,000	–	–	(90,000)	990,000
Consultants	2005	–	1,000,000	–	1,000,000	–	–	–	1,000,000
Employees	2006	–	–	–	–	1,140,000	–	(60,000)	1,080,000
		13,732,400	**1,000,000**	**(2,369,000)**	**12,363,400**	**1,140,000**	**(168,000)**	**(2,934,000)**	**10,401,400**

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28. SHARE-BASED PAYMENTS *(CONTINUED)*

(b) Share incentive scheme *(Continued)*

Details of specific categories of options are as follows:

	Date of grant	Exercise period	Exercise price
2004	27.10.2004	18.11.2005 – 18.11.2009	HK$0.2
2005	22.12.2005	21.12.2006 – 21.12.2010	HK$0.2
2006	14.03.2006	14.03.2007 – 14.03.2011	HK$0.2

The estimated fair value of the options issued in 2006 under the Share Incentive Scheme was calculated using the Black-Scholes Model, whereas the estimated fair value of the options issued in 2004 and 2005 were calculated using the Binomial Option Pricing Model. The inputs into the models were as follows:

	Date of grant			
	27.10.2004 Employees	27.10.2004 Consultants	22.12.2005 Consultants	14.3.2006 Employees
Share price	HK$0.55 (Note)	HK$0.55 (Note)	HK$0.40	HK$0.50
Exercise price	HK$0.2	HK$0.2	HK$0.2	HK$0.2
Expected volatility	44%	44%	44%	59.76%
Expected life (year)	4.5	4.5	5	3.6-5.8
Risk-free rate	2.7%	2.7%	4.6%	4.3%
Expected dividend yield	3.4%	3.4%	3.4%	0%

Note: The share price represents the offer price on listing date as at 18 November 2004.

Expected volatility used for the options issued in 2006 was determined by using the volatility of the Company's share prices over the previous one year. Expected volatility used for the options issued in 2004 and 2005 were determined by using the volatility of companies in similar industry. The expected life used in the models have been adjusted, based on management's best estimate, for the effects of non transferability, exercise restrictions and behavioral considerations.

The Group recognised total expenses of RMB436,533 (2005: RMB1,268,354) related to equity-settled share-based payment transactions during the year.

During the year ended 31 December 2006, options were granted on 14 March 2006 and the estimated fair value per option was RMB0.37. During the year ended 31 December 2005, options were granted on 22 December 2005 and the estimated fair value per option was RMB0.24.

Share options granted to consultants are measured by reference to the fair value of options granted as these consultants provide services similar to those as employees.

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29. OPERATING LEASES

The Group as lessee

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

	2006	2005
	RMB	*RMB*
Within one year	**2,884,000**	2,029,000
In the second to fifth year inclusive	**4,260,000**	588,000
Over 5 years	**292,000**	–
	7,436,000	2,617,000

Leases are negotiated for a terms which ranged from two to seven years and rentals are fixed at inception of the leases.

30. RETIREMENT BENEFITS SCHEME

The Group's subsidiaries in the PRC participate in the retirement benefits scheme established by the government for the qualifying employees in the PRC. The assets of the scheme are held separately from the assets of the Group. Under the scheme, contributions made by the Group are calculated on the basis of 19% to 20% of the enrolled employees' salaries. Apart from the above, the Group has no further obligations under the retirement benefits scheme.

The amount of such contributions charged to the consolidated income statement was RMB2,673,824 (2005: RMB1,294,414).

31. RELATED PARTY DISCLOSURES

Other than the amount due from a related party as disclosed in note 21, the Group entered into the following related party transactions during 2006:

Name of related company	Nature of transaction	2006	2005
		RMB	RMB
Jia Bei Lin	Purchase of materials	**645,810**	–

Compensation of key management personnel

The remuneration of directors and other members of key management during the year was disclosed in notes 11 and 12.

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32. INVESTMENTS IN SUBSIDIARIES

Details of the Company's subsidiaries at 31 December 2006 are as follows:

Name of company	Place of incorporation/ establishment	Issued and fully paid share capital registered capital	Proportion of nominal value of share capital/ registered capital held by the Company	Principal activities
Direct subsidiary				
Modern Age Investments Limited	British Virgin Islands ("BVI")	US$4,600,000	100%	Investment holding
Indirect subsidiaries				
ZZNode (Beijing)	The PRC	RMB27,441,194	100%	Provision of telecommunications and internet technologies related services and products
ZZNode (Shanghai)	The PRC	RMB5,000,000	98%	Provision of telecommunications and internet technologies related services and products
Great Process Limited	BVI	HK$100	100%	Inactive

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

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