Notes to Financial Statements

31 December 2006

1. CORPORATE INFORMATION

The Company was incorporated as an exempted company with limited liability in the Cayman Islands on 26 February 2004 under the Companies Law, Cap.22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands. The principal office of the Company is located at Room 1502, Tower 6, China Hong Kong City, 33 Canton Road, Tsimshatsui, Kowloon, Hong Kong.

During the year, the Company and its subsidiaries (collectively referred to as the "Group") were principally engaged in the research, development, manufacturing and sale of mobile phones.

In the opinion of the directors, the holding company and the ultimate holding company of the Company is TCL Corporation, a limited liability company registered in the PRC and listed in the Shenzhen Stock Exchange.

2. BASIS OF PREPARATION

These financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") (which also include Hong Kong Accounting Standards ("HKASs") and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants, accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention except for the available-for-sale investment, which has been measured at fair value. These financial statements are presented in Hong Kong dollars and all values are rounded to the nearest thousand (HK$'000) except when otherwise indicated.

Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries for the year ended 31 December 2006. The results of subsidiaries are consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases. All significant intercompany transactions and balances within the Group are eliminated on consolidation.

Minority interests represent the interests of outside shareholders not held by the Group in the results and net assets of the Company's subsidiaries.

3. IMPACT OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS

The Group has adopted the following new and revised HKFRSs for the first time for the current year's financial statements. Except for in certain cases, giving rise to new and revised accounting policies and additional disclosures, the adoption of these new and revised standards and interpretation has had no material effect on these financial statements.

HKAS 21 Amendment	Net Investment in a Foreign Operation
HKAS 39 & HKFRS 4 Amendment	Financial Guarantee Contracts
HKAS 39 Amendment	Cash Flow Hedge Accounting of Forecast Intragroup Transactions
HKAS 39 Amendment	The Fair Value Option
HK(IFRIC)-Int 4	Determining whether an Arrangement contains a Lease

3. IMPACT OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS (continued)

The principal changes in accounting policies are as follows:

(a) HKAS 21 The Effects of Changes in Foreign Exchange Rates

Upon the adoption of the HKAS 21 Amendment regarding a net investment in a foreign operation, all exchange differences arising from a monetary item that forms part of the Group's net investment in a foreign operation are recognised in a separate component of equity in the consolidated financial statements irrespective of the currency in which the monetary item is denominated. This change has had no material impact on these financial statements as at 31 December 2006 or 31 December 2005.

(b) HKAS 39 Financial Instruments: Recognition and Measurement

(i) Amendment for cash flow hedge accounting of forecast intragroup transactions

This amendment has revised HKAS 39 to permit the foreign currency risk of a highly probable intragroup forecast transaction to qualify as a hedged item in a cash flow hedge, provided that the transaction is denominated in a currency other than the functional currency of the entity entering into that transaction and that the foreign currency risk will affect the consolidated income statement.

As the Group currently has no such transactions, the amendment has had no effect on these financial statements.

(c) HK (IFRIC)-Int 4 Determining whether an Arrangement contains a Lease

The Group has adopted this interpretation as of 1 January 2006, which provides guidance in determining whether arrangements contain a lease to which lease accounting must be applied. This interpretation has had no material impact on these financial statements.

4. IMPACT OF ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS

The Group has not applied the following new and revised HKFRSs, that have been issued but are not yet effective, in these financial statements.

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

The HKAS 1 Amendment shall be applied for annual periods beginning on or after 1 January 2007. The revised standard will affect the disclosures about qualitative information about the Group's objective, policies and processes for managing capital; quantitative data about what the Company regards as capital; and compliance with any capital requirements and the consequences of any non-compliance.

HKFRS 7 shall be applied for annual periods beginning on or after 1 January 2007. The standard requires disclosures that enable users of the financial statements to evaluate the significance of the Group's financial instruments and the nature and extent of risks arising from those financial instruments and also incorporates many of the disclosure requirements of HKAS 32.

4. IMPACT OF ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS (continued)

HKFRS 8 shall be applied for annual periods beginning on or after 1 January 2009. The standard requires disclosures of information about the operating segments of the Group, the products and services provided by the segments, the geographical areas in which the Group operates, and revenue from the Group's major customers. This standard will separate HKAS 14 Segment Reporting.

HK(IFRIC)-Int 7, HK(IFRIC)-Int 8, HK(IFRIC)-Int 9, HK(IFRIC)-Int 10, HK(IFRIC)-Int 11 and HK(IFRIC)-Int 12 shall be applied for annual periods beginning on or after 1 March 2006, 1 May 2006, 1 June 2006, 1 November 2006, 1 March 2007 and 1 January 2008, respectively.

The Group is in the process of making an assessment of the impact of these new and revised HKFRSs upon initial application. So far, it has concluded that while the adoption of the HKAS 1 Amendment, HKFRS 7 and HKFRS 8 may result in new or amended disclosures, these new and revised HKFRSs are unlikely to have a significant impact on the Group's results of operations and financial position.

5. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Subsidiaries

A subsidiary is an entity whose financial and operating policies the Company controls, directly or indirectly, so as to obtain benefits from its activities.

The results of subsidiaries are included in the Company's income statement to the extent of dividends received and receivable. The Company's investments in subsidiaries are stated at cost less any impairment losses.

Joint ventures

A joint venture is an entity set up by contractual arrangement, whereby the Group and other parties undertake an economic activity. The joint venture operates as a separate entity in which the Group and the other parties have an interest.

The joint venture agreement between the venturers stipulates the capital contributions of the joint venture parties, the duration of the joint venture entity and the basis on which the assets are to be realised upon its dissolution. The profits and losses from the joint venture's operations and any distributions of surplus assets are shared by the venturers, either in proportion to their respective capital contributions, or in accordance with the terms of the joint venture agreement.

A joint venture is treated as:

(a) subsidiary, if the Group/Company has unilateral control, directly or indirectly, over the joint venture;

(b) a jointly-controlled entity, if the Group/Company does not have unilateral control, but has joint control, directly or indirectly, over the joint venture;

(c) an associate, if the Group/Company does not have unilateral or joint control, but holds, directly or indirectly, generally not less than 20% of the joint venture's registered capital and is in a position to exercise significant influence over the joint venture; or

(d) an equity investment accounted for in accordance with HKAS 39, if the Group/Company holds, directly or indirectly, less than 20% of the joint venture's registered capital and has neither joint control of, nor is in a position to exercise significant influence over, the joint venture.

5. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Associates

An associate is an entity, not being a subsidiary or a jointly-controlled entity, in which the Group has a long term interest of generally not less than 20% of the equity voting rights and over which it is in a position to exercise significant influence.

The Group's share of the post-acquisition results and reserves of associates is included in the consolidated income statement and consolidated reserves, respectively. The Group's interest in an associate are stated in the consolidated balance sheet at the Group's share of net assets under the equity method of accounting, less any impairment losses. Goodwill arising from the acquisition of an associate is included as part of the Group's interest in an associate.

The results of an associate are included in the Company's income statement to the extent of dividends received and receivable. The Company's interest in an associate is treated as non-current assets and is stated at cost less any impairment losses.

Goodwill

Goodwill arising on the acquisition of an associate represents the excess of the cost of the business combination over the Group's interest in the net fair value of the acquiree's identifiable assets acquired, and liabilities and contingent liabilities assumed as at the date of acquisition.

Goodwill on acquisitions for which the agreement date is on or after 1 January 2005

Goodwill arising on acquisition is recognised in the consolidated balance sheet as an asset, initially measured at cost and subsequently at cost less any accumulated impairment losses. In the case of associates and jointly-controlled entities, goodwill is included in the carrying amount thereof, rather than as a separately identified asset on the consolidated balance sheet.

The carrying amount of goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired.

For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units. Each unit or group of units to which the goodwill is so allocated:

- represents the lowest level within the Group at which the goodwill is monitored for internal management purposes; and

- is not larger than a segment based on either the Group's primary or the Group's secondary reporting format determined in accordance with HKAS 14 *Segment Reporting*.

Impairment is determined by assessing the recoverable amount of the cash-generating unit (group of cash-generating units) to which the goodwill relates. Where the recoverable amount of the cash-generating unit (group of cash-generating units) is less than the carrying amount, an impairment loss is recognised.

5. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Goodwill (continued)

Where goodwill forms part of a cash-generating unit (group of cash-generating units) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

An impairment loss recognised for goodwill is not reversed in a subsequent period.

Excess over the cost of business combinations

Any excess of the Group's interest in the net fair value of the acquirees' identifiable assets, liabilities and contingent liabilities over the cost of the acquisition of subsidiaries (previously referred to as negative goodwill), after reassessment, is recognised immediately in the income statement.

Impairment of non-financial assets other than goodwill

Where an indication of impairment exists, or when annual impairment testing for an asset is required (other than inventories, deferred tax assets and financial assets), the asset's recoverable amount is estimated. An asset's recoverable amount is calculated as the higher of the asset's or cash-generating unit's value in use and its fair value less costs to sell, and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

An impairment loss is recognised only if the carrying amount of an asset exceeds its recoverable amount. In assessing value in use, estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. An impairment loss is charged to the income statement in the period in which it arises in those expense categories consistent with the function of the impaired asset, unless the asset is carried at a revalued amount, in which case the impairment loss is accounted for in accordance with the relevant accounting policy for that revalued asset.

An assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognised impairment loss of an asset other than goodwill is reversed only if there has been a change in the estimates used to determine the recoverable amount of that asset, however not to an amount higher than the carrying amount that would have been determined (net of any depreciation/amortisation), had no impairment loss been recognised for the asset in prior years. A reversal of such impairment loss is credited to the income statement in the period in which it arises.

5. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Related parties

A party is considered to be related to the Group if:

(a) the party, directly or indirectly through one or more intermediaries, (i) controls, is controlled by, or is under common control with, the Group; (ii) has an interest in the Group that gives it significant influence over the Group; or (iii) has joint control over the Group;

(b) the party is an associate;

(c) the party is a jointly-controlled entity;

(d) the party is a member of the key management personnel of the Group or its parent;

(e) the party is a close member of the family of any individual referred to in (a) or (d);

(f) the party is an entity that is controlled, jointly controlled or significantly influenced by or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (d) or (e); or

(g) the party is a post-employment benefit plan for the benefit of the employees of the Group, or of any entity that is a related party of the Group.

Property, plant and equipment and depreciation

Property, plant and equipment, other than construction in progress, are stated at cost less accumulated depreciation and any impairment losses. The cost of an item of property, plant and equipment comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditure incurred after items of property, plant and equipment have been put into operation, such as repairs and maintenance, is normally charged to the income statement in the period in which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of an item if property, plant and equipment, and where the cost of the item can be measured reliably, the expenditure is capitalised as an additional cost of that asset or as a replacement.

Depreciation is calculated on the straight-line basis to write off the cost or valuation of each asset over its estimated useful life less any estimated residual value. The principal annual rates used for this purpose are as follows:

Buildings	2.86%
Plant and machinery	10% to 20%
Furniture, fixtures and office equipment	20%
Motor vehicles	16.67%-20%

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss on disposal or retirement recognised in the income statement in the year is derecognised as the difference between the net sales proceeds and the carrying amount of the relevant asset.

5. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Property, plant and equipment and depreciation (continued)

Construction in progress represents a building under construction, which is stated at cost less any impairment losses, and is not depreciated. Cost comprises the direct costs of construction and capitalised borrowing costs on related borrowed funds during the period of construction. Construction in progress is reclassified to the appropriate category, plant and equipment when completed and ready for use.

Intangible assets (other than goodwill)

The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at each balance sheet date.

Computer software

Purchased computer software is stated at cost, less any impairment losses, and is amortised on straight-line basis over its estimated useful life of five years.

Intellectual property

Purchased intellectual property is stated at cost, less any impairment losses, and is amortised on the straight-line basis over its estimated useful life.

Research and development costs

All research costs are charged to the income statement as incurred.

Expenditure incurred on projects to develop new products is capitalised and deferred only when the Group can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale, its intention to complete and its ability to use or sell the asset, how the asset will generate future economic benefits, the availability of resources to complete the project and the ability to measure reliably the expenditure during the development. Product development expenditure which does not meet these criteria is expensed when incurred.

Leases

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. Where the Group is the lessor, assets leased by the Group under operating leases are included in non-current assets, and rentals receivable under the operating leases are credited to the income statement on the straight-line basis over the lease terms. Where the Group is the lessee, rentals payable under the operating leases net of any incentives received from the lessor are charged to the income statement on the straight-line basis over the lease terms.

Prepaid land lease payments under operating leases are initially stated at cost and subsequently recognised on the straight-line basis over the lease terms. When the lease payments cannot be allocated reliably between the land and buildings elements, the entire lease payments are included in the cost of the land and buildings as a finance lease in property, plant and equipment.

5. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Investments and other financial assets

Financial assets in the scope of HKAS 39 are classified as financial assets at fair value through profit or loss, loans and receivables and available-for-sale financial assets, as appropriate. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Group considers whether a contract contains an embedded derivative when the Group first becomes a party to it. The embedded derivatives are separated from the host contract which is not measured at fair value through profit or loss when the analysis shows that the economic characteristics and risks of embedded derivatives are not closely related to those of the host contract.

The Group determines the classification of its financial assets after initial recognition and, where allowed and appropriate, re-evaluates this designation at the balance sheet date.

All regular way purchases and sales of financial assets are recognised on the trade date, that is, the date that the Group commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are subsequently carried at amortised cost using the effective interest method. Amortised cost is calculated taking into account any discount or premium on acquisition and includes fees that are an integral part of the effective interest rate and transaction costs. Gains and losses are recognised in the income statement when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

Available-for-sale financial assets

Available-for-sale financial assets are non-derivative financial assets in listed and unlisted equity securities that are designated as available for sale or are not classified in any of the other two categories. After initial recognition, available-for-sale financial assets are measured at fair value, with gains or losses recognised as a separate component of equity until the investment is derecognised or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is included in the income statement.

When the fair value of unlisted equity securities cannot be reliably measured because (a) the variability in the range of reasonable fair value estimates is significant for that investment or (b) the probabilities of the various estimates within the range cannot be reasonably assessed and used in estimating fair value, such securities are stated at cost less any impairment losses.

Fair value

The fair values of investments that are actively trade in organised financial markets is determined by reference to quoted market bid prices at the close of business at the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions, reference to the current market value of another instrument which is substantially the same.

5. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Impairment of financial assets

The Group assesses at each balance sheet date whether there is any objective evidence that financial asset or a group of financial assets is impaired.

Assets carried at amortised cost

If there is objective evidence that an impairment loss on loans and receivables carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount 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). The carrying amount of the asset is reduced either directly or through the use of an allowance account. The amount of the impairment loss is recognised in the income statement.

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, the asset is included in a group of financial assets with similar credit risk characteristics and that group is collectively assessed for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed. Any subsequent reversal of an impairment loss is recognised in the income statement, to the extent that the carrying value of the asset does not exceed its amortised cost at the reversal date.

In relation to trade receivables, a provision for impairment is made when there is objective evidence (such as the probability of insolvency or significant financial difficulties of the debtor) that the Group will not be able to collect all of the amounts due under the original terms of an invoice. The carrying amount of the receivables is reduced through the use of an allowance account. Impaired debts are derecognised when they are assessed as uncollectible.

Assets carried at cost

If there is objective evidence that an impairment loss on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. Impairment losses on these assets are not reversed.

Available-for-sale financial assets

If an available-for-sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortisation) and its current fair value, less any impairment loss previously recognised in the income statement, is transferred from equity to the income statement. Impairment losses on equity instruments classified as available for sale are not reversed through the income statement.

5. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Derecognition of financial assets

A financial asset (or, where applicable, a part of a financial asset or part of the group of similar financial assets) is derecognised where:

- the rights to receive cash flows from the asset have expired;
- the Group retains the rights to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement; or
- the Group has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Where continuing involvement takes the form of a written and/or purchased option (including a cash-settled option or similar provision) on the transferred asset, the extent of the Group's continuing involvement is the amount of the transferred asset that the Group may repurchase, except in the case of a written put option (including a cash-settled option or similar provision) on an asset measured at fair value, where the extent of the Group's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

Financial liabilities at amortised cost (including interest-bearing loans and borrowings)

Financial liabilities including trade and other payables, an amount due to the ultimate holding company and interest-bearing loans and borrowings are initially stated at fair value less directly attributable transaction costs and are subsequently measured at amortised cost, using the effective interest method unless the effect of discounting would be immaterial, in which case they are stated at cost.

Gains and losses are recognised in the income statement when the liabilities are derecognised as well as through the amortisation process.

Convertible notes

The component of convertible notes that exhibits characteristics of a liability is recognised as a liability in the balance sheet, net of transaction costs. On issuance of convertible notes, the fair value of the liability component is determined using a market rate for an equivalent non-convertible notes; and this amount is carried as a long term liability on the amortised cost basis until extinguished on conversion or redemption. The remainder of the proceeds is allocated to the conversion option that is recognised and included in shareholders' equity, net of transaction costs. The carrying amount of the conversion option is not remeasured in subsequent years. Transaction costs are apportioned between the liability and equity components of the convertible notes based on the allocation of proceeds to the liability and equity components when the instruments are first recognised.

5. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Derecognition of financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and a recognition of a new liability, and the difference between the respective carrying amounts is recognised in the income statement.

Derivative financial instruments and hedging

The Group uses derivative financial instruments such as forward currency contracts to hedge its risks associated with foreign currency fluctuations. Such derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

Any gains or losses arising from changes in fair value on derivatives that do not qualify for hedge accounting are taken directly to the income statement.

The fair value of forward currency contracts is calculated by reference to current forward exchange rates for contracts with similar maturity profiles.

For the purpose of hedge accounting, hedges are classified as:

- fair value hedges when hedging the exposure to changes in the fair value of a recognised asset or liability or an unrecognised firm commitment (except for foreign currency risk); or

- cash flow hedges when hedging the exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction, or a foreign currency risk in an unrecognised firm commitment.

At the inception of a hedge relationship, the Group formally designates and documents the hedge relationship to which the Group wishes to apply hedge accounting, the risk management objective and its strategy for undertaking the hedge. The documentation includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the Group will assess the hedging instrument's effectiveness in offsetting the exposure to changes in the hedged item's fair value or cash flows attributable to the hedged risk. Such hedges are expected to be highly effective in achieving offsetting changes in fair value or cash flows and are assessed on an ongoing basis to determine that they actually have been highly effective throughout the financial reporting periods for which they were designated.

Hedges which meet the strict criteria for hedge accounting are accounted for as follows:

Fair value hedges

The change in the fair value of a hedging derivative is recognised in the income statement. The change in the fair value of the hedged item attributable to the risk hedged is recorded as a part of the carrying amount of the hedged item and is also recognised in the income statement.

5. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Derivative financial instruments and hedging (continued)

Fair value hedges (continued)

For fair value hedges relating to items carried at amortised cost, the adjustment to carrying value is amortised through the income statement over the remaining term to maturity. Any adjustment to the carrying amount of a hedged financial instrument for which the effective interest method is used is amortised to the income statement.

Amortisation may begin as soon as an adjustment exists and shall begin no later than when the hedged item ceases to be adjusted for changes in its fair value attributable to the risk being hedged. If the hedged item is derecognised, the unamortised fair value is recognised immediately in the income statement.

When an unrecognised firm commitment is designated as a hedged item, the subsequent cumulative change in the fair value of the firm commitment attributable to the hedged risk is recognised as an asset or liability with a corresponding gain or loss recognised in the income statement. The changes in the fair value of the hedging instrument are also recognised in the income statement.

Cash flow hedges

The effective portion of the gain or loss on the hedging instrument is recognised directly in equity, while the ineffective portion is recognised immediately in the income statement.

Amounts taken to equity are transferred to the income statement when the hedged transaction affects the income statement, such as when hedged financial income or financial expense is recognised or when a forecast sale occurs. Where the hedged item is the cost of a non-financial asset or non-financial liability, the amounts taken to equity are transferred to the income statement in the same period or periods during which the asset acquired or liability assumed affects the income statement.

If the forecast transaction or firm commitment is no longer expected to occur, the amounts previously recognised in equity are transferred to the income statement. If the hedging instrument expires or is sold, terminated or exercised without replacement or rollover, or if its designation as a hedge is revoked, the amounts previously recognised in equity remain in equity until the forecast transaction or firm commitment occurs.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined on weighted average or standard costing basis and, in the case of work in progress and finished goods, comprises direct materials, direct labour and an appropriate proportion of overheads. Net realisable value is based on estimated selling prices less any estimated costs to be incurred to completion and disposal.

Cash and cash equivalents

For the purpose of the consolidated cash flow statement, cash and cash equivalents comprise cash on hand and demand deposits, and short term highly liquid investments which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value and have a short maturity of generally within three months when acquired, less bank overdrafts which are repayable on demand and form an integral part of the Group's cash management.

For the purpose of the balance sheets, cash and cash equivalents comprise cash on hand and at banks, including term deposits, and assets similar in nature to cash, which are not restricted as to use.

5. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Provisions

A provision is recognised when a present obligation (legal or constructive) has arisen as a result of a past event and it is probable that a future outflow of resources will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation.

When the effect of discounting is material, the amount recognised for a provision is the present value at the balance sheet date of the future expenditures expected to be required to settle the obligation. The increase in the discounted present value amount arising from the passage of time is included in finance costs in the income statement.

Provisions for product warranties granted by the Group on certain products are recognised based on sales volume and past experience of the level of repairs and returns, discounted to their present values as appropriate.

Income tax

Income tax comprises current and deferred tax. Income tax is recognised in the income statement, or in equity if it relates to items that are recognised in the same or a different period directly in equity.

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities.

Deferred tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised for all taxable temporary differences, except:

- where the deferred tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognised for all deductible temporary differences, carryforward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward of unused tax credits and unused tax losses can be utilised except:

- where the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

5. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Income tax (continued)

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 deferred tax asset to be utilised. Conversely, previously unrecognised deferred tax assets are reassessed at each balance sheet date and are recognised to the extent that it is probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Deferred tax assets and deferred tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

Government grant

Government grants are recognised at their fair value where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with. When the grant relates to an expense item, it is recognised as income over the periods necessary to match the grant on a systematic basis to the costs that it is intended to compensate. Where the grant related to an asset, the fair value is credited to a deferred income account and is released to the income statement over the expected useful life of the relevant asset by equal annual instalments.

Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Group and when the revenue can be measured reliably, on the following bases:

(a) from the sale of goods, when the significant risks and rewards of ownership have been transferred to the buyer, provided that the Group maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold;

(b) interest income, on an accrual basis using the effective interest method by applying the rate that discounts the estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset;

(c) subsidy income, when there is reasonable assurance that the subsidy will be received and all attaching conditions have been complied with; and

(d) value-added services income, upon provision of the relevant services.

5. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Employee benefits

Share-based payment transactions

The Company operates a share option scheme for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations. Employees (including directors) of the Group receive remuneration in the form of share-based payment transactions, whereby employees render services as consideration for equity instruments ("equity-settled transactions").

The cost of equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted. The fair value is determined by an external valuer using a binomial model, further details of which are given in note 33 and the report of the directors. In valuing equity-settled transactions, no account is taken of any performance conditions, other than conditions linked to the price of the shares of the Company ("market conditions"), if applicable.

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award (the "vesting date"). The cumulative expense recognised for equity-settled transactions at each balance sheet date until the vesting date reflects the extent to which the vesting period has expired and the Group's best estimate of the number of equity instruments that will ultimately vest. The charge or credit to the income statement for a period represents the movement in the cumulative expense recognised as at the beginning and end of that period.

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance conditions are satisfied.

Where the terms of an equity-settled award are modified, as a minimum an expense is recognised as if the terms had not been modified. In addition, an expense is recognised for any modification, which increases the total fair value of the share-based payment arrangement, or is otherwise beneficial to the employee as measured at the date of modification.

Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. However, if a new award is substituted for the cancelled award, and is designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award, as described in the previous paragraph.

The dilutive effect of outstanding options is reflected as additional share dilution in the computation of earnings per share.

Central Pension Scheme

Subsidiaries operating in Mainland China have participated in the central pension scheme (the "CPS") operated by the PRC government for all of their staff. These PRC subsidiaries are required to contribute a certain percentage of their covered payroll to the CPS to fund the benefits. The only obligation of the Group with respect to the CPS is to pay the ongoing required contributions under the CPS. Contributions under the CPS are charged to the profit and loss account as they become payable in accordance with the rules of the CPS.

5. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Employee benefits (continued)

Mandatory Provident Fund

The Company's subsidiaries, incorporated in Hong Kong, operate a defined contribution Mandatory Provident Fund retirement benefits scheme (the "Scheme") under the Mandatory Provident Fund Schemes Ordinance, for all of its employees in Hong Kong. Contributions are made based on a percentage of the employees' basic salaries and are charged to the profit and loss account as they become payable in accordance with the rules of the Scheme. The assets of the Scheme are held separately from those of the Group in an independently administered fund. The employer contributions vest fully with the employees when contributed into the Scheme except for the employer voluntary contributions, which are refunded to the Company and its subsidiaries which are incorporated outside the PRC when an employee leaves employment prior to the contributions vesting fully, in accordance with the rules of the Scheme.

Retirement indemnities

T&A Mobile Phones SAS ("T&A SAS") (formerly TCL & Alcatel Mobile Phones SAS), which is incorporated in France, operates a defined contribution plan (the "contribution plan") and a defined benefit pension plan (the "pension plan"). For the contribution plan, T&A SAS is not liable for any legal or constructive obligations under the contribution plan beyond the contributions paid, and no provision as such is made. For the pension plan, corresponding to retirement indemnities relating to T&A SAS's employees, liabilities and prepaid expenses are determined as follows:

- using the projected unit credit method, with projected final salary, which considers that each period of service gives rise to an additional unit of benefit entitlement and measures each unit separately to build up the final obligation. Actuarial assumptions comprise mortality, rates of employee turnover and projection of future salary levels; and

- recognising, over the expected average remaining working lives of the employees participating in the plan, actuarial gains and losses in excess of more than 10% of the present value of the defined benefit obligation or 10% of the fair value of any plan assets.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, i.e. assets that necessarily take a substantial period of time to get ready for their intended use or sale, are capitalised as part of the cost of those assets. The capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs capitalised. Borrowing costs are recognised as expenses in the income statement in the period in which they are incurred.

Dividends

Final dividends proposed by the directors are classified as a separate allocation of retained profits within the equity section of the balance sheet, until they have been approved by the shareholders in a general meeting. When these dividends have been approved by the shareholders and declared, they are recognised as a liability.

Interim dividends are simultaneously proposed and declared, because the Company's memorandum and articles of association grant the directors the authority to declare interim dividends. Consequently, interim dividends are recognised immediately as a liability when they are proposed and declared.

5. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Foreign currencies

These financial statements are presented in Hong Kong dollars, which is the Company's functional and presentation currency. Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency. Foreign currency transactions are initially recorded using the functional currency rates ruling at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rates of exchange ruling at the balance sheet date. All differences are taken to the income statement. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

The functional currencies of certain overseas subsidiaries are currencies other than the Hong Kong dollar. As at the balance sheet date, the assets and liabilities of these entities are translated into the presentation currency of the Company at the exchange rates ruling at the balance sheet date, and their income statements are translated into Hong Kong dollars at the weighted average exchange rates for the year. The resulting exchange differences are included in a separate component of equity. On disposal of a foreign entity, the deferred cumulative amount recognised in equity relating to that particular foreign operation is recognised in the income statement.

For the purpose of the consolidated cash flow statement, the cash flows of overseas subsidiaries are translated into Hong Kong dollars at the exchange rates ruling at the dates of the cash flows. Frequently recurring cash flows of overseas subsidiaries, which arise throughout the year are translated into Hong Kong dollars at the weighted average exchange rates for the year.

6. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES

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 disclosed below:

Impairment of property, plant and equipment

The Group determines whether property, plant and equipment are impaired when there is an indication of impairment. This requires an estimation of the value in use of the cash-generating units to which the property, plant and equipment were allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. The carrying amount of property, plant and equipment was approximately HK$262,495,000 (2005: HK$360,149,000). More details are set out in note 16.

Management carries out the impairment review on property, plant and equipment by comparing the lower of carrying amount and recoverable amount of property, plant and equipment.

An impairment loss is recognised when the carrying amount of property, plant and equipment exceeds the recoverable amount. An impairment loss is charged to the income statement in the period in which it arises. Management assesses the recoverable amount by the higher of the fair value less costs to sell and the expected value in use which is determined by the expected useful life and the expected discounted net cashflow of property, plant and equipment.

6. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES (continued)

Estimation uncertainty (continued)

Warranty claims

The Group generally offers warranties for its products for 12 to 24 months. Management estimates the related provision for future warranty claims based on historical warranty claim information, as well as recent trends that might suggest that past cost information may differ from the future claims.

Factors that could impact the estimated claim information include the success of the Group's productivity and quality initiatives, as well as parts and labour costs.

Were claims costs to differ by 10% from management's estimates, the warranty provisions would be an estimated amount of approximately HK$8 million higher or lower in the year of 2007.

Cross licensing compensation

The Group received EUR 20 million from Alcatel Participations for covering the potential mobile handsets intellectual property royalties claims by the original cross licensees who had entered into the cross licensing agreement with the Alcatel Group regarding the waived royalties payment among all the cross licensees in respect of the usage of the mobile handsets intellectual properties owned by the respective cross licensees.

Since Alcatel Group had transferred all their mobile handsets intellectual properties to the Group, the Group is in the process of negotiation with all the original cross licensees for a new cross licensing agreement where there might be risk that the Group might need to pay royalties to these cross licensees.

Accordingly, the management had based on their production plan and their past experience on royalties rate estimated the potential exposure on future royalties claims by the original cross licensees.

Were the future royalties claims by the original cross licensees to differ by 10% from management's estimates, the estimated potential exposure on future royalties claims would be an estimated amount of approximately Euro 1 million higher or lower in the future year.

Impairment of goodwill

The Group determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the value in use of the cash-generating units to which the goodwill is allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. The carrying amount of goodwill at 31 December 2006 was approximately HK$8,785,000 (2005: nil). More details are given in note 20.

7. SEGMENT INFORMATION

The Group is principally engaged in the manufacture and sale of mobile phones and related components. All of the Group's products are of a similar nature and subject to similar risk and returns. Accordingly, the Group's operating activities are attributable to a single business segment.

The Group's revenue and assets are principally attributable to subsidiaries located in various geographical regions. Each of the Group's geographical segments represents the location of the business division's production or service facilities, which is subject to risks and returns that are different from those of the other geographical segments.

The following tables present revenue and assets for the Group's geographical segments.

	Europe		Latin America		The PRC (including Hong Kong)		Consolidated	
	Year ended 31 December		Year ended 31 December		Year ended 31 December		Year ended 31 December	
	2006	2005	**2006**	2005	**2006**	2005	**2006**	2005
	HK$'000	HK$'000	**HK$'000**	HK$'000	**HK$'000**	HK$'000	**HK$'000**	HK$'000
Segment revenue:								
Sales to external customers	**1,979,172**	2,167,591	**1,533,940**	1,051,809	**1,988,515**	2,444,296	**5,501,627**	5,663,696

	Europe		Latin America		The PRC (including Hong Kong)		Eliminations		Consolidated	
	31 December		31 December		31 December		31 December		31 December	
	2006	2005	**2006**	2005	**2006**	2005	**2006**	2005	**2006**	2005
	HK$'000	HK$'000	**HK$'000**	HK$'000	**HK$'000**	HK$'000	**HK$'000**	HK$'000	**HK$'000**	HK$'000
Other segment information:										
Segment assets	**944,806**	820,516	**647,568**	509,535	**3,758,371**	6,596,664	**(1,907,077)**	(3,842,947)	**3,443,668**	4,083,768

8. REVENUE, OTHER INCOME AND GAINS

Revenue, which is also the Group's turnover, represents the net invoiced value of mobile phones and related components sold and services rendered during the year, after allowances for returns and trade discounts. All significant intra-group transactions have been eliminated on combination.

An analysis of turnover, other income and gains is as follows:

	2006 HK$'000	2005 HK$'000
Revenue		
Sale of mobile phones and related components	**5,501,627**	5,663,696
Other income		
Interest income	**12,760**	16,522
Subsidy income	**30,438**	22,043
Value-added services income	**4,745**	19,521
Excess fund contributed from minority interest for the release of intellectual properties royalties guarantee	**–**	91,791
Reversal of restructuring reserves contributed from minority interest	**–**	24,258
Deemed gain on dilution of interest in an associate**	**32,435**	–
Exchange gain	**4,479**	–
Royalty income	**18,646**	–
Insurance claim income	**3,465**	–
Others	**16,720**	6,604
	123,688	180,739
Gains		
Gain on disposal of items of property, plant and equipment	**19,293**	–
Excess over the cost of business combination*	**–**	6,812
	19,293	6,812
Other income and gains	**142,981**	187,551

* Excess over the cost of business combination represents the portion of negative goodwill arising on acquisition in expectation of identified future losses and expenses, which did not represent identifiable liabilities as at the date of acquisition, recognised in 2005.

** The deemed gain on dilution of interest in an associate for the year ended 31 December 2006 represented the gain on the dilution of the Company's shareholding interest in JRD Communication Inc. ("JRDC") from 46.25% to 38.54%, net of the disposal of the related positive goodwill of approximately HK$733,000 as a result of the receipt by JRDC of US$16 million for the new share issue in June 2006.

9. PROFIT/(LOSS) BEFORE TAX

The Group's profit/(loss) before tax is arrived at after charging/(crediting):

	Notes	2006 HK$'000	2005 HK$'000
Cost of inventories sold*		**4,720,309**	5,618,840
Depreciation	16	**97,801**	113,240
Prepaid land lease recognised	17	**587**	548
Amortisation of intangible assets	18	**6,475**	22,416
Brand management fee/TCL Brand Common Fund		**4,744**	10,155
Minimum lease payments under operating leases in respect of land and buildings		**20,619**	23,966
Auditors' remuneration		**3,201**	2,864
Employee benefits expense (including directors' remuneration (note 11)):			
Salaries and wages		**318,576**	663,132
Equity-settled share option expense		**15,997**	7,737
Pension scheme contributions			
Defined contribution scheme		**266**	29,304
Defined benefit schemes		**(454)**	(40,349)
		334,385	659,824
Impairment loss/(write back) of trade receivables**		**(26,119)**	32,609
Write-back of impairment loss on other receivables		**(18,056)**	–
Write-back of inventory obsolescence and net realisable value		**(10,573)**	(42,882)
Product warranty provisions	27	**102,502**	156,470
(Gain)/loss on disposal of items of property, plant & equipment		**(19,293)**	6,072

* The write-back of inventory obsolescence and net realisable value is included in "cost of sales" on the face of the consolidated income statement,

** Impairment loss/(write back) of trade receivables is mainly made for the Group's customers operating in the PRC.

10. FINANCE COSTS

	Group 2006 HK$'000	2005 HK$'000
Interest on bank loans, and other loans wholly repayable within five years	**17,445**	12,613
Interest on convertible notes	**5,553**	2,373
Interest on discounted notes and factored trade receivables*	**6,120**	5,881
	29,118	20,867

* The effective interest rates of discounted notes and factored trade receivables are 0.14% per month and 0.16% per month respectively.

11. DIRECTORS' REMUNERATION AND FIVE HIGHEST PAID EMPLOYEES

Directors' remuneration for the year, disclosed pursuant to the Listing Rules and Section 161 of the Hong Kong Companies Ordinance, are as follows:

	Group	
	2006	2005
	HK$'000	HK$'000
Fees	**1,195**	1,623
Other emoluments:		
Salaries, allowances and benefits in kind	**1,460**	2,875
Employee share option benefits	**2,824**	2,073
Pension scheme contributions	**24**	70
	5,503	6,641

During 2005 and 2006, certain directors were granted share options, in respect of their services to the Group, under the share option scheme of the Company, further details of which are set out in note 33 to the financial statements and the director's report. The fair value of such options, which has been recognised to income statement over the vesting period, was determined as at the date of the grant and the amount included in the financial statements for the current year is included in the above directors' remuneration disclosures.

(a) Independent non-executive directors

The fees paid to independent non-executive directors during the year were as follows:

	2006	2005
	HK$'000	HK$'000
Mr. Shi Cuiming	**180**	180
Mr. Wang Chongju	**180**	180
Mr. Lau Siu Ki	**180**	180
	540	540

During 2005 and 2006, all independent non-executive directors were granted share options, in respect of their services to the Group, under the share options scheme of the Company, further details of which are set out in note 33 to the financial statements. The fair value of such options and other share option granted to the independent non-executive directors, which has been recognised to income statement over the vesting period was determined as at the date of the grant and the amount of HK$147,000 (2005: HK$90,000) recognised in the income statement for the current year is included in the above directors' remuneration disclosures.

11. DIRECTORS' REMUNERATION AND FIVE HIGHEST PAID EMPLOYEES (continued)

(b) Executive directors, non-executive directors and five highest paid employees

2006	Fees	Salaries, allowances and benefits in kind	Employee share option benefits	Pension scheme contributions	Total remuneration
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Executive directors:					
Mr. Li Dongsheng	120	10	685	6	821
Dr. Liu Fei	120	1,440	658	12	2,230
Mr. Yan Yong	120	10	123	6	259
Mr. Yuan Xin Cheng (resigned on 8 June 2006)	–	–	298	–	298
Mr. Du Xiaopeng, Simon (retired on 8 June 2006)	53	–	–	–	53
Dr. Guo Aiping, George (retired on 8 June 2006)	53	–	–	–	53
Mr. Wong Toe Yeung, Chambers (retired on 8 June 2006)	53	–	685	–	738
Non-executive directors:					
Mr. Wang Kangping (appointed on 8 June 2006)	68	–	155	–	223
Dr. Zhao Zhicheng (appointed on 8 June 2006)	68	–	73	–	141
	655	1,460	2,677	24	4,816

11. DIRECTORS' REMUNERATION AND FIVE HIGHEST PAID EMPLOYEES (continued)

(b) Executive directors, non-executive directors and five highest paid employees (continued)

2005	Fees HK$'000	Salaries, allowances and benefits in kind HK$'000	Employee share option benefits HK$'000	Pension scheme contributions HK$'000	Total remuneration HK$'000
Executive directors					
Mr. Li Dongsheng	120	10	501	7	638
Mr. Wan Mingjian	–	206	–	7	213
Mr. Yuan Xin Cheng	–	–	300	–	300
Dr. Liu Fei	63	1,435	160	14	1,672
Mr. Yan Yong	120	10	105	7	242
Mr. Du Xiaopeng, Simon	120	318	321	7	766
Dr. Guo Aiping, George	120	851	95	26	1,092
Mr. Wong Toe Yeung, Chambers	540	45	501	2	1,088
	1,083	2,875	1,983	70	6,011

There was no arrangement under which a director waived or agreed to waive any remuneration during the year.

The five highest paid employees during the year included one (2005: two) directors, details of whose remuneration are set out above.

Details of the remuneration of the remaining four (2005: three) non-directors, highest paid employees for the year are as follows:

	2006 HK$'000	2005 HK$'000
Salaries, allowances and benefits in kind	**6,461**	4,280
Employee share option benefits	**917**	–
Pension scheme contributions	**–**	378
	7,378	4,658

11. DIRECTORS' REMUNERATION AND FIVE HIGHEST PAID EMPLOYEES (continued)

(b) Executive directors, non-executive directors and five highest paid employees (continued)

The number of non-directors, highest paid employees whose remuneration fell within the following bands is as follows:

	Number of non-directors	
	2006	2005
Nil to HK$1,000,000	**–**	–
HK$1,000,001 to HK$1,500,000	**1**	1
HK$1,500,001 to HK$2,000,000	**2**	2
HK$2,000,001 to HK$2,500,000	**1**	–
	4	3

During 2005 and 2006, share options were granted to a non-director, highest paid employee in respect of his services to the Group, further details of which are included in the disclosures in note 33 to the financial statements. The fair value of such options, which has been recognised to the income statement over the vesting period, was determined as at the date of the grant and the amount included in the financial statement for the current year was included in the above non-director, highest paid employees' remuneration disclosures.

12. TAX

Group:

	2006	2005
	HK$'000	HK$'000
Current year provision:		
Hong Kong	**–**	323
Mainland China	**–**	2,639
France	**1,029**	–
Mexico	**17,192**	15,914
Deferred (note 31)	**(1,512)**	5,754
Tax charge for the year	**16,709**	24,630

Hong Kong profits tax has been provided at a rate of 17.5% (2005: 17.5%) on the estimated assessable profits arising in Hong Kong during the year. Taxes on profits assessable elsewhere have been calculated at the rate of tax prevailing in the jurisdiction of which the Group operates, based on existing legislation, interpretations and practices in respect thereof.

Huizhou TCL Mobile Communication Co., Ltd. ("TCL Mobile"), a subsidiary of the Company in the PRC, had been accredited as high and new technology enterprise accreditation which had expired on 28 May 2005. It was exempt from the national income tax in 2000 and 2001 and had been subject to a national income tax rate of 7.5% since 2002. The 7.5% income tax rate for TCL Mobile expired at the end of 2004. By the end of 2004, TCL Mobile obtained its advanced technology enterprise accreditation and hence was subject to a national income tax rate of 10% from 2005 to 2007.

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31 December 2006

12. TAX (continued)

According to the Income Tax Law of the PRC on the Enterprises with Foreign Investment and Foreign Enterprises, TCL Mobile Communication (Hohhot) Co., Ltd. ("Mobile Hohhot"), a subsidiary of the Company in the PRC, is entitled to exemption from the PRC corporate income tax for two years commencing from its first profit-making year and thereafter is entitled to a 50% reduction in its PRC corporate income tax for the subsequent three years. Mobile Hohhot also enjoys preferential tax treatment as being foreign investment enterprises located in the western region of China, including 50% reduction in national corporate income tax until 2010. As Mobile Hohhot commenced to make profits in 2002, it was exempt from PRC corporate income tax in 2002 and 2003, and the applicable PRC corporate income tax rate from 2004 to 2006 was 7.5%. Mobile Hohhot is subject to the PRC corporate income tax rate of 15% from 2007 to 2010 and 30% thereafter.

No profits tax has been provided in the PRC as no taxable income arose during the year.

During the year, T&A Mobile Phones SA de CV Limited paid royalties to T&A Mobile Phones SAS for general relations and contract service charge. According to the applicable Mexican withholding tax regulation, the payments characterised as royalties are subject to a 10% tax on payments defined as royalties under the applicable Mexico – France tax treaty.

A reconciliation of the tax expense applicable to profit/(loss) before tax using the statutory rates for the countries in which the Company and its subsidiaries, are domiciled to the tax expense at the effective tax rates, and a reconciliation of the applicable rates (i.e. the statutory tax rates) to the effective tax rates, are as follows:

	2006		2005	
	HK$'000	**%**	HK$'000	%
Profit/(loss) before tax	**32,132**		(1,871,446)	
Tax at the applicable rates	**81,416**	**253.4**	(593,390)	31.7
Lower tax rate for specific provinces or local authority	**(60,447)**	**(188.1)**	258,479	(13.8)
Income not subject to tax	**(29,212)**	**(90.9)**	(20,322)	1.1
Expenses not deductible for tax	**59,720**	**185.8**	6,882	(0.4)
Tax loss utilised	**(127,438)**	**(396.6)**	–	–
Tax loss not recognised	**92,670**	**288.4**	372,981	(19.9)
Tax charge at the Group's effective rate	**16,709**	**52.0**	24,630	(1.3)

13. LOSS ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT

The consolidated profit/(loss) attributable to equity holders of the parent for the year ended 31 December 2006 includes a loss of HK$402,254,000 (2005: HK$1,665,843,000) which has been dealt with in the financial statements of the Company (note 34(b)).

14. DIVIDENDS

No dividend has been paid or declared by the Company for the year ended 31 December 2005 and 2006.

Notes to Financial Statements

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15. EARNINGS/(LOSS) PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT

The calculations of basic and diluted earnings/(loss) per share are based on:

	2006 HK$'000	2005 HK$'000
Earnings/(loss)		
Profit/(loss) attributable to ordinary equity holders of the parent, used in the basic earnings/(loss) per share calculation	**15,423**	(1,608,204)
Loss attributable to minority interest	–	(287,872)
Earnings/(loss) for the purposes of diluted earnings/(loss) per share	**15,423**	(1,896,076)

Shares	Number of shares 2006	2005
Weighted average number of ordinary shares in issue during the year used in the basic earnings/(loss) per share calculation	**5,509,280,895**	2,892,183,904
Effect of diluted weighted average number of ordinary shares:		
Assumed issuance on deemed exercise of option by the minority shareholder of the joint venture formed between the Company and Alcatel (the "Joint Venture") by converting its interest in the Joint Venture into the shares of the Company	–	48,849,041
Assumed issuance upon the exercise of share options	**46,831,228**	–
	5,556,112,123	2,941,032,945

The calculation of the diluted earnings/(loss) per share for the year ended 31 December 2006 has also taken into account the convertible notes and share options outstanding during the year. As the adjusted conversion price of the convertible notes during the year is higher than the fair market value of the ordinary share, any conversion of convertible notes is anti-dilutive. Since the exercise price of certain share option during the year is lower than the fair market value of the ordinary share, the share option outstanding during the year has a dilutive effect to the Company.

The calculation of the diluted loss per share for the year ended 31 December 2005 has also taken into account the convertible notes and share options outstanding during 2005. As the Company incurred loss during 2005, any conversion of convertible notes is anti-dilutive. Since the exercise price of the share option during 2005 is higher than the fair market value of ordinary shares, the share option outstanding during 2005 does not have a dilutive effect to the Company.

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16. PROPERTY, PLANT AND EQUIPMENT

Group

	Buildings HK$'000	Plant and machinery HK$'000	Furniture, fixtures and office equipment HK$'000	Motor vehicles HK$'000	Construction in progress HK$'000	Total HK$'000
31 December 2006						
At 31 December 2005 and at 1 January 2006:						
Cost	90,119	472,778	78,723	12,533	2,636	656,789
Accumulated depreciation and impairment	(6,508)	(227,712)	(54,528)	(7,892)	–	(296,640)
Net carrying amount	83,611	245,066	24,195	4,641	2,636	360,149
At 1 January 2006, net of accumulated depreciation and impairment	83,611	245,066	24,195	4,641	2,636	360,149
Additions	–	16,134	6,675	2,178	–	24,987
Disposals	(845)	(87,269)	(39,174)	(8,316)	–	(135,604)
Depreciation and impairment provided during the year	(3,180)	(85,912)	(7,487)	(1,222)	–	(97,801)
Written back on disposals	121	63,865	28,944	5,524	–	98,454
Transfers	–	2,677	–	–	(2,677)	–
Exchange realignments	2,884	8,415	901	69	41	12,310
At 31 December 2006, net of accumulated depreciation and impairment	82,591	162,976	14,054	2,874	–	262,495
At 31 December 2006:						
Cost	92,453	423,527	48,843	6,705	–	571,528
Accumulated depreciation and impairment	(9,862)	(260,551)	(34,789)	(3,831)	–	(309,033)
Net carrying amount	82,591	162,976	14,054	2,874	–	262,495

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16. PROPERTY, PLANT AND EQUIPMENT (continued)

Group (continued)

	Buildings HK$'000	Plant and machinery HK$'000	Furniture, fixtures and office equipment HK$'000	Motor vehicles HK$'000	Construction in progress HK$'000	Total HK$'000
31 December 2005						
At 31 December 2004 and at 1 January 2005:						
Cost	83,411	442,294	78,272	12,462	1,525	617,964
Accumulated depreciation and impairment	(3,117)	(136,445)	(43,945)	(6,517)	–	(190,024)
Net carrying amount	80,294	305,849	34,327	5,945	1,525	427,940
At 1 January 2005, net of accumulated depreciation and impairment	80,294	305,849	34,327	5,945	1,525	427,940
Additions	5,065	39,849	5,633	667	2,989	54,203
Disposals	(137)	(9,605)	(5,199)	(812)	–	(15,753)
Depreciation and impairment provided during the year	(2,501)	(96,434)	(12,518)	(1,787)	–	(113,240)
Written back on disposals	–	3,835	2,819	560	–	7,214
Transfers	–	1,878	–	–	(1,878)	–
Exchange realignments	890	(306)	(867)	68	–	(215)
At 31 December 2005, net of accumulated depreciation and impairment	83,611	245,066	24,195	4,641	2,636	360,149
At 31 December 2005:						
Cost	90,119	472,778	78,723	12,533	2,636	656,789
Accumulated depreciation and impairment	(6,508)	(227,712)	(54,528)	(7,892)	–	(296,640)
Net carrying amount	83,611	245,066	24,195	4,641	2,636	360,149

During 2005, impairment provision was made in respect of assets that the directors believe the respective recoverable amount in the future is lower than the carrying amount.

16. PROPERTY, PLANT AND EQUIPMENT (continued)

Company

	Leasehold improvements HK$'000	Furniture, fixtures and office equipment HK$'000	Motor vehicles HK$'000	Total HK$'000
31 December 2006				
At 31 December 2005 and at 1 January 2006:				
Cost	**260**	**532**	**429**	**1,221**
Accumulated depreciation and impairment	**(171)**	**(128)**	**(100)**	**(399)**
Net carrying amount	**89**	**404**	**329**	**822**
At 1 January 2006, net of accumulated depreciation and impairment	**89**	**404**	**329**	**822**
Disposals	**–**	**(56)**	**(429)**	**(485)**
Depreciation provided during the year	**(88)**	**(105)**	**(7)**	**(200)**
Depreciation written back on disposals	**–**	**22**	**107**	**129**
At 31 December 2006, net of accumulated depreciation and impairment	**1**	**265**	**–**	**266**
At 31 December 2006:				
Cost	**260**	**476**	**–**	**736**
Accumulated depreciation and impairment	**(259)**	**(211)**	**–**	**(470)**
Net carrying amount	**1**	**265**	**–**	**266**
31 December 2005				
At 31 December 2004 and at 1 January 2005:				
Cost	256	466	429	1,151
Accumulated depreciation and impairment	(42)	(30)	(14)	(86)
Net carrying amount	214	436	415	1,065
At 1 January 2005, net of accumulated depreciation and impairment	214	436	415	1,065
Additions	4	84	–	88
Disposals	–	(18)	–	(18)
Depreciation provided during the year	(129)	(101)	(86)	(316)
Depreciation written back on disposals	–	3	–	3
At 31 December 2005, net of accumulated depreciation and impairment	89	404	329	822
At 31 December 2005:				
Cost	260	532	429	1,221
Accumulated depreciation and impairment	(171)	(128)	(100)	(399)
Net carrying amount	89	404	329	822

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17. PREPAID LAND LEASE PAYMENTS

	2006 HK$'000	2005 HK$'000
Carrying amount at 1 January	**11,400**	11,736
Recognised during the year	**(587)**	(548)
Exchange realignment	**406**	212
Carrying amount at 31 December	**11,219**	11,400

As at 31 December 2006, the Group's land and buildings situated in Mainland China are held under long-term land use rights.

18. INTANGIBLE ASSETS

Group

	Computer software HK$'000	Intellectual property HK$'000	Total HK$'000
31 December 2006:			
Cost at 1 January 2006, net of accumulated amortisation and impairment	2,787	10,754	13,541
Additions	1,815	–	1,815
Disposals	(425)	–	(425)
Amortisation provided during the year	(2,394)	(4,081)	(6,475)
Exchange realignment	276	462	738
At 31 December 2006	2,059	7,135	9,194
At 31 December 2006:			
Cost	15,850	24,271	40,121
Accumulated amortisation and impairment	(13,791)	(17,136)	(30,927)
Net carrying amount	2,059	7,135	9,194

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18. INTANGIBLE ASSETS (continued)

Group

	Computer software HK$'000	Intellectual property HK$'000	Total HK$'000
31 December 2005:			
Cost at 1 January 2005, net of accumulated amortisation and impairment	7,670	26,197	33,867
Additions	4,509	–	4,509
Retirements and disposals	(24)	–	(24)
Amortisation provided during the year	(9,361)	(13,055)	(22,416)
Exchange realignment	(7)	(2,388)	(2,395)
At 31 December 2005	2,787	10,754	13,541
At 31 December 2005:			
Cost	14,184	23,809	37,993
Accumulated amortisation and impairment	(11,397)	(13,055)	(24,452)
Net carrying amount	2,787	10,754	13,541

Company

	Computer software HK$'000
31 December 2006:	
Cost at 1 January 2006, net of accumulated amortisation and impairment	**7**
Amortisation provided during the year	**(2)**
At 31 December 2006	**5**
At 31 December 2006:	
Cost	**10**
Accumulated amortisation and impairment	**(5)**
Net carrying amount	**5**
31 December 2005:	
Cost at 1 January 2005, net of accumulated amortisation and impairment	10
Amortisation provided during the year	(2)
Exchange realignment	(1)
At 31 December 2005	7
At 31 December 2005:	
Cost	10
Accumulated amortisation and impairment	(3)
Net carrying amount	7

19. INTERESTS IN SUBSIDIARIES

	Company	
	2006	2005
	HK$'000	HK$'000
Unlisted shares, at cost	**1,248,039**	1,248,039
Due from subsidiaries	**1,433,911**	974,809
Impairment loss of interests in subsidiaries	**(2,009,963)**	(1,641,848)
	671,987	581,000

The amounts due from subsidiaries included in the Company's current assets are unsecured, interest-free and have no fixed terms of repayment.

Particulars of the principal subsidiaries are as follows:

Name	Place and date of incorporation/ operation	Nominal value of issued and fully paid share capital	Percentage of attributable equity interest Direct	Percentage of attributable equity interest Indirect	Principal Activities
TCL Mobile Communication (HK) Company Limited	Hong Kong 21 April 1999	HK$5,000,000	–	100%	Trading of mobile phones components
Huizhou TCL Mobile Communication Co., Ltd. (Notes(i))	The PRC 29 March 1999	US$79,600,000	–	100%	Manufacturing and sale of mobile phones
TCL Mobile Communication (Hohhot) Co., Ltd. (Notes (i))	The PRC 29 April 2002	RMB30,000,000	–	100%	Manufacturing and sale of mobile phones
T&A Mobile Phones Limited ("T&A")	Hong Kong 17 May 2004	HK$10,000,000	100%	–	Manufacturing and sale of mobile phones
T&A Mobile Phones SAS	France 1 January 2004	EUR87,540,000	–	100%	Development and distribution of mobile phones
T&A Mobile Phones SA de CV Limited	Mexico 24 May 2004	US$4,300	–	100%	Distribution of mobile phones
T&A Mobile Phones Suzhou Limited (Note (i))	The PRC 14 December 1998	US$28,000,000	–	100%	Development and distribution of mobile phones
T&A Mobile Phones International Limited	Hong Kong 11 May 2005	HK$1	–	100%	Development and distribution of mobile phones
T&A Mobile Phones Europe SAS	France 30 August 2005	EUR40,000	–	100%	Distribution of mobile phones

Note:

(i) This is a wholly foreign owned enterprise.

The above table lists the subsidiaries of the Company which, in the opinion of the directors, principally affected the results for the year or formed a substantial portion of the net assets of the Group. To give details of other subsidiaries would, in the opinion of the directors, result in particulars of excessive length.

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20. INTEREST IN AN ASSOCIATE

	Group 2006 HK$'000	Group 2005 HK$'000	Company 2006 HK$'000	Company 2005 HK$'000
Unlisted shares, at cost	–	–	107,474	–
Share of net assets	121,516	–	–	–
Goodwill on acquisition (Note (a))	8,785	–	–	–
	130,301	–	107,474	–

Particulars of the associate is as follows:

Name	Particulars of issued shares held	Place of incorporation	Percentage of ownership interest attributable to the Group	Principal activities
JRD Communication Inc.	Ordinary shares of HK$0.1 each	British Virgin Islands	38.54%	Provision of product design and development services

* Not audited by Ernst & Young Hong Kong or other Ernst & Young International member firms.

The following table illustrates the summarised financial information of the Group's associates extracted from their management accounts:

	2006 HK$'000	2005 HK$'000
Assets	357,697	–
Liabilities	42,399	–
Revenues	46,344	–
Loss	45,743	–

Note (a)

Goodwill

Group

	HK$'000
Cost and net carrying amount at 31 December 2006	8,785

20. INTEREST IN AN ASSOCIATE (continued)

Goodwill acquired through business combinations has been allocated to the mobile hands cash-generating unit for impairment testing.

The recoverable amount of goodwill is determined based on a value in use calculation. The value in use calculation uses cash flow projections based on financial budgets covering a five-year period approved by management. The discount rate applied to the cash flow projections is 5% and cash flows beyond the five-year period extrapolated using a growth rate of ranges from 28% to 39% of revenue. Management has determined the budgeted gross margins based on past performance and its expectation for market development. The discount rates used are before tax and reflect specific risks relating to the relevant units.

21. AVAILABLE-FOR-SALE INVESTMENT

	Group	
	2006	2005
	HK$'000	HK$'000
Unlisted equity investment, at fair value	**20,207**	–

The above investment consists of investment in equity securities which was designated as available-for-sale financial assets and has no fixed maturity date or coupon rate.

During the year, available for-sale investment was stated at cost and in the opinion of the directors, it approximates to its fair value. For details of the available-for-sale investment, please refer to note 38(b) to the financial statements.

22. INVENTORIES

	Group	
	2006	2005
	HK$'000	HK$'000
Raw materials	**345,417**	455,366
Work in progress	**18,450**	20,015
Finished goods	**384,751**	411,676
	748,618	887,057
Provision against inventory obsolescence and net realised value	**(167,202)**	(177,778)
	581,416	709,279

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23. TRADE RECEIVABLES

An aged analysis of the trade receivables as at the balance sheet date, based on the invoice date is as follows:

	Group	
	2006	2005
	HK$'000	HK$'000
Within 3 months	**1,056,795**	996,600
4 to 12 months	**48,708**	174,520
Over 12 months	**25,633**	–
	1,131,136	1,171,120
Impairment loss of trade receivables	**(17,938)**	(44,057)
	1,113,198	1,127,063

24. FACTORED TRADE RECEIVABLES

At 31 December 2006, a subsidiary of the Group factored trade receivables of HK$256,483,000 (2005: HK$106,981,000) to banks on a without-recourse basis for cash. As the subsidiary of the Group still retained the risks and rewards associated with the delay in payment by the customers, the financial asset derecognition conditions as stipulated in HKAS 39 have not been fulfilled. Accordingly, bank advances from the factoring of the Group's trade receivables have been accounted for as liabilities in the consolidated balance sheet. Maturity date ranges from 30 days to 120 days.

25. PLEDGED DEPOSITS, CASH AND CASH EQUIVALENTS

	Group		Company	
	2006	2005	**2006**	2005
	HK$'000	HK$'000	**HK$'000**	HK$'000
Cash and cash equivalents	**531,001**	405,755	**1,633**	3,078
Pledged deposits	**36,603**	54,317	**–**	–
	567,604	460,072	**1,633**	3,078
Less: Pledged deposits:				
– for factored trade receivables (note 24)	**(36,603)**	(18,870)	**–**	–
– for discounted notes	**–**	(35,447)	**–**	–
Cash and cash equivalents	**531,001**	405,755	**1,633**	3,078

At the balance sheet date, the cash and bank balances of the Group denominated in Renminbi ("RMB") amounted to approximately HK$135,922,000 (2005: HK$94,612,000). The RMB is not freely convertible into other currencies. However, under Mainland China's Foreign Exchange Control Regulations and Administration of Settlement, Sale and Payment of Foreign Exchange Regulations, the Group is permitted to exchange RMB for other currencies through banks authorised to conduct foreign exchange business.

Cash at bank earns interest at floating rates based on daily bank deposits rates. The carrying amounts of the cash and cash equivalents and the pledged deposits approximate to their fair values.

26. TRADE AND NOTES PAYABLES

An aged analysis of the Group's trade and notes payables as at the balance sheet date, based on the invoice date, is analysed as follows:

	Group		Company	
	2006	2005	**2006**	2005
	HK$'000	HK$'000	**HK$'000**	HK$'000
Within 6 months	**1,138,334**	1,690,543	**2,097**	3,330
7 to 12 months	**65,618**	42,248	**–**	–
More than 1 year	**8,718**	7,819	**–**	–
	1,212,670	1,740,610	**2,097**	3,330

Trade and notes payables are non-interest-bearing and have an average term of three months.

All trade and notes payables are not secured by the pledged deposits.

27. PROVISION FOR WARRANTIES

The movement of provision for warranties during the year is summarised as follows:

	Group	
	2006	2005
	HK$'000	HK$'000
At beginning of year	**108,294**	143,248
Provision	**102,502**	156,470
Utilized	**(133,751)**	(179,052)
Exchange difference	**3,950**	(12,372)
At end of year	**80,995**	108,294

The Group generally provides one to two years warranty to its customers on all products, under which faulty products are repaired or replaced. The amount of the provision for the warranties is estimated based on sales volumes and past experience of the level of repairs and return. The estimation basis is reviewed on an ongoing basis and revised where appropriate. During the year, the provision of warranties was not discounted, as the effect of discounting was not material.

28. CONVERTIBLE NOTES

On 11 May 2005, the Company entered into the subscription agreement with TCL Corporation, its ultimate controlling shareholder, for the issue of an aggregate of Euro 20,000,000 principal amount (equivalent to HK$185,100,000) of 3% Convertible Notes ("CN") to TCL Corporation. The CN was issued on 29 July 2005. As at the balance sheet date, there was no movement in the number of these CN. The CN has a term of 3 years and TCL Corporation has the right to convert the CN at the conversion price of HK$0.58175 per share in whole or in part in the principal amount into ordinary shares in amounts of not less than HK$10,000,000 on each conversion. Subsequent to the open offer completed on 27 February 2006, the conversion price of CN is adjusted to HK$0.528324 per share.

The Company has the option to redeem, in whole or any part, the CN at 100% of their principal amount plus interest accrued to but excluding the date of redemption after 24 months from the issue date.

The fair value of the liability component was estimated at the issuance date using an equivalent market interest rate for a similar note without a conversion option. The residual amount is assigned as the equity component and is included in shareholder's equity.

The convertible notes have been split as to the liability and equity components, as follows:

	2006 HK$'000	2005 HK$'000
Nominal value of convertible note issued	**185,100**	185,100
Equity component	**(19,430)**	(19,430)
Liability component at the issuance date	**165,670**	165,670
Interest expense	**5,553**	2,373
Interest paid	**(2,799)**	–
Liability component at 31 December	**168,424**	168,043

29. RETIREMENT INDEMNITIES

Retirement indemnities in respect of the defined benefits scheme plan for the year ended 31 December 2006 amounted to HK$496,000 (2005: HK$908,000).

	Group	
	2006	2005
	HK$'000	HK$'000
Present value of fund obligation	**496**	908
Unrealized actuarial losses	**–**	–
Retirement indemnities	**496**	908

Movement of retirement indemnities is as follows:

	Group	
	2006	2005
	HK$'000	HK$'000
Balance at beginning of year	**908**	45,030
Benefit expenses reversed in the consolidated results (note 9)	**(454)**	(40,349)
Exchange realignment	**42**	(3,773)
Balance at end of year	**496**	908

The Group does not have any unfunded obligations.

The main assumptions used in the retirement indemnity computation for the defined benefit plan are as follows:

	Group	
	2006	2005
Discount rate	**4.5%**	3.8%
Future salary increase per annum	**5.0%**	5.0%

30. LONG SERVICE MEDALS

T&A Mobile Phones SAS provides for the probable future long service medals expected to be made to employees. The provision is based on the best estimate of the probable future payments which have been earned by the employees from their service to T&A Mobile Phones SAS to the balance sheet date.

31. DEFERRED TAX ASSETS

Group:

	Product warranty provision HK$'000	Provision against inventory obsolescence HK$'000	Impairment for property, plant and equipment HK$'000	Tax losses HK$'000	Advertising and promotion accruals HK$'000	Total HK$'000
At 1 January 2006	**3,630**	**4,524**	**242**	**419**	**–**	**8,815**
Exchange realignment	**128**	**159**	**9**	**14**	**3**	**313**
Deferred tax credited/(charged) to income statement during the year (note 12)	**(3,758)**	**(4,683)**	**(251)**	**7,849**	**2,355**	**1,512**
Net deferred tax assets at 31 December 2006	**–**	**–**	**–**	**8,282**	**2,358**	**10,640**

At 31 December 2006, there was no significant unrecognised deferred tax liability (2005: Nil) for taxes that would be payable on the unremitted earnings of certain of the Group's subsidiaries as the Group has no liability to additional tax should such amounts be remitted.

The Group has tax losses of HK$1,902,811,000 (2005: HK$2,591,278,000) that are available for offsetting against future taxable profits of the companies in which the losses arose. Deferred tax assets have not been recognised in respect of these losses as they have arisen in subsidiaries that have been loss-making for some time and it is not considered probable that taxable profits will be available against which the tax losses can be utilised.

	Product warranty provision HK$'000	Provision against inventory obsolescence HK$'000	Impairment for property, plant and equipment HK$'000	Tax losses HK$'000	Total HK$'000
At 1 January 2005	9,445	4,524	242	419	14,630
Exchange realignment	(61)	–	–	–	(61)
Deferred tax charged to income statement during the year (note 12)	(5,754)	–	–	–	(5,754)
Net deferred tax assets at 31 December 2005	3,630	4,524	242	419	8,815

32. SHARE CAPITAL

	No of shares	Amount HK$'000
Authorised:		
Ordinary shares of HK$ 0.1 each at 1 January 2005 and 31 December 2005	5,000,000,000	500,000
Increase during the year	3,000,000,000	300,000
Ordinary share of HK$ 0.1 each at 31 December 2006	8,000,000,000	800,000
Issued and fully paid or credited as fully paid:		
Ordinary shares of HK$ 0.1 each at 1 January 2005	2,827,500,000	282,750
Shares allotted and issued pursuant to the Framework Agreement	141,375,000	14,138
At 31 December 2005 and at 1 January 2006	2,968,875,000	296,888
Shares allotted and issued pursuant to the Completion of Open Offer	2,968,875,000	296,887
Share options exercised (note 33)	1,962,052	196
At 31 December 2006	5,939,712,052	593,971

Pursuant to a resolution passed at an extra – ordinary general meeting held on 6 February 2006:

– the authorised share capital of the Company was increased from HK$500,000,000 to HK$800,000,000 by the creation of an additional 3,000,000,000 unissued shares of HK$0.1 each.

– the Company was approved to issue 2,968,875,000 new shares ("Offer Share") at a price of HK$0.2 per share by way of Open Offer, on the basis of one offer share for every one share of the Company held on them. The Open Offer was completed on 27 February 2006 with a net proceeds of approximately HK$587,200,000. Of the net proceeds from the Open Offer of about HK$587.2 million, the Group has utilized approximately HK$150 million to settle the payables incurred in its ordinary business, about HK$237.2 million as general working capital and about HK$200 million in research and development activities of advanced technology of the industry.

Shares issued during the year rank pari passu with the then existing shares in all aspects.

32. SHARE CAPITAL (continued)

As a result of the completion of the Open Offer, the conversion price of the Convertible Notes had been adjusted from HK$0.58175 per share to HK$0.528324 per share in accordance with the relevant terms of Convertible Notes and accordingly the Convertible Notes will now entitle the holder thereof to convert them into up to 350,353,192 shares (instead of 318,177,911 shares as previously envisaged). Further, the exercise price and the number of the share options ("Share Options") granted under the share option scheme adopted by the Company on 13 September 2004 ("Share Option Scheme") and outstanding as at 27 February 2006 has also been adjusted in accordance with the terms of the Share Option Scheme and the relevant requirements of the Listing Rules as follows:

	Before the Open Offer		After the Open Offer	
Grant Date	Exercise per share	No. of outstanding Share Options	Adjusted exercise price per share	Adjusted no. of outstanding Share Options
31 May 2005	HK$0.415	120,570,000	HK$0.3804	131,531,019
16 January 2006	HK$0.230	162,180,000	HK$0.2108	176,923,784
Total:		282,750,000		308,454,803

For further details of the adjustments, please refer to the Company's announcement dated 28 February 2006.

33. SHARE OPTION SCHEME

The Company has adopted the Share Option Scheme for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations. Eligible participants of the Share Option Scheme include employees (including executive and non – executive directors), advisers, consultants, agents, contractors, clients, suppliers, and any other person(s) whom the board of directors of the Company in its sole discretion considers has contributed or may contribute to the Group. The Share Option Scheme became effective on 27 September 2004 and, unless otherwise cancelled or amended, will remain in force for 10 years from that date.

The maximum number of unexercised share options currently permitted to be granted under the Share Option Scheme (as refreshed by shareholders' approval dated 6 February 2006) is an amount equivalent, upon their exercise, to 10% of the shares of the Company in issue as at 6 February 2006 (i. e. up to 296,887,500 shares). The maximum number of shares issuable under share options to each eligible participant in the Share Option Scheme within any 12-month period, is limited to 1% of the shares of the Company in issue at any time. Any further grant of share options in excess of this limit is subject to shareholders' approval in a general meeting.

Share options granted to a director, chief executive or substantial shareholder of the Company, or to any of their respective associates, are subject to approval in advance by the independent non-executive directors. In addition, any share options granted to a substantial shareholder or an independent non-executive director of the Company, or to any of their respective associates, in excess of 0.1% of the shares of the Company in issue at any time and with an aggregate value (based on the closing price of the Company's shares at the date of the grant) in excess of HK$5 million, within any 12-month period, are subject to shareholders' approval in advance in a general meeting.

The exercise price of the share options is determinable by the directors, but may not be less than the higher of: (i) the Stock Exchange closing price of the Company's shares on the date of the grant of the share options; (ii) the average Stock Exchange closing price of the Company's shares for the five trading days immediately preceding the date of the grant; and (iii) the nominal value of a share.

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33. SHARE OPTION SCHEME (continued)

Share options do not confer rights on the holders to dividends or to vote at shareholders' meetings.

The following share options were outstanding under the share option schemes of the Company during the year:

Name or category of participant	Number of share options: At 1 January 2006	Granted during the year	Exercised during the year	Cancelled/ Lapsed during the year	Adjustment *(Note 4)*	Re-classified	At 31 December 2006	Date of grant	Exercise period (both dates inclusive) *(Notes 5, 6 and 7)*	Exercise price *(Note 4)* (HK$)	Closing price immediately before the Date of Grant (HK$)	Price of Company's shares: Immediately before the exercise date	At exercise date of options
Directors													
Mr. LI Dongsheng	5,000,000	–	–	–	454,550	–	5,454,550	31 May, 2005	1 March 2006 to 30 November 2008	0.3804	0.41	N/A	N/A
	–	3,000,000	–	–	2,000,000	–	5,000,000	16 January, 2006	17 July 2006 to 15 January 2008	0.2108	0.22	N/A	N/A
	–	5,000,000	N/A	–	–	–	5,000,000	30 June, 2006	1 April 2007 to 31 December 2009	0.232	0.228	N/A	N/A
	5,000,000	8,000,000	–	–	2,454,550	–	15,454,550						
Dr. LIU Fei	1,600,000	–	–	–	145,456	–	1,745,456	31 May, 2005	1 March 2006 to 30 November 2008	0.3804	0.41	N/A	N/A
	–	10,000,000	–	–	(2,100,000)	–	7,900,000	16 January, 2006	17 July 2006 to 15 January 2008	0.2108	0.22	N/A	N/A
	–	15,500,000	–	–	–	–	15,500,000	30 June, 2006	1 April 2007 to 31 December 2009	0.232	0.228	N/A	N/A
	1,600,000	25,500,000	–	–	(1,954,544)	–	25,145,456						
Mr. YAN Yong	1,050,000	–	–	–	95,456	–	1,145,456	31 May, 2005	1 March 2006 to 30 November 2008	0.3804	0.41	N/A	N/A
	–	3,000,000	–	–	(2,000,000)	–	1,000,000	16 January, 2006	17 July 2006 to 15 January 2008	0.2108	0.22	N/A	N/A
	1,050,000	3,000,000	–	–	(1,904,544)	–	2,145,456						
Mr. WANG Kangping	–	–	–	–	–	1,527,274	1,527,274	31 May, 2005	1 March 2006 to 30 November 2008	0.3804	0.41	N/A	N/A
(Note 1)	–	1,500,000	N/A	–	–	–	1,500,000	30 June, 2006	1 April 2007 to 30 June 2008	0.232	0.228	N/A	N/A
	–	1,500,000	–	–	–	1,527,274	3,027,274						
Mr. ZHAO Zhicheng	–	–	–	–	–	654,546	654,546	31 May, 2005	1 March 2006 to 30 November 2008	0.3804	0.41	N/A	N/A
(Note 1)	–	1,000,000	N/A	–	–	–	1,000,000	30 June, 2006	1 April 2007 to 30 June 2008	0.232	0.228	N/A	N/A
	–	1,000,000	–	–	–	654,546	1,654,546						
Mr. LAU Siu Ki	300,000	–	–	–	27,273	–	327,273	31 May, 2005	1 March 2006 to 30 November 2008	0.3804	0.41	N/A	N/A
	–	800,000	–	–	–	–	800,000	16 January, 2006	17 July 2006 to 15 January 2008	0.2108	0.22	N/A	N/A
	300,000	800,000	–	–	27,273	–	1,127,273						
Mr. SHI Cuiming	300,000	–	–	–	27,273	–	327,273	31 May, 2005	1 March 2006 to 30 November 2008	0.3804	0.41	N/A	N/A
	–	800,000	–	–	–	–	800,000	16 January, 2006	17 July 2006 to 15 January 2008	0.2108	0.22	N/A	N/A
	300,000	800,000	–	–	27,273	–	1,127,273						
Mr. WANG Chongju	300,000	–	–	–	27,273	–	327,273	31 May, 2005	1 March 2006 to 30 November 2008	0.3804	0.41	N/A	N/A
	–	800,000	–	–	–	–	800,000	16 January, 2006	17 July 2006 to 15 January 2008	0.2108	0.22	N/A	N/A
	300,000	800,000	–	–	27,273	–	1,127,273						
Mr. DU Xiaopeng	3,200,000	–	–	(2,327,275)	290,912	(1,163,637)	–	31 May, 2005	1 March 2006 to 30 November 2008	0.3804	0.41	N/A	N/A
(Note 2)	–	6,000,000	–	(2,300,000)	(3,700,000)	–	–	16 January, 2006	17 July 2006 to 15 January 2008	0.2108	0.22	N/A	N/A
	3,200,000	6,000,000	–	(4,627,275)	(3,409,088)	(1,163,637)	–						
Dr. GUO Aiping	950,000	–	–	–	86,365	(1,036,365)	–	31 May, 2005	1 March 2006 to 30 November 2008	0.3804	0.41	N/A	N/A
(Note 2)	–	6,000,000	–	–	(2,450,000)	(3,550,000)	–	16 January, 2006	17 July 2006 to 15 January 2008	0.2108	0.22	N/A	N/A
	950,000	6,000,000	–	–	(2,363,635)	(4,586,365)	–						
Mr. WONG Toe	5,000,000	–	–	–	454,550	(5,454,550)	–	31 May, 2005	1 March 2006 to 30 November 2008	0.3804	0.41	N/A	N/A
Yeung *(Note 2)*	–	3,000,000	–	–	2,000,000	(5,000,000)	–	16 January, 2006	17 July 2006 to 15 January 2008	0.2108	0.22	N/A	N/A
	5,000,000	3,000,000	–	–	2,454,550	(10,454,550)	–						

33. SHARE OPTION SCHEME (continued)

	Number of share options											Price of Company's shares	
Name or category of participant	At 1 January 2006	Granted during the year	Exercised during the year	Cancelled/ Lapsed during the year	Adjustment *(Note 4)*	Re-classified	At 31 December 2006	Date of grant	Exercise period (both dates inclusive) *(Notes 5, 6 and 7)*	Exercise price *(Note 4)* (HK$)	Closing price immediately before the Date of Grant (HK$)	Immediately before the exercise date	At exercise date of options
Mr. YUAN Xin	3,000,000	–	–	–	272,730	(3,272,730)	–	31 May, 2005	1 March 2006 to 30 November 2008	0.3804	0.41	N/A	N/A
Cheng *(Note 3)*	–	3,000,000	–	–	(2,000,000)	(1,000,000)	–	16 January, 2006	17 July 2006 to 15 January 2008	0.2108	0.22	N/A	N/A
	3,000,000	3,000,000	–	–	(1,727,270)	(4,272,730)	–						
Sub-Total	20,700,000	59,400,000	–	(4,627,275)	(6,368,162)	(18,295,462)	50,809,101						
Employees	101,625,000	–	–	(67,999,229)	4,923,345	(7,907,276)	30,641,840	31 May, 2005	1 March 2006 to 30 November 2008	0.3804	0.41	N/A	N/A
	–	96,562,672	1,319,386	6,460,613	8,782,328	(20,718,000)	92,406,999	16 January, 2006	17 July 2006 to 15 January 2008	0.2108	0.22	0.2867	0.2871
	–	174,500,000	–	(2,840,000)	–	(4,500,000)	167,160,000	30 June, 2006	1 April 2007 to 31 December 2009	0.232	0.228	N/A	N/A
Sub-Total	101,625,000	271,062,672	1,319,386	(64,378,616)	13,705,673	(33,125,276)	290,208,839						
Those who have	46,770,000	–	–	(13,675,466)	3,450,956	16,652,738	53,198,228	31 May, 2005	1 March 2006 to 30 November 2008	0.3804	0.41	N/A	N/A
contributed or may	–	33,339,145	642,666	(20,912,666)	3,030,855	30,268,000	46,368,000	16 January, 2006	17 July 2006 to 15 January 2008	0.2108	0.22	0.2867	0.2871
contribute to the Group	–	10,050,000	–	1,450,000	–	4,500,000	16,000,000	30 June, 2006	1 April 2007 to 31 December 2009	0.232	0.228	N/A	N/A
Sub-Total	46,770,000	43,389,145	642,666	(33,138,132)	6,481,811	51,420,738	115,566,228						
Total	169,095,000	373,851,817	1,962,052	(102,144,023)	13,819,322	–	456,584,168						

Notes:

1. Mr. Wang Kangping and Dr. Zhao Zhicheng were appointed as non-executive directors of the Company on 8 June 2006 and their share options under the share option scheme were re-classified under "Directors".

2. Mr. Du Xiaopeng, Dr. Guo Aiping and Mr. Wong Toe Yeung retired as executive directors of the Company on 8 June 2006. The share options held by Mr. Du Xiaopeng and Dr. Guo Aiping under the share option scheme were re-classified under "Employees" and the share options held by Mr. Wong Toe Yeung were re-classified under "Those who have contributed or may contribute to the Group". As a result of Mr. Du Xiaopeng's retirement at the conclusion of the Company's annual general meeting on 8 June 2006, a total of 4,627,275 options held by Mr. Du were lapsed during the year under review.

3. Mr. Yuan Xin Cheng resigned as executive director on 8 June 2006 and his share options under the share option scheme were re-classified under "Those who have contributed or may contribute to the Group".

4. As a result of the completion of the open offer of the Company on 27 February 2006, the exercise prices for shares under each outstanding share option granted on 31 May 2005 and 16 January 2006 were adjusted in accordance with the terms of the Share Option Scheme to HK$0.3804 and HK$0.2108 respectively.

33. SHARE OPTION SCHEME (continued)

Notes: (continued)

5. The share options granted on 31 May 2005 are exercisable from the commencement of the exercise periods until the expiry of the share options which is on 30 November 2008. One-third of such share options are exercisable after the expiry of 9 months from the date of grant, a further one-third is exercisable after the expiry of 18 months from the date of grant, and the remaining one-third is exercisable after the expiry of 27 months from the date of grant.

6. The share options granted on 16 January 2006 are exercisable from the commencement of the exercise period until the expiry of the share options which is on 15 January 2008 (save for the share options granted to the French employees which will expire on 15 April 2010). One-third of such share options are exercisable after the expiry of 6 months from the date of grant, a further one-third is exercisable after the expiry of 12 months from the date of grant, and the remaining one-third is exercisable after the expiry of 18 months from the date of grant.

7. The share options granted on 30 June 2006 are exercisable from the commencement of the exercise period until the expiry of the share options which is on 31 December 2009 (save for the share options granted to the French employees which will expire on 30 September 2010 and the share options granted to certain grantees as mentioned below). Save for the share options granted to certain grantees including Mr. Wang Kangping and Dr. Zhao Zhicheng, which are all exercisable from 1 April 2007 to 30 June 2008, the share options have three exercisable periods: one-third of such share options are exercisable after the expiry of 9 months from the date of grant, a further one-third is exercisable after the expiry of 18 months from the date of grant, and the remaining one-third is exercisable after the expiry of 27 months from the date of grant.

8. The fair value of the options granted in the current year totaled approximately HK$20,811,000. The following assumptions were used to derive the fair value, using the Binomial Model:

Options granted on 16 January 2006

		At Grant Date	Modification on 30 June 2006	
(i)	Exercise Period	17 July 2006 to 15 January 2008	17 July 2006 to 15 January 2008	17 July 2006 to 15 April 2010
(ii)	Expected volatility	50% per annum	50% per annum	55% per annum
(iii)	Estimated average life	1.72 years	1.25 years	2.46 years
(iv)	Average risk-free interest rate	3.66% per annum	4.48% per annum	4.56% per annum
(v)	Early exercise assumption	When the share price is at least 175% of the exercise price	When the share price is at least 175% of the exercise price	When the share price is at least 210% of the exercise price
(vi)	Expected dividend yield	1% per annum		
(vii)	Estimated rate of leaving service	20% per annum for the first year after the Grant Date and a rate of 15% per annum thereafter		

33. SHARE OPTION SCHEME (continued)

Notes: (continued)

Options granted on 30 June 2006

		At Grant Date		
(i)	Exercise Period	1 April 2007 to 31 December 2009	1 April 2007 to 30 September 2010	1 April 2007 to 30 June 2008
(ii)	Expected volatility	55% per annum	55% per annum	50% per annum
(iii)	Estimated average life	2.87 years	3.22 years	1.64 years
(iv)	Average risk-free interest rate	4.59% per annum	4.61% per annum	4.50% per annum
(v)	Early exercise assumption	When the share price is at least 210% of the exercise price	When the share price is at least 210% of the exercise price	When the share price is at least 175% of the exercise price
(vi)	Expected dividend yield		1% per annum	
(vii)	Estimated rate of leaving service		20% per annum for the first year after the Grant Date and a rate of 15% per annum thereafter	

The volatility rate of the share price of the Company was determined with reference to the movement of the Company's and its comparators' share prices.

Watson Wyatt Hong Kong Limited has been appointed to perform the valuation on the 3 batches of share options granted on 31 May 2005, 16 January 2006 and 30 June 2006.

34. RESERVES

(a) Group

The amounts of the Group's reserves and the movements therein for the current and prior years are presented in the consolidated statement of changes in equity on page 52 of the financial statements.

The Group's capital reserve arose mainly from the capital injection.

The Group's contributed surplus represents the difference between the nominal value of the shares and the share premium account of the subsidiaries acquired pursuant to the Group reorganisation prior to the listing of the Company's shares, over the nominal value of the Company's shares issued in exchange therefore.

Pursuant to the relevant laws and regulations in the PRC, a portion of the profits of the Group's subsidiaries established in the PRC should be transferred to the statutory reserves which are restricted as to use.

34. RESERVES (continued)

(b) Company

	Contributed surplus HK$'000	Share premium account HK$'000	Share option reserve HK$'000	Equity Component of Convertible notes HK$'000	Accumulated losses HK$'000	Total HK$'000
Balance at 1 January 2005	669,907	1,093,475	–	–	(62,934)	1,700,448
Issue of new shares for acquisition of 45% shareholding interest of T&A from Alcatel Participants	–	47,360	–	–	–	47,360
Equity settled share options arrangements	–	–	7,737	–	–	7,737
Issue of convertible note	–	–		19,430	–	19,430
Loss for the year	–				(1,665,843)	(1,665,843)
At 31 December 2005	669,907	1,140,835	7,737	19,430	(1,728,777)	109,132

	Contributed surplus HK$'000	Share premium account HK$'000	Share option reserve HK$'000	Equity Component of Convertible notes HK$'000	Accumulated losses HK$'000	Exchange fluctuation reserve HK$'000	Total HK$'000
Balance at 1 January 2006	669,907	1,140,835	7,737	19,430	(1,728,777)	–	109,132
Issue of shares and exercise of share option	–	297,219	(114)	–	–	–	297,105
Share issue expenses	–	(6,988)	–	–	–	–	(6,988)
Equity-settled share option arrangement	–	–	15,997	–	–	–	15,997
Exchange realignment and total income and losses for the year recognised directly in equity	–	–	–	–	–	(110)	(110)
Loss for the year	–	–	–	–	(402,254)	–	(402,254)
At 31 December 2006	669,907	1,431,066	23,620	19,430	(2,131,031)	(110)	12,882

The Company's contributed surplus represents the difference between the nominal value of the shares and the share premium account of the subsidiaries acquired pursuant to the Company reorganisation prior to the listing of the Company's shares, over the nominal value of the Company's shares issued in exchange therefore.

35. CONTINGENT LIABILITIES

(a) One of the Group's subsidiaries, T&A Mobile Phones Suzhou Limited ("T&A Suzhou") was involved in a patent infringement litigation brought by Hubin, Huxuanhua and Dalian Hanpu Applied Technology Co., Ltd. (the "plaintiff") in March 2001. In May 2002, the PRC trial court rendered civil judgement in favour of T&A Suzhou with no damages or expenses to be borne by them. In the same month, the plaintiff appealed to the High Court and up to date, the appellate proceeding has been resolved.

According to the legal opinion from the Group's PRC lawyer, it is very likely for the appellate court to render judgement in favour of T&A Suzhou again. Accordingly, no provision was made for such litigation in the financial statements.

(b) In October 2006, two subsidiaries of the Group, T&A Mobile Phones Europe SAS and T&A Mobile Phones International Limited, were involved in an European claim for disputed amount for patent royalty payment bought by a GSM essential patents holder (the "plaintiff"). The case is proceeding in the European courts as of the date of this report. No judgment or decision has been made in favor or against either party on the merit of the case.

In preparation for the potential claims against T&A Mobile Phones Europe SAS and T&A Mobile Phones International Limited, the Group has made provisions sufficiently to meet the demands pleaded by the plaintiff. The parties have engaged in settlement discussions and continue to meet to settle the disputed royalty amounts amicably.

The directors have estimated that the maximum financial impact to the Group relating to the above claim and have accrued in the Group's financial statements for the year ended 31 December 2006 to provide for the claims and proceedings. In the opinion of the directors, based on legal advice from the Company's lawyers engaged in this action, any resulting liabilities to the subsidiary of the Group regarding the aforesaid claims would not have material or adverse impact on the Group's financial position given the current provisions provided to date. Therefore, no further provision in respect of royalty payment was considered necessary to be made in the financial statements.

36. OPERATING LEASE ARRANGEMENTS

The Group leases certain of its office premises, warehouses and staff dormitories under operating lease arrangements. Leases for these properties are negotiated for terms ranging from one to three years.

At 31 December 2006, the Group had total future minimum lease payments under non-cancellable operating leases falling due as follows:

	Group		Company	
	2006	2005	**2006**	2005
	HK$'000	HK$'000	**HK$'000**	HK$'000
Within one year	**10,124**	22,723	**–**	2,546
In the second to fifth years, inclusive	**16,665**	21,984	**–**	3,458
Over five years	**4,217**	–	**–**	–
	31,006	44,707	**–**	6,004

37. CAPITAL COMMITMENTS

As at the balance sheet date, the Group had no capital commitments/contracted, but not provided for (31 December 2005: HK$18,111,000).

38. RELATED PARTIES TRANSACTIONS

(a) Transaction with related parties

	2006 HK$'000	2005 HK$'000
Transaction with ultimate controlling shareholder		
Brand name management fee/TCL Brand Common Fund	**4,744**	10,155
Interest expenses	**11,460**	10,544
Issuance of convertible note	**–**	185,100
Interest on convertible note	**5,553**	2,373
Short-term loan obtained	**2,562,941**	3,514,194
Transactions with subsidiaries of ultimate controlling shareholder		
Purchases of raw materials*	**1,447,281**	1,456,630
Fund advanced	**2,948**	38,425
Master manufacturing service	**–**	3,463
Rental income	**47**	–
Rental charges	**2,832**	2,380
Sales of finished goods	**2,391**	1,947
Sales of property, plant and equipment	**188**	–
Transactions with a company in which a director of the Company is a shareholder		
Consultancy fee	**–**	975
Transactions with subsidiaries of the Group's minority shareholder		
Administrative and management services obtained	**–**	159,125
Sales support services obtained	**–**	37,573
Transactions with an associate or its subsidiaries		
Technology and software fee	**49,389**	–
Fund advanced	**5,708**	–
Recharge expenses	**22,632**	–
Sales of property, plant and equipment	**45,312**	–
Purchase of property, plant and equipment	**112**	–

* The purchase of raw materials with subsidiaries of ultimate controlling shareholder were made according to prices mutually agreed between two parties.

38. RELATED PARTIES TRANSACTONS (continued)

(b) Other transactions with related parties

On 9 March 2006, TCL Corporation ("TCL Corp") (the ultimate controlling shareholder of the Company) entered into the Investment Agreement with TCL Mobile Communication (Hohhot) Co., Ltd. ("Mobile Hohhot") (an indirect wholly-owned subsidiary of the Company) in relation to establishment of the Finance Company. Pursuant to the Investment Agreement, Mobile Hohhot contributed RMB 20 million as capital contribution to the Finance Company, representing 4% of the registered capital of the Finance Company. All necessary approvals for the setting up of the Finance Company have been obtained and the Finance Company was established on 17 October 2006. Further details of this transaction were set out in the Company's announcement dated 27 October 2006.

(c) Outstanding balance with related parties

Particulars of the amounts due from related companies disclosed pursuant to Section 161B of the Companies Ordinance are as follows:

Group

	Due from related companies		Due to related companies	
	2006	2005	**2006**	2005
	HK$'000	HK$'000	**HK$'000**	HK$'000
Ultimate controlling shareholder	**–**	–	**25,483**	83,893
Subsidiaries of ultimate controlling shareholder	**184,976**	347,750	**338,049**	487,493
An associate or its subsidiaries	**44,383**	–	**81,377**	–
	229,359	347,750	**444,909**	571,386

Company

	Due to related companies	
	2006	2005
	HK$'000	HK$'000
Ultimate controlling shareholder	**2,773**	2,347
Subsidiaries of ultimate controlling shareholder	**–**	773
	2,773	3,120

The amounts due are mainly trading balances, and are unsecured, interest free and have no fixed terms of repayment.

Particulars of the maximum outstanding balance of amounts due from related companies are as follows:

	Year ended 31 December	
	2006	2005
	HK$'000	HK$'000
TCL Integrated Marketing Inc.*	**–**	116
TCL Communication Equipment (Huizhou) Co., Ltd*	**2,628**	4,513
TCL Corporation*	**379,798**	345,658
JRD Communication Inc.	**5,652**	–

* The balances are mainly trading balances, and are unsecured, interest free and have no fixed terms of repayment.

38. RELATED PARTIES TRANSACTONS (continued)

(d) Compensation of key management personnel of the Group

	2006 HK$'000	2005 HK$'000
Short term employee benefits	**13,553**	12,709
Post-employment benefits	**61**	498
Share-based payment	**5,266**	3,045
Total compensation paid to key management personnel	**18,880**	16,252

Further details of directors' emoluments are included in note 11 to the financial statements.

39. FINANCIAL RISKS MANAGEMENT OBJECTIVES AND POLICIES

The main risks arising from the Group's financial instruments are interest rate risk, foreign currency risk, credit risk and liquidity risk. Generally, the Group introduces conservative strategies on its risk management. The Group also enters into forward currency contracts so as to manage the currency risks arising from the Group's operations and its sources of finance. The Group does not hold or issue derivative financial instruments for trading purposes. The board of directors reviews and agrees policies for managing each of these risks and they are summarised as follows:

Interest rate risk

At 31 December 2006, the bank loans of the Group and the Company are a combination of fixed and floating rate debts. The Group and the Company have no significant concentration of interest rate risk.

Foreign currency risk

The Group has transactional currency exposures. Such exposures arise from sales or purchases by operating units in currencies other than the units' functional currency, where the revenue is predominately in Euro, USD and RMB.

It is the Group's policy to negotiate the terms of the hedge derivatives to match the terms of the hedged item to maximise hedge effectiveness.

Credit risk

With respect to credit risk arising from the other financial assets of the Group, which comprise cash and cash equivalents, and trade receivables, the Group's exposure to credit risk arises from default of the counterparty, with a maximum exposure equal to the carrying amount of these instruments.

In order to minimise the credit risk, the management of the Group has delegated a team responsible for determination of credit limits, credit approvals and other monitoring procedures to ensure that follow-up action is taken to recover overdue debts. In addition, the Group reviews regularly the recoverable amount of each individual trade receivables to ensure that adequate impairment losses are made for irrecoverable amounts. Besides, the Group also utilises non-resoures factoring facilities and credit insurance to minimise the credit risk. In this regard, the directors of the Company consider that the Group's credit risk is minimal.

Liquidity risk

The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of bank loans and other interest bearing loans.

40. POST BALANCE SHEET EVENTS

(a) On 18 April 2007, (1) the Company and 5 subscribers ("Subscribers"), who are all independent third parties, entered into a Subscription Agreement pursuant to which the Company has agreed to issue and allot and the Subscribers have agreed to subscribe for 1,215,430,000 Subscription Shares in aggregate at a total consideration of HK$268,093,472, and (2) the Company and the Vendors entered into a Share Purchase Agreement pursuant to which the existing shareholders of JRDC other than the Company (the "vendors") have agreed to sell and the Company has agreed to purchase an aggregate of 147,500,000 JRDC Shares at total consideration of US$39,313,017 (equivalent to approximately HK$306,641,533 (the "Acquisition")).

In order to well position the Company to face keen competition worldwide, the directors consider the business model of outsourcing product development activities to other entities such as JRDC may no longer be beneficial to the Group. Though after the completion of the Acquisition, the Group will have to take over the entire operating costs of JRD Group, in view of the royalty saving and the ability of the Group to gain full control of JRDC, the Board considers that the Acquisition is beneficial to the Group as it can significantly enhance the Group's capability in research and development of mobile technology which will better equip the Group to face the operating environment of the handset industry which remains tough both globally and domestically. For further details of the Acquisition and subscription of new shares, please refer to the announcement of the Company dated 18 April 2007.

(b) On 19 March 2007, the Company entered into a subscription agreement (the "Subscription Agreement") with DBS Bank Ltd. ("DBS"), pursuant to which DBS agreed to subscribe for the Convertible Bonds at an aggregate principal amount of US$27 million (the "Firm Bonds"). The Company has also granted to DBS an option to require the Company to issue up to a further US$18 million in principal amount of the Convertible Bonds (the "Optional Bonds").

The net proceeds from the issue of the Convertible Bonds (excluding the issue of the Optional Bonds), amounting to approximately Hk$204.6 million will be used for general corporate working capital purposes and refinancing of some existing indebtedness.

The option can be exercised by DBS in whole or in part, at any time within a period of 90 calendar days after the increase of sufficient authorised share capital of the Company for issuing of new shares of the Company upon conversion of the Optional Bonds has been approved by Shareholders. An extraordinary general meeting has been held and such approval was obtained on 20 April 2007.

The conversion price per share was initially set at HK$0.3275 subject to adjustment, which represents a premium of approximately 26.2% of the average closing price per share as quoted on the SEHK of HK$0.2595 per Share for the ten consecutive trading days up to and including the last trading day. The maturity date is 2 April 2012 and the yield to maturity is 5.709%.

For further details of issuance of Bonds, please refer to the announcement of the Company dated 20 March 2007.

41. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorized for issue by the board of directors on 27 April 2007.