LifeTec

# 生命科技集團有限公司
# LifeTec Group Limited

(Stock Code: 1180)

# annual report 2005

# CONTENTS

# CORPORATE INFORMATION

## REGISTERED OFFICE

Clarendon House
2 Church Street
Hamilton HM11
Bermuda

## PRINCIPAL REGISTRAR

Butterfield Corporate Services Limited
Rosebank Centre
11 Bermudiana Road
Pembroke
Bermuda

## DIRECTORS

Mr. Jay CHUN *(Chairman and Managing Director)*
Mr. SHAN Shiyong, alias, Mr. SIN Sai Yung
Dr. MA Xianming, alias, Dr. MA Yin Ming
Mr. Frank HU*
Mr. WANG Faqi*
Ms. MA Shiwei*

* *Independent Non-executive Directors*

## COMPANY SECRETARY

Mr. Poon Yick Pang Philip, *CFA, CPA (Aust.)*

## SOLICITORS

Vincent T.K. Cheung, Yap & Co.

## AUDITORS

RSM Nelson Wheeler
*Certified Public Accountants*
7th Floor
Allied Kajima Building
138 Gloucester Road
Hong Kong

## PRINCIPAL OFFICE

Room 907-908, 9/F.
Man Yee Building
68 Des Voeux Road Central
Hong Kong

## PRINCIPAL BANKERS

Bank of China (Hong Kong) Limited
The Hongkong and Shanghai Banking Corporation Limited

## HONG KONG SHARE REGISTRAR

Secretaries Limited
26th Floor
Tesbury Centre
28 Queen's Road East
Wanchai
Hong Kong

# Chairman's Statement

The world has been under imminent threat of avian flu outbreak, the Group has prioritized research efforts in identifying and developing new drugs for the prevention and cure of infectious respiratory diseases.

# CHAIRMAN'S STATEMENT

On behalf of the Board of Directors, I am pleased to present the annual report and audited financial statements of the Company and its subsidiaries (collectively the "Group") for the year ended 31 December 2005.

## BUSINESS REVIEW

The Group's core biopharmaceutical business under LifeTec Pharmaceutical Limited ("LifeTec Pharmaceutical") continued to report strong growth. Sales of LifeTec Pharmaceutical in China increased by 31.9% from about HK$63,476,000 in 2004 to a record high of about HK$83,730,000 in 2005. The rise in pharmaceutical sales was the results of successful implementation of our marketing initiatives. Research and development for new drugs have been making good progress. As the world has been under imminent threat of avian flu outbreak, the Group has prioritized research efforts in identifying and developing new drugs for the prevention and cure of infectious respiratory diseases.

Following the Group's corporate reorganization at the end of 2004, LT Capital Limited ("LT Capital") set up a wholly owned subsidiary in Macau to provide support to the development of live baccarat gaming system. Patent application was filed in the United States and Macau for the novel electronic gaming system. The system combines traditional baccarat card dealing by casino staff and digital network of touch screen betting terminals. The system is designed for mass gaming hall. It has automatic lighting device to guide card dealing process in baccarat games and a computerized payout program to shorten the time for each baccarat game.

### Turnover and Profit

The Group reported a turnover of HK$85,478,000 for the year, representing an increase of 33.2% as compared to HK$64,179,000 for the previous year. Overall gross profit margin for the year dropped from 80% to 30% whereas operating loss of HK$57,991,000 for 2004 narrowed to operating loss of about HK$23,095,000 for the year. The Group reported loss of HK$24,095,000 or 0.9 Hong Kong cents per share in the year compared to a net loss of HK$60,992,000 or 2.4 Hong Kong cents per share in the previous year.

The loss has been mainly attributed to increase in sales discounts in response to the intense market competition. Gross margin would inevitably under pressure as the Group strove for a bigger market presence. Despite the highly competitive market environment, the Group successfully expanded its biopharmaceutical sales in 2005. Our sales operation has been progressing towards economy of scale.

The loss before taxation and minority interests reduced from about HK$58,280,000 in the previous year to about HK$23,203,000 for the year. Finance costs of the Group for the period significantly decreased by 62.6% from about HK$289,000 to HK$108,000. The reduction in finance costs was due to the repayment of bank loans in the year.

### Marketing, Sales and Distribution

The Group continued to strengthen the market position of Wei Jia in China through promotion to the medical community. Our medical representatives attended the National Hepatology Congress held in Beijing and promoted the outstanding treatment results of Wei Jia to top liver diseases experts in China. The Group's promotional efforts resulted in 31 articles published in various medical journals in China on Wei Jia.

# CHAIRMAN'S STATEMENT

The marketing campaign of Wei Jia went well outside China. Two manuscripts on the product were accepted for publication in the prestigious World Journal of Gastroenterology which is the official publication of the Asian Pacific Association for the Study of the Liver and the Asian Pacific Association of Gastroenterology. The journal is also an affiliated publication of the Association for the Study of the Liver, Bangladesh, Gastroenterological Society of Australia, the Hong Kong Society of Gastroenterology and the Thailand Gastroenterology Association. The publication is a strong affirmation of research findings of Wei Jia by top international scientists as only first class research on liver cancer and viral hepatitis is admitted for publication in the journal.

In addition, our lead research scientist on Wei Jia was invited to speak at the Asian Pacific Digestive Week Scientific Conference in Seoul, Korea, and The 3rd Congress of International Drug Discovery Science and Technology in Shanghai. The increased awareness of the superior therapeutic value of Wei Jia amongst world's liver diseases experts opens the great gateway for international sales of the product. Last year, we received trade enquiries from Russia, Israel and Africa for the export of Wei Jia to those countries.

Our agency network expanded according to schedule. While strengthening the support to various hospitals throughout over China, we brought in new distributors to boost the sales. The collaboration with key drug distribution groups in China extended the reach of Group's biopharmaceutical products to small to medium sized hospitals and clinics. Our marketing strategy proved to be a success and resulted in the strong rise in our biopharmaceutical sales. The Group would be in a more favourable position in negotiating sales prices with distributors and agents as our market presence strengthens.

## Research and Development

### *Fibrocorin*

Fibrocorin is a recombinant fusion protein and a potential new drug candidate for anti-cancer and anti-fibrosis applications. It was invented by the Group together with the research team of the City University of Hong Kong. Fibrocorin is a genetically engineered protein comprising an active component to alleviate fibrosis and a human immunoglobulin Fc region to extend degradation rate. This novel recombinant protein has a more sustainable and profound treatment effect. Patent application has been filed by the Group for Fibrocorin in the United States. Pre-clinical trials for Fibrocorin are expected to be completed in 2008.

### *Recombinant Human Augmenter for Liver Regeneration ("rhALR")*

rhALR is a revolutionary compound for the gene therapy of various kinds of liver diseases. rhALR's therapeutic value has been demonstrated in animal tests. The China patent for the specific production techniques for rhALR was granted in late 2005. The Group is conducting laboratory tests and preparing application documents for clinical trials in China. In addition to the on-going development projects, the Group launched advanced research work on rhALR with the research teams at the Shanghai Fudan University and the Shanghai Changzheng Hospital.

# CHAIRMAN'S STATEMENT

### *Other Projects in Pipeline*

Currently there are a number of generic drugs under development, amongst them are: Pazufloxazin for the treatment of bronchitis, complicated urinary tract infections and gonorrhea; Clindamycin Hydrochloride Injection for the treatment of bacterial infections of the respiratory tract; Compound Dextromethorphan Hydrobromide Buccal Tablets for the treatment of common cold, respiratory tract infections and bronchitis; Bromhexine Hydrochloride Injection for the treatment of respiratory disorders; Zinc Gluconate Nasal Spray Gel for the treatment of influenza. The commercial production of Clindamycin Hydrochloride Injection and Bromhexine Hydrochloride Injection is expected to take place before the end of 2006.

## Prospects

LifeTec Pharmaceutical and LT Capital are two key intermediate holding companies which operate the Group's biopharmaceutical and non-biopharmaceutical businesses respectively. Although these two companies will expand at different pace, their income streams would complement each other.

The Group will dedicate resources to extend the reach of LifeTec Pharmaceutical to different parts of China. We would continue to enhance our existing agency network to drive the sales growth. As the operation of LifeTec Pharmaceutical reaches the critical scale, our biopharmaceutical business operating margin will largely enhanced.

The world has never been free from threat of epidemic and recently the possibility of major outbreak is more alarming. Therefore, we will direct more research resources to develop new cures for respiratory or viral related infectious diseases. Our current focus would be on those generic drugs which can be commercialized and launched to the market in a much shorter timeframe. On the other hand, we will continue our research and development on major genetic drug candidates like rhALR and Fibrocorin which will yield promising return in the medium to long term.

Management expect the new projects of LT Capital will achieve significant breakthroughs in the coming year. Several patent applications for our technological know-how and proprietary designs have been filed in the United States and China and the related patents will be granted in due course. Our live baccarat gaming system has been making sound progress and will soon be installed in Macau casino. This flagship project of LT Capital will be an excellent example of how our management transform innovation and sound business ideas to a viable business.

## Liquidity and Financial Resources

As at the balance sheet date, the Group's aggregate bank borrowings stood at HK$171,000 of which HK$135,000 was payable within 12 months, HK$36,000 was payable in the second year. Current liabilities of the Group increased from HK$21,180,000 to HK$24,964,000, representing a rise of 17.9%. The Group's net current assets decreased from HK$111,286,000 to HK$84,235,000 as at the balance sheet date. The Group's liabilities at the balance sheet date totalled HK$34,654,000. The percentage of total liabilities to total assets as at 31 December 2005 stood at 13.5% which is slightly higher than the corresponding figure of 11.0% as at 31 December 2004.

# CHAIRMAN'S STATEMENT

As at 31 December 2005, the cash on hand at the current date are sufficient for financing ongoing activities of the Group.

The Group's operations are primarily based in China and the income derived and expenses incurred are denominated in Reminbi. There were no export sales in the year. On the other hand, the expenses of the headquarters and bank borrowings are denominated in Hong Kong dollars and are financed by Hong Kong dollar capital. Due to the relatively matched position in both Hong Kong and China and the stability of the exchange rates between Reminbi and Hong Kong dollars, the directors consider that specific hedges for currency fluctuation are not necessary.

## PLEDGE OF ASSETS

As at 31 December 2005, fixed assets with a net book value of approximately HK$1,044,000 (2004: HK$1,070,000) were pledged for total borrowing of approximately HK$171,000 (2004: HK$2,895,000).

## ORGANIZATION AND STAFF

The Group has about 70 staff in total as at the date of this report. Majority of the staff are sale and marketing executives located in China. The Group is actively seeking talent to join the sales and marketing team as well as research and development team in order to cope with the fast growing operations.

The terms of employment of the staff, executives and directors conform to normal commercial practice. Share option benefits are granted to and included in the terms of selected senior executives of the Company.

## APPRECIATION

The Group has made significant advancement in 2005 and set a very solid foundation for the strong, sustainable growth for the years to come. Such accomplishment would not be possible without the support from different parties. On behalf of the board of directors of the Company, I would like to thank our shareholders, bankers, professional parties and customers for their continuous support. I would also like to thank our executives and staff for their dedication and professionalism.

By Order of the Board
**Jay Chun**
*Chairman*

Hong Kong, 27 April 2006

# PROFILE OF DIRECTORS AND SENIOR MANAGEMENT

## EXECUTIVE DIRECTORS

**Mr. Jay Chun**, aged 41, Chairman and Managing Director of the Company, is a talented entrepreneur and manager. He has a solid background in information technology and marketing and over 14 years of management and investment experience. He holds a bachelor degree in computer science from the Shanghai University of Science and Technology. Mr. Chun joined the Group and was appointed as Managing Director of the Company in January 1999 and subsequently appointed as Chairman of the Board in July 2002.

**Mr. Shan Shiyong**, alias, Mr. Sin Sai Yung, aged 42, Executive Director and former Chairman of the Company, is an entrepreneur with strong business vision. After completing his studies in economics at the University of Agriculture, Shandong, he started his own business in manufacturing and export. Mr. Shan subsequently diversified to trading, property development and venture capital investment in China. He has over 17 years of dedicated business, investment and management experience at the owner level. Mr. Shan joined the Group and was appointed as an Executive Director in October 1998. He became Chairman of the Company in May 1999 and resigned from Chairmanship in July 2002.

**Dr. Ma Xianming**, alias, Dr. Ma Yin Ming, aged 39, holds a doctoral degree in accounting as well as a bachelor and a master degree in economics from the Central South University. He is an accounting and financial expert and has been appointed as a member of the Auditing Standards Drafting Committee of the China Institute of Certified Public Accountants and as the leader of the Chinese Expert Advisory Group on accounting issues in connection with Asian Development Bank sponsored projects in China. He has also held senior financial positions in the commercial field and over 16 years of management and investment experience. He joined the Group as an Independent Non-executive Director in September 2001 and was re-designated as an Executive Director in August 2003.

## INDEPENDENT NON-EXECUTIVE DIRECTORS

**Mr. Frank Hu**, aged 43, is a seasoned banker and businessman with over 17 years of experience. He holds a bachelor degree in politics from New York University and is currently the chief executive officer of a major private group in Hong Kong. He joined the Group in July 1999.

**Mr. Wang Faqi**, aged 49, has over 26 years of extensive experience in the banking and finance sector. Since 1975, Mr. Wang has been holding various positions in the China Construction Bank (the "Bank"). He had been the General Manager of the International Business Department and Head of Investment Banking of the Bank's Yantai Branch, as well as the Head of the Bank's Yantai Mitsubishi Cement Specific Branch. Mr. Wang was awarded the Bachelor Degree in Economics from the Xiamen University. He also holds the professional qualification of Senior Economist accredited by the Bank's Senior Professional and Technical Positions Supervisory Committee. He joined the Group in August 2003.

**Ms. Ma Shiwei**, aged 49, holds a master degree in business administration from Touro University International. She has over 17 years of experience in management of international trading. Ms. Ma is the General Manager of China Worldbest Group (Hong Kong) Co., Ltd., which is a subsidiary of one of the largest pharmaceutical groups in China. She joined the Group in September 2004.

# PROFILE OF DIRECTORS AND SENIOR MANAGEMENT

## SENIOR MANAGEMENT

**Mr. Zhu Weixiong**, aged 50, is the Group's Associate Director of Sales and Marketing. Mr. Zhu has vast experience in the pharmaceutical industry. Having held senior executive positions in first-class establishments in China, Mr. Zhu has accumulated over 23 years' solid experience in the sales and marketing of pharmaceutical products. Before joining the Group, he was senior management of a number of sizeable pharmaceutical companies in China. Mr. Zhu joined the Group in June 2004.

**Mr. Poon Yick Pang, Philip**, aged 36, is the Group's Senior Vice President – Corporate Investment. He joined the Group in May 2002 and was appointed as Company Secretary of the Company in August 2003. Mr. Poon devoted his last eleven years to major listed companies, prominent broking and private equity firms in Hong Kong. Mr. Poon holds a bachelor of commerce degree from the University of New South Wales and is also a holder of Chartered Financial Analyst charter awarded by the CFA Institute, a Certified Practising Accountant registered with the CPA Australia and a fellow of the Hong Kong Institute of Certified Public Accountants.

**Dr. Chan Pak Li, Bernard**, aged 29, is the Group's Director of Research and Development. Dr. Chan holds a Ph.D. degree in biomedical engineering from Duke University, USA, where he graduated at the top of his class. Dr. Chan has extensive experience in the research of biopharmaceutical drugs, recombinant proteins and biomaterial. Before joining the Group, he was an assistant research professor at Duke University and also served as a senior research scientist at Affinergy, Inc., a company specializing in site-specific biological delivery of drugs, peptides, proteins and cells. Dr. Chan has published numerous peer reviewed scientific articles and conference abstracts, and has given multiple podium presentations at international scientific meetings. Dr. Chan joined the Group in November 2004.

# DIRECTORS' REPORT

The directors present their annual report and the audited financial statements of the Company and its subsidiaries (hereinafter collectively referred to as the "Group") for the year ended 31 December 2005.

## PRINCIPAL ACTIVITIES

The Company is an investment holding company. Its subsidiaries are principally engaged in the research, development, and sale of biopharmaceutical products.

## RESULTS

The results of the Group for the year ended 31 December 2005 are set out in the consolidated income statement on page 25.

## PROPERTY, PLANT AND EQUIPMENT

Details of the movements in property, plant and equipment of the Group during the year are set out in note 17 to the financial statements.

## INVESTMENT PROPERTIES

The investment properties of the Group were re-valued on an open market value basis as at 31 December 2005 as set out in note 18 to the financial statements. There was no surplus or deficit arising on the revaluation as at 31 December 2005.

## SHARE CAPITAL

Details of changes in the Company's share capital during the year are set out in note 31 to the financial statements.

## RESERVES

Movements in the reserves of the Group and the Company during the year are set out in the Consolidated Statement of Changes in Equity on page 29 and in note 34 to the financial statements.

There was no reserve available for distribution to shareholders as at 31 December 2005.

## CHANGE IN AUDITORS

Messrs. Deloitte Touche Tohmatsu retired in the annual general meeting held on 18 July 2005 and Messrs. RSM Nelson Wheeler were appointed in their place.

# DIRECTORS' REPORT

## DIRECTORS AND SERVICE CONTRACTS

The directors of the Company during the year and up to the date of this report were:

### Executive directors:

Mr. Jay Chun, *Chairman and Managing Director* (alternate director to Mr. Shan Shiyong)
Mr. Shan Shiyong (alias, Mr. Sin Sai Yung)
Dr. Ma Xianming (alias, Dr. Ma Yin Ming)

### Independent non-executive directors:

Mr. Frank Hu
Mr. Wang Faqi
Ms. Ma Shiwei

The biographical details of the directors of the Company and senior management of the Group are set out on pages 8 to 10.

In accordance with the Company's Bye-laws, Mr. Frank Hu shall retire and, being eligible, offer himself for re-election at the forthcoming annual general meeting.

Mr. Frank Hu does not have a service contract with the Company or any of its subsidiaries which is not determinable by the Group within one year without payment of compensation, other than statutory compensation.

The terms of office for each independent non-executive director (except Ms. Ma Shiwei) is the period up to his retirement by rotation in accordance with the Company's Bye-laws. The term of office for Ms. Ma Shiwei is a fixed term of two years commencing from 28 September 2004.

The Company has received from each of its independent non-executive directors an annual confirmation of his/her independence pursuant to rule 3.13 of the Rules Governing the Listing of Securities of The Stock Exchange of Hong Kong Limited (the "Listing Rules") and the Company considered them to be independent as at the date of this report.

## DIRECTORS' INTERESTS IN CONTRACT OF SIGNIFICANCE

No contracts of significance to which the Company or any of its subsidiaries was a party and in which a director of the Company had a material interest, whether directly and indirectly, subsisted at the end of the year or at any time during the year.

# DIRECTORS' REPORT

## DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS IN SECURITIES

As at 31 December 2005, the interests and short positions of the directors and the chief executive of the Company in the shares, underlying shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) which were required to be notified to the Company pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which any such director or chief executive was taken or deemed to have under such provisions of the SFO) or which were required, pursuant to section 352 of the SFO, to be entered in the register referred to therein or which were required to be notified to the Company and The Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code"), were as follows:

| Name of Directors | Name of company/ associated corporation | Capacity/ Nature of interests | Interests in shares (other than pursuant to equity derivatives)[1] | Interests in underlying shares pursuant to equity derivatives[1] | Total interests in shares/ underlying shares | Approximate aggregate percentage of interests |
|---|---|---|---|---|---|---|
| Mr. Jay Chun | The Company | Beneficial owner | 68,568,000 | 2,500,000 | 398,558,000 | 14.42% |
| | The Company | Interest of controlled corporation | 327,490,000[2] | – | | |
| Mr. Shan Shiyong, alias, Mr. Sin Sai Yung | The Company | Interest of controlled corporation | 353,190,000[3] | – | 353,190,000 | 12.78% |
| Dr. Ma Xianming, alias, Dr. Ma Yin Ming | The Company | Beneficial owner | – | 1,000,000 | 1,000,000 | 0.04% |

Notes:

(1) All interests in shares stated above represent long positions.

(2) These shares were held by August Profit Investments Limited, a company which is wholly owned by Mr. Jay Chun.

(3) These shares were held by Best Top Offshore Limited, a company which is wholly owned by Mr. Shan Shiyong, alias, Mr. Sin Sai Yung.

Save as disclosed above, none of the directors and the chief executive of the Company was interested or had any short position in any shares, underlying shares or debentures of the Company and its associated corporations (within the meaning of Part XV of the SFO) as at 31 December 2005.

# DIRECTORS' REPORT

## SHARE OPTIONS

On 15 July 2002, the Company terminated the share option scheme of the Company adopted on 3 January 1997 (the "Old Share Option Scheme") and adopted a new share option scheme (the "Existing Share Option Scheme") as a result of the changes in the Listing Rules in relation to share option scheme.

Particulars of the Existing Share Option Scheme are set out in note 32 to the financial statements.

There are no outstanding options granted under the Old Share Option Scheme during the year.

A summary of the movements in share options granted under the Existing Share Option Scheme during the year is as follows:

| | | | | Number of share options | | | |
|---|---|---|---|---|---|---|---|
| | Date of grant | Exercisable period | Exercise price per share HK$ | Outstanding at 1.1.2005 | Granted during the year | Exercised during the year | Outstanding at 31.12.2005 |
| **Category: Directors** | | | | | | | |
| Mr. Jay Chun | 27.11.2003 | 27.11.2003 to 26.11.2008 | 0.088 | 2,500,000 | – | – | 2,500,000 |
| Dr. Ma Xianming | 27.11.2003 | 27.11.2003 to 26.11.2008 | 0.088 | 1,000,000 | – | – | 1,000,000 |
| **Category: Employees** | | | | | | | |
| | 27.11.2003 | 27.11.2003 to 26.11.2008 | 0.088 | 39,325,000 | – | (39,325,000) | – |
| | 13.08.2004 | 01.09.2004 to 12.08.2009 | 0.081 | 4,000,000 | – | – | 4,000,000 |
| **Category: Consultants** | | | | | | | |
| | 27.11.2003 | 27.11.2003 to 26.11.2008 | 0.088 | 23,375,000 | – | – | 23,375,000 |
| | 13.08.2004 | 01.09.2004 to 12.08.2009 | 0.081 | 200,000,000 | – | (75,000,000) | 125,000,000 |
| | 01.11.2004 | 01.11.2004 to 31.10.2009 | 0.086 | 50,000,000 | – | – | 50,000,000 |
| **Total all categories** | | | | 320,200,000 | – | (114,325,000) | 205,875,000 |

No options were granted during the year.

As at the date of this report, the total number of options available for issue under the Existing Share Option Scheme is 1,767,291 options, representing 10% of the shares of the Company in issue as at the date of refreshment of the scheme mandate limit on 18 July 2005 less the number of options granted under the Existing Share Option Scheme pursuant to the scheme mandate limit as refreshed.

# DIRECTORS' REPORT

## WARRANTS

On 23 February 2004, the Company issued, by way of private placement, 340,000,000 warrants at a placing price of HK$0.078 per warrant. The warrants are in registered form, which entitle the holders of the warrants the right to subscribe up to HK$34,680,000 in aggregate in cash for shares of HK$0.01 each in the Company at an initial subscription price of HK$0.102 per share (subject to adjustments) during the period from 23 February 2004 to 26 February 2005 (both dates inclusive). The warrants have been listed on the Stock Exchange since 27 February 2004.

Exercise in full of the warrants would result in an issue of 340,000,000 shares of HK$0.01 each in the Company and the shares to which the warrants relate represent approximately 13.2% of the then existing issued share capital of the Company and approximately 11.7% of the enlarged issued share capital of the Company if the subscription rights attached to the warrants have been exercised in full.

The net proceeds from the issue of warrants of approximately HK$24,567,000 have been used as general working capital for the Group.

During the year, the registered holders of 74,420,000 (2004 : 40,440,000) warrants exercised their rights to subscribe for 74,420,000 (2004: 40,440,000) shares of HK$0.01 each in the Company at HK$0.102 per share. These shares rank pari passu with the existing shares in all respect.

During the year, no warrants were repurchased by the Company and cancelled upon repurchase (2004: 21,960,000).

After 26 February 2005, 203,180,000 warrants were expired. On expiry, the balance of warrant reserve in the sum of approximately HK$14,681,000 was transferred and credited to the accumulated losses in reserve.

A summary of the movements in warrants during the year is as follows:

| | **Warrants in registered form** | |
|---|---|---|
| | **Number** | **Value** |
| | | HK$'000 |
| At 1 January 2005 | 277,600,000 | 20,058 |
| Exercise of warrants | (74,420,000) | (5,377) |
| Lapse of warrants | (203,180,000) | (14,681) |
| At 31 December 2005 | – | – |

# DIRECTORS' REPORT

## DIRECTORS' RIGHTS TO ACQUIRE SHARES OR DEBENTURES

Other than the share option schemes disclosed under the section headed "Share Options" above, at no time during the year was the Company or any of its subsidiaries a party to any arrangements to enable the directors of the Company to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate. In addition, none of the directors, or their spouse or children under the age of 18 had any right to subscribe for the securities of the Company or had exercised any such right during the year.

## SUBSTANTIAL SHAREHOLDERS' INTERESTS IN SHARES

As at 31 December 2005, so far as is known to the directors, the interests and short positions of the persons or corporations, other than directors and chief executive of the Company, in the shares or underlying shares of the Company which have been disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO and as recorded in the register required to be kept by the Company under section 336 of the SFO, were as follows:

| Name | Total interests in shares(1) | Approximate percentage of interests |
|---|---|---|
| Best Top Offshore Limited | 353,190,000 | 12.78% |
| August Profit Investments Limited | 327,490,000 | 11.85% |

Note:

(1) All interests in shares stated above represent long positions.

Save as disclosed above, as at 31 December 2005, the Company had not been notified of any other person who was interested in or had a short position in the shares or underlying shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO and as recorded in the register required to be kept by the Company under section 336 of the SFO.

## MAJOR CUSTOMERS AND SUPPLIERS

For the year ended 31 December 2005, the aggregate amount of turnover attributable to the Group's five largest customers accounted for 69.4% of the Group's total turnover and the turnover attributable to the Group's largest customer was 29.5% of the Group's total turnover.

For the year ended 31 December 2005, the aggregate amount of purchase attributable to the Group's five largest suppliers accounted for 75.3% of the Group's total purchase and the purchase attributable to the Group's largest supplier was 41.8% of the Group's total purchase.

# DIRECTORS' REPORT

None of the directors, their associates or any shareholders (which to the knowledge of the directors owns more than 5% of the Company's issued share capital) has any interest in any of the Group's five largest customers or suppliers.

## CONVERTIBLE SECURITIES, OPTIONS, WARRANTS OR SIMILAR RIGHTS

Other than the share option schemes disclosed under the section headed "Share Options" and warrants disclosed under the section headed "Warrants" above, the Company had no outstanding convertible securities or other similar rights as at 31 December 2005.

## PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S SHARES AND WARRANTS

Neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed shares or warrants during the year.

## PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive rights under the Company's Bye-laws, or the laws of Bermuda, which would oblige the Company to offer new shares on a pro-rata basis to the existing shareholders.

## CORPORATE GOVERNANCE

In the opinion of the board of directors of the Company (the "Board"), the Company has complied with the Code of Corporate Governance Practices (the "Code") set out in Appendix 14 to the Listing Rules throughout the year ended 31 December 2005 except for certain deviations. For further information on the Company's corporate governance practices and details of deviations, please refer to the Corporate Governance Report on pages 18 to 21.

## COMPLIANCE WITH MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers ("Model Code") set out in Appendix 10 to the Listing Rules as the code of conduct regarding securities transactions by its directors. Having made specific enquiry, all directors have confirmed that they have fully complied with the required standard set out in the Model Code during the year.

# DIRECTORS' REPORT

## SUFFICIENCY OF PUBLIC FLOAT

Based on the information that is publicly available to the Company and within the knowledge of the directors of the Company, as at the latest practicable date prior to the date of this report, there is sufficient public float of not less than 25% of the Company's issued shares as required under the Listing Rules.

## AUDITORS

A resolution will be proposed at the forthcoming annual general meeting of the Company to re-appoint Messrs. RSM Nelson Wheeler as auditors of the Company.

On behalf of the Board

**Jay Chun**
*Chairman*

Hong Kong, 27 April 2006

# CORPORATE GOVERNANCE REPORT

In the opinion of the board of directors of the Company (the "Board"), the Company has complied with the Code of Corporate Governance Practices (the "Code") set out in Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") throughout the year ended 31 December 2005 except for certain deviations disclosed herein.

## DIRECTORS' SECURITIES TRANSACTIONS

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers ("Model Code") set out in Appendix 10 to the Listing Rules as the code of conduct regarding securities transactions by its directors. Having made specific enquiry, all directors have confirmed that they have fully complied with the required standard set out in the Model Code during the year.

## BOARD OF DIRECTORS

The Board is responsible for the leadership and control of the Group and oversees the Group's businesses, strategic decisions and performance. The Board has delegated the day-to-day responsibility to the Executive Directors and senior management who perform their duties under the leadership of the Managing Director.

The Board currently consists of three Executive Directors and three Independent non-executive Directors. One of our Independent non-executive Directors has relevant financial management expertise required by the Listing Rules.

The Board schedules four meetings a year and also meets as and when required. During the year, the Board held two regular meetings. The number of regular meetings held during the year fell short of the four times a year as set out in A.1.1 of the Code was due to the conflicting schedules of the members of the Board which rendered it complicated to arrange for such meetings.

The members of the Board and the attendance of each member are as follows:

| **Directors** | **Number of attendance** |
|---|---|
| **Executive Directors** | |
| Mr. Jay Chun *(Chairman and Managing Director)* | 2/2 |
| Mr. Shan Shiyong | 0/2 |
| Dr. Ma Xianming | 0/2 |
| **Independent non-executive Directors** | |
| Mr. Frank Hu | 2/2 |
| Mr. Wang Faqi | 0/2 |
| Ms. Ma Shiwei | 1/2 |

# CORPORATE GOVERNANCE REPORT

The Company has received annual confirmations of independence from Mr. Frank Hu, Mr. Wang Faqi and Ms. Ma Shiwei and the Company considers them to be independent.

Given the nature and business objective of the Company, the Board has a balance of skill and experience appropriate for the requirements of the business of the Company. The list of directors and their respective biographies are set out on pages 8 to 10 of this annual report respectively.

## CHAIRMAN AND MANAGING DIRECTOR

Mr. Jay Chun is the Chairman and the Managing Director of the Company. In the opinion of the Board, the roles of the managing director and the chief executive officer are the same. Although under A.2.1 of the Code, the roles of the Chairman and chief executive officer should be separated and should not be performed by the same individual, the Board considers that the present structure provides the Group with strong and consistent leadership and allows for efficient and effective business planning and execution. Hence, the Board believes that it is in the best interest of the shareholders of the Company that Mr. Jay Chun will continue to assume the roles of the Chairman of the Board and the Managing Director of the Company. However, the Company will review the current structure as and when it becomes appropriate in future.

The annual general meeting held on 18 July 2005 was chaired by Mr. Frank Hu, one of our Independent Non-executive Directors, instead of Mr. Jay Chun. Mr. Jay Chun did not attend the annual general meeting 2005 as he was in bad health at that time. In accordance with the Code, Mr. Jay Chun should attend the annual general meeting of the Company.

## INDEPENDENT NON-EXECUTIVE DIRECTORS

Under A.4.1 of the Code, the independent non-executive directors should be appointed for a specific term, subject to re-election and under A.4.2 of the Code, every director, including those appointed for a specific term, should be subject to retirement by rotation at least once every three years. Currently, only one of the three Independent Non-executive Directors is appointed for a specific term. In addition, under the provisions of the existing Bye-laws of the Company, the Chairman of the Board and the Managing Director of the Company shall not, whilst holding such office, be subject to retirement by rotation or be taken into account in determining the number of directors to retire each year.

Although not all the Independent Non-executive Directors are appointed for a specific term, the Company will propose certain amendments to its Bye-laws at the forthcoming annual general meeting to the effect that, among others, all directors, including the Chairman of the Board and the Managing Director of the Company, shall be subject to retirement by rotation at least once every three years whether or not they are appointed for a specific term. The amendments shall also bring the Bye-laws of the Company up to date and in line with the Code requirements.

# CORPORATE GOVERNANCE REPORT

## REMUNERATION COMMITTEE

The Company has established its Remuneration Committee on 30 September 2005 with a specific written terms of reference. The Remuneration Committee is responsible for making recommendations to the Board on, among other things, the Company's policy and structure for the remuneration of all directors and senior management of the Company and is delegated by the Board with the responsibility to determine on behalf of the Board the specific remuneration packages for all Executive Directors and senior management of the Company.

The Remuneration Committee comprises three Directors including two Independent Non-executive Directors, namely Mr. Frank Hu *(Chairman)* and Ms. Ma Shiwei and an Executive Director, Mr. Jay Chun.

The Remuneration Committee has not held any meeting during the year.

## NOMINATION OF DIRECTORS

The Company has not established a Nomination Committee. The duties and functions of the Nomination Committee recommended in the Code are performed by the Board collectively with no director being involved in fixing his/her own terms of appointment and no Independent Non-executive Director being involved in assessing his/her own independence.

## AUDITORS' REMUNERATION

During the year, the Group was charged about HK$1,036,000 for auditing services only. Out of the auditors' fees, HK$700,000 is charged by Messrs. RSM Nelson Wheeler, the current auditors and HK$336,000 is under provision of former auditors' remuneration.

| **Services rendered** | **Fees paid/payable** |
|---|---|
| | HK$'000 |
| Audit services | 1,036 |
| Non-audit services | Nil |

## AUDIT COMMITTEE

The Audit Committee is responsible for reviewing and supervising the financial reporting process and internal control system of the Group and providing advice and comments to the Board.

# CORPORATE GOVERNANCE REPORT

During the year, the Audit Committee held two meetings. Members of the Audit Committee and the attendance of each member are as follows:

| **Directors** | **Number of attendance** |
|---|---|
| **Independent Non-executive Directors** | |
| Mr. Frank Hu *(Chairman)* | 2/2 |
| Mr. Wang Faqi | 1/2 |
| Ms. Ma Shiwei | 1/2 |

During the year, the Audit Committee has performed the following duties:

- reviewed with the management and the external auditors the audited financial statements for the year ended 31 December 2004 and the unaudited interim financial statements for the six months ended 30 June 2005, with recommendations to the Board for approval;

- reviewed reports on internal control system covering financial, operational, procedural compliance and risk management functions; and

- reviewed the compliance issues with the regulatory and statutory requirements.

The Audit Committee has reviewed with the management of the Company the accounting principles and practices adopted by the Group and the financial statements for the year ended 31 December 2005.

The Chairman of the Audit Committee, Mr. Frank Hu, possesses relevant financial management expertise and meets the requirements of rule 3.21 of the Listing Rules.

## ACCOUNTABILITY

The directors are responsible for the preparation of the accounts of the Group for the relevant accounting periods under applicable statutory and regulatory requirements which give true and fair view of the state of affairs, the results of operations and cashflows of the Group. In preparing the accounts for the six months ended 30 June 2005 and for the year ended 31 December 2005, the directors have adopted suitable accounting policies and applied them consistently. The accounts for the reporting year have been prepared on a going concern basis.

## INTERNAL CONTROLS

The Board has, through the Audit Committee, conducted interim and annual review of the effectiveness of the internal control system of the Group covering the financial, operational, procedural compliance and risk management functions. The internal control system is designed to provide reasonable, but not absolute, assurance of no material misstatement or loss and to manage rather than eliminate risks of failure in operational systems and achievements of the Group's objectives.

# AUDITORS' REPORT

RSM Nelson Wheeler
羅 申 美 會 計 師 行
Certified Public Accountants

**TO THE SHAREHOLDERS OF**
**LIFETEC GROUP LIMITED**
*(incorporated in Bermuda with limited liability)*

We have audited the financial statements on pages 25 to 85 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

## RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The Company's directors are responsible for the preparation of financial statements which give a true and fair view. In preparing financial statements which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently.

It is our responsibility to form an independent opinion, based on our audit, on those financial statements and to report our opinion solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

## BASIS OF OPINION

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants except that the scope of our work was limited as explained below.

An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the circumstances of the Company and the Group, consistently applied and adequately disclosed.

We planned our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatement. However, the evidence available to us was limited as below:

### (1) Scope limitation – Impairment of intangible assets, payments for investments and interests in subsidiaries

(a) As at 31 December 2005, the Group had intangible assets of HK$65,037,000 in connection with the beneficial rights to drugs under development not yet available for use as detailed in note 20 to the financial statements. However, we were unable to obtain sufficient information and explanations to assess whether any impairment in value should be recognised in respect of the intangible assets amounting to HK$65,307,000 as stated in the consolidated balance sheet as at 31 December 2005;

# AUDITORS' REPORT

(b) Included in the payments for investments as at 31 December 2005 was a deposit paid for the acquisition of a subsidiary of HK$19,989,000 as detailed in note 22 to the financial statements. However, we were unable to obtain sufficient information and explanations to assess whether there is any impairment in the underlying values of the assets to be acquired under the deposit, i.e., beneficial rights in a drug under development not yet available for use held by the company to be acquired, and accordingly whether any allowance should be made in respect of the deposit amounting to HK$19,989,000 as included in the consolidated balance sheet as at 31 December 2005;

(c) Included in the payments for investments as at 31 December 2005 were five deposits paid for the acquisition of beneficial interests of five drugs under development not yet available for use of HK$53,654,000 and the corresponding consultancy fees for soliciting the drugs under development projects capitalised of HK$1,148,000 as detailed in note 22 to the financial statements. However, we were unable to obtain sufficient information and explanations to assess whether there is any impairment in the values of the underlying assets to be acquired under the deposits, i.e., beneficial rights to five drugs under development not yet available for use, and accordingly whether any allowance should be made in respect of the deposits amounting to HK$53,654,000 and the corresponding consultancy fees for soliciting the drugs under development projects capitalised of HK$1,148,000 as included in the consolidated balance sheet as at 31 December 2005;

(d) Included in the Company's balance sheet as at 31 December 2005 are interests in subsidiaries at a carrying amount of HK$220,588,000. We were unable to assess whether there is any impairment in the value of the interests in subsidiaries due to the limitations in the scope of our work in respect of the assets held by the related subsidiaries referred to in points 1(a) to 1(c) above.

Any adjustments found to be necessary to the figures set out in points 1(a) to 1(d) above would affect the net assets of the Group and the Company as at 31 December 2005, the loss of the Group for the year then ended and the related disclosures thereof in the financial statements.

## (2) Scope limitation – Prior year's audit scope limitation affecting opening balances

The former auditors issued a qualified opinion arising from limitation of audit scope on the financial statements of the Group and the Company for the year ended 31 December 2004. As detailed in their report dated 28 April 2005 on the financial statements of the Group and the Company for the year ended 31 December 2004, they were unable to obtain sufficient information and evidence to assess whether any impairment in value should be recognised in respect of the intangible assets of HK$46,744,000 and the payments for investments of HK$69,955,000 as stated in the consolidated balance sheet as at 31 December 2004; and in respect of the interests in subsidiaries of HK$226,101,000 as stated in the Company's balance sheet as at 31 December 2004.

# AUDITORS' REPORT

> We were unable to obtain sufficient evidence to assess the impact of the matters mentioned above on the financial statements of the Group and the Company for the year ended 31 December 2005. Any adjustments found to be necessary in respect thereof had we obtained sufficient evidence would have had a consequential effect on the equity of the Group and the Company as at 1 January 2005, the loss of the Group for the year ended 31 December 2005 and the related disclosures thereof in the financial statements for the year ended 31 December 2005.

In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

## QUALIFIED OPINION ARISING FROM LIMITATION OF AUDIT SCOPE

Except for any adjustments that might have been found to be necessary had we been able to obtain sufficient evidence concerning the opening balances mentioned in point 2 of the "Basis of opinion" section; and the intangible assets, the payments for investments and the interests in subsidiaries as mentioned in points 1(a) to 1(d) of the "Basis of opinion" section, in our opinion the financial statements give a true and fair view of the state of affairs of the Company and the Group as at 31 December 2005 and of the loss and cash flows of the Group for the year then ended and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

In respect alone of the limitation on our work relating to the opening balances, the intangible assets, the payments for investments and the interests in subsidiaries, we have not obtained all the information and explanations we considered necessary for the purposes of our audit.

*Certified Public Accountants*
Hong Kong

27 April 2006

# CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2005

| | Notes | 2005<br>HK$'000 | 2004<br>HK$'000 |
|---|---|---|---|
| **Turnover** | 6 | 85,478 | 64,179 |
| Cost of sales | | (59,568) | (12,575) |
| Gross profit | | 25,910 | 51,604 |
| Other operating income | 7 | 4,714 | 3,383 |
| Marketing, selling and distribution costs | | (19,981) | (24,039) |
| Administrative expenses | | (29,159) | (43,355) |
| Research and development expenditure | | (1,706) | (1,500) |
| Loss on disposal of beneficial rights to a drug under development | | – | (400) |
| Loss on disposal of investments in securities | 8 | – | (41,293) |
| Impairment loss for doubtful debts | 9 | (2,873) | (2,391) |
| Loss from operations | 10 | (23,095) | (57,991) |
| Finance costs | 12 | (108) | (289) |
| **Loss before taxation** | | (23,203) | (58,280) |
| Taxation | 13 | (1,197) | (2,504) |
| **Loss for the year** | | (24,400) | (60,784) |
| Attributable to: | | | |
| Equity holders of the Company | | (24,095) | (60,992) |
| Minority interests | | (305) | 208 |
| | | (24,400) | (60,784) |
| Loss per share (HK cents) | 16 | | |
| – Basic | | (0.90) | (2.38) |
| – Diluted | | N/A | N/A |

# CONSOLIDATED BALANCE SHEET

At 31 December 2005

| | Notes | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|---|
| **Non-current assets** | | | |
| Property, plant and equipment | 17 | **4,715** | 4,164 |
| Investment properties | 18 | **3,480** | 3,480 |
| Goodwill | 19 | **–** | 555 |
| Intangible assets | 20 | **65,037** | 46,744 |
| Interests in an associate | 21 | **–** | – |
| Payments for investments | 22 | **74,791** | 69,955 |
| | | **148,023** | 124,898 |
| **Current assets** | | | |
| Inventories | 24 | **37** | – |
| Debtors and prepayments | 25 | **30,799** | 66,227 |
| Promissory notes | 26 | **–** | 10,259 |
| Advances to consulting companies | 27 | **51,650** | 48,069 |
| Bank and cash balances | | **26,713** | 7,911 |
| | | **109,199** | 132,466 |
| Less: **Current liabilities** | | | |
| Creditors and accrued charges | 28 | **20,472** | 15,581 |
| Amounts due to directors | 41 | **1,124** | 524 |
| Bank borrowings – due within one year | 29 | **135** | 2,725 |
| Taxation payable | | **3,233** | 2,350 |
| | | **24,964** | 21,180 |
| **Net current assets** | | **84,235** | 111,286 |
| **Total assets less current liabilities** | | **232,258** | 236,184 |

# CONSOLIDATED BALANCE SHEET

At 31 December 2005

| | Notes | 2005<br>HK$'000 | 2004<br>HK$'000 |
|---|---|---|---|
| **Non-current liabilities** | | | |
| Bank borrowings – due after one year | 29 | **36** | 170 |
| Deferred tax liabilities | 30 | **9,654** | 6,912 |
| | | **9,690** | 7,082 |
| **NET ASSETS** | | **222,568** | 229,102 |
| **Capital and reserves** | | | |
| Share capital | 31 | **27,633** | 25,745 |
| Reserves | | **191,420** | 199,565 |
| Equity attributable to equity holders of the Company | | **219,053** | 225,310 |
| **Minority interests** | | **3,515** | 3,792 |
| **TOTAL EQUITY** | | **222,568** | 229,102 |

Approved by the Board of Directors on 27 April 2006.

**JAY CHUN**
*Director*

**FRANK HU**
*Director*

# BALANCE SHEET

At 31 December 2005

| | Notes | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|---|
| **Non-current asset** | | | |
| Interests in subsidiaries | 23 | **220,588** | 226,101 |
| **Current assets** | | | |
| Debtors and prepayments | | **363** | 373 |
| Bank and cash balances | | **9** | 7 |
| | | **372** | 380 |
| Less: **Current liabilities** | | | |
| Creditors and accrued charges | | **798** | 647 |
| Amounts due to directors | 41 | **1,109** | 524 |
| | | **1,907** | 1,171 |
| **Net current liabilities** | | **(1,535)** | (791) |
| **NET ASSETS** | | **219,053** | 225,310 |
| **Capital and reserves** | | | |
| Share capital | 31 | **27,633** | 25,745 |
| Reserves | 34 | **191,420** | 199,565 |
| **TOTAL EQUITY** | | **219,053** | 225,310 |

Approved by the Board of Directors on 27 April 2006.

**JAY CHUN**
*Director*

**FRANK HU**
*Director*

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2005

| | Attributable to equity holders of the Company | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | Share capital HK$'000 | Share premium HK$'000 | Special reserve HK$'000 (Note a) | Warrant reserve HK$'000 | Option reserve HK$'000 (Note b) | Goodwill reserve HK$'000 (Note c) | Translation reserve HK$'000 | Accumulated losses HK$'000 | Sub-total HK$'000 | Minority interests HK$'000 | Total equity HK$'000 |
| **At 1 January 2004,** | | | | | | | | | | | |
| as previously reported as equity | 25,766 | 313,381 | 88,643 | – | – | 93 | 239 | (172,417) | 255,705 | – | 255,705 |
| **At 1 January 2004,** | | | | | | | | | | | |
| as previously separately reported | | | | | | | | | | | |
| as minority interest | – | – | – | – | – | – | – | – | – | 3,584 | 3,584 |
| **At 1 January 2004,** | | | | | | | | | | | |
| as restated | 25,766 | 313,381 | 88,643 | – | – | 93 | 239 | (172,417) | 255,705 | 3,584 | 259,289 |
| Surplus arising on repurchase | | | | | | | | | | | |
| of warrants not recognised in | | | | | | | | | | | |
| the consolidated income statement | – | – | – | – | – | – | – | 266 | 266 | – | 266 |
| Loss for the year | – | – | – | – | – | – | – | (60,992) | (60,992) | 208 | (60,784) |
| Total recognised income for 2004 | – | – | – | – | – | – | – | (60,726) | (60,726) | 208 | (60,518) |
| Issue of warrants | – | – | – | 26,520 | – | – | – | – | 26,520 | – | 26,520 |
| Expenses incurred in connection | | | | | | | | | | | |
| with the issue of warrants | – | – | – | (1,953) | – | – | – | – | (1,953) | – | (1,953) |
| Issue of shares | 1,459 | 14,872 | – | (2,922) | – | – | – | – | 13,409 | – | 13,409 |
| Repurchase of warrants | – | – | – | (1,587) | – | – | – | – | (1,587) | – | (1,587) |
| Repurchase of shares | (1,480) | (22,039) | – | – | – | – | – | – | (23,519) | – | (23,519) |
| Equity-settled consultancy services | – | – | – | – | 17,461 | – | – | – | 17,461 | – | 17,461 |
| | (21) | (7,167) | – | 20,058 | 17,461 | – | – | – | 30,331 | – | 30,331 |
| **At 31 December 2004** | 25,745 | 306,214 | 88,643 | 20,058 | 17,461 | 93 | 239 | (233,143) | 225,310 | 3,792 | 229,102 |

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2005

| | Attributable to equity holders of the Company | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | Share capital HK$'000 | Share premium HK$'000 | Special reserve HK$'000 (Note a) | Warrant reserve HK$'000 | Option reserve HK$'000 (Note b) | Goodwill reserve HK$'000 (Note c) | Translation reserve HK$'000 | Accumulated losses HK$'000 | Sub-total HK$'000 | Minority interests HK$'000 | Total equity HK$'000 |
| **At 1 January 2005** | | | | | | | | | | | |
| as per above | 25,745 | 306,214 | 88,643 | 20,058 | 17,461 | 93 | 239 | (233,143) | 225,310 | 3,792 | 229,102 |
| Effects of changes in accounting policies | – | – | – | – | – | (93) | – | 93 | – | – | – |
| **At 1 January 2005,** as restated | 25,745 | 306,214 | 88,643 | 20,058 | 17,461 | – | 239 | (233,050) | 225,310 | 3,792 | 229,102 |
| Movement in equity on expiry of warrants | – | – | – | (14,681) | – | – | – | 14,681 | – | – | – |
| Exchange differences arising on translation of financial statements of foreign subsidiaries | – | – | – | – | – | – | 710 | – | 710 | 4 | 714 |
| Net income/(expense) recognised directly in equity | – | – | – | (14,681) | – | – | 710 | 14,681 | 710 | 4 | 714 |
| Loss for the year | – | – | – | – | – | – | – | (24,095) | (24,095) | (305) | (24,400) |
| Total recognised income for 2005 | – | – | – | (14,681) | – | – | 710 | (9,414) | (23,385) | (301) | (23,686) |
| Issue of shares | 1,888 | 27,871 | – | (5,377) | (7,254) | – | – | – | 17,128 | – | 17,128 |
| Capital injection from minority shareholders of subsidiaries | – | – | – | – | – | – | – | – | – | 24 | 24 |
| | 1,888 | 27,871 | – | (5,377) | (7,254) | – | – | – | 17,128 | 24 | 17,152 |
| **At 31 December 2005** | 27,633 | 334,085 | 88,643 | – | 10,207 | – | 949 | (242,464) | 219,053 | 3,515 | 222,568 |

Notes:

(a) Special reserve represents the aggregate of:

(i) the difference between the nominal amount of the share capital issued by the Company and the aggregate of the nominal amount of the issued share capital and the share premium account of LifeTec (Holdings) Limited, the subsidiary which was acquired by the Company pursuant to the group reorganisation in 1996, and

(ii) the effects of the capital reduction, share premium cancellation and elimination of accumulated losses, took place in 1999.

(b) Option reserve represents fair value of the consultancy services provided or to be provided by certain consultants to the Group in the prior year in relation to the scope of services as set out in note 32.

(c) Goodwill reserve at 31 December 2004 represents negative goodwill.

# CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2005

| | Notes | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|---|
| **OPERATING ACTIVITIES** | | | |
| Loss before taxation | | (23,203) | (58,280) |
| Adjustments for: | | | |
| Amortisation of goodwill | | – | 185 |
| Amortisation of intangible assets | | – | 710 |
| Interest income | | (899) | (1,834) |
| Depreciation of property, plant and equipment | | 856 | 1,013 |
| Loss/(gain) on disposal of property, plant and equipment | | 269 | (44) |
| Increase in fair value of investment properties | | – | (280) |
| Loss on disposal of investments in securities | | – | 41,293 |
| Impairment loss for doubtful debts | | 2,873 | 2,665 |
| Loss on disposal of beneficial rights to a drug under development | | – | 400 |
| Impairment of goodwill | | 555 | – |
| Inventories written off | | 179 | – |
| Interest expenses | | 108 | 289 |
| Equity-settled consultancy services | | – | 17,461 |
| Operating cash flows before movements in working capital | | (19,262) | 3,578 |
| (Increase)/decrease in inventories | | (216) | 38 |
| Decrease/(increase) in debtors and prepayments | | 34,828 | (10,415) |
| Increase/(decrease) in creditors and accrued charges | | 4,614 | (2,067) |
| Increase in amounts due to directors | | 600 | 160 |
| Cash generated from/(used in) operations | | 20,564 | (8,706) |
| Income tax paid | | (372) | (161) |
| Net cash generated from/(used in) operating activities | | 20,192 | (8,867) |
| **INVESTING ACTIVITIES** | | | |
| Deposits paid for the acquisition of beneficial rights to drugs under development | | (18,269) | (54,686) |
| Advances to consulting companies | | (150,309) | (48,069) |
| Purchase of investments in securities | | – | (17,650) |
| Purchase of property, plant and equipment | | (1,644) | (1,679) |
| Advance to an associate | | (852) | (632) |
| Proceeds on disposal of investments in securities | | – | 49,600 |
| Promissory notes repaid | | 10,259 | 30,779 |
| Repayment from consulting companies | | 147,681 | 28,286 |
| Proceeds on disposal of beneficial rights to a drug under development | | – | 6,600 |
| Interest received | | 899 | 1,834 |
| Proceeds on disposal of property, plant and equipment | | – | 100 |
| Acquisition of a subsidiary | 35 | (1,395) | – |
| Net cash used in investing activities | | (13,630) | (5,517) |

# CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2005

| | 2005<br>HK$'000 | 2004<br>HK$'000 |
|---|---|---|
| **FINANCING ACTIVITIES** | | |
| Proceeds from issue of warrants, net of expenses | – | 24,567 |
| Proceeds from issue of shares, net of expenses | 17,128 | 13,409 |
| Payment on repurchase of shares, net of expenses | – | (23,519) |
| Repayments of bank and other borrowings | (2,724) | (3,801) |
| Payment on repurchase of warrants | – | (1,321) |
| Capital injection from minority shareholders of subsidiaries | 24 | – |
| Interest on bank borrowings paid | (108) | (269) |
| Repayments of obligations under finance leases | – | (44) |
| Interest on other loan paid | – | (19) |
| Finance charges on finance leases paid | – | (1) |
| Net cash generated from financing activities | 14,320 | 9,002 |
| **NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS** | 20,882 | (5,382) |
| **CASH AND CASH EQUIVALENTS AT BEGINNING OF THE YEAR** | 7,911 | 13,293 |
| **EFFECT OF FOREIGN EXCHANGE RATE CHANGES, NET** | (2,080) | – |
| **CASH AND CASH EQUIVALENTS AT END OF THE YEAR** | 26,713 | 7,911 |
| **ANALYSIS OF THE BALANCE OF CASH AND CASH EQUIVALENTS** | | |
| Bank and cash balances | 26,713 | 7,911 |

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 1. GENERAL

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

The Company is an investment holding company. The activities of its subsidiaries and a principal associate are set out in notes 42 and 43 respectively.

## 2. BASIS OF PREPARATION OF FINANCIAL STATEMENTS

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

### (i) HKAS 1 Presentation of financial statements and HKAS 27 Consolidated and separate financial statements

In previous years, minority interests at the balance sheet date were presented in the consolidated balance sheet separately from liabilities and as a deduction from net assets. Minority interests in the results of the Group for the year were also separately presented in the consolidated income statement as a deduction before arriving at the loss attributable to the equity holders of the Company.

With effect from 1 January 2005, in order to comply with HKAS 1 and HKAS 27, the Group has changed its accounting policy relating to the presentation of minority interests. Under the new policy, minority interests are presented as part of equity, separately from interests attributable to the equity holders of the Company. Further details of the new policy are set out in note 3(a). These changes in presentation have been applied retrospectively with comparatives restated as shown in the financial statements.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 2. BASIS OF PREPARATION OF FINANCIAL STATEMENTS (CONTINUED)

### (ii) HKAS 17 Leases

In previous years, owner-occupied leasehold land and buildings were included in property, plant and equipment and measured using the cost model. In the current year, the Group has applied HKAS 17. Under HKAS 17, the land and buildings elements of a lease of land and buildings are considered separately for the purposes of lease classification, unless the lease payments cannot be allocated reliably between the land and buildings elements, in which case, the entire lease is generally treated as a finance lease. To the extent that the allocation of the lease payments between the land and buildings elements can be made reliably, the leasehold interests in land are reclassified to prepaid lease payments under operating leases, which are carried at cost and amortised over the lease term on a straight line basis. This change in accounting policy has been applied retrospectively.

In the opinion of the directors, the leasehold land and buildings of the Group cannot be allocated reliably between the land and buildings elements, therefore, the entire lease payments of land and buildings are still included in property, plant and equipment and are amortised over the lease terms. Save as disclosed above, this change in accounting policy has had no effect on the financial statements.

### (iii) HKFRS 3 Business Combinations

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

*Goodwill*

In previous years, goodwill arising on acquisitions prior to 1 January 2001 was held in reserves and goodwill arising on acquisitions after 1 January 2001 was capitalised and amortised over its estimated useful life. The Group has applied the relevant transitional provisions in HKFRS 3. With respect to goodwill previously capitalised on the balance sheet, the Group has discontinued amortising such goodwill from 1 January 2005 onwards and goodwill will be tested for impairment at least annually or in the financial year in which the acquisition takes place. Goodwill arising on acquisitions after 1 January 2005 is measured at cost less accumulated impairment losses after initial recognition. As a result of this change in accounting policy, no amortisation of goodwill has been charged in the current year. The amortisation of goodwill in year 2004 was HK$185,000. Comparative figures for year 2004 have not been restated.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 2. BASIS OF PREPARATION OF FINANCIAL STATEMENTS (CONTINUED)

### (iii) HKFRS 3 Business Combinations (continued)

***Excess of the Group's interest in the net fair value of acquiree's identifiable assets, liabilities and contingent liabilities over cost (previously known as "negative goodwill")***

In accordance with HKFRS 3, any excess of the Group's interest in the net fair value of acquiree's identifiable assets, liabilities and contingent liabilities over the cost of acquisition is recognised immediately in profit or loss in the year in which the acquisition takes place. In previous years, negative goodwill arising on acquisitions prior to 1 January 2001 was held in reserves. Negative goodwill arising on acquisitions after 1 January 2001 was presented as a deduction from assets and released to income based on an analysis of the circumstances from which the balance resulted. In accordance with the relevant transitional provisions in HKFRS 3, the Group has derecognised all negative goodwill of HK$93,000 previously recorded in goodwill reserve with a corresponding credit to accumulated losses at 1 January 2005.

At the date of authorisation of these financial statements, HKICPA has issued certain new and revised standards and interpretations that are not yet effective to the financial statements. The directors anticipate that the adoption of these new and revised standards and interpretations in future periods will have no material impact on the financial statements of the Group.

## 3. PRINCIPAL ACCOUNTING POLICIES

The financial statements are prepared under the historical cost convention as modified by the revaluation of investment properties.

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

### (a) Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries made up to 31 December each year. Subsidiaries are those entities in which the Company, directly or indirectly, has the power to govern the financial and operating policies so as to obtain benefits from its activities. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity.

The results of the subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the date of disposal, as appropriate.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 3. PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

### (a) Basis of consolidation (continued)

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

All significant intercompany transactions, balances and unrealised profits on transactions within the Group have been eliminated on consolidation.

The gain or loss on the disposal of a subsidiary represents the difference between the proceeds of the sale and the Group's share of its net assets together with any goodwill or capital reserve which was not previously charged or recognised in the consolidated income statement and also any related accumulated foreign currency translation reserve.

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

In the Company's balance sheet the investments in subsidiaries are stated at cost less impairment losses, if any. The results of subsidiaries are accounted for by the company on the basis of dividends received and receivable.

### (b) Turnover

Turnover represents the amounts received and receivable for goods sold, net of discounts and returns to outside customers during the year.

### (c) Revenue recognition

Sales of goods are recognised on the transfer of risks and rewards of ownership, which generally coincides with the time when the goods are delivered and title has passed to the customers.

Service income is recognised when services are rendered.

Rental income is recognised on a straight line basis over the period of the leases.

Interest income is recognised on a time-proportion basis using the effective interest method.

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

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 3. PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

### (d) Property, plant and equipment

Property, plant and equipment are stated at historical cost less depreciation and impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are expensed in the consolidated income statement during the financial period in which they are incurred.

Depreciation of property, plant and equipment is calculated at rates sufficient to write off their cost over the estimated useful lives and after taking into account their estimated residual value, where appropriate, using the straight line method. The principal annual rates are as follows:

| | **Residual value** | **Annual depreciation rate** |
|---|---|---|
| Leasehold land and buildings | – | Over the remaining terms of the leases |
| Plant and machinery | 0 – 10% | 10 – 15% |
| Furniture, fixtures and office equipment | 0 – 10% | 10 – 20% |
| Motor vehicles | 0 – 10% | 10 – 20% |

The gain or loss on disposal of property, plant and equipment is the difference between the net sales proceeds and the carrying amount of the relevant asset, and is recognised in the consolidated income statement.

The residual values and useful lives of the assets are reviewed and adjusted, if necessary, at each balance sheet date.

Leasehold land and building comprises land held under operating lease and buildings held under finance lease. As it is not possible to measure the land and buildings element reliably, the lease of land and buildings are accounted for together as a finance lease.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 3. PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

### (e) Investment properties

Property that is held for long-term rental yields or for capital appreciation or both, and that is not occupied by the companies in the consolidated Group, is classified as investment property.

Investment property comprises land held under operating leases and related buildings.

Land held under operating leases are classified and accounted for as investment property when the rest of the definition of investment property is met. The operating lease is accounted for as if it were a finance lease.

Investment property is measured initially at its cost, including related transaction costs. After initial recognition, investment property is carried at fair value. Fair value is based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the specific asset. If this information is not available, the Group uses alternative valuation methods such as recent prices on less active markets or discounted cash flow projections. These valuations are performed in accordance with the guidance issued by the International Valuation Standards Committee. These valuations are reviewed annually by external valuers.

Subsequent expenditure is charged to the asset's carrying amount only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance costs are expensed in the consolidated income statement during the financial period in which they are incurred.

Changes in fair values are recognised in the consolidated income statement.

If an investment property becomes owner-occupied, it is reclassified as property, plant and equipment, and its fair value at the date of reclassification becomes its cost for accounting purposes. Property that is being constructed or developed for future use as investment property is classified as property, plant and equipment and stated at cost until construction or development is complete, at which time it is reclassified and accounted for as investment property.

If an item of property, plant and equipment becomes an investment property because its use has changed, any difference resulting between the carrying amount and the fair value of this item at the date of transfer is recognised in equity as a revaluation of property, plant and equipment under HKAS 16. However, if a fair value gain reverses a previous impairment loss, the gain is recognised in the consolidated income statement.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 3. PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

### (f) Impairment of tangible and intangible assets excluding goodwill

At each balance sheet date, the Group reviews the carrying amounts of its tangible and intangible assets (except goodwill) to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the 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.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (or cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (or cash-generating unit) in prior years. A reversal of an impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

### (g) Goodwill

As mentioned in note 2, negative goodwill previously recognised in reserves has been transferred to the Group's accumulated losses at 1 January 2005.

*Capitalised goodwill arising on acquisitions prior to 1 January 2005*

For previously capitalised goodwill arising on acquisitions after 1 January 2001, the Group has discontinued amortisation from 1 January 2005 onwards, and such goodwill is tested for impairment annually, and whenever there is an indication that the cash generating unit to which the goodwill relates may be impaired.

*Capitalised goodwill arising on acquisitions on or after 1 January 2005*

Goodwill arising on the acquisition of a subsidiary represents the excess of the cost of acquisition over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of the subsidiary recognised at the date of acquisition. Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 3. PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

### (g) Goodwill (continued)

*Impairment testing on capitalised goodwill*

For the purpose of impairment testing, goodwill is allocated to each of the Group's cash-generating units expected to benefit from the synergies of the combination. Cash-generating units to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro-rata on the basis of the carrying amount of each asset in the unit. An impairment loss recognised for goodwill is not reversed in a subsequent period.

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

### (h) Patents and beneficial rights to drugs under development

Costs incurred in the acquisition of patents are capitalised and amortised on a straight line basis over their useful economic lives.

Costs incurred in the acquisition of beneficial rights to drugs under development and the subsequent development cost are capitalised and amortised on a straight line basis over their useful economic lives when the underlying drugs are ready for commercial production.

### (i) Investments in associates

Associates are all entities over which the Group has significant influence but not controls, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investments in associates are accounted for by the equity method of accounting and are initially recognised at cost. The Group's investment in associates includes goodwill (net of any accumulated impairment loss) identified on acquisition.

The Group's share of its associates' post-acquisition profits or losses is recognised in the consolidated income statement, and its share of post-acquisition movements in reserves is recognised in reserves. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 3. PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

### (i) Investments in associates (continued)

Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates have been charged where necessary to ensure consistency with the policies adopted by the Group.

In the Company's balance sheet the investments in associated companies are stated at cost less provision for impairment losses. The results of associated companies are accounted for by the Company on the basis of dividend received and receivable.

### (j) Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is calculated using the weighted-average cost method and includes all costs of purchases, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

### (k) Trade and other receivables

Trade and other receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less allowance for impairment. An allowance for impairment of trade and other receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. The amount of the allowance is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate. The amount of the provision is recognised in the consolidated income statement.

### (l) Cash and cash equivalents

Cash and cash equivalents represent cash at bank and on hand, demand deposits with banks and other financial institutions, and short-term highly liquid investments which are readily convertible into known amounts of cash and subject to an insignificant risk of change in value. For the purpose of the cash flow statement, bank overdrafts which are repayable on demand and form an integral part of an enterprise's cash management are also included as a component of cash and cash equivalents.

### (m) Operating leases

Leases where substantially all the risks and rewards of ownership of assets remain with the leasing company are accounted for as operating leases. Rentals applicable to such operating leases net of any incentives received from the lessor are charged to the consolidated income statement on a straight line basis over the lease term.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 3. PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

### (n) Research and development expenditure

Research expenditure is expensed as incurred. Costs incurred on development projects relating to the design and testing of new or improved products are recognised as intangible assets when it is probable that the project will be a success considering its commercial and technological feasibility, and costs can be measured reliably. Other development expenditures are expensed as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period. Development costs with a finite useful life that have been capitalised are amortised from the commencement of the commercial production of the product on a straight-line basis over the period of its expected benefit.

### (o) Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or financial liability, including fees and commissions paid to agents, advisers, brokers and dealers, levies by regulatory agencies and securities exchanges, and transfer taxes and duties. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the consolidated income statement over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

### (p) Foreign currencies translation

#### *(i) Functional and presentation currency*

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated financial statements are presented in Hong Kong dollars, which is the Company's functional and presentation currency.

#### *(ii) Transactions and balances in each entity's financial statements*

Transactions in foreign currencies are translated into the functional currency using the exchange rates prevailing on the transaction dates. Monetary assets and liabilities in foreign currencies are translated at the rates ruling on the balance sheet date. Profits and losses resulting from this translation policy are included in the consolidated income statement, except when deferred in equity as qualifying cash flow hedges or qualifying net investment hedges.

Translation differences on non-monetary items, such as equity instruments held at fair value through profit or loss, are reported as part of the fair value gain or loss. Translation difference on non-monetary items, such as equities classified as available-for-sale financial assets, are included in the fair value reserve in equity.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 3. PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

### (p) Foreign currencies translation (continued)

#### *(iii) Translation on consolidation*

The results and financial position of all the group entities (none of which has the currency of hyperinflationary economy) that have a functional currency different from the Company's presentation currency are translated into the Company's presentation currency as follows:

– assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;

– income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and

– all resulting exchange differences are recognised as a separate component of equity.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities, and of borrowings and other currency instruments designated as hedges of such investments, are taken to shareholders' equity. When a foreign operation is sold, such exchange differences are recognised in the consolidated income statement as part of the gain or loss on sale.

### (q) Employee benefits

#### *(i) Pension obligation*

Obligations for contributions to defined contribution retirement plans, including contributions payable under the Hong Kong Mandatory Provident Fund Schemes Ordinance, are recognised as expenses in the consolidated income statement as incurred.

In addition, the Group contributes on a monthly basis to defined contribution retirement benefit plans organised by the relevant municipal and provincial governments in the PRC. The municipal and provincial governments undertake to assume the retirement benefit obligations of all existing and future retired employees payable under these plans. Contributions to these plans are expensed as incurred.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 3. PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

### (q) Employee benefits (continued)

#### *(ii) Share-based compensation*

The Group operates an equity-settled, share-based compensation plan. The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted, excluding the impact of any non-market vesting conditions. Non-market vesting conditions are included in assumptions about the number of options that are expected to become exercisable. At each balance sheet date, the entity revises its estimates of the number of options that are expected to become exercisable. It recognises the impact of the revision of original estimates, if any, in the consolidated income statement, and a corresponding adjustment to equity over the remaining vesting period.

The proceeds received net of any directly attributable transaction costs are credited to share capital (nominal value) and share premium when the options are exercised.

### (r) Provisions and contingent liabilities

Provisions are recognised for liabilities of uncertain timing or amount when the Group has a present legal or constructive obligation arising as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where the time value of money is material, provisions are stated at the present value of the expenditures expected to settle the obligation.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow is remote.

### (s) Taxation

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

The tax currently payable is based on taxable profit for the year. Taxable profit differs from net profit as reported in the consolidated income statement because it excludes items of income or expense that are taxable or deductible in other years, and it further excludes income statement items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 3. PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

### (s) Taxation (continued)

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

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

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

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

### (t) Related parties

Parties are considered to be related to the Group if the Group has the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Group and the party are subject to common control or common significant influence. Related parties may be individuals (being members of key management personnel, significant shareholders and/or their close family members) or other entities and include entities which are under the significant influence of related parties of the Group where those parties are individuals, and post-employment benefit plans which are for the benefit of employees of the Group or of any entity that is a related party of the Group.

### (u) Event after the balance sheet date

Post-year-end events that provide additional information about the Group's position at the balance sheet date or those that indicate the going concern assumption is not appropriate are adjusting events and are reflected in the financial statements. Post-year-end events that are not adjusting events are disclosed in the notes to the financial statements when material.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

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

### (a) Critical judgements in applying the entity's accounting policies

In the process of applying the Group's accounting policies, which are described in note 3, management has made the following judgements that have the most significant effect on the amounts recognised in the financial statements.

*Distinction between investment properties and owner-occupied properties*

The Group determines whether a property qualifies as investment property. In making its judgement, the Group considers whether the property generates cash flows largely independently of the other assets. Owner-occupied properties generate cash flows that are attributable not only to property but also to other assets used in the production or supply process.

Some properties comprise a portion that is held to earn rentals or for capital appreciation and another portion that is held for use in the production or supply of goods or services or for administrative purposes. If these portions can be sold separately (or leased out separately under a finance lease), the Group will account for the portions separately. If the portions cannot be sold separately, the property is accounted for as investment property only if an insignificant portion is held for use in the production or supply of goods or services or for administrative purposes. The Group considers each property separately in making its judgement.

### (b) Key sources of estimation uncertainty

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

*Impairment for intangible assets*

In connection with the book value of intangible assets and payments for investments, the Group performs ongoing evaluation of status of the drug projects concerned. An independent valuer has also issued a valuation report for the drug projects. The valuation of each drug project as stated in the respective valuation report is no less than the respective book value of each drug. For this reason, the Group believes that there is no impairment for the book value of intangible assets and payments for investments.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 4. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY (CONTINUED)

### (b) Key sources of estimation uncertainty (continued)

***Impairment loss for doubtful debts***

The Group assesses impairment loss for doubtful debtors based upon evaluation of the recoverability of the trade and other debtors at each balance sheet date. The estimates are based on the ageing of the trade and other debtors balances and the historical write-off experience, net of recoveries. If the financial condition of the customers were to deteriorate, additional impairment may be required.

***Income taxes***

The Group is subject to income taxes in numerous jurisdictions. Significant judgement is required in determining the worldwide provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Group recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax liability of these matters is different from the amounts that were initially recorded, such differences will impact the profits tax and deferred tax provisions in the period in which such determination is made.

## 5. FINANCIAL RISK MANAGEMENT

The Group's activities expose it to a variety of financial risks: foreign exchange risk, credit risk, liquidity risk and cash flow interest rate risk. The Group's overall risk management programme seeks to minimise potential adverse effects on the Group's financial performance.

### (a) Foreign exchange risk

The Group mainly operates in the PRC with most of the transactions settled in Renminbi ("RMB"). It did not have significant exposure to foreign exchange risk. Nevertheless, the exchange rate of RMB to Hong Kong dollar is subject to the rules and regulations of foreign exchange control promulgated by the PRC government.

During the year, the Group had not entered into any forward exchange contracts.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 5. FINANCIAL RISK MANAGEMENT (CONTINUED)

### (b) Credit risk

The Group has no significant concentrations of credit risk. It has policies in place to increase the proportion of cash sales and to ensure that credit sales are made to customers with an appropriate credit history or background.

In view of advances to consulting companies, the Group performs ongoing credit evaluations of consulting companies' financial conditions. After the balance sheet date, most advances to consulting companies have been repaid on demand, there is no significant exposure to the credit risk as regards advances to consulting companies.

### (c) Liquidity risk

The Group's policy is to maintain sufficient cash and cash equivalents to meet its liquidity requirements. In view of the bank and cash balances of the Group as at 31 December 2005, the Group has no liquidity risk in the foreseeable future.

### (d) Cash flow interest rate risk

As the Group has no significant interest-bearing assets, the Group's income and operating cash flows are substantially independent of changes in market interest rates.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 6. TURNOVER AND SEGMENT INFORMATION

### Business segments

The Group is principally engaged in research, development and sale of biopharmaceutical products. No business segment analysis is presented as management considers this as one single business segment.

### Geographical segments

The Group's operations and assets are located in Hong Kong and elsewhere in the People's Republic of China.

Segment information of the Group by location of customers is presented as below:

**For the year ended 31 December 2005**

| | People's Republic of China ("PRC") HK$'000 | Kingdom of Cambodia ("Cambodia") HK$'000 (Note) | Hong Kong HK$'000 | Other regions HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|
| **Revenue** | | | | | |
| External sales | 83,742 | – | 1,502 | 234 | 85,478 |
| **Result** | | | | | |
| Segment results | (5,327) | – | 58 | 2 | (5,267) |
| Other operating income | | | | | 4,714 |
| Unallocated corporate expenses | | | | | (22,542) |
| Loss from operations | | | | | (23,095) |
| Finance costs | | | | | (108) |
| Loss before taxation | | | | | (23,203) |
| Taxation | | | | | (1,197) |
| Loss for the year | | | | | (24,400) |

Note: The Group has granted an exclusive distribution right to an independent distributor in Cambodia to distribute a pharmaceutical product in Cambodia, Union of Myanmar and Lao People's Democratic Republic for a period of five years commencing from November 2003.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 6. TURNOVER AND SEGMENT INFORMATION (CONTINUED)

### Geographical segments (continued)

**At 31 December 2005**

| | PRC HK$'000 | Cambodia HK$'000 | Hong Kong HK$'000 | Other regions HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| Segment assets | 15,994 | – | – | – | 15,994 |
| Unallocated corporate assets | | | | | 241,228 |
| Consolidated total assets | | | | | 257,222 |
| **Liabilities** | | | | | |
| Segment liabilities | 2,899 | – | – | – | 2,899 |
| Unallocated corporate liabilities | | | | | 31,755 |
| Consolidated total liabilities | | | | | 34,654 |

**For the year ended 31 December 2005**

| | PRC HK$'000 | Cambodia HK$'000 | Hong Kong HK$'000 | Other regions HK$'000 | Unallocated HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|---|
| Additions in: | | | | | | |
| – Property, plant and equipment | – | – | – | – | 1,644 | 1,644 |
| – Intangible assets | – | – | – | – | 18,280 | 18,280 |
| Depreciation of property, plant and equipment | – | – | – | – | 856 | 856 |
| Loss on disposal of property, plant and equipment | – | – | – | – | 269 | 269 |
| Inventories written off | 179 | – | – | – | – | 179 |
| Impairment of goodwill | – | – | – | – | 555 | 555 |
| Impairment loss for doubtful debts | 2,021 | – | – | – | 852 | 2,873 |

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 6. TURNOVER AND SEGMENT INFORMATION (CONTINUED)

### Geographical segments (continued)

For the year ended 31 December 2004

| | PRC HK$'000 | Cambodia HK$'000 (Note) | Hong Kong HK$'000 | Other regions HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|
| **Revenue** | | | | | |
| External sales | 63,476 | – | – | 703 | 64,179 |
| **Result** | | | | | |
| Segment results | 21,259 | – | – | (13) | 21,246 |
| Other operating income | | | | | 3,383 |
| Loss on disposal of beneficial rights to a drug under development | | | | | (400) |
| Loss on disposal of investments in securities | | | | | (41,293) |
| Unallocated corporate expenses | | | | | (40,927) |
| Loss from operations | | | | | (57,991) |
| Finance costs | | | | | (289) |
| Loss before taxation | | | | | (58,280) |
| Taxation | | | | | (2,504) |
| Loss for the year | | | | | (60,784) |

Note: The Group has granted an exclusive distribution right to an independent distributor in Cambodia to distribute a pharmaceutical product in Cambodia, Union of Myanmar and Lao People's Democratic Republic for a period of five years commencing from November 2003.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 6. TURNOVER AND SEGMENT INFORMATION (CONTINUED)

At 31 December 2004

| | PRC HK$'000 | Cambodia HK$'000 | Hong Kong HK$'000 | Other regions HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| Segment assets | 54,385 | – | – | – | 54,385 |
| Unallocated corporate assets | | | | | 202,979 |
| Consolidated total assets | | | | | 257,364 |
| **Liabilities** | | | | | |
| Segment liabilities | – | – | – | – | – |
| Unallocated corporate liabilities | | | | | 28,262 |
| Consolidated total liabilities | | | | | 28,262 |

For the year ended 31 December 2004

| | PRC HK$'000 | Cambodia HK$'000 | Hong Kong HK$'000 | Other regions HK$'000 | Unallocated HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|---|
| Additions in property, plant and equipment | – | – | – | – | 1,679 | 1,679 |
| Depreciation of property, plant and equipment | – | – | – | – | 1,013 | 1,013 |
| Amortisation of goodwill | – | – | – | – | 185 | 185 |
| Amortisation of intangible assets | 710 | – | – | – | – | 710 |
| Impairment loss for doubtful debts | 2,003 | – | – | – | 662 | 2,665 |
| Equity-settled consultancy services | – | – | – | – | 17,641 | 17,641 |

The geographical location of the segment assets is the same as the geographical location of customers in both years.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 7. OTHER OPERATING INCOME

| | 2005 | 2004 |
|---|---|---|
| | HK$'000 | HK$'000 |
| Interest income | 899 | 1,834 |
| Management fee income | 248 | 379 |
| Increase in fair value of investment properties | – | 280 |
| Sales of mould | – | 177 |
| Gain on disposal of property, plant and equipment | – | 44 |
| Net exchange gain | 2,211 | 13 |
| Sundry income | 1,356 | 656 |
| | 4,714 | 3,383 |

## 8. LOSS ON DISPOSAL OF INVESTMENTS IN SECURITIES

| | 2005 | 2004 |
|---|---|---|
| | HK$'000 | HK$'000 |
| Loss on disposal of investments in securities through: | | |
| The Stock Exchange | – | (19,293) |
| Private dealing (note) | – | (22,000) |
| | – | (41,293) |

Note: During the year 2004, the Group disposed of its entire investment in Mexan Limited, the Group's investment in listed securities, to an independent third party for cash at a consideration of HK$1.50 per share, representing a 31% discount to the closing price on the date of disposal, resulting in a loss of HK$22,000,000.

## 9. IMPAIRMENT LOSS FOR DOUBTFUL DEBTS

| | 2005 | 2004 |
|---|---|---|
| | HK$'000 | HK$'000 |
| Impairment loss for doubtful debts is analysed as follows: | | |
| Impairment loss for amount due from an associate | 852 | 632 |
| Impairment loss for trade debtors | 2,021 | 2,003 |
| Impairment loss for other debtors | – | 30 |
| | 2,873 | 2,665 |
| Recovery from trade debtors | – | (85) |
| Recovery from other debtors | – | (189) |
| | 2,873 | 2,391 |

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 10. LOSS FROM OPERATIONS

Loss from operations has been arrived at after charging:

| | 2005<br>HK$'000 | 2004<br>HK$'000 |
|---|---|---|
| Staff cost | | |
| – Directors' remuneration (note 11) | **5,935** | 6,060 |
| – Other staff | | |
| – Salaries and allowances | **6,393** | 5,504 |
| – Retirement benefit scheme contributions | **238** | 182 |
| | **12,566** | 11,746 |
| Amortisation of goodwill (included in administrative expenses) | **–** | 185 |
| Amortisation of intangible assets (included in administrative expenses) | **–** | 710 |
| Auditors' remuneration | | |
| – current | **700** | 740 |
| – underprovision in previous year | **336** | – |
| Cost of inventories | **59,568** | 12,575 |
| Depreciation | **856** | 1,013 |
| Direct operating expenses in respect of investment properties that did not generate rental income | **26** | 5 |
| Equity-settled consultancy services (note 32) | **–** | 17,461 |
| Impairment of goodwill | **555** | – |
| Loss on disposal of property, plant and equipment | **269** | – |
| Operating lease rentals paid in respect of rented premises (note) | **2,301** | 1,839 |

Note: The amount includes the accommodation benefits provided to a director amounting to HK$840,000 (2004: HK$840,000) as set out in note 11.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 11. DIRECTORS' REMUNERATION AND HIGHEST PAID EMPLOYEES

### Directors' remuneration

The remuneration of every director for the year ended 31 December 2005 is set out below:

| Name | Fees | Salaries and other benefit | Accommodation benefit | Retirement benefit scheme contributions | Total |
|---|---|---|---|---|---|
| | HK$'000 | HK$'000 | HK$'000 | HK$'000 | HK$'000 |
| **Executive directors** | | | | | |
| Mr. Jay Chun | – | 2,160 | 840 | 12 | 3,012 |
| Mr. Shan Shiyong, alias, Mr. Sin Sai Yung | – | 2,400 | – | – | 2,400 |
| Dr. Ma Xianming, alias, Dr. Ma Yin Ming | – | 172 | – | – | 172 |
| **Independent non-executive directors** | | | | | |
| Mr. Frank Hu | 120 | – | – | – | 120 |
| Mr. Wang Faqi | 120 | – | – | – | 120 |
| Ms. Ma Shiwei | 111 | – | – | – | 111 |
| **Total** | 351 | 4,732 | 840 | 12 | 5,935 |

The remuneration of every director for the year ended 31 December 2004 is set out below:

| Name | Fees | Salaries and other benefit | Accommodation benefit | Retirement benefit scheme contributions | Total |
|---|---|---|---|---|---|
| | HK$'000 | HK$'000 | HK$'000 | HK$'000 | HK$'000 |
| **Executive directors** | | | | | |
| Mr. Jay Chun | – | 2,160 | 840 | 12 | 3,012 |
| Mr. Shan Shiyong, alias, Mr. Sin Sai Yung | – | 2,400 | – | – | 2,400 |
| Dr. Ma Xianming, alias, Dr. Ma Yin Ming | – | 368 | – | – | 368 |
| **Independent non-executive directors** | | | | | |
| Mr. Frank Hu | 120 | – | – | – | 120 |
| Mr. Wang Faqi | 120 | – | – | – | 120 |
| Ms. Ma Shiwei | 40 | – | – | – | 40 |
| **Total** | 280 | 4,928 | 840 | 12 | 6,060 |

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 11. DIRECTORS' REMUNERATION AND HIGHEST PAID EMPLOYEES (CONTINUED)

Details of share options granted to the executive and independent non-executive directors are set out in note 32 to the financial statements. None of the directors has waived any emoluments during the year.

### Highest paid employees

The five highest paid employees of the Group included two directors (2004: three directors), details of whose emoluments are set out above. The emoluments of the remaining highest paid employees of the Group, other than directors, were as follows:

| | **2005 HK$'000** | 2004 HK$'000 |
|---|---|---|
| Salaries and other benefits | **1,793** | 1,164 |
| Retirement benefit scheme contributions | **24** | 24 |
| | **1,817** | 1,188 |

Their emoluments were within the following band:

| | **2005 Number of employees** | 2004 Number of employees |
|---|---|---|
| Nil to HK$1,000,000 | **3** | 2 |

During the year, no emoluments have been paid or payable by the Group to the directors or any of the five highest paid individuals as an inducement to join or upon joining the Group or as compensation for loss of office.

The Group remunerates its employees mainly based on industry's practices and individual's performance and experience. On top of regular remuneration, share options may be granted to eligible staff under the share option scheme adopted by the Company on 15 July 2002 by reference to the Group's performance as well as individual's performance.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 12. FINANCE COSTS

| | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|
| Interest on bank borrowings | 108 | 269 |
| Interest on other loan | – | 19 |
| Finance charges on finance leases | – | 1 |
| | 108 | 289 |

## 13. TAXATION

| | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|
| The charge represents: | | |
| Profits tax outside Hong Kong | | |
| – current | 103 | 2,504 |
| – underprovision in previous year | 1,094 | – |
| | 1,197 | 2,504 |

No provision for Hong Kong profits tax has been made in the financial statements since the Group has sufficient tax losses brought forward to set off against current year's assessable profits.

Profits tax outside Hong Kong represents PRC Income Tax which is calculated at the rate of 33% (2004: 33%) prevailing in the PRC with certain tax preference.

Details of the deferred taxation are set out in note 30.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 13. TAXATION (CONTINUED)

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

| | 2005<br>HK$'000 | 2004<br>HK$'000 |
|---|---|---|
| Loss before taxation | **(23,203)** | (58,280) |
| Tax at PRC income tax rate of 33% (2004: 33%) | **(7,657)** | (19,232) |
| Tax effect of expenses not deductible for tax purpose | **5,375** | 16,126 |
| Tax effect of income not taxable for tax purpose | **(904)** | (765) |
| Underprovision in previous year | **1,094** | – |
| Tax effect of tax losses not recognised | **3,560** | 12,613 |
| Utilisation of tax losses previously not recognised | **(127)** | (3,758) |
| Tax effect of temporary differences not recognised | **(144)** | – |
| Income tax on concessionary rate | **–** | (3,004) |
| Others | **–** | 524 |
| Tax charge for the year | **1,197** | 2,504 |

## 14. DIVIDEND

No dividend has been paid or declared by the Company during the year (2004: HK$Nil).

## 15. LOSS ATTRIBUTABLE TO EQUITY HOLDERS OF THE COMPANY

The consolidated loss attributable to equity holders of the Company includes a loss of HK$23,385,000 (2004: HK$13,078,000) which has been dealt with in the financial statements of the Company.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 16. LOSS PER SHARE

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

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| **Loss:** | | |
| Loss for the purposes of basic loss per share: | | |
| – Loss for the year | **(24,095)** | (60,992) |

**Number of shares:**

| | **2005** | 2004 |
|---|---|---|
| Weighted average number of shares for the purposes of basic loss per share | **2,679,944,426** | 2,567,413,269 |

As the exercise of the Company's outstanding share options and warrants during the years ended 31 December 2004 and 2005 would be anti-dilutive, no diluted loss per share was presented in both years.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 17. PROPERTY, PLANT AND EQUIPMENT

| | Leasehold land and buildings HK$'000 | Plant and machinery HK$'000 | Furniture, fixtures and office equipment HK$'000 | Motor vehicles HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|
| **THE GROUP** | | | | | |
| **Cost** | | | | | |
| At 1 January 2004 | 9,126 | 4,294 | 3,201 | 1,874 | 18,495 |
| Additions | – | – | 380 | 1,299 | 1,679 |
| Disposals | – | – | (24) | (389) | (413) |
| At 31 December 2004 | 9,126 | 4,294 | 3,557 | 2,784 | 19,761 |
| Additions | – | 188 | 1,456 | – | 1,644 |
| Disposals | – | (618) | (1,763) | – | (2,381) |
| Exchange realignment | 155 | 73 | 14 | 24 | 266 |
| At 31 December 2005 | 9,281 | 3,937 | 3,264 | 2,808 | 19,290 |
| **Depreciation and impairment loss** | | | | | |
| At 1 January 2004 | 8,031 | 3,889 | 1,751 | 1,270 | 14,941 |
| Provided for the year | 25 | 89 | 501 | 398 | 1,013 |
| Disposals | – | – | (13) | (344) | (357) |
| At 31 December 2004 | 8,056 | 3,978 | 2,239 | 1,324 | 15,597 |
| Provided for the year | 25 | 97 | 459 | 275 | 856 |
| Disposals | – | (618) | (1,494) | – | (2,112) |
| Exchange realignment | 156 | 67 | 6 | 5 | 234 |
| At 31 December 2005 | 8,237 | 3,524 | 1,210 | 1,604 | 14,575 |
| **Net book values** | | | | | |
| At 31 December 2005 | 1,044 | 413 | 2,054 | 1,204 | 4,715 |
| At 31 December 2004 | 1,070 | 316 | 1,318 | 1,460 | 4,164 |

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 17. PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

| | 2005<br>HK$'000 | 2004<br>HK$'000 |
|---|---|---|
| The net book value of the Group's leasehold land and buildings represents property situated in Hong Kong held under long lease | **1,044** | 1,070 |

At 31 December 2005, the net book value of leasehold land and buildings pledged as security for the Group's bank loans amounted to approximately HK$1,044,000 (2004: HK$1,070,000).

## 18. INVESTMENT PROPERTIES

| | THE GROUP<br>HK$'000 |
|---|---|
| **Fair value** | |
| At 1 January 2004 | 3,200 |
| Increase in fair value during year 2004 | 280 |
| At 31 December 2004 and 31 December 2005 | 3,480 |

The investment properties, which are rented out for rental income, were revalued as at 31 December 2005 by Dudley Surveyors Limited, an independent firm of professional valuers, on an open market value basis.

The investment properties are situated in Hong Kong and are held under long lease.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 19. GOODWILL

| | THE GROUP HK$'000 |
|---|---|
| **Cost** | |
| At 1 January 2004 and 31 December 2004 | 925 |
| Elimination of accumulated amortisation upon the adoption of HKFRS 3 (note 2) | (370) |
| At 31 December 2005 | 555 |
| **Amortisation** | |
| At 1 January 2004 | 185 |
| Charge for the year | 185 |
| At 31 December 2004 | 370 |
| Elimination of accumulated amortisation upon the adoption of HKFRS 3 (note 2) | (370) |
| At 31 December 2005 | – |
| **Impairment** | |
| Impairment loss recognised in the year ended 31 December 2005 | 555 |
| **Net book value** | |
| At 31 December 2005 | – |
| At 31 December 2004 | 555 |

As Hainan Kangwei Medicine Co., Ltd. ("Hainan Kangwei") recorded an operating loss during the year, the directors evaluated the business activity and future performance of Hainan Kangwei and considered that the goodwill arising from the acquisition of Hainan Kangwei was impaired. Accordingly, the Group has recognised in the consolidated income statement an impairment loss of HK$555,000 for goodwill attributable to the Group's equity interest in Hainan Kangwei.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 20. INTANGIBLE ASSETS

| | Patent<br>HK$'000 | Beneficial rights to drugs under development<br>HK$'000 | Total<br>HK$'000 |
|---|---|---|---|
| **THE GROUP** | | | |
| **Cost** | | | |
| At 1 January 2004 and 31 December 2004 | 4,705 | 46,744 | 51,449 |
| Acquired on acquisition of a subsidiary | – | 18,280 | 18,280 |
| Exchange realignments | – | 13 | 13 |
| At 31 December 2005 | 4,705 | 65,037 | 69,742 |
| **Amortisation** | | | |
| At 1 January 2004 | 3,995 | – | 3,995 |
| Charge for the year | 710 | – | 710 |
| At 31 December 2004 and 31 December 2005 | 4,705 | – | 4,705 |
| **Net book values** | | | |
| At 31 December 2005 | – | 65,037 | 65,037 |
| At 31 December 2004 | – | 46,744 | 46,744 |

Patent represents the acquired exclusive rights to use certain technologies for the manufacture of certain biopharmaceutical products. The patent is amortised over the remaining period of the exclusive rights assigned to the Group of four years.

No amortisation was provided for beneficial rights to drugs under development not yet available for use during the year. The amortisation of the cost of the beneficial rights to drugs under development will commence when the underlying drugs are fully developed and are ready for commercial production.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 21. INTERESTS IN AN ASSOCIATE

| | THE GROUP | |
|---|---|---|
| | **2005** | 2004 |
| | **HK$'000** | HK$'000 |
| Share of net assets | **–** | – |
| Amount due from an associate | **7,742** | 6,890 |
| | **7,742** | 6,890 |
| Less: Impairment loss for amount due from an associate | **(7,742)** | (6,890) |
| | **–** | – |

Particulars of the Group's principal associate at 31 December 2005 are set out in note 43.

The amount due from an associate is unsecured, interest free and has no fixed terms of repayment.

Summarised financial information in respect of the Group's associates is set out below:

| | **2005** | 2004 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Total assets | **7,316** | 8,110 |
| Total liabilities | **(9,199)** | (8,325) |
| Net liabilities | **(1,883)** | (215) |
| Revenue | **196** | 9,808 |
| Loss for the year | **(1,409)** | (215) |

The Group has not recognised losses amounting to HK$669,000 (2004: HK$103,000) for the Group's associates during the year. The accumulated losses of the Group's associates not recognised were HK$772,000 (2004: HK$103,000) as at 31 December 2005.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 22. PAYMENTS FOR INVESTMENTS

| | THE GROUP | |
|---|---|---|
| | **2005** | 2004 |
| | **HK$'000** | HK$'000 |
| Deposits paid for the acquisition of subsidiaries (note a) | **19,989** | 34,132 |
| Deposits paid for the acquisition of beneficial rights to drugs under development (note b) | **53,654** | 34,697 |
| Consultancy fees for soliciting the drugs under development projects capitalised | **1,148** | 1,126 |
| | **74,791** | 69,955 |

Notes:

(a) On 27 December 2003, LifeTec (Holdings) Limited ("LifeTec Holdings"), a wholly-owned subsidiary of the Company, entered into a conditional sale and purchase agreement with an independent party for the acquisition of the entire issued share capital of LGH Limited for a cash consideration of RMB16,000,000 (equivalent to HK$15,086,000). LGH Limited is a limited liability company incorporated in the British Virgin Islands and holds the rights to a new drug project. As at 31 December 2004, the deposits paid by the Group for the acquisition of LGH Limited amounted to RMB15,000,000 (equivalent to HK$14,143,000). LGH Limited became a subsidiary of the Company during the year and the deposits paid of HK$14,143,000 was transferred to cost of acquisition for LGH Limited. Details of the assets and liabilities of LGH Limited acquired by the Group during the year are set out in note 35.

On 1 March 2004, LifeTec Holdings entered into a conditional sale and purchase agreement with an independent party to acquire 1 ordinary share in Anica Ltd., representing 100% of the issued share capital of Anica Ltd., for a cash consideration of RMB22,200,000 (equivalent to HK$20,932,000). Anica Ltd. is a limited liability company incorporated in the British Virgin Islands and holds the rights of a new drug project. As at 31 December 2004 and 31 December 2005, the deposit paid by the Group for the acquisition of Anica Ltd. amounted to RMB21,200,000 (equivalent to HK$19,989,000).

(b) On 2 June 2004, Hainan Kangwei, a subsidiary of the Company, entered into an agreement with an independent party to acquire the beneficial rights to a drug development project for a cash consideration of RMB15,000,000 (equivalent to HK$14,423,000 (2004: HK$14,143,000)). The amount paid by the Group amounting to RMB14,000,000 (equivalent to HK$13,462,000 (2004: HK$13,200,000)) at 31 December 2004 and 31 December 2005 represents the partial consideration paid under the agreement.

On 8 October 2004, Hainan Kangwei entered into an agreement with an independent party to acquire the beneficial rights to a drug development project for a cash consideration of RMB12,000,000 (equivalent to HK$11,538,000 (2004: HK$11,314,000)). The amount paid by the Group amounting to RMB11,000,000 (equivalent to HK$10,577,000 (2004: HK$10,371,000)) at 31 December 2004 and 31 December 2005 represents the partial consideration paid under the agreement.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 22. PAYMENTS FOR INVESTMENTS (CONTINUED)

Notes: (continued)

(b) (continued)

On 2 November 2004, Hainan Kangwei entered into an agreement with an independent party to acquire the beneficial rights to a drug development project for a cash consideration of RMB12,800,000 (equivalent to HK$12,308,000 (2004: HK$12,087,000)). The amount paid by the Group amounting to RMB11,800,000 (equivalent to HK$11,346,000 (2004: HK$11,126,000)) at 31 December 2004 and 31 December 2005 represents the partial consideration paid under the agreement.

On 5 January 2005, Hainan Kangwei entered into an agreement with an independent party to acquire the beneficial rights to a drug development project for a cash consideration of RMB10,000,000 (equivalent to HK9,615,000). The amount paid by the Group amounting to RMB9,000,000 (equivalent to HK$8,654,000) at 31 December 2005 represents the partial consideration paid under the agreement.

On 18 February 2005, Hainan Kangwei entered into an agreement with an independent party to acquire the beneficial rights to a drug development project for a cash consideration of RMB11,000,000 (equivalent to HK$10,577,000). The amount paid by the Group amounting to RMB10,000,000 (equivalent to HK$9,615,000) at 31 December 2005 represents the partial consideration paid under the agreement.

## 23. INTERESTS IN SUBSIDIARIES

| | THE COMPANY | |
|---|---|---|
| | **2005** | 2004 |
| | **HK$'000** | HK$'000 |
| Unlisted shares, at cost | **48,726** | 48,726 |
| Impairment loss | **(48,726)** | (48,726) |
| | **–** | – |
| Amount due from a subsidiary less allowance | **220,588** | 226,101 |
| | **220,588** | 226,101 |

The cost of the unlisted shares is based on the underlying net tangible assets of the subsidiaries attributable to the Group as at the date on which the Company became the ultimate holding company of the Group under the group reorganisation in 1996.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 23. INTERESTS IN SUBSIDIARIES (CONTINUED)

Particulars of the Company's subsidiaries as at 31 December 2005 are set out in note 42.

The amount due from a subsidiary is unsecured and interest free. The directors expect that the amount will not be repayable within the next twelve months.

## 24. INVENTORIES

| | THE GROUP | |
|---|---|---|
| | **2005** | 2004 |
| | **HK$'000** | HK$'000 |
| Finished goods, at cost | **37** | – |

## 25. DEBTORS AND PREPAYMENTS

The Group normally allows a credit period of 90 to 180 days to its trade debtors. The ageing analysis of the trade debtors, based on date of invoice, is as follows:

| | THE GROUP | |
|---|---|---|
| | **2005** | 2004 |
| | **HK$'000** | HK$'000 |
| Trade debtors | | |
| Within 30 days | **6,105** | 2,633 |
| 31 – 60 days | **2,135** | 1,303 |
| 61 – 90 days | **1,344** | 1,915 |
| 91 – 180 days | **2,964** | 9,370 |
| 181 – 365 days | **3,275** | 36,112 |
| Over 365 days | **171** | 3,052 |
| | **15,994** | 54,385 |
| Amount due from a former subsidiary | **10,745** | 4,330 |
| Loan to an independent third party | **–** | 3,133 |
| Balance of consideration receivable resulting from disposal of beneficial rights to a drug under development | **–** | 943 |
| Other debtors and prepayments | **4,060** | 3,436 |
| | **30,799** | 66,227 |

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 25. DEBTORS AND PREPAYMENTS (CONTINUED)

The directors consider that the carrying amount of debtors and prepayments approximates their fair value.

The loan to an independent third party is unsecured, carries interest at 3% per annum and fully settled during the year.

## 26. PROMISSORY NOTES

The promissory notes are secured by a first mortgage over the entire issued share capital of Goldstone International Holdings Limited ("Goldstone"), a former subsidiary of the Company, and the assignment of the benefit of all the shareholders' loan to Goldstone after the disposal and before the full repayment of the promissory notes. The promissory notes bear interest at the rate of 3% per annum and is repayable in four equal installments each following the maturity dates on 30 December 2003, 30 May 2004, 30 October 2004 and 30 March 2005.

During the year, the final installment of the promissory notes has been fully settled.

## 27. ADVANCES TO CONSULTING COMPANIES

The amount represents the outstanding receivables from five (2004: four) consulting companies established in the PRC. Pursuant to the agreements entered into between these consulting companies and Shanghai Youheng Biotechnology Limited ("Youheng"), a subsidiary of the Company, Youheng has appointed these consulting companies:

(a) to solicit potential biopharmaceutical investments projects in the PRC and to provide consultancy services to the related investments for a service fee of 3% on the amount to be invested in the projects by Youheng; and

(b) to make payment of earnest money for potential investment projects or cost of investment on behalf of the Group after obtaining the approval from Youheng.

The outstanding receivables are unsecured, carry interests at 1% per annum and RMB53,499,000 (equivalent to HK$51,441,000) have been settled after the balance sheet date.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 28. CREDITORS AND ACCRUED CHARGES

| | THE GROUP | |
|---|---|---|
| | **2005** | 2004 |
| | **HK$'000** | HK$'000 |
| The ageing analysis of trade creditors is as follows: | | |
| Within 30 days | **2,096** | – |
| 31 – 60 days | **598** | – |
| More than 90 days | **205** | – |
| | **2,899** | – |
| Value added tax payable | **7,155** | 6,611 |
| Other creditors and accrued charges | **10,418** | 8,970 |
| | **20,472** | 15,581 |

The directors consider that the carrying amount of creditors and accrued charges approximates their fair value.

## 29. BANK BORROWINGS

| | THE GROUP | |
|---|---|---|
| | **2005** | 2004 |
| | **HK$'000** | HK$'000 |
| Mortgage loans | **171** | 298 |
| Bank loans | **–** | 2,597 |
| | **171** | 2,895 |
| Of which: | | |
| Secured | **171** | 298 |
| Unsecured | **–** | 2,597 |
| | **171** | 2,895 |

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 29. BANK BORROWINGS (CONTINUED)

The terms of repayment of the bank borrowings are analysed as follows:

| | THE GROUP | |
|---|---|---|
| | **2005** | 2004 |
| | **HK$'000** | HK$'000 |
| Within one year or on demand | **135** | 2,725 |
| More than one year, but not exceeding two years | **36** | 135 |
| More than two years, but not exceeding five years | **–** | 35 |
| | **171** | 2,895 |
| Less: Amount due within one year shown under current liabilities | **(135)** | (2,725) |
| Amount due after one year | **36** | 170 |

The effective interest rates on bank borrowings were 6.7% (2004: 5.8%).

The directors consider that the carrying amount of non-current bank borrowings approximates their fair value.

## 30. DEFERRED TAX LIABILITIES

| | THE GROUP |
|---|---|
| | HK$'000 |
| At 1 January 2004 and 31 December 2004 | 6,912 |
| Addition on acquisition of a subsidiary | 2,742 |
| At 31 December 2005 | 9,654 |

The balances as at 31 December 2004 and 31 December 2005 represent the deferred tax liabilities recognised in respect of the temporary difference attributable to the intangible assets acquired through the acquisition of interests in certain subsidiaries.

At 31 December 2005, the Group has unused tax losses of HK$53,875,000 (2004: HK$43,450,000) available to offset against future taxable profits. No deferred tax asset has been recognised in respect of such losses due to the unpredictability of future profit streams. Included in unrecognised tax losses are losses of HK$3,912,000 (2004: HK$1,656,000) that will be expired from 2008 to 2010. Other losses may be carried forward indefinitely.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 31. SHARE CAPITAL

| | 2005 Number of shares | 2004 Number of shares | 2005 HK$'000 | 2004 HK$'000 |
|---|---|---|---|---|
| Shares of HK$0.01 each | | | | |
| Authorised: | | | | |
| At beginning and at end of the year | **10,000,000,000** | 10,000,000,000 | **100,000** | 100,000 |
| Issued and fully paid: | | | | |
| At beginning of the year | **2,574,552,919** | 2,576,618,919 | **25,745** | 25,766 |
| Issue of shares upon exercise of share options (note 32) | **114,325,000** | 105,500,000 | **1,144** | 1,055 |
| Issue of shares upon exercise of warrants (note 33) | **74,420,000** | 40,440,000 | **744** | 404 |
| Repurchase of shares (note (a)) | **–** | (148,006,000) | **–** | (1,480) |
| At end of the year | **2,763,297,919** | 2,574,552,919 | **27,633** | 25,745 |

Notes:

(a) During the year 2004, the Company repurchased its own shares through the Stock Exchange as follows:

| **Month of repurchase** | **Number of shares repurchased** | **Price per share Highest** HK$ | **Lowest** HK$ | **Aggregate consideration paid** HK$'000 |
|---|---|---|---|---|
| March 2004 | 36,506,000 | 0.157 | 0.146 | 5,549 |
| April 2004 | 530,000 | 0.167 | 0.167 | 89 |
| May 2004 | 49,654,000 | 0.169 | 0.155 | 8,093 |
| June 2004 | 13,200,000 | 0.171 | 0.166 | 2,232 |
| July 2004 | 48,116,000 | 0.170 | 0.144 | 7,556 |
| | 148,006,000 | | | 23,519 |

The above shares were cancelled upon repurchase.

(b) All the new shares issued during the years 2004 and 2005 rank pari passu in all respects with the existing shares.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 32. SHARE OPTIONS

The existing share option scheme was adopted by the Company on 15 July 2002 (the "Share Option Scheme") for the purpose of providing incentives or rewards for the contribution by the directors and employees of the Group; any supplier of goods or services to the Group; any customer of the Group; any adviser or consultant of the Group; any person or entity that provides research, development or other technological support to the Group; or any shareholders of the Group. The period within which the shares must be taken up under an option of the Share Option Scheme shall not be more than 5 years from the date of the option is granted. There is no minimum period for which an option must be held before it can be exercised. HK$1 is payable on acceptance of an option within 21 days from the date of grant.

Initially, the total number of shares in respect of which options may be granted under the Share Option Scheme must not in aggregate exceed 10% of the shares in issue as at 15 July 2002, being the date of adoption of the Share Option Scheme, without prior approval from the Company's shareholders. Pursuant to ordinary resolutions passed by the shareholders at a special general meeting held on 19 April 2004 and at an annual general meeting held on 18 July 2005, the numbers of shares in respect of which options may be granted have been refreshed to 10% of the numbers of shares in issue as at 19 April 2004 and 18 July 2005 respectively. The total number of shares issued and to be issued upon exercise of the options granted to each individual in any twelve-month period up to the date of grant shall not exceed 1% of the shares in issue at the date of grant without prior approval from the Company's shareholders. Options granted to substantial shareholders or independent non-executive directors in excess of 0.1% of the Company's share capital or with a value in excess of HK$5,000,000 must be approved in advance by the Company's shareholders.

Options may be exercised at any time from the date of grant of the share option to the fifth anniversary of the date of grant. The exercise price is determined by the directors of the Company, and will not be less than the highest of (i) the closing price of the Company's shares on the date of grant; (ii) the average closing price of the shares for the five business days immediately preceding the date of grant; and (iii) the nominal value of the shares on the offer date.

The total number of shares may be issued upon exercise of all outstanding options granted and yet to be exercised under the Share Option Scheme must not exceed 30% of the shares in issue from time to time.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 32. SHARE OPTIONS (CONTINUED)

Details of the movements in share options granted under the Share Option Scheme during each of the two years ended 31 December 2005 are set out as follows:

| | | | Number of share options | | | |
|---|---|---|---|---|---|---|
| **Date of grant** | **Exercisable period** | **Exercise price per share** | **Outstanding at 1.1.2005** | **Granted during the year** | **Exercised during the year** | **Outstanding at 31.12.2005** |
| | | HK$ | | | | |
| Category: Directors | | | | | | |
| 27.11.2003 | 27.11.2003 to 26.11.2008 | 0.08800 | 3,500,000 | – | – | 3,500,000 |
| Category: Employees | | | | | | |
| 27.11.2003 | 27.11.2003 to 26.11.2008 | 0.08800 | 39,325,000 | – | (39,325,000) | – |
| 13.08.2004 | 01.09.2004 to 12.08.2009 | 0.08100 | 4,000,000 | – | – | 4,000,000 |
| Category: Consultants | | | | | | |
| 27.11.2003 | 27.11.2003 to 26.11.2008 | 0.08800 | 23,375,000 | – | – | 23,375,000 |
| 13.08.2004 | 01.09.2004 to 12.08.2009 | 0.08100 | 200,000,000 | – | (75,000,000) | 125,000,000 |
| 01.11.2004 | 01.11.2004 to 31.10.2009 | 0.08600 | 50,000,000 | – | – | 50,000,000 |
| Total all categories | | | 320,200,000 | – | (114,325,000) | 205,875,000 |
| Weighted average exercise price (HK$) | | | 0.0832 | – | 0.0834 | 0.0831 |

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 32. SHARE OPTIONS (CONTINUED)

| Date of grant | Exercisable period | Exercise price per share HK$ | Number of share options: Outstanding at 1.1.2004 | Granted during the year | Exercised during the year | Outstanding at 31.12.2004 |
|---|---|---|---|---|---|---|
| Category: Directors | | | | | | |
| 27.11.2003 | 27.11.2003 to 26.11.2008 | 0.0880 | 3,500,000 | – | – | 3,500,000 |
| Category: Employees | | | | | | |
| 27.11.2003 | 27.11.2003 to 26.11.2008 | 0.0880 | 76,825,000 | – | (37,500,000) | 39,325,000 |
| 13.08.2004 | 01.09.2004 to 12.08.2009 | 0.0810 | – | 4,000,000 | – | 4,000,000 |
| Category: Consultants | | | | | | |
| 27.11.2003 | 27.11.2003 to 26.11.2008 | 0.0880 | 91,375,000 | – | (68,000,000) | 23,375,000 |
| 13.08.2004 | 01.09.2004 to 12.08.2009 | 0.0810 | – | 200,000,000 | – | 200,000,000 |
| 01.11.2004 | 01.11.2004 to 31.10.2009 | 0.0860 | – | 50,000,000 | – | 50,000,000 |
| Total all categories | | | 171,700,000 | 254,000,000 | (105,500,000) | 320,200,000 |
| Weighted average exercise price (HK$) | | | 0.0880 | 0.0820 | 0.0880 | 0.0832 |

The options outstanding at the end of the year have a weighted average remaining contractual life of 3.6 years (2004: 4.5 years).

The Company has granted share options to certain consultants pursuant to the consultancy agreements entered into between LifeTec Holdings and each of the consultants for a period of five years commencing from the respective dates of the consultancy agreements. Pursuant to the consultancy agreements, the consultants agreed to:

(a) identify potential strategic investors and financial investors for the Group;

(b) assist the Group in negotiating with the potential strategic investors and financial investors;

(c) provide consultancy services in relation to the drug development business of the Group; and

(d) carry out other duties as appropriate and as agreed with LifeTec Holdings.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 32. SHARE OPTIONS (CONTINUED)

The fair values of the 91,375,000 share options and 250,000,000 share options granted by the Company to the consultants during the years ended 31 December 2003 and 31 December 2004 amounted to HK$3,718,000 and HK$13,743,000 respectively. An amount of HK$17,461,000 was credited to option reserve of the Company and the Group during the year 2004. In the opinion of the directors of the Company, as the future economic benefits in relation to the services to be provided by these consultants are uncertain, the whole amount of HK$17,461,000 had been charged to the consolidated income statement for the year 2004.

The fair values of options granted to the consultants on 13 August 2004 and 1 November 2004 determined using the Black-Scholes valuation model were HK$11,966,000 and HK$1,777,000 respectively. The significant inputs into the model were as follows:

| | Share option grant date | |
|---|---|---|
| | 13 August 2004 | 1 November 2004 |
| Share price at the grant date | HK$0.070 | HK$0.085 |
| Exercise price | HK$0.081 | HK$0.086 |
| Expected volatility based on historical volatility of share prices | 144.87% | 42.32% |
| Expected annual dividend yield, based on historical dividend | – | – |
| Expected life of options | 5 years | 5 years |
| Hong Kong Exchange Fund Notes rate for corresponding estimated expected life indicated at the date of grant | 3.18% | 3.18% |

Expected volatility was determined by calculating the historical volatility of the Company's share price over the previous 30 days. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions and behavioural considerations.

Total consideration received during the year 2004 from directors, employees and consultants for accepting the options granted amounted to HK$12.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 33. WARRANTS

| | Warrants in registered form | |
|---|---|---|
| | Number | Value |
| | | HK$'000 |
| Issued on 23 February 2004 (note a) | 340,000,000 | 26,520 |
| Expenses incurred in connection with the issue of warrants | – | (1,953) |
| Exercise of warrants (note b) | (40,440,000) | (2,922) |
| Repurchase of warrants (note c) | (21,960,000) | (1,587) |
| At 31 December 2004 | 277,600,000 | 20,058 |
| Exercise of warrants (note b) | (74,420,000) | (5,377) |
| Lapse of warrants (note d) | (203,180,000) | (14,681) |
| At 31 December 2005 | – | – |

Notes:

(a) On 23 February 2004, the Company issued, by way of private placement, 340,000,000 warrants at a placing price of HK$0.078 per warrant. The warrants were in registered form, which entitled the holders of the warrants the right to subscribe up to HK$34,680,000 in aggregate in cash for shares of HK$0.01 each in the Company at an initial subscription price of HK$0.102 per share (subject to adjustments) during the period from 23 February 2004 to 26 February 2005 (both dates inclusive). The warrants had been listed on the Stock Exchange since 27 February 2004.

Exercise in full of the warrants would result in an issue of 340,000,000 shares of HK$0.01 each in the Company and the shares to which the warrants relate represent approximately 13.2% of the then existing issued share capital of the Company and approximately 11.7% of the enlarged issued share capital of the Company if the subscription rights attached to the warrants are exercised in full.

The net proceeds from the issue of warrants of approximately HK$24,567,000 had been used as general working capital for the Group.

(b) During the year, the registered holders of 74,420,000 (2004: 40,440,000) warrants exercised their rights to subscribe for 74,420,000 (2004: 40,440,000) shares of HK$0.01 each in the Company at HK$0.102 per share. These shares rank pari passu with the existing shares in all respect.

(c) During the year, no warrants were repurchased by the Company and were cancelled upon repurchase (2004: 21,960,000).

(d) After 26 February 2005, 203,180,000 warrants were expired. On expiry, the balance of warrant reserve in sum of approximately HK$14,681,000 was transferred and credited to the accumulated losses in reserve.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 34. RESERVES

| | Share premium HK$'000 | Contributed surplus HK$'000 (Note) | Warrant reserve HK$'000 | Option reserve HK$'000 | Accumulated losses HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|---|
| **THE COMPANY** | | | | | | |
| At 1 January 2004 | 313,381 | 110,223 | – | – | (241,579) | 182,025 |
| Issue of warrants | – | – | 26,520 | – | – | 26,520 |
| Expenses incurred in connection with the issue of warrants | – | – | (1,953) | – | – | (1,953) |
| Issue of shares | 14,872 | – | (2,922) | – | – | 11,950 |
| Repurchase of warrants | – | – | (1,587) | – | – | (1,587) |
| Surplus arising on repurchase of warrants | – | – | – | – | 266 | 266 |
| Repurchase of shares | (22,039) | – | – | – | – | (22,039) |
| Equity-settled consultancy services | – | – | – | 17,461 | – | 17,461 |
| Loss for the year | – | – | – | – | (13,078) | (13,078) |
| At 31 December 2004 | 306,214 | 110,223 | 20,058 | 17,461 | (254,391) | 199,565 |
| Issue of shares | 27,871 | – | (5,377) | (7,254) | – | 15,240 |
| Movement in equity on expiry of warrants | – | – | (14,681) | – | 14,681 | – |
| Loss for the year | – | – | – | – | (23,385) | (23,385) |
| At 31 December 2005 | 334,085 | 110,223 | – | 10,207 | (263,095) | 191,420 |

Note: Contributed surplus represents the aggregate of:

(i) the difference between the consolidated shareholders' funds of LifeTec Holdings at the date on which the group reorganisation became effective and the nominal amount of the share capital of the Company issued under the group reorganisation and after distributions, and

(ii) the effects of the capital reduction, share premium cancellation and elimination of accumulated losses, took place in 1999.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 34. RESERVES (CONTINUED)

In addition to the retained profits, under the Companies Act 1981 of Bermuda (as amended), contributed surplus is also available for distribution to shareholders. However, the Company cannot declare or pay a dividend, or make a distribution out of contributed surplus if:

(a) the Company is, or would after the payment be, unable to pay its liabilities as they become due; or

(b) the realisable value of the Company's assets would thereby be less than the aggregate of its liabilities and its issued share capital and share premium accounts.

In the opinion of the directors, the Company did not have reserves available for distribution to shareholders as at 31 December 2004 and 31 December 2005.

## 35. ACQUISITION OF A SUBSIDIARY

During the year, the Group acquired the entire interest in the share capital of LGH Limited for a consideration of approximately HK$15,538,000. Details of the net assets of the subsidiary acquired were as follows:

| | **Acquiree's carrying amount** | **Fair value** |
|---|---|---|
| | HK$ | HK$'000 |
| Net assets acquired: | | |
| Intangible assets | 8 | 18,280 |
| Deferred tax liability | – | (2,742) |
| Total consideration | 8 | 15,538 |
| Satisfied by: | | |
| Cash | | 1,395 |
| Deposits paid in year 2003 (note 22) | | 14,143 |
| | | 15,538 |
| Net cash outflow arising on acquisition: | | |
| Cash consideration paid | | (1,395) |

The subsidiary acquired during the year did not contribute any turnover and profit from operations to the Group for the period between the date of acquisition and the balance sheet date.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 36. CONTINGENT LIABILITIES

On 15 September 1999, LifeTec Enterprise Limited ("LifeTec Enterprise"), a subsidiary of the Company, was named as a defendant in a High Court action in respect of an alleged failure to repay a loan in amount of HK$20,000,000. The plaintiff took out an application for summary judgement under Order 14 of the Rules of the High Court on 6 October 1999 and in the hearing of the application on 25 October 1999, LifeTec Enterprise was given unconditional leave to defend the plaintiff's claim in the above action. LifeTec Enterprise filed its Defence on 8 November 1999. The plaintiff should have filed its reply, if any, 14 days thereafter, but LifeTec Enterprise had not received any reply from the plaintiff and the time for the plaintiff to file the same has long expired and the pleadings should be deemed to be closed. The directors believe that there is no ground for the above claim and it will not have any material adverse impact on the Group's operations.

## 37. OPERATING LEASE COMMITMENTS

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

| | THE GROUP | | THE COMPANY | |
|---|---|---|---|---|
| | **2005** | 2004 | **2005** | 2004 |
| | **HK$'000** | HK$'000 | **HK$'000** | HK$'000 |
| Within one year | **1,736** | 1,665 | **1,187** | 736 |
| In the second to fifth year inclusive | **1,306** | 101 | **593** | – |
| | **3,042** | 1,766 | **1,780** | 736 |

Leases are negotiated for average terms of one to three years and rentals are fixed throughout the terms of respective leases.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 38. CAPITAL AND OTHER COMMITMENTS

| | THE GROUP | |
|---|---|---|
| | **2005** | 2004 |
| | **HK$'000** | HK$'000 |
| Capital expenditure contracted for but not provided in the financial statements in respect of: | | |
| Acquisition of the beneficial rights to drugs under development | **5,770** | 4,714 |
| Acquisition of property, plant and equipment | **1,721** | – |
| | **7,491** | 4,714 |
| Research and development expenditure contracted for but not provided in the financial statements | **13,153** | 12,925 |

## 39. RETIREMENT BENEFIT SCHEMES

### Hong Kong

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

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

The Group's contribution under the MPF Scheme for the year amounted to HK$119,000 (2004: HK$109,000).

### PRC

According to the relevant laws and regulations in the PRC, the Group's subsidiaries in the PRC are required to contribute a specified percentage of the payroll of their employees to the retirement benefit schemes to fund the retirement benefits of their employees. The only obligation of the Group with respect to the retirement benefit schemes is to make the required contributions under the respective schemes.

The Group's contribution under the respective schemes for the year amounted to HK$131,000 (2004: HK$85,000).

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 40. POST BALANCE SHEET EVENTS

On 3 January 2006 and 20 February 2006, 12,000,000 share options and 254,000,000 share options were granted to employees and consultants at exercise price of HK$0.081 per share option with the expiry dates on 2 January 2011 and 19 February 2011 respectively.

## 41. RELATED PARTY TRANSACTIONS

### Trading transactions

During the year, the Group and the Company entered into the following related party transactions:

| | Directors | | Associate | |
|---|---|---|---|---|
| | **2005** | 2004 | **2005** | 2004 |
| | **HK$'000** | HK$'000 | **HK$'000** | HK$'000 |
| **THE GROUP** | | | | |
| Management fee income from (note a) | **–** | – | **240** | 240 |
| Maintenance expenses paid to (note a) | **–** | – | **120** | 120 |
| Amount due from (note b & c) | **–** | – | **7,742** | 6,890 |
| Amounts due to (note b) | **1,124** | 524 | **–** | – |
| **THE COMPANY** | | | | |
| Amounts due to (note b) | **1,109** | 524 | **–** | – |

Notes:

(a) The transactions were charged at predetermined amount agreed between the parties involved.

(b) The amounts are unsecured, interest free and have no fixed terms of repayment. No guarantees have been given or received.

(c) HK$852,000 (2004: HK$632,000) impairment has been made for the year for the loan made to an associate.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 41. RELATED PARTY TRANSACTIONS (CONTINUED)

### Compensation of key management personnel

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

| | 2005<br>HK$'000 | 2004<br>HK$'000 |
|---|---|---|
| Directors' fees | **351** | 280 |
| Salaries and allowances | | |
| – Directors | **5,572** | 5,768 |
| – Other staff | **2,176** | 1,798 |
| Retirement benefit scheme contributions | **63** | 53 |
| | **8,162** | 7,899 |

The remuneration of directors and key management personnel is determined by the remuneration committee having regard to the performance of individuals and market trends.

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 42. SUBSIDIARIES

Particulars of the Group's subsidiaries as at 31 December 2005 are as follows:

| Name of subsidiary | Place of incorporation/ registration | Issued and fully paid share capital/ registered capital | Proportion of ownership interest | | | Principal activities |
|---|---|---|---|---|---|---|
| | | | Group's effective interest | Held by the Company | Held by subsidiaries | |
| Asset Manager Enterprises Limited | Hong Kong | HK$100 | 100% | – | 100% | Property holding |
| CTI Limited | Hong Kong | HK$10 | 70% | – | 70% | Design and trading of home appliances |
| Gold Corner International Limited | British Virgin Islands | US$1 | 100% | – | 100% | Investment holding |
| Gold Eagle Technology Limited | British Virgin Islands | US$1 | 100% | – | 100% | Research and development of biopharmaceutical products |
| Golden Butterfly Investments Limited | British Virgin Islands | US$100 | 95% | – | 95% | Investment holding |
| Hainan Kangwei Medicine Co., Ltd. (note a) | PRC | RMB2,000,000 | 98.5% | – | 100% | Trading of biopharmaceutical products |
| Hop Fu (Hong Kong) Trading Company Limited | Hong Kong | HK$10,000 | 100% | – | 100% | Inactive |
| LGH Limited | British Virgin Islands | US$1 | 100% | – | 100% | Research and development of biopharmaceutical products |
| LifeTec Enterprise Limited | Hong Kong | HK$100 | 100% | – | 100% | General trading and provision of management services |
| LifeTec Group (China) Limited | British Virgin Islands | US$1 | 100% | – | 100% | Inactive |
| LifeTec (Holdings) Limited | British Virgin Islands | HK$141,176 | 100% | 100% | – | Investment holding |

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 42. SUBSIDIARIES (CONTINUED)

| Name of subsidiary | Place of incorporation/ registration | Issued and fully paid share capital/ registered capital | Proportion of ownership interest | | | Principal activities |
|---|---|---|---|---|---|---|
| | | | Group's effective interest | Held by the Company | Held by subsidiaries | |
| LifeTec Pharmaceutical Limited | British Virgin Islands | US$1 | 100% | – | 100% | Investment holding |
| LT Card Limited | British Virgin Islands | US$1 | 100% | – | 100% | Investment holding |
| LT Capital Limited | British Virgin Islands | US$1 | 100% | – | 100% | Investment holding |
| LT Finance Limited | British Virgin Islands | US$1 | 100% | – | 100% | Investment holding |
| LT Game Limited | British Virgin Islands | US$1 | 100% | – | 100% | Development of electronic gaming system |
| LT (Macau) Limited | Macau | MOP25,000 | 100% | – | 100% | Membership card service |
| LT Union Limited | British Virgin Islands | US$1 | 100% | – | 100% | Investment holding |
| Loan San Enterprise Limited | Hong Kong | HK$50,000 | 36% | – | 52% | General trading |
| Longkou Sunny Link Leathering Co., Ltd. (note b) | PRC | US$3,100,000 | 68% | – | 68% | Manufacture and sale of PVC products |
| Master Mind Technology Limited | British Virgin Islands | US$1 | 100% | – | 100% | Research and development of biopharmaceutical products |
| Shanghai Youheng Biotechnology Limited (note c) | PRC | HK$5,600,000 | 95% | – | 100% | Research and development of biopharmaceutical products |
| Sino Flow Investments Limited | British Virgin Islands | US$1 | 100% | – | 100% | Inactive |
| Sunny Link Trading Limited | Hong Kong | HK$2 | 100% | – | 100% | General trading |
| Weihai Genen Biotech Limited (note c) | PRC | US$2,000,000 | 100% | – | 100% | Research and development of biopharmaceutical products |
| Yip Hing Toys Manufactory Limited | Hong Kong | HK$100,000 | 100% | – | 100% | Inactive |

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

## 42. SUBSIDIARIES (CONTINUED)

Notes:

(a) The subsidiary is established in the PRC as a domestic enterprise.

(b) The subsidiary is established in the PRC as cooperative joint venture.

(c) The subsidiaries are established in the PRC as wholly owned foreign enterprises.

Apart from Hainan Kangwei Medicine Co., Ltd., Longkou Sunny Link Leathering Co., Ltd., Shanghai Youheng Biotechnology Limited and Weihai Genen Biotech Limited which carry out their principal activities in the PRC; and LT Game Limited and LT (Macau) Limited which carry out their principal activities in Macau, the principal activities of the remaining subsidiaries are carried out in Hong Kong.

None of the subsidiaries had any debt securities subsisting at 31 December 2005 or at any time during the year.

## 43. ASSOCIATE

Particulars of the Group's principal associate as at 31 December 2005 are as follows:

| Name of associate | Form of business structure | Place of incorporation | Attributable proportion of nominal value of issued share capital indirectly held by the Group | Principal activities |
|---|---|---|---|---|
| LT3000 Online Limited | Incorporated | British Virgin Islands | 47.47% | Development and trading of computer hardware & software and provision of business consultancy services |

# FINANCIAL SUMMARY

## RESULTS

| | For the year ended 31 December | | | | |
|---|---|---|---|---|---|
| | 2001 HK$'000 | 2002 HK$'000 | 2003 HK$'000 | 2004 HK$'000 | **2005 HK$'000** |
| Turnover | 22,318 | 31,009 | 57,213 | 64,179 | **85,478** |
| (Loss)/profit before taxation | (62,704) | (18,107) | 38,559 | (58,280) | **(23,203)** |
| Taxation | – | – | (7) | (2,504) | **(1,197)** |
| (Loss)/profit for the year | (62,704) | (18,107) | 38,552 | (60,784) | **(24,400)** |
| Attributable to: | | | | | |
| Equity holders of the Company | (57,258) | (23,318) | 36,848 | (60,992) | **(24,095)** |
| Minority Interests | (5,446) | 5,211 | 1,704 | 208 | **(305)** |
| | (62,704) | (18,107) | 38,552 | (60,784) | **(24,400)** |

## ASSETS AND LIABILITIES

| | At 31 December | | | | |
|---|---|---|---|---|---|
| | 2001 HK$'000 | 2002 HK$'000 | 2003 HK$'000 | 2004 HK$'000 | **2005 HK$'000** |
| Total assets | 119,416 | 151,295 | 289,834 | 257,364 | **257,222** |
| Total liabilities | (64,948) | (32,428) | (30,545) | (28,262) | **(34,654)** |
| Total equity | 54,468 | 118,867 | 259,289 | 229,102 | **222,568** |