
INDUSTRY OVERVIEW

The Group is a business equipment and tax control equipment provider in the PRC whose principal products include printers, LCD projectors, and tax control equipment, which collectively accounted for 91.3%, 79.6% and 81.5% of the Group's total turnover during the three years ended 31st December, 2004 respectively.

A detailed analysis of the market environment for these respective products is set out below.

(I) Printer market in China

(a) *Technology segments of printer market*

There are many different types of printers, which could be categorised into the following three main categories according to technology utilisation:

(i) *SDM printers*

SDM printers use vertical arrays of tiny wires in a print head that shuttle across the page. They create an image on paper by striking pins against an inked ribbon. The ink is transferred to the paper as closely shaped dots that form each character. SDM printers are commonly used by commercial sector and governmental agencies for printing invoices, purchase orders, shipping forms, expense reports, and other multi-part forms. SDM printers can print through multi-part forms in a single pass.

(ii) *Laser/LED/electron beam printers*

Laser/LED/electron beam printers utilise a laser beam or light-emitting diode to produce an image on a drum. The light of the laser or light-emitting diode alters the electrical charge on the drum wherever it hits. The drum is then rolled through a reservoir of toner, which is picked up by the charged portions of the drum. Finally, the toner is transferred to the paper through a combination of heat and pressure. Laser/ LED/ electron beam printers produce very high quality text and graphics.

(iii) *Ink-jet printers*

A type of printer that works by spraying ionised ink at a sheet of paper. Magnetised plates in the ink's path direct the ink onto the paper in the desired shapes. Ink-jet printers are capable of producing high quality print approaching that produced by laser printers. In general, the price of ink-jet printers is lower than that of laser printers; however, they are also considerably slower.

(b) *Current development of printer market in China*

The printers sector was the largest sector in the computer peripherals market in China accounting for approximately 77.6% of total sales of computer peripherals market and amounted to approximately RMB10.6 billion in 2003, according to Euromonitor International. They consider that the printers sector should remain the largest sector, accounting for approximately 70% of total sales of computer peripherals market in 2008. Euromonitor International predicted that sales of printers will reach approximately RMB16.1 billion in 2008, representing a compound annual growth rate of approximately 8.7% between 2003 and 2008.

According to the "China printer forecast and analysis report" issued in July 2004 and April 2005 respectively by IDC, the overall printer shipment units in China increased by 35.2% from approximately 5.4 million units in 2002 to approximately 7.3 million units in 2004. In addition, the SDM printer shipment

INDUSTRY OVERVIEW

units increased by 30.0% from approximately 1.0 million units in 2002 to approximately 1.3 million units in 2004. According to IDC, the SDM printers accounted for approximately 18.2% and 33.8% of the total printers shipment units and total printers shipment value in 2004 respectively.

According to the data issued in April 2005 by IDC, the SDM printers market in China was dominated by three Japanese branded products which accounted for approximately 67.7% of the total SDM printers shipments in China during 2004.

IDC ranked the number of Jolimark branded SDM printers shipped during 2004 as the fourth largest in China, having accounted for approximately 8.3% of the total SDM printers shipments in China during 2004.

(c) The impact of the “Golden Tax Project” on the SDM printers market

VAT is a kind of turnover tax levied on the value added in the course of the import and sales of goods in China. VAT invoices are issued by the seller to the buyer upon the sale of goods for the purpose of calculating the output VAT payable/input VAT creditable for the seller/buyer. VAT registration is required for an enterprise to qualify as a general VAT taxpayer which can issue VAT invoices. VAT invoices are the irreplaceable documents required before credit in respect of input VAT could be obtained.

In order to prevent and combat theft, fraud and other criminal activities related to VAT, the Chinese government started to establish a nation-wide computerised monitoring system known as the second phase of the “Golden Tax Project” in 1994.

Under the second phase of the “Golden Tax Project”, a nationwide computer network is to be developed to match input tax claims made by taxpayers against the corresponding output tax filed by the issuer of the VAT invoice to which the input tax claim relates. It was intended that on full implementation of the second phase of the Golden Tax Project, taxpayers and tax officials should be able to verify the VAT invoices received via their own “anti-VAT-fraud monitoring system” while the tax authorities can monitor all the VAT invoices issued by general VAT taxpayers in China.

The second phase of the “Golden Tax Project” was substantially implemented in 2003. According to the announcement issued by State Administration of Taxation on 9th June, 2003, effective since 1st July, 2003, general VAT payers from 23 provinces (municipalities or areas), including Beijing, Tianjin, Shanxi, Jilin, Jiangsu, Anhui, Fujian, Xiamen, Henan, Hubei, Guangdong, Shenzhen, Sichuan and Chongqing are required to issue computerised VAT invoices through the “anti-VAT-fraud monitoring system” rather than use handwritten invoices. Handwritten VAT invoices obtained by general VAT payers after 1st August, 2003 are not deductible for VAT purposes.

The special equipment for “anti-VAT-fraud monitoring system” for the second phase of the “Golden Tax Project” includes tax monitoring card, tax monitoring IC card and card reader, while general equipment for the “anti-VAT-fraud monitoring system” includes computers and anti-fraud invoice printers (VAT invoice) used for issuing computerised VAT invoices under the “anti-VAT-fraud monitoring system”. Due to its handling capacity for multi-part forms and the regulatory requirement for selecting SDM printers for printing invoices, SDM printers are commonly used as anti-fraud invoice printers (VAT invoice) for issuing computerised VAT invoices under the “anti-VAT-fraud monitoring system”. Thus, the implementation of “anti-VAT-fraud monitoring system” in major cities of China in 2003 has stimulated the demand for SDM printers.

INDUSTRY OVERVIEW

It is expected that the third phase of the “Golden Tax Project” will begin in the second half of 2005. According to IDC, as this nationwide project will be implemented for many years and will last much longer than any previous phases of the “Golden Tax Project”, the potential market of SDM printers will be further stimulated.

(d) *The impact of the implementation of the “Twelve Gold Projects” on the demand for SDM printers at governmental and commercial sectors*

In addition to the “Golden Tax Project”, the Chinese government has launched a series of separate E-government infrastructure initiatives which aim at developing an information economy and building administrative capabilities (such initiatives and the “Golden Tax Project” are collectively known as the “Twelve Gold Projects”). The “Twelve Gold Projects” cover the whole range of IT systems for intra-government communications, education, health care and medical research, and agriculture. The Directors consider that, similar to the “Golden Tax Project”, the implementation of the “Twelve Gold Projects” will prompt the replacement of handwritten records by the usage of computerised information systems, in turn, more hardcopy documents, including computerised reports, forms, certificates and invoices, will be generated by printers in both governmental and commercial sectors. Printing of such computerised information will be carried out largely by SDM printers. Ultimately, the implementation of the “Twelve Gold Projects” could lead to an increase in demand for SDM printers at governmental and commercial sectors in China.

To the best knowledge of the Directors, the third phase of the “Golden Tax Project” — tax control ECR will begin in the second half of 2005. The expected completion time for the third phase of the “Golden Tax Project” has not yet been announced by the China Tax Authority.

Taking into account the fact that (1) the second phase of “Golden Tax Project” took around ten years for full implementation in the PRC; and (2) “Golden Tax Project” is a nationwide project for the computerisation of the tax collection system in the PRC, the Directors consider it very unlikely that the entire “Golden Tax Project” will be completed in the short run.

(e) *The mini-printers market in China*

The “mini-printer” is the small and portable printer used as a peripheral for tax control ECR and other POS devices for printing sales receipt in roll paper. In general, mini-printers can be categorised into two main areas according to the technology utilisation, namely, SDM mini-printer and thermal mini-printer.

CCW Research predicted in its report in March 2005 that, the outlook for the mini-printers market over the next few years is optimistic and the market demand for mini-printers will benefit from the commencement of the third phase of the “Golden Tax Project”. CCW Research projected that the market demand for mini-printer in China will reach approximately 494,100 units in 2008.

The following table shows the projected market demand for mini-printers in China from 2005 to 2008.

Year	Mini-printers (thousand units)	YoY (%)
2005	25.2	—
2006	325.1	1,190.1
2007	383.5	18.0
2008	494.1	28.8

Source: *China’s tax control equipment market analysis report, CCW Research, March 2005*

(II) Tax control equipment market in China

(a) *Introduction to the tax control equipment market*

The implementation of “Golden Tax Project” in China since 1994 not only has directly stimulated the demand for SDM printers in the governmental and commercial sectors in China, it has also created a sizeable market for a range of tax control equipment. In general, tax control equipment can be categorised into the following two groups:

- (1) Tax control ECRs, external tax control devices and tax control printers; and
- (2) Anti-fraud invoice printers (business tax invoice and VAT invoice).

Tax control ECR



External tax control device



Tax control printer



Anti-fraud invoice printer (VAT invoice)



Anti-fraud invoice printer (business tax invoice)



INDUSTRY OVERVIEW

Set out below is the product description for such group of tax control equipment:

Products	Product description
1 (a) Tax control ECR	An electronic cash register which can be utilised for (1) cash transaction management; (2) invoice printing through built-in mini-printer; (3) invoice data recording through its tax monitoring black box; and (4) transmission of invoice data to the regulatory tax control invoice issuing system operated by China tax authority, through its built-in modem
(b) External tax control device	An external device which is used for (1) invoice data recording through its tax monitoring black box; and (2) transmission of invoice data to the regulatory tax control invoice issuing system operated by China tax authority, through its built-in modem
(c) Tax control printer	A printer which can be utilised for (1) invoice printing; (2) invoice data recording through its tax monitoring black box; and (3) transmission of invoice data to the regulatory tax control invoice issuing system operated by China tax authority
2 (a) Anti-fraud invoice printer (VAT invoice)	An SDM printer which is used for printing VAT invoice in accordance with the encryption requirements under the “anti-VAT-fraud monitoring system”
(b) Anti-fraud invoice printer (business tax invoice)	An SDM printer which is used as a peripheral for external tax control devices for printing business tax invoices.

(b) *The market for tax control ECRs, external tax control devices and tax control printers in China*

Before the publication of the “Notice on the Strengthening of Monitoring and Controlling Tax Sources by Promoting the Application of Cash Registers for Tax Control Purposes” 《關於推廣應用稅控收款機加強稅源監控的通知》 in April 2004, the application of tax control ECRs, which is also known as the third phase of the “Golden Tax Project”, was only on trial run in 42 selected cities in China. Compared with the second phase of the “Golden Tax Project” which aimed at preventing and combating theft, fraud and other criminal activities related to VAT in China, the State Administration of Taxation puts more emphasis on strengthening its control on (1) the issuance of business tax invoices and (2) the collection of business taxes at both the state and local government level through the application of tax control ECRs, external tax control devices and tax control printers.

According to the “China’s tax control equipment market analysis report” issued in March 2005 by CCW Research, it is expected that the market for tax control ECRs, external tax control devices and tax control printers will develop very quickly after the commencement of the third phase of the “Golden Tax Project”. CCW Research projected that the demand for tax control ECRs, external tax control devices and tax control printers in China will reach approximately 1.8 million units in 2006 with a sales volume of approximately RMB5.4 billion, compared to approximately 150,200 units in 2005 with a sales volume of approximately RMB423 million.

INDUSTRY OVERVIEW

The following tables show the projected market demand for tax control ECRs, external tax control devices and tax control printers in China from 2005 to 2008.

The projected market demand for tax control ECRs, external tax control devices and tax control printers from 2005 to 2008 (in thousand units)

Year	Tax control ECRs	External tax control devices	Tax control printers	Total	YoY (%)
2005	72.0	77.3	0.9	150.2	—
2006	928.7	687.3	166.3	1,782.3	1,086.6
2007	1,095.7	728.8	186.9	2,011.4	12.9
2008	1,411.7	716.9	223.5	2,352.1	16.9
Total	3,508.1	2,210.3	577.6	6,296.0	—

Source: *China's tax control equipment market analysis report, CCW Research, March 2005*

The projected market demand for tax control ECR, external tax control devices and tax control printers from 2005 to 2008 (in RMB million)

Year	Tax control ECRs	External tax control devices	Tax control printers	Total	YoY (%)
2005	269	151	3	423	—
2006	3,480	1,340	532	5,352	1,165.3
2007	4,128	1,421	598	6,147	14.9
2008	5,295	1,398	715	7,408	20.5
Total	13,172	4,310	1,848	19,330	—

Source: *China's tax control equipment market analysis report, CCW Research, March 2005*

As illustrated above, the demand for tax control equipment is expected to grow significantly after the commencement of the third phase of the “Golden Tax Project” in the second half of 2005.

(c) *Anti-fraud invoice printers (VAT invoice and business tax invoice) market in China*

(i) *Anti-fraud invoice printers (VAT invoice) market*

As mentioned before, the primary purpose for the second phase of the “Golden Tax Project” is the prevention and combating of theft, fraud and other criminal activities related to VAT, especially the issuance of VAT invoices by general VAT taxpayers in China.

In China, general VAT taxpayers mainly refer to enterprises whose annual taxable sales value exceeds RMB1 million (for enterprises engaged in the production of goods or the provision of taxable services) and RMB1.8 million (for enterprises engaged in wholesale or retail businesses). Under the second phase of the “Golden Tax Project”, general VAT taxpayers are required to install the “anti-VAT-fraud monitoring system” to issue computerised VAT invoices through anti-fraud invoice printers (VAT invoice). According to CCW Research, there were approximately 1.8 million general VAT taxpayers who installed the “anti-VAT-fraud monitoring system” at the end of 2004.

INDUSTRY OVERVIEW

CCW Research predicted that the outlook for the anti-fraud invoice printers (VAT invoice) market in China over the next few years is optimistic as the number of general VAT taxpayers in China will continue to grow in view of continue growth of the PRC economy continues and that the relevant tax authorities in China have adopted a policy to lower the classification requirement for general VAT taxpayers. CCW Research projected that the market demand for anti-fraud invoice printers (VAT invoice) in China will reach approximately 279,300 units in 2008.

According to the “China’s tax control equipment market analysis report” issued in March 2005 by CCW Research, Jolimark was ranked as the largest domestic brand and the second largest provider of anti-fraud invoice printers (VAT invoice) in China in terms of unit shipment during 2004.

The following table shows the projected market demand for anti-fraud invoice printers (VAT invoice) and anti-fraud invoice printers (business tax invoice) in China from 2005 to 2008.

Year	Anti-fraud invoice printers (VAT invoice)	YoY (%)	Anti-fraud invoice printers (business tax invoice)	YoY (%)
	(thousand units)		(thousand units)	
2005	232.9	—	69.6	—
2006	255.9	9.9	618.6	788.8
2007	286.6	12.0	655.9	6.0
2008	<u>279.3</u>	<u>(2.5)</u>	<u>645.2</u>	<u>(1.6)</u>
Total	<u><u>1,054.7</u></u>	<u><u>—</u></u>	<u><u>1,989.3</u></u>	<u><u>—</u></u>

Source: China’s tax control equipment market analysis report, CCW Research, March 2005

(ii) Anti-fraud invoice printers (business tax invoice) market

According to CCW Research, the size of invoices printed by mini-printers or tax control ECRs cannot meet the specific requirements for certain industries in China, for example, transportation and service sectors. As a result, users in these industries must install an external tax control device along with an anti-fraud invoice printers (business tax invoice) to satisfy the requirement of the third phase of the “Golden Tax Project”.

According to the “China’s tax control equipment market analysis report” issued in March 2005, CCW Research predicted that the demand for anti-fraud invoice printers (business tax invoice) will grow substantially in 2006 due to the launch of the third phase of the “Golden Tax Project” in the second half of 2005. In 2006, demand for anti-fraud invoice printers (business tax invoice) is expected to reach approximately 618,600 units. In 2008, the demand for anti-fraud invoice printers (business tax invoice) is expected to further increase to approximately 645,200 units.

(III) Projectors market in China

A projector is a device that integrates a light source, optics system, electronics and display for the purpose of projecting an image from a computer or video device onto a wall or screen for large image viewing. In terms of the technology utilised, projectors fall into the following two main categories:

Liquid Crystal Display (LCD):

LCD projectors control colors through three panels. The features of LCD projectors are superior color saturation and greater light efficiency.

Digital Light Processing (DLP):

DLP projectors use a single chip with thousands of micro mirrors to modulate the lamp's light and to project it through the lens. The features of DLP projectors are that they have good black-level performance and are smaller and lighter in size than LCD projectors.

According to data released by CCID, an IT consulting institution in China, in April 2004, the sales of projectors in China achieved a remarkable growth in 2003. The sales of projectors market increased by approximately 32.7% from approximately RMB2,750 million in 2002 to RMB3,649 million in 2003. In terms of unit sales, the projectors market in China increased by approximately 61.0% from approximately 101,398 units in 2002 to 163,200 units in 2003.

CCID predicted the outlook for the China projectors market over the next five years to be optimistic and the overall projectors market in China will reach approximately 868,000 units in 2008 with a sales volume of approximately RMB7,870 million, representing a compound annual growth rate of approximately 38.1% and 14.5%, respectively, between 2004 and 2008.

The following table shows the estimated unit sales and sales volume of projectors in China from 2004 to 2008.

Year	Unit sales (units)	Sales volume (RMB million)
2004	239,000	4,580
2005	323,000	5,420
2006	469,000	6,580
2007	655,000	7,760
2008	868,000	7,870

Source: CCID, 2004

GOVERNMENT LAWS AND REGULATIONS IN THE PRC

Government laws and regulations applicable to the Group's products

The legal framework for the production and distribution of the Group's business equipment and other tax control products is laid down by the national laws and regulations of the PRC, as well as regional laws and regulations. The principal laws and regulations applicable to the Group's operation and products in the PRC include the following:

- The Product Quality Law of the PRC (《中華人民共和國產品質量法》) promulgated by the Standing Committee of the National People's of Congress on 22nd February, 1993 regulates liability for general product quality in the interests of consumers.
- The Measures on the Management of Licences for Production of Industrial Products (《工業產品生產許可證管理辦法》) promulgated by Administration for Quality Supervision, Inspection and Quarantine (國家質量監督檢驗檢疫總局) implemented on 1st June, 2002 regulates the licensing of producing industrial products and product quality inspection.
- The regulations for Compulsory Product Certification (《強制性產品認證管理規定》) promulgated by the State Council on 1st May, 2002 covers product safety licensing and product quality certifications for products listed on the Catalogue of Products Subject to Compulsory Product Certification (《實施強制性產品認證的產品目錄》).
- In view of strengthening the monitoring of VAT collection, the State Administration of Taxation first promulgated the use of tax control ECRs in 1997 in the business service and entertainment industries. Initially the use of tax control system was implemented in Beijing, Jinan, Qingdao, Hefei, Changsha, Xian and Jiangmen in accordance with the rules and regulations set out by the local municipal governments. In 2003 the standards for tax control ECRs were laid down by the State Administration of Taxation. The regulations for the use of tax control ECRs, a category of tax control equipment in designated industries such as restaurants, entertainment and transportation industries are set out in the Notice on the Strengthening of Monitoring and Controlling Tax Sources by Promoting the Application of Cash Registers for Tax Control Purposes (《關於推廣應用稅控收款機加強稅源監控的通知》) (the "Notice"). According to the Notice, the Detailed Rules for the Implementation of the Licenses for Production of Cash Registers for Tax Control Purposes (《稅控收款機產品生產許可證實施細則》) will be formulated to allow only qualified manufacturers granted the requisite production licence to produce and distribute tax control ECRs. The Company has been advised by its PRC legal adviser that the Notice applies to mass production and distribution only and not to trial production. In addition, manufacturers obtaining the relevant production licence of tax control ECRs do not automatically have the right to distribute their products. Before a specific model of tax control ECR could be distributed in a province, autonomous region or municipality, it must be sanctioned by the relevant local government. Only specific models of tax control ECRs that are sanctioned by the local governments can be used by the end-users in those area. The Notice provides that manufacturers may decide whether to sell their tax control ECRs direct to end users or through distributors. The Group has set up joint ventures to help future distribution and liaise with the local governments so as to facilitate future applications for sanction of the Group's tax control ECRs. The Directors believe that the Group could capitalise on its joint venture partners' experience in dealing with the local governments and their local distribution network. The Notice currently does not specify and limit the types of entities that could distribute tax control ECRs, ie. there is no provision that only manufacturers can distribute such products. The Company has been advised by its PRC legal adviser that the distribution joint ventures

INDUSTRY OVERVIEW

established and manufacturers of tax control ECRs may apply for sanction of tax control ECRs by the relevant local government. Pursuant to the Notice about the Timing of Commencing Work on Cash Registers for Tax Control Purposes (《關於稅控收款機推廣應用工作啓動時間問題的通知》) and Notice of Opinions on the Application and Implementation of Cash Registers for Tax Control Purposes (《稅控收款機推廣應用實施意見的通知》), the rules and regulations on the production licence, Measures on the Management of Tax Control ECR Manufacturing Companies Qualification (《稅控收款機生產企業資質管理辦法》) (the “Measures”) was promulgated and became effective on 1st December, 2004. According to the Measures, a company first has to apply to the MII for a certificate of qualification which will only be issued after the MII is satisfied that certain criteria as set out in the Measures are met by the applicant. After the applicant obtains the certificate of qualification, it will be eligible for application for a production licence from the PRC quality inspection authorities.

Certificates, permits and licences for the Group’s operation and manufacturing business in the PRC

The following certificates, permits and licences from the relevant government authorities are required by the Group to manufacture and distribute its products:

1. a Licence for Manufacturing Industrial Products (《工業產品生產許可證》) issued pursuant to the Measures on the Management of Licences for Manufacturing Industrial Products (《工業產品生產許可證管理辦法》);
2. the China Compulsory Certification (《國家強制性產品認證證書》) issued pursuant to the Regulations for Compulsory Product Certification (《強制性產品認證管理規定》);
3. an Automatic Import Permit for Electrical and Mechanical Products (《機電產品自動進口許可證》) issued pursuant to the Measures on the Management of Import of Electrical and Mechanical Products (《機電產品進口管理辦法》);
4. an Export Quality Permit (《出口質量許可證》) issued pursuant to the Measures on the Management of Quality Permits for Export of Electrical and Mechanical Products (《出口機電產品質量許可證管理辦法》);
5. a Certificate of Quality for Explosion-proof Purpose (《防爆合格證》) issued pursuant to the Detailed Rules for the Implementation on the Replacement (Issuance) of the Licences for Production of Explosion-proof Electrical Products (《防爆電氣產品生產許可證換(發)證實施細則》);
6. According to the Detailed Rules for the Implementation on the Licences for Production of Cash Registers for Tax Control Purposes (《稅控收款機產品生產許可證實施細則》) to be promulgated, production of tax control ECR will only be allowed upon the issuance of a License for Production of Cash Registers for Tax Control Purposes (《稅控收款機產品生產許可證》).

The Group has obtained all the certificates, permits and licences mentioned above (except the Licence for Production of Cash Registers for Tax Control Purposes) for the manufacture and distribution of the Group’s products. All of such certificates, permits or licences obtained are valid and effective. According to the Notice about the Timing of Commencing Work on Cash Registers for Tax Control Purposes (《關於稅控收款機推廣應用工作啓動時間問題的通知》) and Notice of Opinions on the Application and Implementation of Cash Registers for Tax Control Purposes

INDUSTRY OVERVIEW

(《稅控收款機推廣應用實施意見的通知》) promulgated by the State Tax Administration, Kongyue Information has applied to the MII in June 2004 for their inspection of its qualification for producing tax control ECRs in preparation for the application for the production licence.

Kongyue Information submitted the formal application for the licence for production of tax control ECRs to Guangdong Information Industry Bureau (“GIIB”) (廣東省信息產業廳) on 15th December, 2004. From the letter issued by GIIB to the Information Industry Department (信息產業部) on 31st December, 2004, it was stated that after preliminary review of the application of Kongyue Information and three other companies by GIIB, GIIB was satisfied that Kongyue Information and the other three companies complied with the requirements for production of tax control ECRs in principle and recommended that licences be granted to them. According to the announcement issued by Ministry of Information Industry on 4th April, 2005, Kongyue Information is one of the manufacturers that have complied with the requirements for production of tax control ECRs. It is expected that the production licence will be granted to Kongyue Information within the third quarter of 2005.

Notwithstanding the fact that the application for production licence is in progress, apart from the manufacturing of Jolimark branded tax control ECRs on trial run basis and manufacturing of tax control ECRs for other third parties on an OEM basis before the promulgation of the Notice, the Group is not allowed to produce tax control ECRs for distribution on a mass production basis and no such mass production has commenced. The Group has been advised by its PRC legal adviser that there appears no legal impediment for Kongyue Information to obtain such licence production according to the current laws and regulations.

Generally, a company incorporated in the PRC may only carry on the business of distributing products not manufactured by it, if and to the extent such business activity is specified in the scope of business shown on its business licence. The Administrative Rules of the PRC governing the Registration of Corporate Legal Representatives (《中華人民共和國企業法人登記管理條例》) and the Administrative Measures on the Administrative Rules of the PRC governing the Registration of Corporate Legal Representatives (《中華人民共和國企業法人登記管理條例施行細則》) require that an enterprise engages only in its registered scope of business.

The Measures on the Trial of Foreign Investment in Merchandising Enterprises (《外商投資商業企業試點辦法》) (the “Trial Measures”) promulgated on 25th June, 1999 sets out the regulatory framework for the establishment of foreign invested companies which engage in trading activities. Under the Trial Measures, WFOEs may not engage in such activities. They further provide that foreign invested commercial enterprises established in the PRC to carry on businesses which are specified in their business licences. The range of business activities in which foreign invested enterprises may engage have been and still are subject to certain restrictions.

The Guideline Catalogue of Foreign Investment Industries (the “Catalogue”) (外商投資產業指導目錄) promulgated in 2004 provides for the opening up to foreign invested enterprises of sales agency and wholesale of goods (other than those manufactured by the enterprise itself). The Catalogue provides that (i) enterprises having not more than 50% foreign investment; (ii) enterprises which are controlled by foreign investors and (iii) WFOEs, may from 11th December 2004 be authorised to engage in such activities. With effect from 1st June, 2004, the Trial Measures were replaced by Administrative Measures on Foreign Investment in Merchandising Area (《外商投資商業領域管理辦法》) which allowed foreign enterprises not engaged in trading business, to engage in sales agency and wholesale of goods by changing the scope of business in their business licence accordingly.

INDUSTRY OVERVIEW

Two subsidiaries of the Company, Kongyue Information and Kongyue Jolimark had engaged in the distribution of SDM printers, which were not manufactured by them, when such distribution activities were not specified in their business licences. The Group had relied on The Notice for the Retransmission of the Report of the City Industrial and Commercial Administrative Bureau on the Improvement of Management of Industrial and Commercial Administration and Support of Reform and Open Policy to Enhance Economic Development (the “Notice for Retransmission”) (《轉發市工商局關於改進工商行政管理工作支持改革開放促進經濟發展的報告的通知》) issued by the Jiangmen City People’s Government on 1st September, 1992 pursuant to which the Group understood that foreign investment enterprises registered within Jiangmen City are permitted to engage in the sale of their products designated for domestic sale and similar products manufactured by other enterprises. It only subsequently came to the Directors’ knowledge (in the course of the preparation for the listing of the Shares) that the Notice for Retransmission was inconsistent with the then PRC national laws described above.

During the Track Record Period, the Group distribution activities involved the sales of Epson branded SDM printers not manufactured by the Group and the turnover arising from the distribution of such products amounted to approximately RMB142.5 million, RMB181.0 million and RMB242.6 million respectively. However, upon application of Kongyue Information, it has in September 2004 received the approval for an expanded scope of business which includes distribution and provision of after sales services for electronic products of other companies (excluding restricted products). The products distributed by the Group are not restricted products. On 8th September, 2004, each of Kongyue Information and Kongyue Jolimark was fined RMB5,000 by Jiangmen City Industrial and Commercial Administrative Bureau which confirmed that no further penalty will be imposed and the business licences of Kongyue Information and Kongyue Jolimark will not be revoked, provided in the case only of Kongyue Jolimark, it refrains from further distribution activities before it obtains a business licence which allows it to do so. The Company has been advised by its PRC legal adviser that Jiangmen City Industrial and Commercial Administrative Bureau is the administering authority that has jurisdiction over Kongyue Information and Kongyue Jolimark. Since the bureau has already imposed a penalty on Kongyue Information and Kongyue Jolimark, the Company has been advised by its PRC legal adviser that according to the principles and implementation of the PRC Administrative Penalty Law (《行政處罰法》), Kongyue Information and Kongyue Jolimark will not be penalised again by the Industrial and Commercial Administrative Bureau.

The Group has taken measures to prevent similar breaches in future. Kongyue Information has obtained in September 2004 the approval from the Guangdong Province Foreign Trade and Economic Cooperative Bureau to extend its business scope to include distribution and provisions of after sales services of other companies’ information electronic products under the Foreign Investor Business Management Measures (《外商投資商業領域辦法》) implemented in June 2004. This allows Kongyue Information to engage in the distribution of information electronic products produced by other companies. Kongyue Jolimark has issued a confirmation on 9th September, 2004 to Jiangmen City Industrial and Commercial Administrative Bureau that before its business scope is extended and approved by the relevant authority, it will not engage in distribution and provisions of after sales services of other companies’ electronic products. In December 2004, Kongyue Jolimark has applied to relevant authorities to expand its business scope in order to engage in distribution and provisions of after sales services for other electronic companies’ electronic products. On 14th March, 2005, Kongyue Jolimark obtained the approval for an expanded scope of business from Jiangmen City Industrial and Commercial Administrative Bureau.