中软国际

CHINASOFT INTERNATIONAL LIMITED

中軟國際有限公司*

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 8216)

ANNUAL RESULTS ANNOUNCEMENT FOR THE YEAR 2006

CHARACTERISTICS OF THE GROWTH ENTERPRISE MARKET ("GEM") OF THE STOCK EXCHANGE OF HONG KONG LIMITED (THE "STOCK EXCHANGE")

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This announcement, for which the directors ("the Directors") of Chinasoft International Limited (the "Company" and, together with its subsidiaries, the "Group") collectively and individually accept full responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (the "GEM Listing Rules") for the purpose of giving information with regard to the Company. The Directors, having made all reasonable enquiries, confirm that, to the best of their knowledge and belief:– (1) the information contained in this announcement is accurate and complete in all material respects and not misleading; (2) there are no other matters the omission of which would make any statement in this announcement misleading; and (3) all opinions expressed in this announcement have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

* *For identification purpose only*

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Six Years Financial Summary

RESULTS

	For the year ended 31 December					
	2001	2002	2003	2004	2005	**2006**
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	**RMB'000**
Turnover	53,264	114,485	166,055	293,896	382,275	**355,236**
Profit(loss) before taxation	20,474	22,857	30,798	39,052	48,714	**(51,972)**
Taxation	–	–	(2,735)	(3,841)	(5,718)	**(11,881)**
Profit(loss) for the year	10,474	22,857	28,063	35,211	42,996	**(63,853)**
Attributable to:						
Equity holders of the parent	8,899	19,409	23,953	32,205	39,656	**(66,593)**
Minority interests	1,575	3,448	4,110	3,006	3,340	**2,740**
	10,474	22,857	28,063	35,211	42,996	**(63,853)**
Dividend	–	5,406	–	6,784	7,394	**18,309**

ASSETS AND LIABILITIES

	At 31 December					
	2001	2002	2003	2004	2005	**2006**
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	**RMB'000**
Total assets	73,232	96,898	183,117	331,325	438,765	**661,221**
Total liabilities	(12,210)	(19,386)	(42,824)	(131,930)	(129,730)	**(427,566)**
	61,022	77,512	140,293	199,395	309,035	**233,655**

Notes:

1. The results for each of the two years ended 31 December 2001 and 31 December 2002 were extracted from the prospectus of the Company dated 10 June 2003.

2. Assets and liabilities of the Group as at 31 December 2001 and 2002 were extracted from the prospectus of the Company dated 10 June 2003.

3. Loss attributable to Equity holders of the parent of RMB66,593,000 for year 2006 was due to two exception items which include 1) Loss arising from changes in fair value of redeemable convertible preferred shares of RMB110,558,000 and 2) Redeemable convertible preferred shares issue expenses of RMB10,764,000. If the above two exceptional items were added back, there should be profit attributable to Equity holders of the parent of RMB54,729,000.

Milestones 2006

January	• undertook the development project of application software for the re-engineering process of tobacco production and operation decision system of the tobacco industry by Guangdong Zhongyan Industrial Company
February	• The first phase of the "e-Audit Project" expanded into Sanya of Hainan
March	• Secured the "bar-coding cigarettes by carton and order collection system project from the State Tobacco Control bureau • Undertook the first phase of the tobacco industry market monitoring system project • Undertook the development project of application software for the re-engineering process of tobacco production and operation decision system of the tobacco industry by Guangdong Zhongyan Industrial Company • Entered into contract in respect of the feasibility study report on the phase 1 of the "e-Farming" project so as to expand in the software market for "e-Farming" • The first phase of "e-Audit" project expanded into Shenzhen of Guangdong, Anyang of Henan and Dalin of Liaoning
April	• Launched the maintenance of phases 1 and 2 of the "tobacco production and operation decision system of the tobacco industry" • Undertook the development of "Social Insurance Intranet Audit Software" for the Audit Bureau of Qingdao City • Phase 1 of the "e-Audit" project expanded to the Audit Bureau of Changning District, Shanghai
May	• Phase 1 of the "e-Audit" project expanded to the Audit Bureau of Hongkou District, Shanghai • Successfully acquired the entire interests in Powerise International
June	• Phase 1 of the "e-Audit" project expanded to Hunan Province • Started planning for phase 1 of the provincial "e-Audit" project for the Audit Bureau of Sichuan Province • Secured the further development of the analyzing capability of the State Audit Bureau's AO2005 version software • Initiated the promotion and implementation o the "bar-coding cigarettes by carton and order collection system" of the State Tobacco Control Bureau, covering 15 provinces and cities in the first phase • Secured the industry data application and economic operation analysis platform project

Milestones 2006

June

- Undertook the development of the statistics merge module of the "tobacco production and operation decision system of the tobacco industry"
- Successfully acquired 50% of the equity interest in Cyber Resource
- Successfully acquired the Microsoft outsourcing business of Opportune Technology
- Established a subsidiary in the United States

July

- Entrusted to develop Version AO2007
- Our management system deployment, implementation and services contracts were examined by Shenyang Municipal Bureau of audit
- OA deployment was audited by Shaoxing, Zhejiang Province

August

- Undertook to develop the "tobacco sales management system of the decision-making management system" for tobacco production and operation of 紅塔集團 (Pagoda Group)
- Undertook to develop the "tobacco business management and information system" for Tibet Autonomous Region Tobacco Monopoly Administration (Company)
- Shanghai Municipal Bureau of Audit OA deployment (Songjiang)
- Wenzhou Municipal Bureau of Audit OA deployment
- Department of Audit of Henan Province OA deployment

September

- The "bar-coding cigarettes by carton and order collection system" project of the State Tobacco Control Bureau was approved after discussion and evaluation by experts
- Won the Tender for Tobacco Industry Applications Integrated Service Project of Liaoning Province
- Won the Tender for Data Centre System for Tobacco Monopoly Administration (Company) of Yunnan Province
- Our management system (local version) deployment, implementation and services contracts were examined by Dali Municipal Bureau of audit
- OA deployment was audited by Simao
- OA deployment was audited by Huzhou, Zhejiang Province
- OA deployment was audited by Kaifeng, Henan Province

Milestones 2006

September	• Our management system deployment was examined by Audit Department of Hainan Province • Our management system deployment was examined by Nanchang Municipal Bureau of Audit • Our management system deployment was examined by Chongqing Municipal Bureau of Audit • Incorporated "中軟海晟信息技術有限公司" in Fujian Province
October	• Signed with Shanghai Tobacco (Group) the application expansion project of the barcoding cigarettes by carton and decision making system • Won the tender for the upgrading project of product digital tracking system for Guizhou Huangguoshu Tobacco Group Company • Undertook the group model upgrading project for Zhejiang Zhongyan Industrial Company • Undertook the group model upgrading project for Chuanyu Zhongyan Industrial Company • Our management system deployment, implementation and services were examined by Department of Audit of Heilongjiang Province • Bureau of Audit of Jiaxing, Zhejiang Province OA deployment • Bureau of Audit of Ningbo, Zhejiang Province OA deployment • Bureau of Audit of Huangpu District, Shanghai OA deployment
November	• Upgrading project of tobacco calling center of Anhui Province • Bureau of Audit of Changzhi, Shanxi Province OA deployment • Bureau of Audit of Jincheng, Shanxi Province OA deployment • Bureau of Audit of Zhoushan, Zhejiang Province OA deployment • Harbin Municipal Bureau of Audit OA deployment • Bureau of Audit of Yangquan, Shanxi Province OA deployment • Bureau of Audit of Daqing, Heilongjiang Province OA deployment • Foshan Municipal Bureau of Audit OA deployment • Bureau of Audit of Nanyan, Henan Province OA deployment • Anhui CIQ Inspection and Quarantine Ta Tong Guan Platform 2006

Milestones 2006

December

- Signed the project of developing social insurance fund monitoring software for the e-Insurance project
- Signed the project of the central budgeting department implementing intranet audit
- Signed the project of foreign audit software development and services
- Department of Audit of Anhui Province (OA deployment throughout the province)
- Fuzhou Municipal Bureau of Audit OA deployment
- Department of Audit of Guizhou Province OA deployment
- Chengdu Municipal Bureau of Audit OA deployment
- Our management system deployment, implementation and services were examined by Bureau of Audit of Shangqiu, Henan Province
- Our management system deployment, implementation and services were examined by Dalian Municipal Bureau of Audit
- Districts and counties of Hongkou District, Shanghai realized intranet audit
- Phase 1 of “e-Audit” project“ was awarded the prize of 2006 China Informatized Construction Project by China IT Fortune Annual Conference and China Information Supervisor Annual Conference
- Recognized as Key Software Enterprise 2006 within State Planning by National Development and Reform Commission, the Ministry of Information Industry, the Ministry of Commerce and the State Administration of Taxation
- Awarded by Deloitte as one of the ”500 Fastest Growing Hi-tech Enterprises in Asia Pacific 2006“ for the second time

Managing Director's Report

REVIEW

The year 2006 marked the third year of the Company's listing, and also a year of setting further milestones for Chinasoft. During the past year, the Company's business kept growing at high speed with significant increase in market capitalization, better coordination among the management team, rapid expansion of its work force, all led to the nourishment of more sophisticated corporate culture.

To begin, I would like to share with our shareholders some of the admiring financial and operating performance of the Group in 2006:

For the year ended 31 December 2006, turnover of the Group amounted to RMB355,236,000, discounting the impact of the redeemable convertible preferred shares of RMB121,322,000 due to adjustment of the financial standards, profit attributable to shareholders was RMB54,729,000, an increase of 38% over the previous year, earnings per share were 32% higher to reach RMB0.0733.

During the reporting period, the Group moved forward in full scale its major service-oriented business strategy, focusing on advisory service and offering solutions to its domestic clients, as well as software service outsourcing catered for multi-national corporations. This strategy has secured the continual stable growth of the Company's business turnover, and in terms of revenue structure, revenue from multi-national corporations has now accounted for almost half of the Company's turnover.

During the reporting period, the Group continued to leverage on its integrated strength in advisory and solutions business accumulated over the years and its advanced core technological capabilities, consolidated its position in an industry it has already had a competitive edge and expanded its market share in order to leave its competitors further behind. As we have maintained stable relationship with our clients, we also gained more trust from them which enabled us to secure their contracts in key projects. The result was that we have reinforced our leading position in the industry so we can spare more efforts in developing new clients and diversify into other relevant businesses while maintaining our share of the established market. This new business approach was proved successful, client concentration was obviously reduced and business revenue structure was more healthy. The Group now plays a more important role in the trade for others to follow suite.

During the reporting period, the Group grasped the good opportunity offered by multi-national corporations in seeking Chinese vendors for their software service outsourcing business. Targeting at the business of its strategic clients, the Group has started with acquiring the sophisticated outsourcing management models and established a qualified outsourcing team. The Group has now become a pioneering enterprise in the software service outsourcing market. Through the provision of quality all-rounded services to a number of multi-national corporations, the Group could satisfy in full the stringent demands of its clients from cultural, management process and regulation in every of its operating units, which promoted to a large extent the internationalization process of the Company.

Managing Director's Report

During the reporting period, the Group established the Chinasoft International training base to transform its training business towards employment training. The Group has built up close cooperation relation with more than 40 higher education institutions in China to enroll postgraduate and undergraduate students for field training. Through these practical training at the Chinasoft training base, it can provide direct training to talents that are needed in the real commercial world. Such move would ensure that the Company has sufficient supply of new technical staff and their quality in an industry with rapidly rising demand for software outsourcing professionals; at the same time, the Group can build up its professional and market leader image among various education institutions and the pool of potential software talents.

During the reporting period, the Group speeded up the progress in mergers and acquisitions. To expand its overseas business, the Group acquired the Japanese customer outsourcing business of Powerise International, making its successful venture into the Japanese market and effectively adjusted the overall outsourcing business structure of the Group. Furthermore, the Group also took a series of tactical moves in the acquisition of some of its strategic clients, such as the purchase of the Microsoft outsourcing business of Oppertune Technology and increasing its stake in Cyber Resource. By way of organic growth combined with mergers and acquisitions, the Group has formed a solid foundation for sustained growth with stability in development while maintaining its rapid expanding business network. In short, the Company's strategic business scale is taking shape.

PROSPECTS

The software service industry is developing rapidly in China which is taken by the Group as a golden opportunity for its future development. The Company hopes that in around three years' time, it can become the most established software service enterprise based in China with clients all over the world, an enterprise most attractive to the market and offering true value for investment.

The prime objective of the Group in 2007 is to achieve its strategic business scale, establish itself as a service platform based in China and servicing the world which covers five major countries and regions, and more than 10 key cities in China with staffing of about 5,000. It plans to provide all-rounded services in the industry including ITO, BPO and end-to-end solutions.

The Group will continue to maintain its leading position in the technically advanced industry while expanding into new businesses with an edge, aiming at securing its position as the top information service provider in China. To this end, the Group will focus on both the domestic and overseas markets and accelerate its pace of internationalization, so that it can ultimately become the preferred software service outsourcing provider for multi-national corporations in China.

The Group will further strengthen the development of its existing business with stable growth. At the same time, it will speed up the mergers and acquisitions of other software service enterprises in the market which offer good investment potential and fit in the Company's strategic development. Through effective business integration, utilization of competitive strengths and harmonizing the different corporate cultures, the core competitiveness of the Group will be enhanced. The year 2007 is a year with great expectation for us. Let's continue to strive for progress and achieve our goals.

Managing Director's Report

APPRECIATION

I would like to take this opportunity to extend my sincere gratitude to all of you for your understanding and support over the past year; to our shareholders who render us strength for growth of the Group, our clients who create the room for our continued development, our business partners for their cooperation as well as all members of staff for their dedicated work and contribution.

Dr. Chen Yuhong
Managing Director

Beijing, The PRC
30 March 2007

Management Discussion and Analysis

FINANCIAL REVIEW

The Management would like to draw our shareholders and potential investors attention to the reason why there was a great deviation of Unaudited Profit attributable to Shareholders of RMB39,974,000 for the nine months ended September 30, 2006 and the Audited Loss attributable to Shareholders of RMB66,593,000 for the year ended December 31, 2006 was mainly due to an amount of RMB110,558,000 of Fair value loss on derivative liability of the Redeemable Convertible Preferred Shares of USD20Million issued to both Microsoft and International Finance Corporation on January 6, 2006 and another amount of RMB10,764,000 of Redeemable convertible preferred share issue expenses.

On January 6, 2006, the Group issued USD20million Redeemable Convertible Preferred Shares of HKD0.10 each at a conversion price of HKD0.80 per share from date of issue to the sixth anniversary of the First closing date (i.e. January 6, 2006) unless earlier redeemed or converted into Ordinary Shares.

As the functional currency of the Group is RMB and the issuance of the Redeemable Convertible Preferred Shares were in USD, our Auditor is in the view of the Redeemable Convertible Preferred Shares are a Financial Instrument rather than Equity Instrument and therefore, the Auditor has applied Hong Kong Accounting Standard 39, HKAS39, "Financial Instruments: Recognition and Measurement".

Under the Hong Kong Accounting Standard 39 (“HKAS39”), if the convertible bond is denominated in a currency other than the functional currency, the conversion option is required to be stated at fair value and the resulting change in the fair value would have an impact on the income statement. The change in value of the conversion option is principally affected by the price and the volatility of the stock.

For instance, if the stock performance of the Company is good and the stock price exceeds the conversion price, a loss would occur, notwithstanding the fact that the change in value of the conversion right does not affect the cashflow or adversely impact the overall financial position of the Company.

The Management are concerned that the accounting treatment as prescribed under HKAS39 may not fairly present the operating results of the Company and the Group for the year, its adoption has been necessary in order to fully comply with the prevailing accounting standards, thus avoiding a qualified opinion on the financial statements by the auditors.

Given the above reasons, the management has done an analysis of Profit excluding the exceptional items (see below table). Excluding the exceptional items, profit attributable to equity holders of the company increased by 38% to RMB54,729,000 as compared to last year.

Management Discussion and Analysis

ANALYSIS OF PROFIT EXCLUDING EXCEPTIONAL ITEMS

	2006	2005
	RMB'000	RMB'000
As reported	**(66,593)**	39,656
Exceptional items		
Add: Effect of adoption of HKAS 39 in relation to redeemable convertible preferred shares	**110,558**	–
Issue expenses for redeemable convertible preferred shares	**10,764**	–
Adjusted profit attributable to equity holders of the Company	**54,729**	39,656

Besides, shareholders and investors should draw attention on two special non cash items before the Profit from Operation which include 1) Rmb 8,364,000 of Amortisation of intangible assets and trademark use right (Please refer to Note 14 of the notes to the Accounts for the breakdown) and 2) Rmb 1,087,000 of Impairment loss recognized in respect of technical expertise. Out of Rmb8,364,000 of Amortisation of intangible assets and trademark use right, there was Rmb1,223,000 of amortization of Technical expertise. As for the Technical expertise, both are related to the Group acquisition of the technical expertise of Powerise and Opportune Technology during the year (Please refer to Note 32 of the notes to the Accounts for the details).

For the fiscal year ended December 31, 2006, the Company reported a total turnover of approximately RMB355,236,000 and net loss attributable to shareholders of approximately RMB66,593,000 (for your reference: Net profit attributable to shareholders excluding exceptional items of approximately RMB54,729,000) as compared to a turnover of approximately RMB382,275,000 and net profit of approximately RMB39,656,000 in 2005, representing a decrease of about 7% for the Turnover and an increase of about 38% for the Net Profit attributable to shareholders excluding exceptional items compared to Net Profit attributable to shareholders in 2005.

Loss per share is approximately RMB0.0891 and Earning per share based on Net Profit attributable to shareholders excluding exceptional items is approximately RMB0.0732.

Net assets per share of the Group is approximately RMB0.31.

Management Discussion and Analysis

ANALYSIS OF TURNOVER

The turnover of the Group for the year ended 31 December 2006 can be classified by categories of services and products:

(1) Products Segment

	2006		2005		
	Turnover RMB'000	**Portion**	Turnover RMB'000	Portion	Increase (decrease) in turnover %
Solutions	**193,513**	**55%**	301,075	79%	(36)%
IT Outsourcing	**127,821**	**36%**	53,034	14%	141%
IT Consulting and Training Services	**12,184**	**3%**	7,552	2%	61%
Sale of Standalone Software and Hardware Products	**21,718**	**6%**	20,614	5%	5%
Total	**355,236**	**100%**	382,275	100%	7%

Note: As revealed above, the turnover of solutions businesses in 2006 was lower than that in 2005. The main reason is: in accordance with the strategic plan towards service–oriented transformation, as at the reporting period, the business focus of the Group's solutions businesses is software development and service business revenue, reducing significantly the business revenue from third party software and hardware product portfolio so as to enhance the Company's overall profit level.

(2) Geographical segment

For the year ended 31 December 2006, the turnover by geographical segment is as follows:

Geographical segment	**Revenue**	**%**
Mainland market	**263,722**	70%
European and American market	**102,191**	27%
Japanese market	**9,550**	3%
Total	**375,463**	100%

Note: During this reporting period, the Group placed great emphasis in expanding software outsourcing business, the revenue coming from overseas market, particularly the European and American market has accounted for 30% of the Company's total revenue.

Management Discussion and Analysis

RESULTS

For the year ended December 31, 2006, the Group reported a turnover of approximately RMB355,236,000, representing a decrease of 7% as compared with last year. The decrease in turnover was attributable to the business transformation of the Group as to focus on software development, IT outsourcing and BPO and reduce the portion of hardware business.

For the year ended December 31, 2006, the Group recorded a gross profit, operating profit, net profit attributable to shareholders excluding exceptional items and net loss attributable to shareholders of RMB168,898,000, RMB66,861,000, RMB54,729,000 and RMB(66,593,000) respectively (2005: RMB117,996,000, RMB48,714,000, RMB39,656,000 and RMB39,656,000, representing an increase of 43%, 37%, 38% and a decrease of 168% as compared with last year. Basic Loss per share was approximately RMB0.0891 (2005: RMB0.0556 Earnings).

The gross profit margin and the operating profit margin of the Group for the year ended December 31, 2006 was approximately 48% and 19% respectively (2005: approximately 31% and 13% respectively representing an increase of approximately 17% and 6% respectively as compared to the last year 2005. The remarkable increase in both gross profit margin and operating profit margin of the Group was attributable to the business transformation of the Group as to focus on software development and whole-range IT services provider.

In respect of professional talent, the Group employs a total of 2,382 staff, representing a significant addition of 430 staff compared to 1,952 staff in the previous quarter. The increase in headcount was mainly due to the rising number of staff in outsourcing. The Group currently has 1,329 staff being engaged in outsourcing business.

In respect of the business itself, solutions and IT outsourcing business, two of the Group's main businesses, accounted for 54% and 36% of the turnover (2005: approximately 79% and 14%).

The ratio of distribution costs to turnover was 5.8%, representing an increase of 0.8% as compared to 5% of last year since the ratio of selling expenses of software development is comparatively higher but with a higher gross profit margin. The percentage of administrative expenses to turnover was 22% representing an increase of 10% as compared to 12% of last year. With the increasing expansion in outsourcing business from average head count of 520 staff in financial year 2005 to average head count of 1,952 staff in current year and an expansion of the size of the Group's operations, the increase in administrative expenses due to the increase in IT outsourcing head count and technical support staff and increase in amortization and depreciation are reasonable. The increase is also partly attributable to the legal and consultancy fees related to acquisitions.

Management Discussion and Analysis

FINANCIAL RESOURCES AND WORKING CAPITAL

As at December 31, 2006, shareholders' funds of the Group amounted to approximately RMB233,655,000. Current assets amounted to RMB416,188,000 of which approximately RMB133,571,000 were Cash and Bank deposits. The Group had non-current liabilities including Deferred tax liabilities of RMB2,588,000 and Redeemable convertible preferred shares of RMB268,480,000 and its current liabilities amounted to approximately RMB156,498,000.

Significant Investments

Save as disclosed elsewhere on the Management Discussion and Analysis, the Group had no other significant investments held.

Acquisition and Disposal of Subsidiaries and Associated Companies

For the year ended 31 December 2006, the Group had made acquisition of the business of Powerise International Software Co. Ltd., Opportune Technology and Cyber Resources, and no material disposals of subsidiaries and affiliated companies.

Charge on Group Assets

As at 31 December 2006, there were no charges on group assets.

Future Plans for Material Investments and Expected Sources of Funding

Except in relation to the acquisition of Hinge Global Resource Group in the year of 2007, as at 31 December 2006, the Group had no future plans for material investments.

The management will continue to monitor the industry and review its business expansion plans regularly, so as to take necessary measures in the Group's best interests.

Exposure to Fluctuations in Exchange Rates

During the year ended 31 December 2006, the Group experiences only immaterial exchange rate fluctuations as most of the Group's monetary assets and liabilities are denominated in Renminbi, and the Group conducted its business transactions principally in Renminbi, which was relatively stable during the year under review. The Group considered that as the exchange rate risks of the Group is considered to be minimal, the Group did not employ any financial instruments for hedging purposes.

Capital Commitment

As at 31 December 2006, the Group have RMB1,196,000 capital expenditure contracted for but not provided in the financial statements in respect of acquisition of software.

Contingent liabilities

As at 31 December 2006, the Group did not have any material or contingent liabilities.

Management Discussion and Analysis

BUSINESS REVIEW

In the year of 2006, the Group obtained satisfactory results in each of the businesses:

Consulting and Solutions Businesses

The Group's solutions businesses have been profit-driven and target-based. During the year of 2006, the turnover from the Group's solutions businesses amounted to approximately RMB19.4 million, of which revenue from services amounted to RMB15.2 million, representing an increase of 39% when compared with 2005.

During the reporting period, by virtue of the continuous growth in consulting services and solutions businesses in Mainland China, and through deepened communication and fostering good relationship with important clients, the Group could safeguard the signing of major contracts, further enhancing its leading position in the industry. On the other hand, by leveraging on its technical expertise and resources, the Group was active in developing new businesses and identifying new clients so as to lessen its client concentration and make the revenue structure of the Company healthier.

Industry with leading position

1. Tobacco Industry

   Tobacco industry is the major industry in the Group's consulting services and solutions businesses. During the reporting period, the Group further explored the demand from the industry. While solving users' enquiries immediately, the high quality proposals offered were highly regarded by the clients, which consolidated and expanded the Group's revenue from the industry.

   What is worth mentioning is that in March 2006, the Group completed the overall acceptance inspection of phase 1 and phase 2 of the Tobacco Production and Operation Decision System for the State Tobacco Control Bureau (no.1 project). The project covered 31 provinces in the nation and more than 400 cities. Through the inspection of the no.1 project, the Group fully demonstrated the organization capability and quality management control system for large projects, realizing the effective management from aspects of quality, progress, cost control and risk management, ensuring client satisfaction and safeguarding public recognition in the industry and ultimately rewarded us with the three-phase contract of no.1 project of "Bar-coding Cigarettes by Carton and Order Collection System for the State Tobacco Bureau". This is another large project involving integrated development and portfolio implementation in national scale.

Management Discussion and Analysis

Leveraging on the thorough development of strategic partnership between the Group and the State Tobacco Control Bureau, and the successful deployment of the nation-wide platform of the tobacco industry, the Group further enhanced the cooperation with tobacco industry groups and provincial tobacco companies, enlarging the Group's market share in the regional IT service in the tobacco industry.

(1) Commissioned to develop phase 3 of "tobacco production and operation decision system of the tobacco industry" – signing of "Bar-coding cigarettes by carton and order collection system for the State Tobacco Control Bureau" and secured the promotion implementation contracts in 15 provinces.

During the reporting period, the Group launched phase 3 of the "tobacco production and operation decision system of the tobacco industry" project (that is, the "Bar-coding cigarettes by carton and order collection system for the State Tobacco Control Bureau"). Based mainly on phases 1 and 2 of the project, this phase provides more accurate and timely data to the State Tobacco Monopoly Administration. Data collection has been upgraded from box-based to carton-based. The amount of data will be multiplied by 50 times to 9 billion items. The Group expects the scale of this project to exceed the aggregate of phases 1 and 2. It plans to promote the project to 350 commercial firms, 318 warehouses and 27 provincial commercial enterprises. Promotion has been implemented in 15 provinces including Sichuan, Hubei, Yunnan, Shandong and Heilongjiang. All the promotion activities have been scheduled to be completed at the end of the next year and the project will bring about considerable revenue to the Group.

(2) Secured tobacco industry market monitoring system (phase 1) project

Since the Group succeeded in establishing "operation decision management system", the State Tobacco Control Bureau has been exploring the potential of this system. During the reporting period, the Group was also commissioned to develop "tobacco industry marketing monitoring system (phase 1) project", to expand and enhance the function of "operation and decision management system of tobacco industry". For the "tobacco industry market monitoring system project", it will establish the production cost, fee data collection and analysis system relating to the cost of tobacco leaves, and commence a development model based on the cost of tobacco leaves as well as establish an assessment system for the tobacco leave pricing policy. The Group will establish the management system of smuggled cigarettes and slow moving cigarettes based on the cigarette production operation and decision management system (including data collection, integrated enquiry and statistics analysis), realizing the integration of the existing cigarette cost data management system and cigarette production and operation management system.

(3) Undertook the development of the statistics merge application system of the "tobacco production and operation decision system of the tobacco industry"

Through the "tobacco production and operation decision system of the tobacco industry" project, the Group has finished establishing an IT application platform for integrating and transmitting data in a later stage. Therefore, the State Tobacco Control Bureau decided to commission the Group to enhance the merging of the development and statistics based on the original platform, including control of collection procedure by calling for data, reporting update and supplementary reporting and checking function at the issuance of report.

(4) Secured the tobacco industry data application and economic operation analysis platform project

With the State Tobacco Monopoly Administration's adoption and application of the "tobacco production and operation decision system of the tobacco industry", the various aspects of production, operation and management of the tobacco industry have formed a massive data collection network. Collection and processing of data at each stage of tobacco production and operation eventually led to the birth of a data center. To further analyze and apply such data, the Group has designed an "industry data application and economic operation analysis platform".

(5) Yunnan Province Tobacco Monopoly Administration (Company) Data Centre System, phase 2 of the data center system project of Guizhou Huangguoshu (Tobacco) Group Co. Ltd. and the Yunnan Pagoda data centre project

The data centre for the tobacco industry comprises three levels, which are the state bureau, provincial bureau and industrial companies and industrial and commercial enterprises at the base level, and eventually converges on the top. Under the unified administration of the data centres of the state bureau and the headquarters, the data will be integrated so that the industry information can be transmitted both bottom-up and top-down. Subject to certain rules and authorizations, information can be accessed within the industry whenever needed through the control of authorization. Industry information can therefore be exchanged horizontally and vertically.

This is where the technological advantage of the Group lies. By virtue of successful establishment of applicable platform in the industry, as well as the advantages of industry solutions in respects of data centers, BI analysis and system application integration, save as the construction projects of the above enterprises, the Group has secured sales contracts from over 10 industrial, commercial enterprises, establishing a leading position in the industry.

(6) Launched the maintenance of phases 1 and 2 of the "tobacco production and operation decision system of the tobacco industry"

Upon the full implementation of phases 1 and 2 of the "tobacco production and operation decision system of the tobacco industry" which the Group developed for the tobacco industry, the Group began, during the reporting period, to provide the tobacco industry with maintenance service and technical support for these two phases of the project with service companies within the industry in the form of service outsourcing. This marks the successful establishment of cooperation mode with users in the industry.

2. Audit Industry

Audit Industry is one of the industries which the Group possesses particular strengths. With the successful implementation of the phase 1 of "e-Audit" project", the Group has endeavored to promote the implementation deployment of audit application system throughout the nation. In 2006, the Group commenced the OA deployment work in the audit bureaus of 13 provincial departments, 86 cities and 762 counties. On the other hand, the Group has succeeded in developing the solutions in on-site audit implementation system and intranet audit system, further enriching and enhancing the Group's solutions in the audit industry and laying a good foundation for the phase 2 of "e-Audit project". During the reporting period, the audit businesses of the Group have developed steadily, the results from the regional promotion and services of phase 1 "e-Audit project" exceeded our expectation.

In the meantime, the Group has fully utilized the Know-How accumulation in the audit business sector, further motivating the expansion and development of internal audit of large enterprises in the market, including large enterprises such as PetroChina, China Telecom and China Development Bank.

(1) During the reporting period, the deployment of the phase 1 of "e-Audit project" has been fully promoted in the nation. OA system implementation deployment has been commenced in 13 provincial departments, 86 cities and 762 counties in Shanghai, Anhui and others. The projects signed all employed the on-site audit implementation system and on-site audit management system.

(2) Undertook the expansion and development of the analyzing capability of AO (Auditing Office) version and the development and services of A2007 version software (online computer portion) of the State Audit Bureau. The Group accepted the commission from the State Audit Bureau to upgrade its on-site audit implementation system originally developed by the Group, increasing its functions and application module.

(3) Signed budget execution intranet audit project for the Central government, and secured projects like "social insurance intranet audit software" of Qingdao Audit Bureau as well as the intranet audit of Hong Kou District in Shanghai

Intranet auditing is an important task of the phase 2 of "e-Audit project", allowing auditors to conduct off-site intranet audit with the internet. Intranet audit is highly efficient, cross boundary, and real-time. This will further expand the market share and business revenue of the Group.

Now that the conditions for development of the social insurance intranet audit have matured, the introduction of the country's "e-Securities Project" has proceeded quite fast. Among the 400 cities, 80 cities have utilized the "e-Securities" internet platform. The unified data management platform has also laid a strong foundation for development of the social insurance intranet audit.

Management Discussion and Analysis

Businesses under development:

During the reporting period, on the strength of the successful business mode and project experience of industries the Group has advantages and satisfaction and public recognition gained from users, the Group has further expanded into other government and large enterprise business market.

On one hand, the Group introduced matured solutions to new industries to gain new market share. On the other hand, based on its successful business model, the Group explored the business demand of the industries under development, striving for breakthroughs in new industries and business growth.

A few typical achievements are as follows,

- Starting with high-end consultancy service, the Group gained progressive achievements in the internal audit of State-owned Assets Supervision and Administration Commission, and entered into the computerized account checking system project of the supervisory committee of the State-owned Assets Supervision and Administration Commission.

- The Group made breakthrough in the social insurance industry by signing contract for the “e-Securities” social insurance fund supervisory software development project with the Ministry of Labour and Social Security Department and entered into the development service contracts of medical and social security project.

- The Group entered into the contract for preparing a feasibility report of “e-Farming project” (phase 1) for the Ministry of Agriculture. This will lay a solid foundation for the further expansion of e-Farming software market.

- Signed business platform integration and service contracts with General Administration of Quality Supervision, Inspection and Quarantine and cities and provinces like Beijing, Shanghai, Anhui, Jiangsu etc.

Software Service Outsourcing Business

The outsourcing businesses of the Group have been scale-driven and target-based. During the year of 2006, through a combination of organic growth and mergers and acquisitions, the number of staff of the Group grew rapidly from 530 at the beginning of the year to 1,329 at year end, representing an increase of 151%. Income from the outsourcing businesses of the Group also increased from RMB53 million to RMB153 million, representing an increase of 189% and accounting for 48.12% of the overall services income of the Group.

The outsourcing business section of the Group, being the transformation of business towards more service-oriented, gained much momentum during 2006, and achieved significant growth in aspects ranging from staff to business revenue. This in turn enabled us to attain scale advantage for such business, and became the leading enterprise in the software service outsourcing service market.

Management Discussion and Analysis

During the reporting year, the Group firstly strengthened the development and maintenance of strategic clients and achieved outstanding results. The Group has endeavored to foster interactive partnership with clients. Through providing service to multi-national corporations, each business unit met the demand from clients in aspects of culture, operation flow, control and business specification, effectively raising the Group's overall outsourcing service capability and enhancing the internationalization of the Company. Through a series of strategic acquisitions with strategic clients, for instance, the acquisition of the Microsoft business from Opportune Technology, the Group can offer more product types to the strategic clients and form better bonding relationship with clients.

During the reporting period, the Group has achieved long term development in enhancing the integrated service capability of the IT service outsourcing business. On one hand, through introducing overseas talents and strengthening internal training, the Group not only ensured the quality of this business, but also explored more thoroughly the clients' demand. This further expanded the business sector of the outsourcing service, for instance, obtaining test items of a higher grade, obtaining outsourcing service of integrated items, and undertaking clients' product development projects by way of Online-Lab. On the other hand, through the successful acquisition of 50% equity interest in Cyber Resources, the Group integrated and strengthened its capability in project development in IT service outsourcing sector and BPO service.

During the reporting period, the Group has also achieved groundbreaking development in expanding IT service outsourcing business and realizing global service provision. Through establishing a subsidiary in the United States, the Group further strengthened the capability in business expansion and service provision. Through effective BD organization, the Group has gained groundbreaking development in the European outsourcing business market. On the other hand, through the acquisition of Powerise International, the Group entered into the Japanese outsourcing service market, effectively adjusting the Group's outsourcing business structure, and laying an important foundation in the globalization of the Group's IT service.

Training Business

During the reporting period, the training business of the Group which have passed the mode innovation, has undergone rapid growth both in terms of scale and training capability. The Chinasoft training centre has become a base of Chinasoft International for training personnel. It not only provides larger number of ready personnel, but also Improves the Technical capabilities and project management of existing staff, so that they are able to become key personnel to fulfill any work requirements within a short period of time.

In 2006, the growth in demand for talents by software outsourcing was rapid. In order to adapt to the development strategies of the market and the Group, Chinasoft International training centre has been transformed into career training while safeguarding the traditional training business. The establishment of the practical training base of Chinasoft International indicates that the Group has established a new business mode for training business. The base has formed partnership with more than 40 universities in China. From April 2006 to end of December 2006, there were more than 600 students coming to the base for practical training. For the undergraduate and postgraduate students, Chinasoft practical training base has become a bridge linking school with software enterprise. "Chinasoft Training" has gained brand reputation in all the universities and training institutes. With this mode, the training centre not only can help foster software talents for the market, but also attract more talents to join the Group.

Acquisitions and Mergers

During the reporting period, in order to adapt to the software outsourcing market development and form a scale advantage rapidly, the Group speeded up its pace of acquisition and merger and underwent a series of acquisitions and mergers, for instance:

ACQUISITION, MERGER AND ESTABLISHMENT

Acquired the Japan operations of Powerise International

The Group entered into an agreement with Powerise Information Technology Co., Ltd. (hereinafter referred to as "Powerise") to acquire all the businesses of Powerise International Software Co., Ltd. (hereinafter referred to as "Powerise International"). The business of Powerise International came mainly from NEC, Ozburn-Hessey Logistics, NYU. Services provided by Powerise International include design/encoding/test/documentation and other services, data entry, IT consultancy, staff training and deployment of technical personnel.

The acquisition of Powerise International operations enhances our rapid expansion into the Japanese market. Powerise International has more than one hundred employees experienced in the Japanese market. Although Chinasoft International has attained great success in the European and U.S. outsourcing markets, entering the Japanese market is no doubt a complement to Chinasoft International's outsourcing operation on the whole. It marks also the expansion of Chinasoft International into the Japanese market.

Successfully acquired the Microsoft outsourcing business of Opportune Technology

The Group entered into an acquisition agreement with Opportune Technology Co. Ltd. (hereinafter referred to as "Opportune Technology") to acquire the latter's Microsoft outsourcing operation.

Opportune Technology is a company engaged in IT servicing. Its outsourcing services include localization, QA test, specified software development, mobile platform development and embedded software development. The operation that Chinasoft International acquired this time originates from Microsoft and involves a team from Opportune Technology of over 60 professionals in the above fields, being part of the acquisition.

As one of the Group's major strategic clients, Microsoft's outsourcing business has always been an important area for development by the Group. With the acquisition of Powerise International and Opportune Technology, the Group is rapidly enlarging its market share in Microsoft business.

Management Discussion and Analysis

Successfully acquired 50% of the equity interest in Cyber Resource

The clients of Cyber Resource include IBM, MOTOROLA, PANASONIC, EPSON and HP, all of them are strategic clients that the Group plans to further serve. Furthermore, the business of Cyber Resource has been growing steadily over the years. Its profit margin has remained at a comparatively high level among the industry. When compared with the Group's net profit in the same period, its net profit up to 31 December 2005 was 17.78% of the Group's. To further exploit the potential of Cyber Resource, to coordinate and plan for the Group's development in outsourcing business regarding strategic clients and to generate profit for the Group, the Group decided to increase its holding of Cyber Resource's equity interest to 76% by means of acquisition. The acquisition carries strategic meanings to the Company' s expansion in outsourcing business in addition to generating stable and long-term revenue.

Newly established companies

Established a subsidiary in the United States

The Group has established a subsidiary in the United States, Chinasoft International Inc (USA). Branches were set up in the Silicon Valley of California, the State of Washington and New Jersey. An establishment and opening ceremony for the branches was held in Redmond, Washington at the research center of one of Microsoft and Chinasoft International's strategic partners. Over 50 clients including Microsoft attended to express their congratulations.

The establishment of Chinasoft International USA demonstrates the relationship between Chinasoft International and Microsoft as well as all their strategic partners and clients around the world is further strengthened. It helps to bridge the gap between the Group and its U.S. clients. It is also part of the Group's strategy to enhance globalization and an important step towards providing world-class software service and IT solutions to clients.

Established 中軟國際(湖南)信息技術有限公司

The Group has set up 中軟國際(湖南)信息技術有限公司 for the purpose of taking over the business teams of Powerise International and continuing and developing the related businesses.

Established 中軟海晟信息技術有限公司 by way of joint venture

The Group jointly established a joint venture named 福建中軟海晟信息技術有限公司 (hereinafter referred to as "中軟海晟") with 福建海晟集團有限公司 ("中軟海晟"). 中軟海晟 is owned as to 51% by the Chinasoft International and the remaining 49% by 福建海晟.

福建海晟 is a subsidiary of Fujian Tobacco Company, which is a well-known enterprise committing to provide services to the tobacco, information technology and property industries and is relatively strong in technology and resources.

The joint venture will be mainly responsible for the research and sale of the core products that are related to the tobacco business system e-commerce overall solutions. The two parties to the investment complement each other with their own advantages through 中軟海晟 and continuously increase their market share in the market of tobacco industry business system.

This is another close cooperation with the tobacco industry following the Group's investment in the equity of Beijing China Tobacco Information Technology Company Limited (北京中煙信息技術有限公司) and the establishment of Wuhan Chinasoft International (武漢中軟國際) with Hubei Tobacco Company (湖北省煙草公司) in 2005. The relationship between the Group and its clients has been successfully developed from single direction solution sales and interactive project planning in the past to "strong-plus-strong" joint forces of today. In the future, the Group will actively strengthen its leading position in the information technology solutions market of the champion tobacco industry by focusing on in-depth market penetration.

Awards received

Recognized as outstanding software enterprise of year 2006 defined by the National Development Bureau of the PRC

With the audit and recognition jointly carried out by the National Development and Reform Commission, Ministry of Information Industry, Ministry of Commerce and State Administration of Taxation, as Chinasoft International is in compliance with the related provisions of the "Policies For Encouraging the Development of Software and Integrated Circuit Industries" and the "Most Outstanding Software Enterprise as defined by the National Development Bureau of the PRC", it has been recognized as one of the most outstanding software enterprises of 2006 as defined by the National Development Bureau of the PRC.

Named by Deloitte as one of the "500 Fastest Growing Hi-tech Enterprises of 2006 in the Asia Pacific"

During the reporting period, the Group is pleased to be named as one of the "500 Fastest Growing Hi-tech Enterprises of 2006 in the Asia Pacific". Chinasoft International has been named in the list for two consecutive years so far, and has been recognized by the peers in the industry as one of the hi-tech companies with the highest growing rate in the Asia Pacific region.

HUMAN RESOURCES

As at 31 December 2006, the Company had a total of 2,382 employees, 1,827 of whom have a bachelor degree. For the year ended 31 December 2006, the total staff cost paid by the Company to its staff was approximately RMB 87,200,000 (2005: approximately RMB 61,894,000).

A breakdown of the number of employees of the Company as at 31 December 2006 and 2005 was as follows:

Departments	**2006**	2005
Management	**170**	42
Finance and administration	**71**	55
Research and development	**2,035**	795
Sales, technical support and marketing	**106**	163
Total	**2,382**	1,055

The pay scale of the Company's employees is maintained at a competitive level and employees are rewarded based on their performance according to the general framework of the Company's salaries and bonus systems, which is reviewed annually. The Group will implement a provident fund scheme for its staff in Hong Kong in compliance with the requirements of the Mandatory Provident Fund Schemes Ordinance (Chapter 485 of the Laws of Hong Kong). The Group will also provide a medical insurance scheme for its staff in Hong Kong. According to the relevant PRC regulations, the Group is required to participate in the employee retirement scheme administered by the relevant local government bureau in the PRC and to make contributions for its employees who are eligible to participate in the scheme.

PROSPECTS OF PERFORMANCE

The software and servicing industries in PRC achieved great progress in the year. As a result of the remarkable performance of the Group attained and the forward looking fast growing situation, the Group anticipates that its business scale will reach 5,000 persons in the year of 2007.

To achieve this target, the Group will further strengthen the development of its established operations to maintain steady growth on one hand, while accelerate the pace of merger and acquisition on the other to acquire those software and servicing entities which coincide with the strategic development and planning of the Company and possess investment potentials. With the effective consolidation of its operations, utilization in full of the competitive advantages and harmonization of different corporate culture, the core competitive edges of the Group will further be complemented and enhanced.

Furthermore, the Group will continue to maintain its leading position in the hi-tech industry and undertake throughout exploration to develop other promising segments in order for it to become a leading IT service provider in the PRC as well as the preferred IT service provider for overseas clients.

Biographical Details of Directors and Senior Management

The following sets out the profile of the Directors and senior management of the Company:

DIRECTORS

Executive Directors

Dr. Chen Yuhong (陳宇紅), aged 44, is the managing director and the chief executive officer of the Company and is responsible for the overall business development of the Group. He has over 10 years experience in software development and corporate management. Dr. Chen holds a doctorate degree in optics from 北京理工大學 (Beijing Polytechnic University) in 1991. Prior to joining the Group on 25 April 2000, Dr. Chen was the vice president of CS&S in 2000 and was appointed senior vice-president of CNTC (中軟網絡信息技術有限公司) in December 2003. He has also been appointed a director of Chinasoft Resources. He was a manager of the research department from October 1996 to April 2000. He was also a director of 中軟賽博資源軟件技術(天津)有限公司 (CS&S Cyber Resources Software Technology (Tianjin) Co., Ltd.), an associate company of CS&S from 1999 to March 2002. From June 1991 to October 1996, he was the deputy general manager of China Great Wall Computer Software Co., Ltd.

Dr. Tang Zhenming (唐振明), aged 44, is the senior vice president. He is responsible for the human resources of the Group and our newly acquired Training Centre. Prior to joining the Group on 25 April 2000, Dr. Tang was employed by Beijing Institute of Technology Industrial Company (北京理工大學產業總公司) as deputy general manager from May 1995 to March 2000 and by American W&P Company, Beijing Office (美國W&P公司北京辦事處) as officer from December 1993 to March 1995. Dr. Tang is also a director of Chinasoft Resources and Wuhan Chinasoft International. He holds a bachelor's degree in vehicle engineering from Tsinghua University (清華大學) in 1985 and a doctorate degree in motor electronic control from Beijing Polytechnic University (北京理工大學) in 1994.

Mr. Wang Hui (王暉), aged 34, is the senior vice president and chief technical officer. He is responsible for the designing of technical solutions and consulting. Mr. Wang graduated from 天津大學 (Tianjin University) in 1995. He has 6 years experience in systems analysis and in the design of system infrastructure. Prior to joining the Group on 25 April 2000, Mr. Wang was a manager of China Greatwall Computer Software Co., Ltd from 1995 to 2000.

Non-executive Directors

Madam Tang Min (唐敏), aged 62, is the chairman of the Company and is the chairman of the PRC Software Alliance and a vice-chairman of the Chinasoft Software Association. Ms. Tang obtained a bachelor's degree in physics from Peking University, the PRC and has the professional qualification of senior engineer in computer science. She has more than 30 years experience at the management level in the IT industry in the PRC. Madam Tang is the President of China National Software and Service Company Limited ("CNSS"), a joint stock limited company established under the laws of the PRC, the A-shares of which are listed on the Shanghai Stock Exchange. She also holds directorships in a number of the subsidiaries and associate companies of CNSS including CS&S (HK), a corporate shareholder holding approximately 24% of the total issued ordinary shares of the Company and approximately 18.96% of the total voting rights at all general meetings of shareholders of the Company.

Biographical Details of Directors and Senior Management

Dr. Cui Hui *(崔輝)*, aged 45, is responsible for the financial management of the Group. Dr. Cui has about 20 years experience in corporate management. Dr. Cui graduated from Jilin University (吉林大學) in the PRC in 1983 with a doctorate degree in economics. Prior to joining the Group on 25 April 2000, Dr. Cui worked for CS&S as deputy department head from August 1983 to April 1992, deputy general manager from July 1999 to January 2000 and was the vice president of China National Software & Technology Service Corporation ("CS&S") in 2000. From May 1992 to December 1997, Dr. Cui was the deputy general manager and general manager of Oriental Technology (Beijing) Company Ltd (東方科技(北京)有限公司) . He was the general manager of Chinasoft Tonghe Systems Integration Company Ltd (中軟同和系統集成有限公司) from January 1998 to June 1999. In December 2003, he was appointed senior vice-president of CNTC (中軟網絡信息技術有限公司) (which changed its name to that of CNSS). Dr. Cui currently holds a directorship position in CNSS.

Mr. Duncan Chiu (邱達根), aged 32, has been involved in the management of the Group since joining in January 2000. Mr. Chiu graduated with a bachelor's degree in business administration from Pepperdine University of California in 1996. Mr. Chiu currently serves as vice chairman and treasurer of The Chamber of Hong Kong Listed Companies, vice president of Innovation & Technology Association and is a committee member of All-China Youth Federation. Mr. Chiu is as a director among the Far East Group of Companies. He serves as the managing director and chief executive officer of Far East Technology International Limited ("Far East Technology") and also a non-executive director of Far East Hotel & Entertainment Limited.

Mr. Liu Zheng (劉征), aged 34, was appointed on 14 June 2002. He has been a general manager of ITG since April 2000. From 1997 to 2000, he was the general manager of DingRong Investment Management Co., Ltd (鼎榮投資管理公司). Mr. Liu worked for China Everbright Bank from 1992 to 1997. Mr. Liu has 10 years experience in the financial industry and graduated from the Finance and Banking Institute of China (中國金融學院) in 1992 with a bachelor's degree in economics.

Mr. Timothy Chen Yung Cheng (陳永正), aged 50, is the corporate vice president of Microsoft Corporation and its chief executive officer of the greater China region. Prior to joining Microsoft Corporation in September 2003, Mr. Chen was the chairman and president of Motorola Corp.'s China subsidiary. He was appointed as corp. vice president of Motorola Inc, chairman and president of Motorola (China) Electronics Ltd in September 2001. From June 2000 to September 2001, Tim was the chief executive officer of 21CN Cybernet (a listed company in Hong Kong on the Main Board of the Stock Exchange). Before joining 21CN Cybernet, since 1992, Tim held various positions in Motorola including the general manager of Motorola's Greater China Cellular Infrastructure Division. He worked in Lucent (then AT&T Bell Labs) in U.S.A. as research and development manager and marketing manager prior to 1992. Tim holds a master's degree in business administration from University of Chicago and two master's degrees in computer science and mathematics.

Independent non-executive Directors

Mr. He Ning (何寧), aged 48, was appointed on 2 July 2002. Mr. He has been the chief executive officer of Beijing CCG Technology Co. Ltd. since September 2000. From January 1997 to August 2000, he was the vice president of the Beijing representative office of Merrill Lynch. Mr. He was the assistant officer of the China Stock Exchange Executive Council from July 1993 to December 1996. He also worked for Morgan Stanley as manager from May 1990 to June 1993. Mr. He obtained a master's degree in business administration from the University of Texas in 1984. Mr. He has over 10 years experience in investment banking, direct investment and venture business management in the PRC and the USA.

Mr. Zeng Zhijie (曾之杰), aged 39, was appointed on 21 April 2003. Mr. Zeng obtained a master's degree in business administration from Stanford University in June 2001, and is a vice president of Walden International since October 2001, a global venture capital firm with an investment focus on the communications, electronics, software & IT services, semiconductors and life sciences/healthcare industries.

Dr. Leung Wing Yin Patrick (梁永賢), aged 50, was appointed on 22 March 2006. Dr. Leung holds a doctor's degree in accounting from the University of New South Wales, Australia, and a member of Certified Public Accountants of Australia, a member of the Hong Kong Institute of Certified Public Accountants and a member of the Hong Kong Securities Institute. He is an Assistant Professor and a Doctor Student Supervisor at the School of Accounting and Finance of the Hong Kong Polytechnic University. Dr. Leung previously worked as a consultant in a firm of Certified Public Accountants and as a Senior Lecturer at Charles Sturt University, Australia and the City University of Hong Kong. He has over three years working experience in internal auditing and corporate finance in banks.

SENIOR MANAGEMENT

Mr. Fok Ming Fuk, William (霍銘福) aged 45, is the qualified accountant and company secretary of the Company. He has over twenty years experience in auditing and financial management. Prior to joining the Group on May 17, 2004, Mr. Fok worked as the chief financial officer of Portolan Commerce Solutions, a software developer engaged in enterprise resources planning in Germany. Mr. Fok got a master's degree in business administration from England and is a fellow member of the Hong Kong Institute of Certified Public Accountants, a fellow member of the Association of Chartered Certified Accountants, an associate member of the Institute of Chartered Accountants in England and Wales, a fellow member of the Taxation Institute of Hong Kong and a member of Hong Kong Securities Institute.

Mr. Simon Chung (鍾鎮銘) aged 46, is the chief operating officer of the Company and is responsible for the overall daily operation of the Group. He has over 18 years experience in IT professional services covering account management, service delivery management, technical sales, quality assurance and control, project management and customer support operation in the area of public government, telecom and finance sectors. Prior to joining the Group, he was a project director of Atos Origin responsible for the management of large scale projects and service delivery for major clients in Asia Pacific from 1996 to 2005. He was an information technology officer and manager from 1991 to 1995 for the department of defense in Australia (Navy division). He was an IT database leader in the financial department of a government sector from 1989 to 1991. He holds a bachelor's degree in computing science from the University of Wollongong in Australia.

Ms. Yan Juanjue (嚴雋珏女士), aged 63, is the newly acquired outsourcing general manager. Ms. Yan joined the Group on 28 April 2005, before that she acted as the general manager of Chinasoft Resources. She acted as the vice general manager of 北大計算機系統工程公司 between 1994 and 2001, the officer of the Training Centre of the Peking University between 1992 and 1994 and a lecturer in the Peking University between 1977 and 1992. Ms. Yan graduated from the Peking University in 1967.

QUALIFIED ACCOUNTANT AND COMPANY SECRETARY

Mr. Fok Ming Fuk, William (霍銘福), is the qualified accountant and company secretary of the Company. Please refer to the paragraph headed "Senior Management" in this section above for further details regarding his background.

COMPLIANCE OFFICER

Dr. Chen Yuhong (陳宇紅), is the compliance officer of the Company. Please refer to the paragraph headed "Directors" in this section above for further details regarding his background.

Report of the Directors

The Directors present their annual report and the audited financial statements of the Group for the year ended 31 December 2006.

PRINCIPAL ACTIVITIES

The Company acts as an investment holding company. The principal activities of its subsidiaries are set out in note 1 to the financial statements. During the year under review, there were no significant changes in the Group's principal activities.

RESULTS AND DIVIDENDS

The results of the Group for the year ended 31 December 2006 are set out in the consolidated income statement on page 50.

The Directors recommend the payment of a final dividend of HK$0.001 (equivalent to RMB0.001) per share to the shareholders on the register of members on 16 May 2007, amounting to HK$758,817 (equivalent to RMB758,817).

FINANCIAL SUMMARY

A summary of the published results and assets and liabilities of the Group for the past six years, as extracted from the audited financial statements, is set out on page 4. This summary does not form part of the audited financial statements.

DISTRIBUTABLE RESERVES

The reserves available for distribution to shareholders as at 31 December 2006 are RMB592,602.

SHARE CAPITAL

Details of movements during the year in the share capital of the Company are set out in note 29 to the financial statements.

PROPERTY, PLANT AND EQUIPMENT

Details of movements during the year in the Group's property, plant and equipment are set out in note 13 to the financial statements.

Report of the Directors

DIRECTORS

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

Executive Directors:

Dr. Chen Yuhong (Managing Director)	
Mr. Wang Hui	
Dr. Tang Zhenming	
Mr. Peng Jiang	(resigned on 22 March 2006)

Non-executive Directors:

Madam Tang Min (Chairman)	(formerly an executive Director and re-designated as non-executive Director on 22 March 2006)
Dr. Cui Hui	(formerly an executive Director and re-designated as non-executive Director on 22 March 2006)
Mr. Duncan Chiu	(formerly an executive Director and re-designated as non-executive Director on 22 March 2006)
Mr. Timothy Chen Yung Cheng	(appointed on 22 March 2006)
Mr. Liu Zheng	
Mr. David Chiu	(resigned on 22 March 2006)

Independent non-executive Directors:

Mr. He Ning	
Mr. Zeng Zhijie	
Mr. Au Yeung Shiu Kau Peter	(resigned on 22 March 2006)
Dr. Leung Wing Yin Patrick	(appointed on 22 March 2006)

The Company has received, from each of the independent non-executive Directors, an annual confirmation of his independence pursuant to Rule 5.09 the GEM Listing Rules. The Company considers all of the independent non-executive Directors as independent.

In accordance with article 87 of the Company's Articles of Association, Mr. Duncan Chiu, Mr. Zeng Zhijie and Mr. Wang Hui (who have been longest in office since their last election) will retire from office by rotation and, being eligible, offer themselves for re-election.

DIRECTORS' SERVICE CONTRACTS

Dr. Chen Yuhong, Dr. Cui Hui, Mr. Duncan Chiu and Madam Tang Min have each entered into a service agreement with the Company. Particulars of these contracts, except as indicated, are in all material respects identical and are set out below:

(i) each service contract is of two years duration commencing on 20 June 2003 except for that of Madam Tang Min, which commenced on 30 September 2004. The service contract shall continue thereafter until terminated by either party giving to the other not less than three months' prior written notice, such notice not to be given before the expiry of the initial term of two years;

(ii) the monthly salary for Dr. Chen Yuhong, Dr. Cui Hui and Mr. Duncan Chiu for the first year of appointment commencing on 20 June 2003 is RMB70,000, RMB10,000 and RMB10,000 respectively and the monthly salary of Madam Tang Min commencing from 30 September 2004 is RMB10,000. Such salary is to be reviewed annually by the board of Directors. For the period from the expiry of the first year of appointment, the salary of these four executive Directors shall be determined by the board of Directors but shall not be more than 120 percent of the annual salary of such Director for the preceding year;

(iii) Dr. Chen Yuhong, Dr. Cui Hui, Mr. Duncan Chiu and Madam Tang Min are each entitled to management bonus by reference to the consolidated net profits of the Group after taxation and minority interests but before extraordinary items as shown in the Group's audited consolidated accounts for the relevant financial year (the "Net Profits") as the Board may approve, provided that the aggregate amount of management bonuses payable to all executive Directors in respect of any financial year of the Group shall not exceed 5 percent of the Net Profits; and

(iv) each such Director shall abstain from voting and shall not be counted in the quorum in respect of the resolution regarding the amount of management bonus payable to himself/herself.

Dr. Tang Zhenming, Mr. Wang Hui and Dr. Leung Wing Yin Patrick have not entered into service agreements with the Group. The annual director's fee for both Mr. He Ning and Mr. Zeng Zhijie is HK$120,000, while the monthly remuneration for Dr. Tang Zhenming, Mr. Wang Hui and Mr. Au Yeung Shiu Kau Peter is RMB23,500, RMB37,500 and HK$5,000 respectively. Mr. David Chiu, Mr. Liu Zheng and Mr. Timothy Chen Yung Cheng receive no remuneration for holding their office as non-executive Director.

Mr. He Ning and Mr. Zeng Zhijie were appointed as independent non-executive Directors pursuant to letters of appointment for a term of 2 years from 20 June, 2003, and their appointments have continued since expiry of such term. Each of them receives an annual remuneration of HK$120,000 for his office.

Dr. Leung Wing Yin Patrick was appointed as an independent non-executive Director on 22 March 2006 and his annual remuneration is HK$120,000 for his office.

None of the Directors has entered into any service agreements 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.

Details of the Directors' remuneration are set out in note 10 to the financial statements. Save as disclosed in note 10 to the financial statements, there are no other emoluments, pension and any compensation arrangements for the Directors and past Directors as is specified in Section 161 and 161A of the Companies Ordinance (Chapter 32 of the Laws of Hong Kong).

DIRECTORS' INTERESTS IN SHARES

As at 31 December 2006, the following Directors had interests in the shares and underlying shares of the Company and shares in an associated corporation (as defined in Part XV of the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong) ("SFO")) of the Company as set out below and recorded in the register required to be kept under section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to the required standard of dealings by directors of listed issuers as referred to in Rule 5.46 of the GEM Listing Rules:

Long positions in shares of HK$0.05 each in the capital of the Company ("Shares")

Name of Director	No. of Shares	Approximate percentage of total issued share capital of the Company
Chen Yuhong	22,967,472	3.02%
Cui Hui	20,000,000	2.64%
Wang Hui	7,017,838	0.92%
Tang Zhenming	10,207,765	1.35%

Options to subscribe for Shares

Name of Director	Exercise Price (HK$)	No. of share options outstanding as at 31 December 2006	Percentage of total issued share capital of the Company	No. of underlying Shares interested in	Note
Chen Yuhong	0.58	1,200,000	0.16%	7,400,000	(1)
	0.65	5,000,000	0.66%		(2)
	0.97	1,200,000	0.16%		(3)
Cui Hui	0.65	500,000	0.07%	500,000	(2)
Duncan Chiu	0.65	1,000,000	0.13%	1,000,000	(2)
Wang Hui	0.58	1,000,000	0.13%	5,500,000	(1)
	0.65	3,500,000	0.46%		(2)
	0.97	1,000,000	0.13%		(3)
Tang Zhenming	0.58	320,000	0.04%	3,720,000	(1)
	0.65	2,600,000	0.34%		(2)
	0.97	800,000	0.11%		(3)

Notes:

(1) The above share options were offered on 13 August 2003 under the share option scheme of the Company adopted on 2 June 2003 (the "Share Option Scheme") and were accepted on 27 August 2003. The share options are exercisable for a period of ten years from the date of offer, subject to the following conditions:

Exercisable Period		
Commencing	**Ending**	**Number of share options exercisable**
13/08/2004	12/08/2013	25% of the total number of share options granted
13/08/2005	12/08/2013	25% of the total number of share options granted
13/08/2006	12/08/2013	25% of the total number of share options granted
13/08/2007	12/08/2013	25% of the total number of share options granted

(2) The above share options were offered on 13 May 2004 under the Share Option Scheme and were accepted on 10 June 2004. The share options are exercisable for a period of ten years from the date of offer, subject to the following conditions:

Exercisable Period		
Commencing	**Ending**	**Number of share options exercisable**
13/05/2004	12/05/2014	25% of the total number of share options granted
13/05/2005	12/05/2014	25% of the total number of share options granted
13/05/2006	12/05/2014	25% of the total number of share options granted
13/05/2007	12/05/2014	25% of the total number of share options granted

(3) The above share options were offered on 30 March 2006 under the Share Option Scheme and were accepted on 27 April 2006. The share options are exercisable for a period of ten years from the date of offer, subject to the following conditions:

Exercisable Period		
Commencing	**Ending**	**Number of share options exercisable**
30/03/2006	29//03/2016	25% of the total number of share options granted
30/03/2007	29//03/2016	25% of the total number of share options granted
30/03/2008	29//03/2016	25% of the total number of share options granted
30/03/2009	29//03/2016	25% of the total number of share options granted

Save as disclosed above and so far as was known to the Directors, as at 31 December 2006 none of the Directors or chief executive of the Company had any interests or short positions in the shares, debentures or underlying shares of the Company or its associated corporations (as defined in Part XV of the SFO) which were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which he is 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, pursuant to the required standard of dealings by directors of listed issuers as referred to in Rules 5.46 of the GEM Listing Rules, to be notified to the Company and the Stock Exchange.

As at 31 December 2006, none of the Directors had any direct or indirect interest in any assets which had been, since 31 December 2006 (being the date to which the latest published audited accounts of the Company were made up), acquired or disposed of by, or leased to the Company or any member of the Group, or were proposed to be acquired or disposed of by, or leased to, any member of the Group.

As at 31 December 2006, none of the Directors were materially interested in any subsisting contract or arrangement which was significant in relation to the business of the Group.

DIRECTORS' RIGHTS TO ACQUIRE SHARES

During the year ended 31 December 2006, save as disclosed above. none of the Directors was granted any options to subscribe for shares of the Company. As at 31 December 2006, none of the Directors had any rights to acquire shares in the Company save as disclosed above.

REQUIRED STANDARD OF SECURITIES DEALINGS BY DIRECTORS

During the year ended 31 December 2006, the Company had adopted a code of conduct for directors' securities transactions on terms no less exacting than the required standard of dealings set out in Rules 5.48 to 5.67 of the GEM Listing Rules. Having made specific enquiry with all the Directors, the Directors had complied with the required standard of dealings and the code of conduct for directors' securities transactions during the year ended 31 December 2006.

SHARE OPTION SCHEME

As at 31 December 2006, share options allowing for the subscription of an aggregate of 78,210,000 Shares granted to certain directors and employees of the Group pursuant to the Share Option Scheme were outstanding, with terms on the exercise of such share options granted as set out in Notes (1), (2) and (3) in the section headed "Directors' Interests in Shares" above.

Save as disclosed above, no share options have been granted, exercised or have lapsed pursuant to the Share Option Scheme as at 31 December 2006.

ARRANGEMENTS TO PURCHASE SHARES OR DEBENTURES

Other than as disclosed above, at no time during the year was the Company or any of its subsidiaries a party to any arrangements to enable the Directors to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate. None of the Directors, or their spouses or children under 18 years of age, had any rights to subscribe for the shares of the Company, or had exercised any such rights during the period.

DIRECTORS' INTERESTS IN CONTRACTS OF SIGNIFICANCE

Save as disclosed in note 38 to the financial statements, no contracts of significance in relation to the Group's business to which the Company, any of its subsidiary, its holding company or any subsidiary of its holding company was a party and in which a Director had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

CONNECTED TRANSACTIONS

During the year, the Group had entered into continuing connected transactions as set out below.

1. Commercial Agreement with Microsoft

Date of agreement	:	26 September, 2005
Parties	:	the Company
		Microsoft, which had entered into an agreement to subscribe for convertible preferred shares of the Company and was expected to hold more than 10% of the voting rights at general meetings of the Company and thus a connected person of the Company.

The Company and Microsoft entered into the agreement for a term of three years and agreed to drive revenue associated with delivering software solutions using certain software products of Microsoft to assist the Company in growing its IT service business in the PRC. Under such agreement, the Company will achieve a target revenue of US$3.0 million, US$4.5 million and US$6.75 million respectively for the three years commencing from the closing date for subscription for convertible preferred shares of the Company by Microsoft.

The Commercial Agreement constituted a continuing connected transaction of the Company. The annual cap amounts for the transactions contemplated under the Commercial Agreement are US$4.18 million, US$5.83 million and US$8.35 million for the three years ending 31 December, 2008.

2. Lease of (i) 9th Floor of Block A, 3rd Floor of Block C and 3rd Floor, West Tower of Block B of 55 Xue Yuan Nan Road, Haidian District, Beijing, PRC, (ii) 5th Floor, Block B of 55 Xue Yuan Nan Road, Haidian District, Beijing, PRC, and (iii) 8th Floor of Block A of 55 Xue Yuan Nan Road, Haidian District, Beijing, PRC entered with CNSS

Date of lease	:	1 January 2006
Floor area of leased premises	:	2693.9025 square meters in aggregate
Term	:	1 January 2006 to 31 December 2006
Monthly rent	:	RMB176,177.56 (equivalent to about HK$169,401.50)
User	:	as office premises

3. Master Services Agreement

Date of agreement	:	27 October 2006
Parties	:	(1) the Company
		(2) Microsoft

The Company and Microsoft entered into the agreement for a term of five years and agreed to provide certain services including but not limited to the development and/or delivery of any materials, inventories, ideas, designs, concepts, techniques, discoveries, or improvements. The expected annual fee income generated from the provision of the services will not exceed US$7.2 million, US$9.4 million, US$12.2 million, US$15.9 million, US$20.7 million and US$20.2 million respectively for the six years ending 31 December 2011.

The Master Service Agreement constituted a continuing connected transaction of the Company. The annual cap amounts for the transactions contemplated under the Master Service Agreement are US$7.2 million, US$9.4 million, US$12.2 million, US$15.9 million, US$20.7 million and US$20.2 million respectively for the six years ending 31 December 2011.

The Directors consider that the above continuing connected transactions of the Group have been entered into under normal commercial terms and in the ordinary and usual course of business, and the terms are fair and reasonable and in the interests of the shareholders of the Company as a whole.

The Company has complied with the disclosure requirements in accordance with Chapter 20 of the GEM Listing Rules in respect of the above transactions.

Save as disclosed therein, there were no other transactions required to be disclosed as connected transactions and/or continuing connected transactions in accordance with the requirements of the GEM Listing Rules.

MAJOR CUSTOMERS AND SUPPLIERS

During the year, the aggregate turnover attributable to the Group's five largest customers accounted for less than 30% of the Group's total turnover and the Group's largest customer accounted for approximately 13% of the Group's total turnover.

The aggregate purchases during the year attributable to the Group's five largest suppliers was approximately 39% of the Group's total purchases and the Group's largest supplier accounted for approximately 10% of the Group's total purchases.

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

SUBSTANTIAL SHAREHOLDERS

As at 31 December 2006, so far as is known to the Directors, the following persons (other than a Director or chief executive of the Company) had an interest in the 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:

Long positions in Shares

Name	**Nature of interest**	**Approximate number of Shares** (million)	**Approximate percentage of total issued share capital of the Company**
CS&S (HK) (Note 1)	Beneficial interest	199.01	26.23%
CNSS (Note 1)	Interest of controlled corporation	199.01	26.23%
Chinasoft (HK) (Note 2)	Interest of persons acting in concert	199.01	26.23%
Far East Technology (Note 3)	Beneficial interest	130.13	17.15%
IFC (Note 4)	Beneficial interest	97.25	12.82%
Microsoft (Note 4)	Beneficial interest	97.25	12.82%

Notes:

1 CNSS is taken to be interested in the Shares in which CS&S (HK) is interested. CNSS holds approximately 99.3% of the total voting rights of CS&S (HK). The number of Shares in which CS&S (HK) is interested includes 23,248,302 Shares which may be issued by the Company to CS&S (HK) pursuant to an acquisition agreement between Chinasoft (HK) and CS&S (HK) dated 28th April 2005 subject to fulfillment of a condition and the exercise of a cash option.

2. Chinasoft (HK) and CS&S (HK) are parties to agreements to acquire interests in the Company which include provisions imposing restrictions with respect to the disposal of interests acquired, and Chinasoft (HK) is taken to be interested in the Shares in which CS&S (HK) is interested pursuant to section 318 of the SFO.

3. Mr. Duncan Chiu and Mr. David Chiu, who were an executive Director and a non-executive Director of the Company respectively as at 31 December 2005, are nominated by Far East Technology. Both Mr. Duncan Chiu and Mr. David Chiu are directors of Far East Technology.

4. IFC and Microsoft were each interested in 97,250,000 Shares which could be issued to each of them upon the conversion of the 97,250,000 Series A Preferred Shares agreed to be subscribed for by each of them pursuant to a subscription agreement with the Company dated 26th September 2005 subject to the satisfaction of condition precedents set forth in the subscription agreement.

Save as disclosed above, as at 31 December 2006, no other interest or short position in the Shares or underlying shares of the Company were recorded in the register required to be kept under section 336 of the SFO.

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES

Neither the Company nor any of its subsidiaries purchased, sold or redeemed any listed securities of the Company during the year under review.

PRE-EMPTIVE RIGHTS

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

Report of the Directors

COMPETING INTERESTS

As at 31 December 2006, Dr. Cui Hui, an non-executive Director, was interested in approximately 1.34% of the issued share capital of CNSS. Dr. Cui Hui also served as a director of CNSS. In addition, Madam Tang Min (an non-executive Director and Dr. Chen Yuhong (an executive Director) had been appointed as directors of CNSS since August 2000 and April 2004 respectively. Although the Directors are of the view that the principal activities of CNSS do not directly compete with those of the Group currently, the Group and CNSS however are both engaged in the provision of information technology outsourcing.

Save as disclosed above, as at 31 December 2006, none of the Directors or the management shareholders of the Company and their respective associates (as defined under the GEM Listing Rules) had any interest in a business which competed or might compete with the business of the Group.

POST BALANCE SHEET EVENTS

A list of events which happened after the date of the consolidated balance sheet of the Group of 31 December 2006 are set out in note 39 to the financial statements.

AUDITORS

A resolution will be submitted to the annual general meeting of the Company to re-appoint Messrs. Deloitte Touche Tohmatsu as auditors of the Company.

On behalf of the Board

Dr. Chen Yuhong
Managing Director

Beijing, 30 March 2007

Corporate Governance Report

CORPORATE GOVERNANCE PRACTICES

The board of directors of the Company believes that corporate governance is essential to the success of the Company and has adopted various measures to ensure that a high standard of corporate governance is maintained. The code provisions in the Code on Corporate Governance Practices contained in Appendix 15 of the GEM Listing Rules (the "Code on Corporate Governance Practices") have served as guideposts for the Company to follow in its implementation of corporate governance measures. The Company complied with all the code provisions in the Code on Corporate Governance Practices during the year under review, particularly with respect to the management of the board of directors, financial reporting, communication with shareholders and the procedures for conduct of shareholders' meetings.

DIRECTORS' SECURITIES TRANSACTIONS

The Company has adopted a code of conduct regarding Directors' securities transactions on terms no less exacting than the required standard of dealings as set out in Rules 5.48 to 5.67 of the GEM Listing Rules. Having made specific enquiry of all the Directors, the Directors complied with such code of conduct and the required standard of dealings and its code of conduct regarding securities transactions by the Directors throughout the year ended 31 December 2006.

BOARD OF DIRECTORS

During the year in review and up to the date of this report, the board of directors of the Company comprises:

Executive directors:

Dr. Chen Yuhong	
Mr. Wang Hui	
Dr. Tang Zhenming	
Mr. Peng Jiang	(resigned on 22 March 2006)

Non-executive directors:

Madam Tang Min (Chairman)	(formerly an executive Director and re-designated as non-executive Director on 22 March 2006)
Dr. Cui Hui	(formerly an executive Director and re-designated as non-executive Director on 22 March 2006)
Mr. Duncan Chiu	(formerly an executive Director and re-designated as non-executive Director on 22 March 2006)
Mr. Liu Zheng	
Mr. Timothy Chen Yung Cheng	(appointed on 22 March 2006)
Mr. David Chiu	(resigned on 22 March 2006)

Independent non-executive directors:

Mr. He Ning	
Mr. Zeng Zhijie	
Dr. Leung Wing Yin Patrick	(appointed on 22 March 2006)
Mr. Au Yeung Shiu Kau Peter	(resigned on 22 March 2006)

During the year ended 31 December 2006, four full board meetings were held and the attendance of each director is set out as follows:

Name of Director	Number of board meetings attended in 2006	Attendance rate
Executive Directors:		
Dr. Chen Yuhong	4	100%
Mr. Wang Hui	4	100%
Dr. Tang Zhenming	4	100%
Mr. Peng Jiang	–	N/A
Non-executive Directors:		
Madam Tang Min	4	100%
Dr. Cui Hui	4	100%
Mr. Duncan Chiu	4	100%
Mr. Timothy Chen Yung Cheng	4	100%
Mr. Liu Zheng	4	100%
Mr. David Chiu	–	N/A
Independent non-executive Directors:		
Mr. He Ning	4	100%
Mr. Zeng Zhijie	4	100%
Mr. Au Yeung Shiu Kau Peter	–	N/A
Dr. Leung Wing Yin Patrick	4	100%

The Board is currently responsible for corporate strategy and development, overseeing the business operations of the Group, financial reporting, legal and regulatory compliance, directors' appointments, risk management, major acquisitions, disposals and capital transactions. Major corporate matters delegated by the Board to management include preparation of annual and interim accounts for board approval, execution of business strategies and initiatives adopted by the Board and implementation of internal control system.

Details of backgrounds and qualifications of the chairman of the Company and the other Directors are set out in the section headed "Report of the Directors" in this Annual Report. All Directors have given sufficient time and attention to the affairs of the Group. Each executive Director are suitably qualified for his or her position, and has sufficient experience to hold the position so as to carry out his duties effectively and efficiently.

Madam Tang Min and Dr. Cui Hui are both directors of CNSS, a substantial shareholder of the Company. Dr. Chen Yuhong and Dr. Cui Hui have been appointed as senior vice presidents of CNSS since December, 2003. Mr. Duncan Chiu is the brother of Dato' David Chiu, a non-executive Director who resigned on 22 March 2006. Both Mr. Duncan Chiu and Dato' David Chiu are directors of Far East Technology, a substantial shareholder of the Company. Save as aforesaid, there are no other relationships among the members of the board of Directors.

The three independent non-executive Directors appointed by the Company have appropriate and sufficient experience and qualification to carry out their duties so as to protect the interests of shareholders. Each independent non-executive Director gives an annual confirmation of his independence to the Company, and the Company considers these Directors to be independent under Rule 5.09 of the GEM Listing Rules.

CHAIRMAN AND CHIEF EXECUTIVE OFFICER

The post of the chairman of the board (held by Madam Tang Min) and the post of the chief executive officer (held by Dr. Chen Yuhong, the Managing Director) are segregated. Madam Tang is responsible for leadership and organization of the board of directors, whereas Dr. Chen Yuhong is in charge of management of the overall business operations of the Group.

APPOINTMENT OF NON-EXECUTIVE DIRECTORS

Madam Tang Min, Dr. Cui Hui and Mr. Duncan Chiu were re-designated as non-executive Directors for a term of two years from 22 March 2006 and are subject to termination by one month's notice by the Company or himself or herself. Mr. Timothy Chen Yung Cheng was appointed as a non-executive Director for two years from 22 March 2006, subject to termination by one month's notice by the Company or himself. The term of appointment of Mr. Liu Zheng as a non-executive Director expired on 20 June 2005 and has continued subject to termination by one month's notice by the Company or himself. Mr. David Chiu resigned as non-executive Director with effect from 22 March 2006.

REMUNERATION COMMITTEE

The remuneration committee was established on 28 June 2005. During the year under review, the chairman of the committee was Madam Tang Min, and other members included Mr. He Ning, Dr. Chen Yuhong Mr. Zeng Zhijie and Dr. Leung Wing Yin Patrick. Dr. Chen Yuhong is executive Director, Madam Tang Min is non-executive Director and the remaining three members are independent non-executive Directors.

The role and function of the remuneration committee included the determination of the specific remuneration packages of all executive Directors, including benefits in kind, pension rights and compensation payments, including any compensation payable for loss or termination of their office or appointment, and making recommendations to the board of Directors for the remuneration of non-executive Directors. The remuneration committee will consider factors such as salaries paid by comparable companies, time commitment and responsibilities of the Directors, employment conditions elsewhere in the Group and desirability of performance-based remuneration.

Details of attendance of the meeting of the Remuneration Committee are set out as follows:

Name of Director	Number of Meetings attended in 2006	Attendance rate
Madam Tang Min	1	100%
Dr. Chen Yuhong	1	100%
Mr. He Ning	1	100%
Mr. Zeng Zhijie	1	100%
Dr. Leung Wing Yin Patrick	1	100%

The board of Directors considered that the existing terms of appointment and levels of remuneration of the Directors are fair and reasonable, and resolved that a review be carried out again in the year ending 31 December 2007.

The Company adopted a share option scheme on 2 June 2003, which serves as an incentive to attract, retain and motivate talented eligible staff, including the Directors. Details of the share option scheme are set out in note 30* to the financial statements. The emolument payable to Directors will depend on their respective contractual terms under employment contracts, if any, and as recommended by the Remuneration Committee. Details of the Directors' remuneration are set out in note 11 to the financial statements.

NOMINATION OF DIRECTORS

During the year under review, one meeting was held by the board of Directors to consider the appointment and removal of Directors. Details of attendance of the nomination of Directors meeting are set out as follows:

Name of member	Number of meetings attended in 2006	Attendance rate
Madam Tang Min	1	100%
Dr. Chen Yuhong	1	100%
Mr. Duncan Chiu	1	100%
Dr. Leung Wing Yin Patrick	1	100%

Prior to the convening of the annual general meeting of the Company in April 2006, the board of Directors resolved that Dr. Chen Yuhong and Mr. He Ning should retire and stand for re-election at the annual general meeting in accordance with the requirements under the Articles of Association of the Company.

ACCOUNTABILITY AND AUDIT

The Directors are responsible for overseeing the preparation of accounts for each financial period, which give a true and fair view of the state of affairs of the Group and of tie results and cash flow for that period. In preparing the accounts for the year ended 31 December 2006, the Directors have selected suitable accounting policies and have applied them consistently, adopted appropriate Hong Kong Financial Reporting Standards ("HKFRSs") and Hong Kong Accounting Standards ("HKASs") which are pertinent to its operations and relevant to the financial statements, made judgements and estimates that are prudent and reasonable, and have prepared the accounts on the going concern basis.

THE AUDIT COMMITTEE

The Company established an audit committee on 2 June 2003 and amended its written terms of reference to comply with the requirements in the Code on Corporate Governance Practices as set out in Appendix 15 of the GEM Listing Rules. The primary duties of the audit committee are to review and to supervise the financial reporting process and internal control system of the Group. During the year ended 31 December 2006, the audit committee comprised of two independent non-executive Directors, Mr. He Ning and Mr. Zeng Zhijie, and an independent non-executive Director, Mr. Au Yeung Shiu Kau, Peter until his replacement by Dr. Leung Wing Yin Patrick on 22 March 2006. Dr. Leung Wing Yin Patrick is the Chairman of the audit committee. The audit committee met on a quarterly basis during the year ended 31 December 2006.

The Group's unaudited quarterly and interim results and annual audited results during the year ended 31 December 2006 have been reviewed by the audit committee, which was of the opinion that the preparation of such results complied with the applicable accounting standards and requirements and that adequate disclosure has been made.

During the year under review, four meetings were held by the audit committee. Details of attendance of audit committee meetings are set out as follows:

Name of member	**Number of meetings attended in 2006**	**Attendance rate**
Mr. He Ning	4	100%
Mr. Zeng Zhijie	4	100%
Dr. Leung Wing Yin Patrick	4	100%
Mr. Au Yeung Shiu Kau, Peter	–	N/A

AUDITORS' REMUNERATION

The audit committee of the Company is responsible for considering the appointment of the external auditor and reviewing any non-audit functions performed by the external auditor, including whether such non-audit functions could lead to any potential material adverse effect on the Company. During the year under review, the Group was required to pay an aggregate of approximately HK$2.4 million to the external auditors for their services including audit, due diligence and other advisory services.

INTERNAL CONTROL

During the year under review, the Company periodically conducted reviews of its system of internal control to ensure its effectiveness and adequacy. The Company periodically convened meetings to discuss financial, operational and risk management control.

INVESTORS RELATIONS

The Company has disclosed all necessary information to the shareholders in compliance with GEM Listing Rules. Meetings are held with media and investors periodically. The Company also replied to the enquires from shareholders in a timely manner. The Directors host a annual general meeting each year to meet the shareholders and answer their enquiries.

Deloitte.
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TO THE MEMBERS OF CHINASOFT INTERNATIONAL LIMITED
(incorporated in the Cayman Islands with limited liability)

We have audited the consolidated financial statements of Chinasoft International Limited (the" Company") and its subsidiaries (collectively referred to as the" Group") set out on pages 50 to 112, which comprise the consolidated balance sheet as at 31 December 2006, and the consolidated income statement, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

DIRECTORS' RESPONSIBILITY FOR THE CONSOLIDATED FINANCIAL STATEMENTS

The directors of the Company are responsible for the preparation and the true and fair presentation of these consolidated financial statements in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants and the disclosure requirements of the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these consolidated financial statements based on our audit 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. We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and true and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

OPINION

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Group as at 31 December 2006 and of the Group's loss and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

Deloitte Touche Tohmatsu
Certified Public Accountants
Hong Kong
30 March 2007

Consolidated Income Statement

for the year ended 31 December 2006

	NOTES	2006 RMB'000	2005 RMB'000
Turnover	6	**355,236**	382,275
Cost of sales		**(186,338)**	(264,279)
Gross profit		**168,898**	117,996
Other operating income		**9,147**	4,649
Selling and distribution costs		**(20,631)**	(18,918)
Administrative expenses		**(78,082)**	(44,564)
Allowance for doubtful debts		**(2,033)**	(9,264)
Amortisation of intangible assets and trademark use right		**(8,364)**	(2,950)
Impairment loss recognised in respect of technical expertise		**(1,087)**	–
Impairment loss recognised in respect of goodwill	31(b)	**(988)**	–
Discount on acquisition of additional interests in a subsidiary		**1**	–
Profit from operations		**66,861**	46,949
Finance costs	7	**–**	(25)
Share of net results of associates		**2,489**	1,790
Loss arising from changes in fair value of redeemable convertible preferred shares	28	**(110,558)**	–
Redeemable convertible preferred shares issue expenses	28	**(10,764)**	–
(Loss) profit before taxation		**(51,972)**	48,714
Taxation	8	**(11,881)**	(5,718)
(Loss) profit for the year	9	**(63,853)**	42,996
Attributable to:			
Equity holders of the parent		**(66,593)**	39,656
Minority interests		**2,740**	3,340
		(63,853)	42,996
Dividend	11	**18,309**	7,394
(Loss) earnings per share	12		
Basic		**RMB(0.0891)**	RMB0.0556
Diluted		**N/A**	RMB0.0543

Consolidated Balance Sheet

at 31 December 2006

	NOTES	2006 RMB'000	2005 RMB'000
Non-current assets			
Property, plant and equipment	13	**42,326**	23,288
Intangible assets	14	**48,894**	18,003
Goodwill	15	**140,157**	79,168
Interests in associates	16	**8,452**	8,303
Trademark use right	17	**1,550**	–
Payment for acquisition of software		**3,654**	–
Prepaid lease payments	38(v)	**–**	216
		245,033	128,978
Current assets			
Inventories	18	**34,107**	22,670
Trade and other receivables	19	**233,963**	182,113
Trade receivable from an associate	20	**1,091**	–
Trade receivables from related companies	21	**11,292**	–
Trademark use right	17	**189**	–
Held-for-trading investment	22	**501**	–
Amount due from a related company	21	**–**	1,815
Loan to a related company	38(vi)	**–**	1,450
Pledged deposits	23	**1,474**	1,653
Bank balances and cash	23	**133,571**	100,086
		416,188	309,787
Current liabilities			
Trade and other payables	24	**107,670**	98,270
Trade payable to a related company	25	**195**	–
Bills payable	26	**24,252**	26,781
Amount due to a shareholder	25	**–**	9
Amounts due to related companies	25	**501**	–
Dividend payable to shareholders		**74**	–
Taxation payable		**4,715**	2,846
Deferred consideration	32(b)	**15,600**	–
Consideration payable on acquisition of a subsidiary and technical expertise	31(a) & 32(a)	**3,491**	–
		156,498	127,906
Net current assets		**259,690**	181,881
Total assets less current liabilities		**504,723**	310,859
Non-current liabilities			
Deferred tax liabilities	27	**2,588**	1,824
Redeemable convertible preferred shares	28	**268,480**	–
		271,068	1,824
		233,655	309,035

Consolidated Balance Sheet

at 31 December 2006

	NOTES	2006 RMB'000	2005 RMB'000
Capital and reserves			
Share capital	29	**40,184**	38,816
Reserves	30	**172,651**	256,187
Equity attributable to equity holders of the parent		**212,835**	295,003
Minority interests		**20,820**	14,032
Total equity		**233,655**	309,035

The consolidated financial statements on pages 50 to 112 were approved and authorised for issue by the board of directors on 30 March 2007 and are signed on its behalf by:

Dr. Chen Yuhong
DIRECTOR

Duncan Chiu
DIRECTOR

Consolidated Statement of Changes in Equity

for the year ended 31 December 2006

	Attributable to the equity holders of the parent												
	Share capital RMB'000	Share premium RMB'000 (note 30)	Issuable shares RMB'000	Translation reserve RMB'000	Share options reserve RMB'000	General reserve fund RMB'000 (note 30)	Statutory enterprise expansion fund RMB'000 (note 30)	Statutory surplus reserve fund RMB'000 (note 30)	Statutory public welfare fund RMB'000 (note 30)	Accumulated profits RMB'000	Total RMB'000	Minority interests RMB'000	Total RMB'000
At 1 January 2005	36,968	85,185	–	90	3,492	1,250	589	–	–	71,932	199,506	–	199,506
Exchange differences arising from translation of overseas operations and net loss recognised directly in equity	–	–	–	(2,137)	–	–	–	–	–	–	(2,137)	–	(2,137)
Profit for the year	–	–	–	–	–	–	–	–	–	39,656	39,656	3,340	42,996
Total recognised (expense) income for the year	–	–	–	(2,137)	–	–	–	–	–	39,656	37,519	3,340	40,859
New issue of shares (see note 29(a))	1,848	35,487	–	–	–	–	–	–	–	–	37,335	–	37,335
Shares issuable on acquisition of subsidiaries	–	–	24,420	–	–	–	–	–	–	–	24,420	–	24,420
Acquisition of subsidiaries	–	–	–	–	–	–	–	–	–	–	–	10,692	10,692
Recognition of equity-settled share-based payments	–	–	–	–	3,617	–	–	–	–	–	3,617	–	3,617
Transfer of share options reserve to accumulated profits upon lapse of share options	–	–	–	–	(11)	–	–	–	–	11	–	–	–
Appropriations	–	–	–	–	–	139	139	63	32	(373)	–	–	–
Share of changes in equity of an associate	–	–	–	–	–	184	–	–	–	(184)	–	–	–
Dividend for 2005	–	–	–	–	–	–	–	–	–	(7,394)	(7,394)	–	(7,394)
At 31 December 2005	38,816	120,672	24,420	(2,047)	7,098	1,573	728	63	32	103,648	295,003	14,032	309,035
Exchange differences arising from translation of overseas operations and loss gain recognised directly in equity	–	–	–	(4,895)	–	–	–	–	–	–	(4,895)	–	(4,895)
Loss (profit) for the year	–	–	–	–	–	–	–	–	–	(66,593)	(66,593)	2,740	(63,853)
Total recognised (expense) income for the year	–	–	–	(4,895)	–	–	–	–	–	(66,593)	(71,488)	2,740	(68,748)
New issue of shares (see note 29(b))	1,368	26,536	(24,420)	–	–	–	–	–	–	–	3,484	–	3,484
Acquisition of a subsidiary	–	–	–	–	–	–	–	–	–	–	–	2,215	2,215
Acquisition of additional interests in subsidiaries	–	–	–	–	–	–	–	–	–	–	–	(12,867)	(12,867)
Capital contribution from a minority shareholder of a subsidiary	–	–	–	–	–	–	–	–	–	–	–	14,700	14,700
Recognition of equity-settled share-based payments	–	–	–	–	4,145	–	–	–	–	–	4,145	–	4,145
Appropriations	–	–	–	–	–	8,141	8,140	246	–	(16,527)	–	–	–
Transfer (see note 30)	–	–	–	–	–	–	–	32	(32)	–	–	–	–
Dividend for 2006	–	(18,309)	–	–	–	–	–	–	–	–	(18,309)	–	(18,309)
At 31 December 2006	40,184	128,899	–	(6,942)	11,243	9,714	8,868	341	–	20,528	212,835	20,820	233,655

Consolidated Cash Flow Statement

for the year ended 31 December 2006

	2006 RMB'000	2005 RMB'000
Operating activities		
(Loss) profit before taxation	**(51,972)**	48,714
Adjustments for:		
Share of net results of associates	**(2,489)**	(1,790)
Finance costs	**–**	25
Interest income	**(3,676)**	(548)
Amortisation of intangible assets and trademark use right	**8,364**	2,950
Impairment loss recognised in respect of technical expertise	**1,087**	–
Impairment loss recognised in respect of goodwill	**988**	–
Discount on acquisition of additional interest in a subsidiary	**(1)**	–
Loss arising from changes in fair value of redeemable convertible preferred shares	**110,558**	–
Expenses on issue of redeemable convertible preferred shares	**10,764**	–
Depreciation of property, plant and equipment	**6,496**	3,646
Gain on disposal of property, plant and equipment	**(2)**	–
Allowance for doubtful debts	**2,033**	9,264
Allowance for inventories	**138**	1,181
Share option expenses	**4,114**	3,578
Operating cash flows before movements in working capital	**86,402**	67,020
(Increase) decrease in inventories	**(9,946)**	12,113
Increase in trade and other receivables	**(45,854)**	(17,882)
Increase in trade receivable from an associate	**(1,091)**	–
Increase in trade receivables from related companies	**(11,292)**	–
Increase in held-for-trading investment	**(501)**	–
Increase (decrease) in trade and other payables	**1,490**	(11,613)
Increase in trade payable to a related company	**195**	–
Decrease in bills payable	**(2,529)**	(1,633)
Cash generated from operations	**16,874**	48,005
Interest paid	**–**	(25)
PRC Enterprise Income Tax paid	**(9,446)**	(3,696)
Net cash from operating activities	**7,428**	44,284

Consolidated Cash Flow Statement

for the year ended 31 December 2006

	NOTES	**2006** **RMB'000**	2005 RMB'000
Investing activities			
Dividend received from an associate		**–**	1,768
Repayment from employees		**–**	310
Interest received		**3,676**	548
Acquisition of subsidiaries, net of cash and cash equivalents acquired	31	**(27,811)**	15,214
Acquisition of additional interests in subsidiaries		**(41,892)**	–
Acquisition of contract-based customer-related intangible and technical expertise	32	**(10,920)**	–
Additions of development costs		**(9,410)**	(5,424)
Purchase of technical knowhow		**–**	(500)
Purchase of software		**–**	(120)
Payment for acquisition of software		**(3,654)**	–
Proceeds from disposal of property, plant and equipment		**116**	–
Purchases of property, plant and equipment		**(24,014)**	(11,421)
Establishment of an associate		**–**	(2,300)
Acquisition of an associate		**–**	(4,200)
Decrease (increase) in pledged deposits		**179**	(560)
Net cash used in investing activities		**(113,730)**	(6,685)
Financing activities			
Proceeds from issue of redeemable convertible preferred shares		**161,824**	–
Expenses on issue of redeemable convertible preferred shares		**(10,764)**	–
Dividend paid		**(18,235)**	(7,892)
Advances to related companies		**(2,840)**	–
Loan to related companies		**–**	(1,450)
Capital contribution from a minority shareholder of a subsidiary		**14,700**	–
Repayment to a shareholder		**(9)**	(41)
Net cash from (used in) financing activities		**144,676**	(9,383)
Net increase (decrease) in cash and cash equivalents		**38,374**	28,216
Cash and cash equivalents at beginning of the year		**100,086**	74,029
Effect of foreign exchange rate changes		**(4,889)**	(2,159)
Cash and cash equivalents at end of the year, representing bank balances and cash		**133,571**	100,086

Notes to the Consolidated Financial Statements

for the year ended 31 December 2006

1. GENERAL INFORMATION OF THE COMPANY

The Company was incorporated as an exempted company with limited liability in the Cayman Islands on 16 February 2000 under the Companies Law, Cap. 22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands.

The shares of the Company are listed on the Growth Enterprise Market (the "GEM") of The Stock Exchange of Hong Kong Limited (the "Stock Exchange") with effect from 20 June 2003.

The addresses of the registered office and principal places of business of the Company are disclosed in the "Corporate Information" section to the annual report.

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

The Company is an investment holding company. The principal activities of the Group are development and provision of solutions, provision of information technology ("IT") consulting, training, outsourcing services and sale of standalone software and hardware products.

Particulars of the Company's subsidiaries at 31 December 2006 are set out as follows:

Name of company	Place of incorporation or establishment/ operation	Issued and fully paid share capital/ registered capital	Percentage of nominal value of issued share capital/registered capital held by the Company		Principal activities
			Directly	Indirectly	
Chinasoft International Holdings Limited*	Samoa/ Hong Kong	US$1	100%	–	Investment holding
Chinasoft International (Hong Kong) Limited ("Chinasoft (HK)")**	Hong Kong	HK$100	–	100%	Investment holding and trading of standalone software products
Chinasoft International Treasury Management (Hong Kong) Limited**	Hong Kong	HK$1	–	100%	Securities trading
Chinasoft Resource (International) Limited**	Hong Kong	HK$100,000	–	100%	Provision of information technology outsourcing services
Chinasoft International Inc.	United States of America	US$0.01	–	100%	Provision of information technology outsourcing services

1. GENERAL INFORMATION OF THE COMPANY – Continued

Name of company	Place of incorporation or establishment/ operation	Issued and fully paid share capital/ registered capital	Percentage of nominal value of issued share capital/registered capital held by the Company		Principal activities
			Directly	Indirectly	
北京中軟國際信息技術有限公司 Chinasoft International Information Technology Limited ("Chinasoft Beijing")***	People's Republic of China ("PRC")	RMB50,000,000	–	100%	Provision of solutions, information technology outsourcing, information technology consulting services, software development and trading of standalone software and hardware products
中軟國際(廣州)信息技術有限公司 Chinasoft International (Guang Zhou) Information Technology Limited ("Chinasoft Guangzhou")***	PRC	HK$5,000,000	–	100%	Provision of solutions, information technology outsourcing, information technology consulting services and trading of standalone software and hardware products
中軟國際(杭州)信息技術有限公司 Chinasoft International (Hang Zhou) Information Technology Limited ("Chinasoft Hangzhou")***	PRC	HK$5,000,000	–	100%	Provision of solutions, information technology outsourcing, information technology consulting services and trading of standalone software and hardware products
中軟總公司計算機培訓中心****	PRC	RMB500,000	–	100%	Provision of information technology consultancy and training services
中軟國際(昆明)信息技術有限公司 Chinasoft International (Kunming) Information Technology Limited*** ("Chinasoft Kunming")	PRC	HK$8,000,000	–	100%	Provision of solutions, information technology outsourcing, information technology consulting services and trading of standalone software and hardware products

Notes to the Consolidated Financial Statements

for the year ended 31 December 2006

1. GENERAL INFORMATION OF THE COMPANY – Continued

Name of company	Place of incorporation or establishment/ operation	Issued and fully paid share capital/ registered capital	Percentage of nominal value of issued share capital/registered capital held by the Company		Principal activities
			Directly	Indirectly	
中軟國際(湖南)信息技術有限公司 Chinasoft International (Hunan) Information Technology Limited ("Chinasoft Hunan")***	PRC	US$1,000,000	–	100%	Provision of solutions, information technology outsourcing, information technology consulting services and trading of standalone software and hardware products
中軟賽博資源軟件技術(天津)有限公司 CS&S Cyber Resources Software Technology (Tianjin) Co., Ltd. ("Cyber Resources")*****	PRC	RMB5,000,000	–	76%	Provision of information technology outsourcing services
廈門中軟海晟信息技術有限公司 ******	PRC	RMB30,000,000	–	51%	Provision of solutions, information technology outsourcing, information technology consulting services and trading of standalone software and hardware products
北京中軟資源信息科技服務有限公司 Chinasoft Resources Information Technology Services Limited*** ("Chinasoft Resources Beijing")	PRC	US$800,000	–	100%	Provision of information technology outsourcing services
深圳市中軟資源技術服務有限公司 Shenzhen Chinasoft Resources Information Technology Services Limited**** ("Chinasoft Resources Shenzhen")	PRC	RMB5,000,000	–	100%	Provision of information technology outsourcing services

1. GENERAL INFORMATION OF THE COMPANY – Continued

Name of company	Place of incorporation or establishment/ operation	Issued and fully paid share capital/ registered capital	Percentage of nominal value of issued share capital/registered capital held by the Company		Principal activities
			Directly	Indirectly	
上海中軟資源技術服務有限公司 Shanghai Chinasoft Resources Information Technology Services Limited****** ("Chinasoft Resources Shanghai")	PRC	RMB3,000,000	–	60%	Provision of information technology outsourcing services

*	International company
**	Limited liability company
***	Wholly foreign-owned enterprise
****	中華人民共和國事業單位
*****	Sino-foreign equity joint venture enterprise
******	Sino foreign-owned enterprise

None of the subsidiaries had any debt securities subsisting at 31 December 2006 or at any time during the year.

2. APPLICATION OF NEW HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs")

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

The Group has not early applied the following new Hong Kong Accounting Standard ("HKAS"), Hong Kong Financial Reporting Standards ("HKFRSs") and Interpretations ("HK(IFRIC)-INT") that have been issued but are not yet effective. The directors of the Company anticipate that the application of these HKAS, HKFRS and Interpretations will have no material impact on how the results and the financial position of the Group are prepared and presented.

2. APPLICATION OF NEW HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs") – Continued

HKAS 1 (Amendment)	Capital disclosures [1]
HKFRS 7	Financial instruments: Disclosures [1]
HKFRS 8	Operating segments [2]
HK(IFRIC) – Int 7	Applying the restatement approach under HKAS 29 Financial Reporting in Hyperinflationary Economies [3]
HK(IFRIC) – INT 8	Scope of HKFRS 2 [4]
HK(IFRIC) – INT 9	Reassessment of embedded derivatives [5]
HK(IFRIC) – INT 10	Interim financial reporting and impairment [6]
HK(IFRIC) – Int 11	HKFRS 2 – Group and Treasury Share Transactions [7]
HK(IFRIC) – Int 12	Service concession arrangements [8]

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

3. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared on the historical cost basis except for certain financial instruments which are measured at fair value.

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

Basis of consolidation

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

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

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

3. SIGNIFICANT ACCOUNTING POLICIES – Continued

Basis of consolidation – Continued

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

Minority interests in the net assets of consolidated subsidiaries are presented separately from the Group's equity therein. Minority interests in the net assets consist of the amount of those interests at the date of the original business combination and the minority'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.

Business combinations

The acquisition of subsidiaries is accounted for using the purchase method. The cost of the acquisition is measured at the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree, plus any costs directly attributable to the business combination. The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under HKFRS 3 "Business Combinations" are recognised at their fair values at the acquisition date.

Goodwill arising on acquisition is recognised as an asset and initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognised. If, after reassessment, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in profit or loss.

The interest of minority shareholders in the acquiree is initially measured at the minority's proportion of the net fair value of the assets, liabilities and contingent liabilities recognised.

Acquisition of additional interests in subsidiaries

When the Group increases its interest in an entity that is already controlled by the Company, goodwill (if any) arising on such acquisition represents the difference between the cost of additional interest acquired and the increase in the Group's share of the fair value of the identifiable assets, liabilities and contingent liabilities. No revaluation surplus or deficit on revaluating all of the identifiable assets, liabilities and contingent liabilities of the subsidiary to current fair value is recognised in the consolidated balance sheet. The difference between the fair value, representing the amount of consideration less the amount of goodwill, and the carrying amount of the net assets attributable to the additional interest acquired is recognised as a reserve movement and will be transferred to accumulated profits upon the disposal of the subsidiary. This difference represents the portion of the revaluation difference that arose since the original acquisition date that is attributable to the Group's increased interest in the subsidiary.

3. SIGNIFICANT ACCOUNTING POLICIES – Continued

Revenue recognition

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

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

Service income from solutions and IT outsourcing on project-based IT development contracts (see policy below) is recognised on the percentage of completion method by reference to the value of work carried out during the year.

Income from provision of IT outsourcing, IT consulting and training services is recognised when the services are provided.

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

Project-based IT development contracts

When the outcome of a contract for project-based IT development can be estimated reliably, contract revenue and costs are charged to the income statement by reference to the stage of completion of the contract activity at the balance sheet date, as measured by the proportion that costs incurred to date bear to estimated total costs for each contract.

When the outcome of a contract cannot be estimated reliably, contract costs are recognised as an expense in the period in which they are incurred. Contract revenue is recognised to the extent of contract costs incurred that it is probable will be recoverable.

Where it is probable that the total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately.

Government grants

Government grants represent incentive subsidies from the government for the Group's IT, technology research and development activities. There are no specific conditions attached to the grants and, therefore, they are recognised by the Group when they are received or receivable.

Tax incentive subsidies is recognised when it becomes receivable.

3. SIGNIFICANT ACCOUNTING POLICIES – Continued

Leasing

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

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

Retirement benefit costs

Payments to the state-managed retirement benefit schemes or the Mandatory Provident Fund Scheme are charged as an expense when employees have rendered service entitling them to the contributions.

Taxation

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

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

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the corresponding tax 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 profits will be available to allow all or part of the asset to be recovered.

3. SIGNIFICANT ACCOUNTING POLICIES – Continued

Taxation – Continued

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

Property, plant and equipment

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

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

Leasehold improvements	18% – $33^1/_3$%
Furniture, fixtures and equipment	9% – 20%
Motor vehicles	9% – 20%

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

Intangible assets

Intangible assets acquired separately and with finite useful lives are carried at costs less accumulated amortisation and any accumulated impairment losses.

Intangible assets acquired in a business combination are identified and recognised separately from goodwill where they satisfy the definition of an intangible asset and their fair values can be measured reliably. The cost of such intangible assets is their fair value at the acquisition date.

Subsequent to initial recognition, intangible assets with finite useful lives are carried at costs less accumulated amortisation and any accumulated impairment losses. Amortisation for intangible assets with finite useful lives is provided on a straight-line basis over their estimated useful lives. Alternatively, intangible assets with indefinite useful lives are carried at cost less any subsequent accumulated impairment losses.

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

3. SIGNIFICANT ACCOUNTING POLICIES – Continued

Research and development expenditures

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

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

The amount initially recognised for internally-generated intangible asset is the sum of the expenditure incurred from the date when the intangible asset first meets the recognition criteria. Where no internally-generated intangible asset can be recognised, development expenditure is charged to profit or loss in the period in which it is incurred.

Subsequent to initial recognition, internally-generated intangible asset is reported at cost less accumulated amortisation and accumulated impairment losses.

Goodwill

Goodwill arising on acquisitions prior to 1 January 2005

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

For previously capitalised goodwill, 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 ("CGU") to which the goodwill relates may be impaired (see the accounting policy below).

Goodwill arising on acquisitions on or after 1 January 2005

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

Capitalised goodwill arising on an acquisition of a subsidiary is presented separately in the consolidated balance sheet. Capitalised goodwill arising on an acquisition of an associate (which is accounted for using the equity method) is included in the cost of the investment of the relevant associate.

3. SIGNIFICANT ACCOUNTING POLICIES – Continued

Goodwill – Continued

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

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

Interests in associates

An associate is an entity, including an unincorporated entity such as a partnership, over which the investor has significant influence and that is neither a subsidiary nor an interest in a joint venture.

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

Any excess of the cost of acquisition over the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities of the associate recognised at the date of acquisition is recognised as goodwill. The goodwill is included within the carrying amount of the interests in associates and is assessed for impairment as part of the interests.

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

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

3. SIGNIFICANT ACCOUNTING POLICIES – Continued

Trademark use right

Trademark use right is amortised on a straight-line basis over the effective period stipulated on the trademark license registration certificate.

Inventories

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

Impairment losses (other than goodwill (see the accounting policy in respect of goodwill))

At each balance sheet date, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is recognised as an expense immediately.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, so that the increased carrying amount does not exceed the carrying amount that would have been determined to have no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised as income immediately.

Financial instruments

Financial assets and financial liabilities are recognised on the balance sheet when a group entity becomes a party to the contractual provisions of the instrument. Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in profit or loss.

Financial assets

The Group's financial assets are classified into one of the two categories, including financial assets at fair value through profit or loss and loans and receivables. All regular way purchases or sales of financial assets are recognised and derecognised on a trade date basis. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace. The accounting policies adopted in respect of each category of financial assets are set out below.

3. SIGNIFICANT ACCOUNTING POLICIES – Continued

Financial assets – Continued

Financial assets at fair value through profit or loss

The Group's financial assets at fair value through profit or loss comprise of held-for-trading investment.

At each balance sheet date subsequent to initial recognition, financial assets at fair value through profit or loss are measured at fair value, with changes in fair value recognised directly in profit or loss in the period in which they arise.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. At each balance sheet date subsequent to initial recognition, loans and receivables (including trade and other receivables, trade receivable from an associate, trade receivables from related companies, amount due from a related company, loan to a related company, pledged deposits and bank balances) are carried at amortised cost using the effective interest method, less any identified impairment losses. An impairment loss is recognised in profit or loss when there is objective evidence that the asset is impaired, and is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate. Impairment losses are reversed in subsequent periods when an increase in the asset's recoverable amount can be related objectively to an event occurring after the impairment was recognised, subject to a restriction that the carrying amount of the asset at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

Financial liabilities and equity

Financial liabilities and equity instruments issued by a group entity are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument.

An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities. The accounting policies adopted in respect of financial liabilities and equity instruments are set out below.

3. SIGNIFICANT ACCOUNTING POLICIES – Continued

Financial liabilities and equity – Continued

Financial liabilities at fair value through profit or loss

The Group's financial liabilities at fair value through profit or loss comprise of financial liabilities designated at fair value through profit or loss on initial recognition.

Redeemable convertible preferred shares issued by the Company that comprise of the host debt instrument and the embedded derivatives (including the redemption option and conversion option for the holder to convert the preferred shares into ordinary shares which will be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the Company's own equity instruments which does not meet the equity classification under HKAS 32) are designated as financial liabilities at fair value through profit or loss on initial recognition. At each balance sheet date subsequent to initial recognition, the entire redeemable convertible preferred shares are measured at fair value with changes in fair value recognised in profit or loss.

Transaction costs that relate to the issue of the redeemable convertible preferred shares designated as financial liabilities at fair value through profit or loss are charged to profit or loss immediately.

Other financial liabilities

Other financial liabilities including trade and other payables, trade payable to a related company, bills payable, amount due to a shareholder, amounts due to related companies and deferred consideration are subsequently measured at amortised cost, using the effective interest method.

Equity instruments

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

Derecognition

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

Financial liabilities are derecognised when the obligation specified in the relevant contract is discharged, cancelled or expires. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in profit or loss.

3. SIGNIFICANT ACCOUNTING POLICIES – Continued

Foreign currencies

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

Exchange differences arising on the settlement of monetary items, and on the translation of monetary items, are recognised in profit or loss in the period in which they arise, except for exchange differences arising on a monetary item that forms part of the Group's net investment in a foreign operation, in which case, such exchange differences are recognised in equity in the consolidated financials statements. Exchange differences arising on the retranslation of non-monetary items carried at fair value are included in profit or loss for the period except for differences arising on the retranslation of non-monetary items in respect of which gains and losses are recognised directly in equity, in which cases, the exchange differences are also recognised directly in equity.

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

Goodwill and fair value adjustments on identifiable assets acquired arising on an acquisition of a foreign operation on or after 1 January 2005 are treated as assets and liabilities of that foreign operation and translated at the rate of exchange prevailing at the balance sheet date. Exchange differences arising are recognised in the translation reserve.

Equity-settled share-based payment transactions

Share options granted to employees of the Group, employees of an associate of the Group and customers of the Group

The Group has applied HKFRS 2 to share options granted on or after 1 January 2005. In relation to share options granted before 1 January 2005, the Group chose not to apply HKFRS 2 with respect to share options granted on or before 7 November 2002 and vested before 1 January 2005 in accordance with the transitional provisions of HKFRS 2. The Group has applied HKFRS 2 to share options that were granted after 7 November 2002 and had not yet vested on 1 January 2005.

3. SIGNIFICANT ACCOUNTING POLICIES – Continued

Equity-settled share-based payment transactions – Continued

Share options granted to employees of the Group, employees of an associate of the Group and customers of the Group – Continued

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

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

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

4. 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.

Allowance for doubtful debts

In determining whether there is objective evidence of allowance for doubtful debts, the Group takes into consideration the collectability, aging analysis of trade receivables and estimation of future cash flows. A considerable amount of judgment is required in assessing the ultimate realisation of these receivables, including the current creditworthiness and the past collection history of each customer. The amount of the allowance for doubtful debts is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). Where the actual future cash flows are less than expected, an allowance for doubtful debts may arise.

Estimated impairment of goodwill

Determining whether goodwill is impaired requires an estimation of the recoverable amount of the CGUs to which goodwill has been allocated. The Group has obtained business valuations of the relevant CGUs prepared by independent professional valuers for the purpose of goodwill impairment testing. The valuations are based on an estimation of a weighted average of market multiples based on comparable companies in the relevant industry. As at 31 December 2006, the carrying amount of goodwill was RMB140,157,000 (2005: RMB79,168,000). Details of the business valuations are disclosed in note 15. Should there be any change in the market conditions, it may lead to a change in the results of the valuations and an impairment to goodwill may be required.

4. KEY SOURCES OF ESTIMATION UNCERTAINTY – Continued

Fair value of redeemable convertible preferred shares

The fair value of the financial liability component of the redeemable convertible preferred shares is calculated using the effective interest method. The amount is estimated by using a discount cash flow model with assumptions on estimating the discount rate. The fair value of the derivative component of the redeemable convertible preferred shares is calculated using the binomial option pricing model. The model involves assumptions on the Company's share price, exercise price, time to maturity, risk free rate, share price volatility and others.

Should any of the assumptions be changed, it may lead to a material change to the fair value of the redeemable convertible preferred shares.

5. FINANCIAL INSTRUMENTS

Financial risk management objectives and policies

The Group's major financial instruments include trade and other receivables, bank balances, trade and other payables, bills payables and redeemable convertible preferred shares. Details of these financial instruments are disclosed in respective notes. The risks associated with these financial instruments and the policies on how to mitigate these risks are set out below. The management manages and monitors these exposures to ensure appropriate measures are implemented on a timely and effective manner.

Currency risk

It is the Group's policy for each operating entity to operate in local currency as far as possible to minimise currency risk. The Group's principal businesses are conducted in Renminbi. Since the impact of foreign exchange exposure is minimal, no hedging against foreign currency exposure has been carried out by the management.

Fair value interest rate risk

The Group is exposed to fair value interest rate risk in respect of the redeemable convertible preferred shares which carry a fixed cumulative dividend of 5.5% per annum. The Group currently does not have an interest rate hedging policy and will consider hedging significant interest rate exposure should the need arises.

Cash flow interest rate risk

The Group is exposed to cash flow interest rate risk through the impact of rate changes on interest bearing financial assets which are mainly short-term bank deposits at market rates. Since the bank deposits are all short-term in nature, any future variation in interest rates will not have a significant impact on the results of the Group.

5. FINANCIAL INSTRUMENTS – Continued

Financial risk management objectives and policies – Continued

Credit risk

The Group's maximum exposure to credit risk in the event of the counterparties failure to perform their obligations as at 31 December 2006 in relation to each class of recognised financial assets is the carrying amount of those assets as stated in the consolidated balance sheet. The Group reviews the recoverable amount of each individual trade receivable at each balance sheet date to ensure that adequate impairment losses, if necessary, are made for irrecoverable amounts.

In this regard, the directors of the Company consider that the Group's credit risk is significantly reduced.

The credit risk on liquid funds is limited because the counterparties are banks with high credit ratings assigned by international credit-rating agencies.

The Group's concentration of credit risk by geographical locations is mainly in the PRC. The Group has no significant concentration of credit risk, with exposure spread over a number of counterparties and customers.

Price risk

The Group is exposed to security price risk in respect of the conversion option embedded in the redeemable convertible preferred shares, which allows the holders to convert to its own equity instruments.

Fair value

The fair value of financial assets and financial liabilities are determined as follows:

- the fair value of financial assets and financial liabilities with standard terms and conditions and traded on active liquid markets are determined with reference to quoted market bid prices and ask prices respectively; and

- the fair value of other financial assets and financial liabilities are determined in accordance with generally accepted pricing models based on discounted cash flow analysis or using prices from observable current market transactions.

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

6. TURNOVER AND SEGMENT INFORMATION

Turnover represents the net amounts received and receivable for goods sold and services rendered during the year.

Business segments

For management purposes, the Group is currently organised into four operating divisions-solutions, IT outsourcing, IT consulting and training services, and sale of standalone software and hardware products. These divisions are the basis on which the Group reports its primary segment information.

Segment information about these businesses is presented as follows:

INCOME STATEMENT
For the year ended 31 December 2006

	Solutions RMB'000	IT outsourcing RMB'000	IT consulting and training services RMB'000	Sale of standalone software and hardware products RMB'000	Consolidated RMB'000
Turnover	193,513	127,821	12,184	21,718	355,236
Segment result	103,502	25,060	545	7,570	136,677
Unallocated other operating income					9,147
Unallocated corporate expenses					(66,492)
Allowance for doubtful debts					(2,033)
Amortisation of intangible assets and trademark use right					(8,364)
Impairment loss recognised in respect of technical expertise					(1,087)
Impairment loss recognised in respect of goodwill					(988)
Discount on acquisition of additional interests in a subsidiary					1
Share of net results of associates					2,489
Loss arising from changes in fair value of derivative financial instruments					(110,558)
Redeemable convertible preferred shares issue expenses					(10,764)
Loss before taxation					(51,972)
Taxation					(11,881)
Loss for the year					(63,853)

6. TURNOVER AND SEGMENT INFORMATION – Continued

Business segments – Continued

INCOME STATEMENT
For the year ended 31 December 2005

	Solutions RMB'000	IT outsourcing RMB'000	IT consulting and training services RMB'000	Sale of standalone software and hardware products RMB'000	Consolidated RMB'000
Turnover	301,075	53,034	7,552	20,614	382,275
Segment result	96,597	8,743	133	5,252	110,725
Unallocated other operating income					4,649
Unallocated corporate expenses					(56,211)
Allowance for doubtful debts					(9,264)
Amortisation of intangible assets					(2,950)
Finance costs					(25)
Share of net results of associates					1,790
Profit before taxation					48,714
Taxation					(5,718)
Profit for the year					42,996

No business segment information for the assets, liabilities, capital additions, depreciation and amortisation and other non-cash expenses of the Group is shown as all the assets and liabilities are shared by the business segments and cannot be separately allocated.

Geographical segments

No geographical segment information of the Group is shown as the operating businesses of the Group are substantially carried out in the PRC and the Group's assets and liabilities are substantially located in the PRC.

7. FINANCE COSTS

	2006 RMB'000	2005 RMB'000
Interest on borrowings wholly repayable within five years:		
Bank loans	–	3
Other borrowings	–	22
	–	25

8. TAXATION

	THE GROUP	
	2006 RMB'000	2005 RMB'000
The charge comprises:		
Hong Kong Profits Tax	19	–
PRC Enterprise Income Tax	11,098	5,115
	11,117	5,115
Deferred tax (note 27)	764	603
	11,881	5,718

Hong Kong Profits Tax is calculated at 17.5% of the estimated assessable profit for the year.

No provision for Hong Kong Profits Tax has been made for the year ended 31 December 2005 as the Group had no assessable profit in Hong Kong for the year.

The statutory rate of PRC Enterprise Income Tax is 33%.

Certain group companies are subject to certain tax exemption arrangements as set out below.

Pursuant to an approval document issued by the State Bureau of Beijing Haidian District dated 21 November 2000, 北京中軟國際信息技術有限公司 ("Chinasoft Beijing"), a subsidiary of the Company, had been designated as an advanced technology enterprise and its income tax rate was reduced from 33% to 15%. Moreover, Chinasoft Beijing was entitled to the three year's exemption from income tax followed by three years of 50% tax reduction commencing from the first profit-making year with effect from 2000. As a result, Chinasoft Beijing is subject to the income tax computed at the rate of 7.5% for the three years ended 31 December 2005 and at the rate of 15% on its taxable profit thereafter.

8. **TAXATION** – Continued

Pursuant to an approval document issued by the Guangzhou Science and Technology Bureau dated 31 March 2004, 中軟國際(廣州)信息技術有限公司 ("Chinasoft Guangzhou"), a subsidiary of the Company, had been designated as an advanced technology enterprise and its income tax rate was reduced from 33% to 15%. Moreover, pursuant to another approval document issued by the Guangzhou National Tax Bureau dated 2 June 2004, Chinasoft Guangzhou was entitled to the two year's exemption from income tax followed by three years of 50% tax reduction commencing from the first profit-making year with effect from 2003.

Pursuant to an approval document issued by the Hunan Science and Technology Bureau dated 13 June 2006, 中軟國際(湖南)信息技術有限公司 ("Chinasoft Hunan"), a subsidiary of the Company, had been designated as an advanced technology enterprise and its income tax rate was reduced from 33% to 15%. Moreover, Chinasoft Hunan was entitled to the two year's exemption from income tax followed by three years of 50% tax reduction commencing from the first profit-making year.

Pursuant to an approval document issued by the State Bureau of Tianjing Economic and Technology Development Zone dated 20 February 2003, 中軟賽博資源軟件技術(天津)有限公司 ("Cyber Resources"), a subsidiary of the Company, was established before the end of the year 1995 and was approved as an production enterprise and its income tax rate was reduced from 33% to 15%.

Pursuant to an approval document issued by the Beijing Science and Technology Commission dated 25 June 2004, 北京中軟資源信息科技服務有限公司 ("Chinasoft Resources Beijing"), a subsidiary of the Company, had been designated as an advanced technology enterprise and its income tax rate was reduced from 33% to 15%. Moreover, Chinasoft Resources Beijing was entitled to the two year's exemption from income tax followed by three years of 50% tax reduction commencing from the first profit-making year with effect from 2004.

Pursuant to an approval document issued by the State Bureau of Shenzhen Nanshan District dated 1 March 2005, 深圳市中軟資源技術服務有限公司 ("Chinasoft Resources Shenzhen"), a subsidiary of the Company, had been designated as a newly established software enterprise. As a result, Chinasoft Resources Shenzhen was entitled to the two year's exemption from income tax followed by three years of 50% tax reduction commencing from the first profit-making year with effect from 2004.

8. **TAXATION** – Continued

The tax charge for the year can be reconciled to profit before taxation as follows:

	2006 **RMB'000**	2005 RMB'000
(Loss) profit before taxation	**(51,972)**	48,714
Tax at PRC Enterprise Income Tax rate of 33%	**(17,151)**	16,076
Tax effect of share of net results of associates	**(821)**	(592)
Tax effect attributable to tax exemptions and concessions granted to PRC subsidiaries	**(19,609)**	(15,718)
Tax effect of expenses not deductible for tax purpose	**49,268**	3,974
Tax effect of income not taxable for tax purpose	**(947)**	(7)
Tax effect of utilisation of tax losses previously not recognised	**(612)**	–
Tax effect of tax losses not recognised	**1,240**	261
Effect of different tax rate of subsidiaries	**513**	1,405
Others	**–**	319
Tax charge for the year	**11,881**	5,718

9. (LOSS) PROFIT FOR THE YEAR

	2006 RMB'000	2005 RMB'000
(Loss) profit for the year has been arrived at after charging:		
Directors' remuneration (note 10)	**3,636**	2,489
Other staff costs	**89,956**	53,901
Retirement benefit costs	**6,856**	3,182
Share option expenses	**2,907**	2,322
Total staff costs	**103,355**	61,894
Less: Staff costs capitalised as development costs	**(9,053)**	(5,424)
	94,302	56,470
Share option expenses		
- granted to employees of an associate	**31**	150
- granted to customers	**224**	465
	255	615
Allowance for inventories	**138**	1,181
Research and development costs expensed	**4,153**	8,890
Auditors' remuneration	**2,288**	1,518
Cost of inventories recognised as an expense	**55,880**	195,608
Depreciation of property, plant and equipment	**6,496**	3,646
Minimum lease payments in respect of land and buildings	**8,997**	4,605
Share of taxation of associates (included in share of net results of associates)	**189**	283
and after crediting:		
Gain on fair value change on held-for-trading investment	**150**	–
Interest income	**3,676**	548
Government grants	**4,422**	–
Gain on disposal of property, plant and equipment	**2**	–
Net foreign exchange gains	**410**	–
Tax incentive subsidies	**394**	3,441

10. DIRECTORS' AND EMPLOYEES' EMOLUMENTS

Directors' emoluments

Details of emoluments to the directors of the Company for the year ended 31 December 2006 are as follows:

	Executive director							Non-executive director						Independent non-executive director				
	Chen Yuhong RMB'000	Peng Jiang RMB'000	Duncan Chiu RMB'000	Cui Hui RMB'000	Tang Min RMB'000	Wang Hui RMB'000	Tang Zhenming RMB'000	Duncan Chiu RMB'000	Cui Hui RMB'000	Tang Min RMB'000	David Chiu RMB'000	Liu Zheng RMB'000	Timothy Chen Yung Cheng RMB'000	He Ning RMB'000	Zeng Zhijie RMB'000	Au Yeung Shiu Kau Peter RMB'000	Leung Wing Yin Patrick RMB'000	Total RMB'000
Fees for:																			
Executive directors	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
Non-executive directors	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
Independent non-executive directors	–	–	–	–	–	–	–	–	–	–	–	–	–	105	105	15	–	225
Other emoluments for executive directors:																		
Salaries and other benefits	772	99	–	–	–	629	413	116	116	116	–	–	–	–	–	–	–	2,261
Share option expense	356	99	–	–	–	278	208	28	14	–	–	–	–	–	–	–	–	983
Retirement benefit costs	26	5	–	–	–	26	18	–	–	–	–	–	–	–	–	–	–	75
	1,154	203	–	–	–	933	639	144	130	116	–	–	–	105	105	15		3,544
Other emoluments for non-executive directors	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
Other emoluments for independent non-executive directors	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	92	92
	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	92	92
Total directors' remuneration	1,154	203	–	–	–	933	639	144	130	116	–	–	–	105	105	15	92	3,636

Details of emoluments to the directors of the Company for the year ended 31 December 2005 are as follows:

	Executive director							Non-executive director			Independent non-executive director			
	Chen Yuhong RMB'000	Peng Jiang RMB'000	Duncan Chiu RMB'000	Cui Hui RMB'000	Tang Min RMB'000	Wang Hui RMB'000	Tang Zhenming RMB'000	David Chiu RMB'000	Chen Qiwei RMB'000	Liu Zheng RMB'000	He Ning RMB'000	Zeng Zhijie RMB'000	Au Yeung Shiu Kau Peter RMB'000	Total RMB'000
Fees for:														
Executive directors	–	–	–	–	–	–	–	–	–	–	–	–	–	–
Non-executive directors	–	–	–	–	–	–	–	–	–	–	–	–	–	–
Independent non-executive director	–	–	–	–	–	–	–	–	–	–	64	64	64	192
Other emoluments for executive directors:														
Salaries and other benefits	495	405	120	120	120	47	35	–	–	–	–	–	–	1,342
Share option expense	352	214	62	–	–	31	21	–	–	–	–	–	–	680
Retirement benefit costs	14	14	–	–	–	2	1	–	–	–	–	–	–	31
Discretionary bonus (note)	–	–	–	–	–	–	–	–	–	–	–	244	–	244
	861	633	182	120	120	80	57	–	–	–	64	308	64	2,489
Other emoluments for non-executive directors	–	–	–	–	–	–	–	–	–	–	–	–	–	–
Other emoluments for independent non-executive directors	–	–	–	–	–	–	–	–	–	–	–	–	–	–
	–	–	–	–	–	–	–	–	–	–	–	–	–	–
Total directors' remuneration	861	633	182	120	120	80	57	–	–	–	64	308	64	2,489

Note: After a review by the board of directors ("BOD") on 7 October 2005, the BOD resolved to pay a special bonus of RMB244,000 to Mr. Zeng Zhijie in recognition of his duties, responsibilities and satisfactory performance.

10. DIRECTORS' AND EMPLOYEES' EMOLUMENTS – Continued

Employees' emoluments – Continued

Of the five individuals with the highest emoluments in the Group, two (2005: three) were directors of the Company whose emoluments were included above. In 2005, one of the three highest paid directors was promoted from an employee to a director. The emoluments of the remaining three (2005: two) highest paid individuals, (2005: including the employee's emoluments of the director before his promotion) were as follows:

	2006	2005
	RMB'000	RMB'000
Salaries and other benefits	**2,193**	1,420
Share option expenses	**261**	364
Retirement benefit costs	**50**	40
Discretionary bonus	**189**	143
	2,693	1,967

Their emoluments were within the following bands:

	No. of employees	
	2006	2005
HK$nil to HK$1,000,000 (equivalent to RMB1,000,000)	**3**	4
HK$1,000,001 to HK$1,500,000 (equivalent to RMB 1,500,000)	**2**	1
	5	5

During both years, no emoluments were paid by the Group to the five highest paid individuals (including directors and employees) as an inducement to join or upon joining the Group, or as compensation for loss of office.

None of the directors waived any emoluments during both years.

11. DIVIDEND

	2006	2005
	RMB'000	RMB'000
Dividend recognised as distribution during the year:		
Final paid in respect of prior year - HK2.5 cents per share (2005: HK1 cent), equivalent to RMB2.6 cents per share (2005: RMB1.06 cents)	**18,309**	7,394

A final dividend of HK$0.001 (equivalent to RMB0.001) per share has been proposed by the directors and is subject to approval by the shareholders in general meeting.

12. (LOSS) EARNINGS PER SHARE

The calculation of the basic and diluted (loss) earnings per share attributable to the ordinary equity holders of the parent is based on the following data:

	2006	2005
	RMB'000	RMB'000
(Loss) earnings for the purposes of calculating basic and diluted (loss) earnings per share	**(66,593)**	39,656

	Number of shares	
	2006	2005
Weighted average number of ordinary shares for the purpose of calculating basic (loss) earnings per share	**747,120,005**	713,455,342
Effect of dilutive potential ordinary shares issuable under the Company's share option scheme		17,278,640
Weighted average number of ordinary shares for the purpose of calculating diluted earnings per share		730,733,982

The diluted loss per share for the year ended 31 December 2006 was not presented as the exercise of the share options and conversion of the redeemable convertible preferred shares outstanding would result in a decrease in loss per share.

13. PROPERTY, PLANT AND EQUIPMENT

	Leasehold improvements RMB'000	Furniture, fixtures and equipment RMB'000	Motor vehicles RMB'000	Total RMB'000
COST				
At 1 January 2005	3,623	10,280	3,047	16,950
Exchange adjustments	(3)	(2)	–	(5)
Additions	963	6,929	3,529	11,421
Acquired on acquisition of subsidiaries	635	3,198	–	3,833
Written off	–	(21)	–	(21)
At 31 December 2005	5,218	20,384	6,576	32,178
Exchange adjustments	(7)	(4)	–	(11)
Additions	1,720	20,122	2,172	24,014
Acquired on acquisition of subsidiaries	–	1,491	149	1,640
Disposals	(3)	–	(145)	(148)
At 31 December 2006	6,928	41,993	8,752	57,673
DEPRECIATION				
At 1 January 2005	1,537	3,269	462	5,268
Exchange adjustments	(2)	(1)	–	(3)
Provided for the year	843	2,454	349	3,646
Eliminated on written off	–	(21)	–	(21)
At 31 December 2005	2,378	5,701	811	8,890
Exchange realignment	(4)	(1)	–	(5)
Provided for the year	943	4,860	693	6,496
Eliminated on disposals	–	–	(34)	(34)
At 31 December 2006	3,317	10,560	1,470	15,347
CARRYING VALUES				
At 31 December 2006	3,611	31,433	7,282	42,326
At 31 December 2005	2,840	14,683	5,765	23,288

14. INTANGIBLE ASSETS

	Development costs RMB'000	Technical knowhow RMB'000	Software RMB'000	Contract-based customer-related intangible RMB'000	Technical expertise RMB'000	Total RMB'000
COST						
At 1 January 2005	9,628	6,222	–	–	–	15,850
Additions	5,424	500	120	–	–	6,044
At 31 December 2005	15,052	6,722	120	–	–	21,894
Acquired on acquisitions (note 32)	–	–	–	19,704	11,080	30,784
Additions	9,410	–	–	–	–	9,410
At 31 December 2006	24,462	6,722	120	19,704	11,080	62,088
AMORTISATION/IMPAIRMENT						
At 1 January 2005	617	324	–	–	–	941
Provided for the year	2,272	678	–	–	–	2,950
At 31 December 2005	2,889	1,002	–	–	–	3,891
Impairment loss recognised for the year	–	–	–	–	1,087	1,087
Provided for the year	4,322	672	29	1,970	1,223	8,216
At 31 December 2006	7,211	1,674	29	1,970	2,310	13,194
CARRYING VALUES						
At 31 December 2006	17,251	5,048	91	17,734	8,770	48,894
At 31 December 2005	12,163	5,720	120	–	–	18,003

Development costs are internally generated. All of the Group's technical knowhow, software, contract-based customer-related intangible and technical expertise were acquired from third parties.

The above intangible assets have definite useful lives and are amortised on a straight-line basis over the following periods:

Development costs and software	3-5 years
Technical knowhow	10 years
Contract-based customer-related intangible	5 years
Technical expertise	5 years

15. GOODWILL

	RMB'000
COST	
At 1 January 2005	27,226
Arising on acquisition of subsidiaries	51,942
At 31 December 2005	79,168
Arising on acquisition of subsidiaries (note 31 (a) and (b))	32,951
Arising on acquisition of additional interests in a subsidiary	29,026
Impairment loss recognised for the year	(988)
At 31 December 2006	140,157

Impairment testing on goodwill

As explained in note 6, the Group uses business segments as its primary segment for reporting segment information. For the purposes of impairment testing, the carrying amount of goodwill (net of impairment loss) as at 31 December 2006 has been allocated as follows:

	2006 **RMB'000**	2005 RMB'000
IT outsourcing		
– Cyber Resources	**31,963**	–
– Chinasoft Resources Beijing	**80,968**	51,942
	112,931	51,942
IT consulting and training services	**830**	830
Chinasoft Beijing (note)	**26,396**	26,396
	140,157	79,168

Note: The carrying amount of goodwill of RMB26,396,000 was resulted from the acquisition of additional interest of Chinasoft Beijing in 2004. The goodwill contributes to the cash flows of multiple business segments which cannot be allocated on a non-arbitrary basis to individual business segments.

During the year ended 31 December 2006, the Group recognised an impairment loss of RMB988,000 in relation to goodwill arising on acquisition of Chinasoft Resource (International) Limited. Chinasoft Resource (International) Limited is engaged in the business of provision of IT outsourcing services. As the management of the Group would take up the net liabilities of RMB988,000 incurred by the sole former shareholder on the date of acquisition of Chinasoft Resource (International) Limited, full impairment on the carrying amount of goodwill was made. Save as the aforesaid, management of the Group determines that there are no impairments of any of its CGUs containing goodwill.

The basis of the recoverable amounts of the above CGUs and the methodology used for the year are summarised below:

15. GOODWILL – Continued

IT outsourcing

The recoverable amount of this CGU is fair value less costs to sell and has been determined based on the valuation at 31 December 2006 prepared by independent professional valuers. The valuation is based on the management's 2006 financial information and a weighted average of market value of invested capital over earnings before taxation of 14 and that over earnings of 17 based on comparable companies in the relevant industry. Management believes that any reasonably possible change in any of these assumptions will not cause the aggregate carrying amount of the CGU to exceed its aggregate recoverable amount.

IT consulting and training services

The recoverable amount of this CGU is fair value less costs to sell and has been determined based on the valuation at 31 December 2006 prepared by independent professional valuers. The valuation is based on the management's 2006 financial information and a weighted average of market value of invested capital over earnings before taxation of 14 and that over earnings of 17 based on comparable companies in the relevant industry. Management believes that any reasonably possible change in any of these assumptions will not cause the aggregate carrying amount of the CGU to exceed its aggregate recoverable amount.

Chinasoft Beijing

The recoverable amount of this CGU is fair value less costs to sell and has been determined based on the valuation at 31 December 2006 prepared by independent professional valuers. The valuation is based on the management's 2006 financial information and a weighted average of market value of invested capital over earnings before taxation of 14 and that over earnings of 17 based on comparable companies in the relevant industry. Management believes that any reasonably possible change in any of these assumptions will not cause the aggregate carrying amount of the CGU to exceed its aggregate recoverable amount.

16. INTERESTS IN ASSOCIATES

	2006 RMB'000	2005 RMB'000
Unlisted cost of investments in associates	**6,500**	8,069
Share of post-acquisition profits, net of dividend received	**1,952**	234
	8,452	8,303

Particulars of the Group's associates at 31 December 2006 are as follows:

Name of associate	**Form of business structure**	**Place of establishment**	**Principal place of operation**	**Proportion of registered capital held by the Group**	**Nature of business**
武漢中軟國際信息技術有限公司 Wuhan Chinasoft International Information Technology Limited ("Chinasoft Wuhan")	Equity joint venture enterprise	PRC	PRC	46%	Provision of solutions and information technology consulting services
北京中烟信息技術有限公司 China National Tobacco Information Company Limited ("China Tobacco")	Equity joint venture enterprise	PRC	PRC	20%	Maintenance of a policy making system for the production, operation and management of the tobacco industry

Included in the unlisted cost of investments in associates is goodwill of RMB3,052,000 arising on acquisition of China Tobacco in 2005.

17. TRADEMARK USE RIGHT

	RMB'000
COST	
Additions and at 31 December 2006	**1,887**
AMORTISATION	
Provided for the year and balance at 31 December 2006	**148**
CARRYING VALUE	
At 31 December 2006	**1,739**
Analysed for reporting purposes as:	
Non-current assets	**1,550**
Current assets	**189**
	1,739

The trademark use right is amortised on a straight-line basis over 10 years.

18. INVENTORIES

	2006 RMB'000	2005 RMB'000
Computer hardware, equipment and software products	**34,107**	22,670

19. TRADE AND OTHER RECEIVABLES

	2006 RMB'000	2005 RMB'000
Trade receivables	**208,273**	142,593
Advances to suppliers	**6,929**	2,362
Deposits, prepayments and other receivables	**18,761**	37,158
	233,963	182,113

The credit terms of the Group range from 30 to 90 days. An aged analysis of trade receivables is as follows:

	2006 RMB'000	2005 RMB'000
Within 90 days	**124,536**	83,047
Between 91-180 days	**16,504**	12,740
Between 181-365 days	**33,966**	24,503
Between 1-2 years	**27,362**	11,333
Over 2 years	**5,905**	10,970
	208,273	142,593

20. TRADE RECEIVABLE FROM AN ASSOCIATE

At the balance sheet date, the trade receivable is aged between 181 and 365 days.

21. TRADE RECEIVABLES FROM RELATED COMPANIES/AMOUNT DUE FROM A RELATED COMPANY

At the balance sheet date, the trade receivables are aged within 90 days. The amount due from a related company as at 31 December 2005 was unsecured, non-interest bearing and repayable on demand.

22. HELD-FOR-TRADING INVESTMENT

	2006 RMB'000	2005 RMB'000
Equity securities listed in Hong Kong, at quoted market price	**501**	–

23. PLEDGED DEPOSITS/BANK BALANCES

Pledged deposits

The amount represents deposits pledged to two banks as guarantees for short-term trade facilities granted to the Group and are therefore classified as current assets.

The deposits carry interest at the prevailing market interest rate at 0.72% per annum. The pledged deposits will be released upon the settlement of relevant trade facilities.

Bank balances

The amounts comprise short-term bank deposits carry at the prevailing market interest rates which range from 2.25% to 2.80% per annum with an original maturity of three months or less.

24. TRADE AND OTHER PAYABLES

	2006 RMB'000	2005 RMB'000
Trade payables	**64,579**	80,438
Deposits received from customers	**2,593**	906
Other payables and accrued charges	**40,498**	16,926
	107,670	98,270

An aged analysis of trade payables is as follows:

	2006 RMB'000	2005 RMB'000
Within 90 days	**17,715**	28,978
Between 91-180 days	**7,193**	11,167
Between 181-365 days	**14,443**	15,931
Between 1-2 years	**13,453**	24,280
Over 2 years	**11,775**	82
	64,579	80,438

25. TRADE PAYABLE TO A RELATED COMPANY/AMOUNT(S) DUE TO A SHAREHOLDER/RELATED COMPANIES

At the balance sheet date, the trade payable is aged within 90 days. The amount due to a shareholder and amounts due to related companies are unsecured, non-interest bearing and repayable on demand.

26. BILLS PAYABLE

An aged analysis of bills payable is as follows:

	2006	2005
	RMB'000	RMB'000
Within 90 days	**22,771**	14,420
Between 91-180 days	**1,481**	12,361
	24,252	26,781

27. DEFERRED TAX LIABILITIES

The following are the major deferred tax liabilities recognised by the Group in respect of development costs and movement thereon during the current and prior year:

	RMB'000
At 1 January 2005	1,221
Charge to the consolidated income statement	603
At 31 December 2005	1,824
Charge to the consolidated income statement	764
At 31 December 2006	2,588

At the balance sheet date, the Group had unused tax losses available for offset against future profits of approximately RMB5,697,000 (2005: RMB1,766,000) which may be carried forward indefinitely except losses of approximately RMB1,674,000 (2005: RMB1,856,000) which will expire in 2011. No deferred tax asset has been recognised in respect of such deductible temporary difference due to the unpredictability of future profit streams.

28. REDEEMABLE CONVERTIBLE PREFERRED SHARES

Redeemable convertible preferred shares of HK$0.50 each:	**Number of shares**	**Nominal amount** HK$'000
Authorised		
Increase in authorised preferred share capital		
and balance at 31 December 2005 and 2006	625,000,000	31,250
Issued and fully paid		
Issued during the year and		
balance at 31 December 2006	194,500,000	9,725

At the extraordinary general meeting of the Company held on 28 December 2005, ordinary and special resolutions approving the following were passed and the following took effect:

(i) the Re-stated Memorandum and Articles of the Company (the "M&A") was adopted and replaced the then M&A of the Company;

(ii) the authorised share capital of the Company was increased from HK$75,000,000 divided into 1,500,000,000 ordinary shares of HK$0.05 each to HK$106,250,000 divided into 1,500,000,000 ordinary shares of HK$0.05 each and 625,000,000 redeemable convertible preferred shares (the "Series A Preferred Shares") of HK$0.05 each, with the respective rights and privileges, and subject to the restrictions, set forth in the Re-stated M&A.

(iii) the issue by the Company of the Series A Preferred Shares pursuant to the terms of the Subscription Agreement, the Investors' Rights Agreement and the relevant provision in the Re-stated M&A and the grant of anti-dilution rights to the holders of the Series A Preferred Shares stated in the Re-stated M&A.

On 6 January 2006, the Company announced the completion of the first subscription of a total of 194,500,000 Series A Preferred Shares of the Company by Microsoft Corporation ("Microsoft") and International Finance Corporation ("IFC"). Under the first subscription arrangement, 97,250,000 Series A Preferred Shares with a par value of HK$0.05 each were allotted and issued at a price of HK$0.8 each to each of Microsoft and IFC, raising a total of approximately RMB162,240,000 (equivalent to US$19,999,990) for the Company. Details of the issue of Series A Preferred Shares and first subscription were set out in a circular dated 2 December 2005 issued by the Company.

28. REDEEMABLE CONVERTIBLE PREFERRED SHARES – Continued

The Series A Preferred Shares are denominated in Hong Kong dollars. Holders of the Series A Preferred Shares shall be entitled to a fixed cumulative dividend of 5.5% per annum of the principal amount of the Series A Preferred Shares to be first payable on a quarterly basis following the expiry of a six-month period after 6 January 2006. They entitle the holders to convert them into ordinary shares of the Company at any time between the date of issue and up to the maturity date on the sixth anniversary of 6 January 2006 and without payment of any additional consideration, at the initial conversion rate of 1:1, subject to adjustment in respect of anti-dilution protections from time to time as provided in the M&A.

If the Company fails to complete the baseline amount of US$2,000,000 (equivalent to RMB15,560,000) as set forth in the commercial agreement dated 26 September 2005 entered into between Microsoft and the Company prior to the first anniversary of 6 January 2006, upon receipt of a written notice by Microsoft, the Company shall redeem in cash such number of the Series A Preferred Shares then held by Microsoft plus the accrued and unpaid dividends thereon at any time with an aggregate amount of up to US$5,000,000 (equivalent to RMB38,900,000). If all the Series A Preferred Shares then held by Microsoft are redeemed by the Company, IFC shall have a right, to require the Company, to redeem the Series A Preferred Shares held by it in an aggregate amount of not more than US$5,000,000 (equivalent to RMB38,900,000). All accrued and unpaid dividends payable on the Series A Preferred Shares held by IFC shall also be payable by the Company at that time.

If the Series A Preferred Shares have not been converted or redeemed, they will be mandatorily redeemed by the Company on the sixth anniversary of 6 January 2006.

All the detailed terms and conditions, including the above, are set out, inter alia, in the circular dated 2 December 2005 issued by the Company.

The Group incurred expenses of RMB10,764,000 for the issuance of the Series A Preferred Shares. Such expenses have been recognised in the consolidated income statement for the year.

The Series A Preferred Shares contain the financial liability and embedded derivatives and the entire instrument is designated as financial liability at fair value through profit or loss on initial recognition.

At the date of issue and balance sheet date, the fair value of the financial liability of the Series A Preferred Shares was estimated by using market interest rates of 10.04% and 9.79% respectively. The fair value of the embedded derivatives is calculated using the binomial option pricing model. The inputs into the model were as follows:

Share price	HK$0.92-HK$1.73
Exercise price	HK$0.8
Time to maturity	5-6 years
Risk free rate	3.69%-4.00%
Share price volatility	36.52%-52.09%

28. REDEEMABLE CONVERTIBLE PREFERRED SHARES – Continued

Share price volatility was estimated by the average annualised standard deviations of the continuously compounded rates of return on the Company's share prices.

The movement of the fair value of the Series A Preferred Shares for the year is set out as below:

	RMB$'000
Carrying amount at 6 January 2006	161,824
Loss arising on changes of fair value	110,558
As at 31 December 2006	272,382

Included in the loss arising on changes of fair value, there is an interest expense of RMB 3,902,000 determined using the effective interest method. As at 31 December 2006, interest payable to preferred shareholders of RMB3,902,000 was included in trade and other payables in the consolidated balance sheet.

29. SHARE CAPITAL

Ordinary shares of HK$0.05 each:	**Number of shares**	**Nominal amount** HK$'000
Authorised		
At 1 January 2005, 31 December 2005 and 2006	1,500,000,000	75,000

	Notes	**Number of shares**	**Amount** HK$	**Amount shown in the financial statements** RMB'000
Issued and fully paid				
At 1 January 2005		697,500,000	34,875,000	36,968
Issue of new shares	(a)	34,872,453	1,743,623	1,848
At 31 December 2005		732,372,453	36,618,623	38,816
Issue of new shares	(b)	26,445,023	1,322,251	1,368
At 31 December 2006		758,817,476	37,940,874	40,184

Notes:

(a) Pursuant to an ordinary resolution passed by the shareholders of the Company on 22 June 2005, 34,872,453 new shares of the Company of HK$0.05 each were allotted and issued as fully paid to China National Computer Software & Technology Service Corporation (Hong Kong) Limited ("CS&S (HK)") as the first portion of consideration shares of HK$1.01 each for the acquisition of 51% equity interest in the registered capital of Chinasoft Resources Beijing.

(b) Pursuant to an ordinary resolution passed by the shareholders of the Company on 22 June 2005 and after the achievement of the Performance Hurdle as described in the circular of the Company dated 6 June 2005, 23,248,302 new shares of the Company of HK$0.05 each were allotted and issued as fully paid to CS&S (HK) as the second portion of consideration shares of HK$1.01 each for the acquisition of 51% equity interest in the registered capital of Chinasoft Resources Beijing during the year.

Pursuant to a resolution passed by the directors of the Company on 4 July 2006, 3,196,721 new shares of the Company of HK$0.05 each were allotted and issued as fully paid to Beijing Opportune Technology Development Company Ltd. ("Opportune Technology") as the consideration shares of HK$1.09 each for the acquisition of the Mobile and Embedded Divison of Opportune Technology.

All the shares which were issued by the Company during the year rank pari passu with each other in all respects.

30. RESERVES

Share premium

In accordance with the Companies Law of the Cayman Islands, the share premium account is distributable to the equity shareholders of the Company provided that immediately following the date on which the dividend is proposed to be distributed, the Company will be in a position to pay off its debts as they fall due in the ordinary course of business. The share premium may also be distributed in the form of fully paid bonus shares.

Pursuant to an ordinary resolution passed by the directors of the Company on 30 March 2006, dividend for 2006 in the amount of RMB18,309,000 was paid and distributed out of the share premium account.

General reserve fund and statutory enterprise expansion fund

As stipulated by the relevant laws and regulations in the PRC, Chinasoft Beijing, Chinasoft Guangzhou, Chinasoft Hangzhou, Chinasoft Kunming, Chinasoft Hunan, Cyber Resources, Chinasoft Resources Beijing, and Chinasoft Resources Shanghai (the "Chinasoft subsidiaries") are required to provide for the general reserve fund and the statutory enterprise expansion fund. Appropriations to such reserve funds are made out of net profit after taxation as reported in the statutory financial statements of the Chinasoft subsidiaries prepared in accordance with accounting principles generally accepted in the PRC and the amount and allocation basis are decided by its board of directors annually. The general reserve fund can be used to make up prior year losses of the Chinasoft subsidiaries, if any, and can be applied in conversion into capital by means of capitalisation issue. The statutory enterprise expansion fund is used for expanding the capital base of the Chinasoft subsidiaries by means of capitalisation issue.

Statutory surplus reserve fund and statutory public welfare fund

As stipulated by the relevant laws and regulations in the PRC, 廈門中軟海晟信息技術有限公司 and Chinasoft Resources Shenzhen is required to provide for the statutory surplus reserve fund and the statutory public welfare fund. Appropriations to such funds are made out of 5% to 10% of the net profit after taxation as reported in the statutory financial statements of 廈門中軟海晟信息技術有限公司 and Chinasoft Resources Shenzhen prepared in accordance with accounting principles generally accepted in the PRC. The statutory surplus reserve fund can be used to make up prior year losses, to expand production operations or to increase registered capital of 廈門中軟海晟信息技術有限公司 and Chinasoft Resources Shenzhen. The statutory public welfare fund can be used for employees' collective welfare benefits.

Pursuant to a notice issued by the Ministry of Finance regarding the change of accounting treatment of profit appropriation of statutory public welfare fund after the implementation of PRC Company Law, no statutory public welfare fund will be accrued from 2006 onwards. The remaining balance of statutory public welfare fund was transferred to statutory surplus reserve fund.

31. ACQUISITION OF SUBSIDIARIES

(a) In July 2006, the Group acquired an additional 50% equity interest in the registered capital of Cyber Resources for a cash consideration of RMB36,605,000. Cyber Resources is engaged in the business of provision of IT outsourcing services. It was previously an associate of the Group in which the Group had a 26% equity interest. At the acquisition date, the carrying amount of the interest in an associate amounted to RMB2,371,000. Acquisition of the subsidiary was accounted for by the purchase method.

The fair values of the identifiable assets and liabilities of the subsidiary acquired during the year have no significant differences from their respective carrying amounts. The net assets acquired in the transaction, representing the acquiree's carrying amount and fair value, and the goodwill arising, are as follows:

	2006 RMB'000
Net assets acquired:	
Property, plant and equipment	**1,626**
Inventories	**1,629**
Trade and other receivables	**7,367**
Amount due from a related company	**911**
Bank balances and cash	**1,901**
Trade and other payables	**(4,008)**
Taxation payable	**(198)**
	9,228
Minority interests	**(2,215)**
Goodwill on acquisition	**31,963**
Total consideration	**38,976**
Satisfied by:	
Cash	**33,894**
Consideration payable	**2,711**
Reclassification of interest in an associate	**2,371**
	38,976
Net cash outflow arising on acquisition:	
Cash consideration paid	**33,894**
Bank balances and cash acquired	**(1,901)**
Net outflow of cash and cash equivalents in respect of the acquisition of a subsidiary	**31,993**

31. ACQUISITION OF SUBSIDIARIES – Continued

(b) In August 2006, the Group acquired the entire interest in the issued share capital of Chinasoft Resource (International) Limited for a cash consideration of HK$1 (equivalent to RMB1). Chinasoft Resource (International) Limited is engaged in the business of provision of IT outsourcing services. Acquisition of the subsidiary was accounted for by the purchase method.

The fair values of the identifiable assets and liabilities of the subsidiary acquired during the year have no significant differences from their respective carrying amounts. The net liabilities assumed in the transaction, representing the acquiree's carrying amount and fair value, and the goodwill arising, are as follows:

	2006 **RMB'000**
Net liabilities assumed:	
Property, plant and equipment	**14**
Trade receivables	**662**
Bank balances and cash	**4,182**
Amounts due to related companies	**(5,846)**
	(988)
Goodwill on acquisition	**988**
Total consideration	**–**
Inflow of cash and cash equivalents in respect of the acquisition of a subsidiary	**4,182**

The goodwill arising on the acquisition of Cyber Resources is attributable to the anticipated profitability of the provision of the Group's services in the IT outsourcing market and the anticipated future operating synergies from the combination. The goodwill arising on the acquisition of Chinasoft Resource (International) Limited was fully impaired at the date of acquisition.

Cyber Resources and Chinasoft Resource (International) Limited contributed RMB24,690,000 and RMB2,520,000 respectively to the Group's turnover and profit of RMB7,306,000 and loss of RMB261,000 respectively to the Group's loss for the year between the date of acquisition and the balance sheet date.

If the acquisitions had been completed on 1 January 2006, total Group turnover for the year would have been RMB375,705,000, and loss for the year would have been RMB62,677,000. The proforma information is for illustrative purposes only and is not necessarily an indication of turnover and results of operations of the Group that actually would have been achieved had the acquisition been completed on 1 January 2006, nor is it intended to be a projection of future results.

31. ACQUISITION OF SUBSIDIARIES – Continued

(c) In July 2005, the Group acquired 51% equity interest in the register capital of Chinasoft Resources Beijing for a consideration of the issuance of a total of 58,120,755 ordinary shares of the Company from CS&S (HK), a shareholder of the Company. Chinasoft Resources Beijing has two subsidiaries, namely Chinasoft Resources Shenzhen and Chinasoft Resources Shanghai. Acquisition of the subsidiaries was accounted for by the purchase method.

The fair values of the identifiable assets and liabilities of the subsidiaries acquired during the year had no significant differences from their respective carrying amounts. The net assets acquired in the transaction, representing the acquiree's carrying amount and fair value, and the goodwill arising, were as follows:

	2005 RMB'000
Net assets acquired:	
Property, plant and equipment	3,833
Inventories	1,479
Trade and other receivables	9,540
Bank balances and cash	15,214
Trade and other payables	(9,562)
	20,504
Minority interests	(10,692)
Goodwill on acquisition	51,942
Total consideration	61,754
Satisfied by:	
Shares issued and to be issued (note)	61,754
Inflow of cash and cash equivalents in respect of the acquisition of subsidiaries	15,214

31. ACQUISITION OF SUBSIDIARIES – Continued

Note:

The consideration for the acquisition of Chinasoft Resources Beijing was satisfied by the issuance of 34,872,453 ordinary shares of the Company with nominal value per share of HK$0.05 each during the year (the "first portion of consideration shares") and the remaining 23,248,302 ordinary shares (the "second portion of consideration shares") would be issued in the year ended 31 December 2006 subject to the achievement of the Performance Hurdle as described in the circular of the Company dated 6 June 2005. The directors were of the opinion that the Performance Hurdle would be achieved. The fair value of the first and second portion of consideration shares, determined using the published price available at the date of the acquisition at HK$1.01, amounted to RMB37,334,000 (equivalent to HK$35,221,000) and RMB 24,420,000 (equivalent to HK$23,481,000) respectively. The amount of the second portion of consideration shares of RMB24,420,000 was presented as issuable shares in the consolidated statement of changes of equity.

The goodwill arising on the acquisition of Chinasoft Resources Beijing was attributable to the anticipated profitability of the distribution of the Group's products in the IT outsourcing market and the anticipated future operating synergies from the combination.

Chinasoft Resources Beijing contributed RMB30,680,000 to the Group's turnover and RMB6,997,000 to the Group's profit for the year between the date of acquisition and the balance sheet date.

If the acquisition had been completed on 1 January 2005, total Group turnover for the period would have been RMB420,800,000, and profit for the year would have been RMB44,374,000. The proforma information was for illustrative purposes only and was not necessarily an indication of turnover and results of operations of the Group that actually would have been achieved had the acquisition been completed on 1 January 2005, nor was it intended to be a projection of future results.

32 ACQUISITION OF CONTRACT-BASED CUSTOMER-RELATED INTANGIBLE AND TECHNICAL EXPERTISE

(a) In May 2006, the Group acquired the technical expertise of Powerise International Software Co., Ltd. and Powerise Japan Co., Ltd., representing employees with experience in enterprise resource planning system and in the Japanese market, for a cash consideration of US$1,000,000 (equivalent to RMB7,800,000). The acquisition of the technical expertise enhances the Group's advantageous position in Microsoft business and rapid expansion into the Japanese market. Acquisition of the technical expertise was accounted for as an intangible asset (see note 14) and represented the cash consideration of US$1,000,000 (equivalent to RMB7,800,000). The outflow of cash and cash equivalents in respect of the acquisition of technical expertise was US$900,000 (equivalent to RMB7,020,000) and the remaining US$100,000 (equivalent to RMB780,000) was included in consideration payable on acquisition of a subsidiary and technical expertise at the balance sheet date.

32 ACQUISITION OF CONTRACT-BASED CUSTOMER-RELATED INTANGIBLE AND TECHNICAL EXPERTISE – Continued

(b) In July 2006, the Group acquired the Mobile and Embedded Division from Opportune Technology. The acquired assets comprised of the contract-based customer relationship with Microsoft and employees with strong expertise in the outsourcing operation of Microsoft. As one of the Group's major strategic clients, Microsoft's outsourcing business has always been an important area for development by the Group. With the acquisition, the Group is rapidly enlarging its market share in Microsoft business.

The total consideration of the acquisition is US$3,000,000 (equivalent to RMB23,400,000), comprising a cash consideration of US$500,000 (equivalent to RMB3,900,000) and the issuance of consideration shares which amount to a maximum of US$2,500,000 (equivalent to RMB19,500,000). During the year, the Company has issued 3,196,721 ordinary shares with nominal value per share of HK$0.05 each (the "first portion of consideration shares") for the acquisition and the remaining ordinary shares (the "second portion of consideration shares") will be issued after 1 July 2007 subject to the achievement of the revenue and the entering into a master contract with Microsoft as described in the announcement of the Company dated 4 July 2006. The directors are of the opinion that the revenue will be achieved. The fair value of the first and second portion of consideration shares, determined using the published price available at the date of the acquisition at HK$1.09, amounted to RMB3,484,000 (equivalent to HK$3,484,000) and RMB15,600,000 (equivalent to HK$15,600,000) respectively. The amount of the second portion of consideration shares of RMB15,600,000 was presented as deferred consideration in the consolidated balance sheet.

Acquisition of the contract-based customer-related intangible and technical expertise was accounted for as intangible assets (see note 14) and represented the total consideration of RMB22,984,000. The outflow of cash and cash equivalents in respect of the acquisition was US$500,000 (equivalent to RMB3,900,000).

33 MAJOR NON-CASH TRANSACTIONS

Pursuant to an ordinary resolution passed and after the achievement of the Performance Hurdle, the issuance of the second portion of consideration shares of the Company for the acquisition of 51% equity interest in the registered capital of Chinasoft Resources Beijing by Chinasoft (HK), a subsidiary of the Group from CS&S (HK) was effected (see note 29(b)).

Pursuant to a resolution passed by the directors of the Company, Chinasoft (HK) acquired the Mobile and Embedded Division of Opportune Technology. Part of the consideration was satisfied by the issuance of new shares of the Company (see note 32(b)).

During the year ended 31 December 2005, pursuant to an agreement entered into between CS&S (HK) and Chinasoft (HK), a subsidiary of the Group on 28 April 2005, Chinasoft (HK) acquired 51% equity interest in the registered capital of Chinasoft Resources Beijing from CS&S (HK). The consideration is to be satisfied by the issuance of new shares of the Company.

34. OPERATING LEASE COMMITMENTS

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

	2006	2005
	RMB'000	RMB'000
Within one year	**13,512**	2,170
In the second to fifth year inclusive	**15,554**	5,105
	29,066	7,275

Operating lease payments represent rentals payable by the Group for certain office properties. Certain lease agreements for offices properties were replaced by new agreements entered into during the year. Leases are negotiated for lease terms ranging from a half year to three years (2005: a half year to six years) for the Group and rentals are normally fixed during the lease period.

35. CAPITAL COMMITMENT

	2006	2005
	RMB'000	RMB'000
Capital expenditure contracted for but not provided in the consolidated financial statements in respect of acquisition of software	**1,196**	–

36. SHARE OPTION SCHEME

The Company's share option scheme (the "Share Option Scheme") was adopted pursuant to a resolution passed on 2 June 2003 by the then shareholders for the purpose of providing incentives and rewards to the people and the parties working for the interest of the Group. Under the Share Option Scheme, the board of directors may grant options to eligible participants including the directors, full-time and part-time employees of the Company or any of its subsidiaries or associates, and suppliers and customers of the Company or any of its subsidiaries or associates to subscribe for shares in the Company in accordance with the terms of the Share Option Scheme. An offer for the grant of options must be accepted within 30 days from the date of offer, and a consideration of HK$1.00 is payable by each of the participants on acceptance of the grant of options. The Share Option Scheme will remain valid for a period of ten years commencing on 2 June 2003. An option may be exercised in accordance with the terms of the Share Option Scheme at any time during a period of not more than ten years after the date on which an offer of the grant of an option is accepted. The subscription price for shares under the Share Option Scheme will be a price determined by the board of directors and notified to each grantee and will be no less than the highest of (i) the closing price of the shares as stated in the Stock Exchange's daily quotations sheet on the date of offer, which must be a trading day; (ii) the average closing price of the shares as stated in the Stock Exchange's daily quotations sheets for the five trading days immediately preceding the date of offer and; (iii) the nominal value of a share.

The Company may grant options under the Share Option Scheme and any other share option schemes of the Company entitling the grantees to exercise up to an aggregate of 10% of the total number of shares in issue immediately upon the listing of the shares on the Stock Exchange and subject to renewal with shareholders' approval. However, the maximum number of shares which may be issued upon exercise of all outstanding options granted and yet to be exercised under the Share Option Scheme and any other share option schemes of the Company shall not exceed 30% of the total number of shares in issue from time to time. The number of shares in respect of which options may be granted to any individual in aggregate within any 12-month period is not permitted to exceed 1% of the shares of the Company in issue, without prior approval from the Company's shareholders. Options granted to substantial shareholders or independent non-executive directors in any one year exceeding the higher of 0.1% of the Company's shares in issue and with a value in excess of HK$5,000,000 must be approved by the Company's shareholders.

36. SHARE OPTION SCHEME – Continued

The movements of the share options granted to the directors and employees of the Group during the year ended 31 December 2006 are as follows:

Type of option holders	Date of grant	Exercise price	Vesting period	Exercise period	Number of share options Outstanding at 1.1.2006	Granted during the year	Reclassification during the year	Outstanding at 31.12.2006
Directors:								
Dr. Chen Yuhong	13.8.2003	HK$0.58	13.8.2003-12.8.2004	13.8.2004-12.8.2013	300,000	–	–	300,000
			13.8.2003-12.8.2005	13.8.2005-12.8.2013	300,000	–	–	300,000
			13.8.2003-12.8.2006	13.8.2006-12.8.2013	300,000	–	–	300,000
			13.8.2003-12.8.2007	13.8.2007-12.8.2013	300,000	–	–	300,000
	13.5.2004	HK$0.65	Nil	13.5.2004-12.5.2014	1,250,000	–	–	1,250,000
			13.5.2004-12.5.2005	13.5.2005-12.5.2014	1,250,000	–	–	1,250,000
			13.5.2004-12.5.2006	13.5.2006-12.5.2014	1,250,000	–	–	1,250,000
			13.5.2004-12.5.2007	13.5.2007-12.5.2014	1,250,000	–	–	1,250,000
	30.3.2006	HK$0.97	Nil	30.3.2006-29.3.2016	–	300,000	–	300,000
			30.3.2006-29.3.2007	30.3.2007-29.3.2016	–	300,000	–	300,000
			30.3.2006-29.3.2008	30.3.2008-29.3.2016	–	300,000	–	300,000
			30.3.2006-29.3.2009	30.3.2009-29.3.2016	–	300,000	–	300,000
Mr. Peng Jiang	13.8.2003	HK$0.58	13.8.2003-12.8.2004	13.8.2004-12.8.2013	200,000	–	(200,000)	–
			13.8.2003-12.8.2005	13.8.2005-12.8.2013	200,000	–	(200,000)	–
			13.8.2003-12.8.2006	13.8.2006-12.8.2013	200,000	–	(200,000)	–
			13.8.2003-12.8.2007	13.8.2007-12.8.2013	200,000	–	(200,000)	–
	13.5.2004	HK$0.65	Nil	13.5.2004-12.5.2014	750,000	–	(750,000)	–
			13.5.2004-12.5.2005	13.5.2005-12.5.2014	750,000	–	(750,000)	–
			13.5.2004-12.5.2006	13.5.2006-12.5.2014	750,000	–	(750,000)	–
			13.5.2004-12.5.2007	13.5.2007-12.5.2014	750,000	–	(750,000)	–
Mr. Duncan Chiu	13.5.2004	HK$0.65	Nil	13.5.2004-12.5.2014	250,000	–	–	250,000
			13.5.2004-12.5.2005	13.5.2005-12.5.2014	250,000	–	–	250,000
			13.5.2004-12.5.2006	13.5.2006-12.5.2014	250,000	–	–	250,000
			13.5.2004-12.5.2007	13.5.2007-12.5.2014	250,000	–	–	250,000
Dr. Cui Hui	13.5.2004	HK$0.65	Nil	13.5.2004-12.5.2014	125,000	–	–	125,000
			13.5.2004-12.5.2005	13.5.2005-12.5.2014	125,000	–	–	125,000
			13.5.2004-12.5.2006	13.5.2006-12.5.2014	125,000	–	–	125,000
			13.5.2004-12.5.2007	13.5.2007-12.5.2014	125,000	–	–	125,000
Mr. Wang Hui	13.8.2003	HK$0.58	13.8.2003-12.8.2004	13.8.2004-12.8.2013	250,000	–	–	250,000
			13.8.2003-12.8.2005	13.8.2005-12.8.2013	250,000	–	–	250,000
			13.8.2003-12.8.2006	13.8.2006-12.8.2013	250,000	–	–	250,000
			13.8.2003-12.8.2007	13.8.2007-12.8.2013	250,000	–	–	250,000
	13.5.2004	HK$0.65	Nil	13.5.2004-12.5.2014	875,000	–	–	875,000
			13.5.2004-12.5.2005	13.5.2005-12.5.2014	875,000	–	–	875,000
			13.5.2004-12.5.2006	13.5.2006-12.5.2014	875,000	–	–	875,000
			13.5.2004-12.5.2007	13.5.2007-12.5.2014	875,000	–	–	875,000
	30.3.2006	HK$0.97	Nil	30.3.2006-29.3.2016	–	250,000	–	250,000
			30.3.2006-29.3.2007	30.3.2007-29.3.2016	–	250,000	–	250,000
			30.3.2006-29.3.2008	30.3.2008-29.3.2016	–	250,000	–	250,000
			30.3.2006-29.3.2009	30.3.2009-29.3.2016	–	250,000	–	250,000
Dr. Tang Zhenming	13.8.2003	HK$0.58	13.8.2003-12.8.2004	13.8.2004-12.8.2013	80,000	–	–	80,000
			13.8.2003-12.8.2005	13.8.2005-12.8.2013	80,000	–	–	80,000
			13.8.2003-12.8.2006	13.8.2006-12.8.2013	80,000	–	–	80,000
			13.8.2003-12.8.2007	13.8.2007-12.8.2013	80,000	–	–	80,000
	13.5.2004	HK$0.65	Nil	13.5.2004-12.5.2014	650,000	–	–	650,000
			13.5.2004-12.5.2005	13.5.2005-12.5.2014	650,000	–	–	650,000
			13.5.2004-12.5.2006	13.5.2006-12.5.2014	650,000	–	–	650,000
			13.5.2004-12.5.2007	13.5.2007-12.5.2014	650,000	–	–	650,000
	30.3.2006	HK$0.97	Nil	30.3.2006-29.3.2016	–	200,000	–	200,000
			30.3.2006-29.3.2007	30.3.2007-29.3.2016	–	200,000	–	200,000
			30.3.2006-29.3.2008	30.3.2008-29.3.2016	–	200,000	–	200,000
			30.3.2006-29.3.2009	30.3.2009-29.3.2016	–	200,000	–	200,000
					18,920,000	3,000,000	(3,800,000)	18,120,000
Other employees	13.8.2003	HK$0.58	13.8.2003-12.8.2004	13.8.2004-12.8.2013	1,697,500	–	200,000	1,897,500
			13.8.2003-12.8.2005	13.8.2005-12.8.2013	1,697,500	–	200,000	1,897,500
			13.8.2003-12.8.2006	13.8.2006-12.8.2013	1,697,500	–	200,000	1,897,500
			13.8.2003-12.8.2007	13.8.2007-12.8.2013	1,697,500	–	200,000	1,897,500
	13.5.2004	HK$0.65	Nil	13.5.2004-12.5.2014	7,275,000	–	750,000	8,025,000
			13.5.2004-12.5.2005	13.5.2005-12.5.2014	7,275,000	–	750,000	8,025,000
			13.5.2004-12.5.2006	13.5.2006-12.5.2014	7,275,000	–	750,000	8,025,000
			13.5.2004-12.5.2007	13.5.2007-12.5.2014	7,275,000	–	750,000	8,025,000
	30.3.2006	HK$0.97	Nil	30.3.2006-29.3.2016	–	3,100,000	–	3,100,000
			30.3.2006-29.3.2007	30.3.2007-29.3.2016	–	3,100,000	–	3,100,000
			30.3.2006-29.3.2008	30.3.2008-29.3.2016	–	3,100,000	–	3,100,000
			30.3.2006-29.3.2009	30.3.2009-29.3.2016	–	3,100,000	–	3,100,000
Customers	13.5.2004	HK$0.65	Nil	13.5.2004-12.5.2014	2,000,000	–	–	2,000,000
			13.5.2004-12.5.2005	13.5.2005-12.5.2014	2,000,000	–	–	2,000,000
			13.5.2004-12.5.2006	13.5.2006-12.5.2014	2,000,000	–	–	2,000,000
			13.5.2004-12.5.2007	13.5.2007-12.5.2014	2,000,000	–	–	2,000,000
					62,810,000	15,400,000	–	78,210,000
Exercisable at the end of the year								50,957,500

36. SHARE OPTION SCHEME – Continued

The movements of the share options granted to the directors and employees of the Group during the year ended 31 December 2005 are as follows:

					Number of share options		
Type of option holders	Date of grant	Exercise price	Vesting period	Exercise period	Outstanding at 1.1.2006	Lapsed during the year	Outstanding at 31.12.2006
Directors:							
Dr. Chen Yuhong	13.8.2003	HK$0.58	13.8.2003-12.8.2004	13.8.2004-12.8.2013	300,000	–	300,000
			13.8.2003-12.8.2005	13.8.2005-12.8.2013	300,000	–	300,000
			13.8.2003-12.8.2006	13.8.2006-12.8.2013	300,000	–	300,000
			13.8.2003-12.8.2007	13.8.2007-12.8.2013	300,000	–	300,000
	13.5.2004	HK$0.65	Nil	13.5.2004-12.5.2014	1,250,000	–	1,250,000
			13.5.2004-12.5.2005	13.5.2005-12.5.2014	1,250,000	–	1,250,000
			13.5.2004-12.5.2006	13.5.2006-12.5.2014	1,250,000	–	1,250,000
			13.5.2004-12.5.2007	13.5.2007-12.5.2014	1,250,000	–	1,250,000
Mr. Peng Jiang	13.8.2003	HK$0.58	13.8.2003-12.8.2004	13.8.2004-12.8.2013	200,000	–	200,000
			13.8.2003-12.8.2005	13.8.2005-12.8.2013	200,000	–	200,000
			13.8.2003-12.8.2006	13.8.2006-12.8.2013	200,000	–	200,000
			13.8.2003-12.8.2007	13.8.2007-12.8.2013	200,000	–	200,000
	13.5.2004	HK$0.65	Nil	13.5.2004-12.5.2014	750,000	–	750,000
			13.5.2004-12.5.2005	13.5.2005-12.5.2014	750,000	–	750,000
			13.5.2004-12.5.2006	13.5.2006-12.5.2014	750,000	–	750,000
			13.5.2004-12.5.2007	13.5.2007-12.5.2014	750,000	–	750,000
Mr. Duncan Chiu	13.5.2004	HK$0.65	Nil	13.5.2004-12.5.2014	250,000	–	250,000
			13.5.2004-12.5.2005	13.5.2005-12.5.2014	250,000	–	250,000
			13.5.2004-12.5.2006	13.5.2006-12.5.2014	250,000	–	250,000
			13.5.2004-12.5.2007	13.5.2007-12.5.2014	250,000	–	250,000
Dr. Cui Hui	13.5.2004	HK$0.65	Nil	13.5.2004-12.5.2014	125,000	–	125,000
			13.5.2004-12.5.2005	13.5.2005-12.5.2014	125,000	–	125,000
			13.5.2004-12.5.2006	13.5.2006-12.5.2014	125,000	–	125,000
			13.5.2004-12.5.2007	13.5.2007-12.5.2014	125,000	–	125,000
Mr. Wang Hui	13.8.2003	HK$0.58	13.8.2003-12.8.2004	13.8.2004-12.8.2013	250,000	–	250,000
			13.8.2003-12.8.2005	13.8.2005-12.8.2013	250,000	–	250,000
			13.8.2003-12.8.2006	13.8.2006-12.8.2013	250,000	–	250,000
			13.8.2003-12.8.2007	13.8.2007-12.8.2013	250,000	–	250,000
	13.5.2004	HK$0.65	Nil	13.5.2004-12.5.2014	875,000	–	875,000
			13.5.2004-12.5.2005	13.5.2005-12.5.2014	875,000	–	875,000
			13.5.2004-12.5.2006	13.5.2006-12.5.2014	875,000	–	875,000
			13.5.2004-12.5.2007	13.5.2007-12.5.2014	875,000	–	875,000
Dr. Tang Zhenming	13.8.2003	HK$0.58	13.8.2003-12.8.2004	13.8.2004-12.8.2013	80,000	–	80,000
			13.8.2003-12.8.2005	13.8.2005-12.8.2013	80,000	–	80,000
			13.8.2003-12.8.2006	13.8.2006-12.8.2013	80,000	–	80,000
			13.8.2003-12.8.2007	13.8.2007-12.8.2013	80,000	–	80,000
	13.5.2004	HK$0.65	Nil	13.5.2004-12.5.2014	650,000	–	650,000
			13.5.2004-12.5.2005	13.5.2005-12.5.2014	650,000	–	650,000
			13.5.2004-12.5.2006	13.5.2006-12.5.2014	650,000	–	650,000
			13.5.2004-12.5.2007	13.5.2007-12.5.2014	650,000	–	650,000
					18,920,000	–	18,920,000
Other employees	13.8.2003	HK$0.58	13.8.2003-12.8.2004	13.8.2004-12.8.2013	1,830,000	(132,500)	1,697,500
			13.8.2003-12.8.2005	13.8.2005-12.8.2013	1,830,000	(132,500)	1,697,500
			13.8.2003-12.8.2006	13.8.2006-12.8.2013	1,830,000	(132,500)	1,697,500
			13.8.2003-12.8.2007	13.8.2007-12.8.2013	1,830,000	(132,500)	1,697,500
	13.5.2004	HK$0.65	Nil	13.5.2004-12.5.2014	7,275,000	–	7,275,000
			13.5.2004-12.5.2005	13.5.2005-12.5.2014	7,275,000	–	7,275,000
			13.5.2004-12.5.2006	13.5.2006-12.5.2014	7,275,000	–	7,275,000
			13.5.2004-12.5.2007	13.5.2007-12.5.2014	7,275,000	–	7,275,000
Customers	13.5.2004	HK$0.65	Nil	13.5.2004-12.5.2014	2,000,000	–	2,000,000
			13.5.2004-12.5.2005	13.5.2005-12.5.2014	2,000,000	–	2,000,000
			13.5.2004-12.5.2006	13.5.2006-12.5.2014	2,000,000	–	2,000,000
			13.5.2004-12.5.2007	13.5.2007-12.5.2014	2,000,000	–	2,000,000
					63,340,000	(530,000)	62,810,000
Exercisable at the end of the year							31,405,000

No share options have been exercised or cancelled during both years.

36. SHARE OPTION SCHEME – Continued

The estimated fair values of the share options granted on 30 March 2006 ranged from HK$0.34 to HK$0.41 and were calculated using the Binomial model. The inputs into the model were as follows:

Share price on grant date	HK$0.97
Exercise price	HK$0.97
Expected volatility	41.55%
Time to maturity	10 years
Risk-free rate	4.53%
Expected dividend yield	1.3%

Expected volatility was determined by using the historical volatility of the Company's share price over a period of 260 days.

The Group recognised a total expense of RMB4,145,000 for the year ended 31 December 2006 (2005: RMB3,617,000) in relation to share options granted by the Company.

37. RETIREMENT BENEFIT SCHEMES

As stipulated by the rules and regulations in the PRC, the Group contributes to state-sponsored retirement plans for its employees in the PRC. The Group is required to contribute a certain percentage of the basic salaries of its employees to the retirement plans, and has no further obligation for the actual payment of the previous or post retirement benefits. The relevant state-sponsored retirement plans are responsible for the entire present obligation to retired employees.

In accordance with the relevant mandatory provident fund laws and regulations of Hong Kong, the Group operates a Mandatory Provident Fund ("MPF") scheme ("MPF Scheme") for all qualifying Hong Kong employees. The assets of the scheme are held separately from those of the Group and under the control of an independent MPF service provider. 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 in respect of the MPF Scheme is to make the required contributions under the scheme.

During the year, the total cost of retirement benefit contributions charged to the consolidated income statement of RMB6,931,000 (2005: RMB3,214,000) represents contributions to the schemes made by the Group at rates specified in the rules of the respective schemes. No forfeited contributions may be used by the employers to reduce the existing level of contributions.

38. RELATED PARTY TRANSACTIONS

(i) During the year, the Group had the following transactions with the following companies:

	Notes	2006 RMB'000	2005 RMB'000
Provision of software and installation services for a management system software development and technology project			
– a customer of CNSS	(a) & (b)	–	1,374
– 鄭州中軟信息技術有限公司 (Zhengzhou Chinasoft Information Technology Co., Ltd. ("Chinasoft Zhengzhou"))	(c)	10	–
– Chinasoft Wuhan	(d)	1,768	–
Provision of technical development services			
– CNSS	(a), (b) & (vii)	1,711	–
– CS&S(HK)	(e) (vii)	320	–
Provision of IT outsourcing services			
– Microsoft	(f) (ix)	4,775	–
– Microsoft (China) Co., Ltd.	(f) (ix)	49,707	–
Subcontracting costs			
– Chinasoft Zhengzhou	(c) (viii)	190	243
– Chinasoft Wuhan	(d)	800	–
– 山東中軟信息技術有限公司 (Shandong Chinasoft Information Technology Co., Ltd. ("Shandong Chinasoft"))	(c)	97	96
– CNSS	(a) & (b)	–	88
Rental expenses			
– CNSS	(a) & (b)	4,364	2,889
– 中國計算機軟件與技術服務總公司 China National Computer Software & Technology Service Corporation ("CS&S")	(g)	–	118

38. RELATED PARTY TRANSACTIONS – Continued

Notes

(a) CNSS was a holding company of a shareholder of the Company.

(b) Mr. Cui Hui, a director of the Company, is also a director of CNSS.

(c) Chinasoft Zhengzhou and Shandong Chinasoft were subsidiaries of CNSS.

(d) Chinasoft Wuhan is an associate of the Group.

(e) CS&S (HK) is a shareholder of the Company.

(f) Microsoft was a holder of the Series A Preferred Shares of the Company. Microsoft (China) Co., Ltd. is a subsidiary of Microsoft.

(g) CS&S was a holding company of a shareholder of the Company from 19 August 2004 to 30 September 2004 and a minority shareholder of a subsidiary of the Company from 1 January 2004 to 18 August 2004. During the year ended 31 December 2004, CNSS acquired CS&S and took over its assets and liabilities pursuant to an acquisition agreement dated 18 August 2004 and CS&S was subsequently de-registered under the laws of the PRC on 25 April 2005.

(ii) Pursuant to a trademark license agreement ("Trademark Licence Agreement") entered into between CS&S and the Company on 20 December 2003, CS&S granted to the Company an exclusive right to use a trademark of 中軟總公司計算機培訓中心 as defined on the Trademark Licence Agreement for a period of 25 years pending registration of such trademark with the Trademark Bureau of the PRC for a consideration of RMB2,000,000. Such amount, which is refundable on unsuccessful registration, has been paid to CS&S and was included in the amount due from a related company at 31 December 2005. During the year, CNSS obtained the trademark registration certificate from the Trademark Bureau. The effective period of the registration is from 21 March 2006 to 20 March 2016. Accordingly, the amount due from a related company of RMB2,000,000 was reclassified as trademark use right in the consolidated balance sheet in 2006.

38. RELATED PARTY TRANSACTIONS – Continued

(iii) Pursuant to an agreement entered into between CS&S (HK), a subsidiary of CNSS, and Chinasoft (HK) on 28 April 2005, Chinasoft (HK) acquired 51% equity interest in the registered capital of Chinasoft Resources Beijing from CS&S (HK). The consideration of the acquisition was satisfied by the allotment and issue of 58,120,755 new shares of the Company of HK$0.05 each to CS&S (HK). The acquisition was completed on 18 July 2005. The acquisition constituted a connected transaction of the Company under the GEM Listing Rules as CS&S (HK) is a connected person (as defined under the GEM Listing Rules) of the Company. The independent non-executive directors of the Company considered that the terms of the acquisition were fair and reasonable and in the interest of the Company and its shareholders as a whole, and the acquisition was approved by the independent shareholders at an extraordinary general meeting on 22 June 2005.

(iv) Pursuant to an agreement entered into between CS&S (HK), a subsidiary of CNSS, and Chinasoft (HK) on 15 November 2005, Chinasoft (HK) conditionally agreed to acquire the remaining 49% equity interest in the registered capital of Chinasoft Resources Beijing from CS&S (HK). The consideration of the acquisition would be satisfied by cash in a maximum aggregate amount of RMB43,556,000 (equivalent to HK$41,881,000) subject to satisfaction of certain conditions. The acquisition was completed during the year. The acquisition constituted a connected transaction of the Company under the GEM Listing Rules as CS&S (HK) is a connected person (as defined under the GEM Listing Rules) of the Company. The independent non-executive directors of the Company considered that the terms of the acquisition were fair and reasonable and in the interest of the Company and its shareholders as a whole, and the acquisition was approved by the independent shareholders at an extraordinary general meeting on 28 December 2005.

(v) Pursuant to a rental agreement entered into between Chinasoft Beijing and CNSS on 1 June 2005, Chinasoft Beijing prepaid a rent of RMB866,000 to CNSS for the lease of office premises for a term commencing from 1 April 2006 to 31 March 2007. At 31 December 2005, the prepaid lease payments were analysed for reporting purposes as a non-current asset of RMB216,000 and current asset of RMB650,000 which was included in trade and other receivables in the consolidated balance sheet. The prepaid lease payments were expensed during the year.

38. RELATED PARTY TRANSACTIONS – Continued

(vi) Pursuant to an agreement entered into between 北京中軟賽博中文信息技術有限責任公司 (Beijing Chinasoft Cyber-Chinese Information Technology Company Ltd.) ("Beijing Cyber-Chinese"), an associate of CNSS, and Chinasoft Beijing on 1 December 2005, Chinasoft Beijing advanced a loan of RMB1,450,000 to Beijing Cyber-Chinese for a term of 6 months from 1 December 2005 to 31 May 2006. The loan was unsecured, non-interest bearing and fully repaid by Beijing Cyber-Chinese in March 2006.

(vii) During the year, Chinasoft Guangzhou and Chinasoft Resource (International) Limited provided technical development services of RMB1,711,000 and RMB320,000 to CNSS and CS&S (HK) respectively. At 31 December 2006, the amount of RMB1,711,000 was included in trade receivables from related companies in the consolidated balance sheet.

(viii) During the year, Chinasoft Zhengzhou, a subsidiary of CNSS, provided subcontracting service of RMB190,000 (2005: RMB243,000) to Chinasoft Beijing. At 31 December 2006, the amount of RMB190,000 (2005: RMB68,000) was included in trade payable to a related company (2005: trade and other payables) in the consolidated balance sheet.

(ix) In September 2005, the Company entered into a Commercial Agreement with Microsoft for a period of three years. Pursuant to the Commercial Agreement, the Company and Microsoft agreed to drive revenue associated with delivering software solutions using certain Microsoft software products and to assist the Company in growing its IT service business in the PRC. The transactions under the Commercial Agreement constitute non-exempt continuing connected transactions for the Company under the GEM Listing Rules as Microsoft is a connected person (as defined under the GEM Listing Rules) of the Company after subscription of the Series A Preferred Shares on 6 January 2006. The independent non-executive directors of the Company considered that the continuing connected transactions contemplated thereunder were entered into in the ordinary and usual course of the Group and on normal commercial terms, and the terms of the Commercial Agreement were fair and reasonable and in the interest of the Company and the shareholders as a whole. The above were approved by the independent shareholders at an extraordinary general meeting held by the Company on 28 December 2005.

38. RELATED PARTY TRANSACTIONS – Continued

(x) During the year, the Company entered into a Global Master Services Agreement ("the GMS Agreement") with Microsoft for a term of five years to provide a framework of the agreed general terms and conditions for the provision of the IT outsourcing services by subsidiaries of the Group. Each project to be undertaken by subsidiaries of the Group for Microsoft under the GMS Agreement would be subject to specific terms on the amount of fee, particulars of the project and expected timetable. The entering into the GMS Agreement, and the projects undertaken by subsidiaries of the Group thereunder, will constitute non-exempt continuing connected transactions for the Company under the GEM Listing Rules as Microsoft is a connected person (as defined under the GEM Listing Rules) of the Company. The independent non-executive directors of the Company considered that the GMS Agreement and the transactions contemplated thereunder were entered into in the ordinary and usual course of the Group and on normal commercial terms, and the terms of the GMS Agreement and the annual caps for the transactions contemplated under the GMS Agreement for each of six financial years ended 31 December 2011 were fair and reasonable and in the interest of the Company and the shareholders as a whole. The above were approved by the independent shareholders at an extraordinary general meeting held by the Company on 27 October 2006. At 31 December 2006, an amount of RMB 9,381,000 was included in trade receivables from related companies in the consolidated balance sheet in respect of provision of IT outsourcing services to Microsoft and Microsoft (China) Co., Ltd.

(xi) In August 2006, Chinasoft Resources Beijing acquired the entire interest in the issued share capital of Chinasoft Resources (International) Limited from Ms. Yan Junjue, a director of Chinasoft Resources Beijing, Chinasoft Resources Shanghai, Chinasoft Resources Shenzhen and Chinasoft Resource (International) Limited for a cash consideration of HK$1.

Compensation of key management personnel

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

	2006	2005
	RMB'000	RMB'000
Short-term employee benefits	**5,085**	3,448
Share option expenses	**1,244**	1,257
	6,329	4,705

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

39. POST BALANCE SHEET EVENT

On 2 January 2007, the Company entered into a conditional sale and purchase agreement and a supplementary agreement with Hinge Global Resource Inc. ("HGR") and its shareholders for the acquisition of an aggregate of 7,249,419 HGR Shares, representing approximately 96.61% of the then HGR shares. HGR and its subsidiaries are principally engaged in the IT outsourcing business. The consideration of the acquisition will be satisfied by way of cash and a maximum of 482,625,000 consideration shares in the aggregate amount of not exceeding US$55,000,000 million (equivalent to approximately RMB429,000,000). The acquisition constitutes a major transaction under the GEM Listing Rules for the Company and is subject to the approval of the independent shareholders.

Details of the above are set out in the announcement dated 5 January 2007 issued by the Company. The acquisition has yet to be completed at the date of approval of the consolidated financial statements.

Final Dividend and Closure or Register of Members

The Board recommend the payment of a final dividend of HKD0.001 (2005: HKD0.025 final dividend) per share for the year ended December 31, 2006, totaling approximately Rmb758,817 (2005: Rmb18,309,000), to shareholders.

The register of members of the Company will be closed from 14 May 2007 to 16 May 2007, both days inclusive, during which period no transfer of shares will be effected. In order to qualify for the final dividend, all transfer documents accompanied by the relevant share certificates, must be lodged with the Company's Hong Kong branch share registrar, Computershare Hong Kong Investor Services Limited at 46th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong, no later than 4:30 p.m. on 11 May 2007. Subject to the approval of the final dividend by shareholders at the forthcoming annual general meeting, the relevant dividend warrant will be despatched to shareholders on 8 June 2007.

As at the date hereof, the Board comprises three executive directors, namely, Dr. Chen Yuhong, Mr. Wang Hui, Dr. Tang Zhenming, five non-executive directors, namely, Madam Tang Min (Chairman), Dr. Cui Hui, Mr. Duncan Chiu, Mr. Timothy Chen Yung Cheng, Mr. Liu Zheng and three independent non-executive directors, namely, Mr. He Ning, Mr. Zhen Zhijie and Dr. Leung Wing Yin Patrick.

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