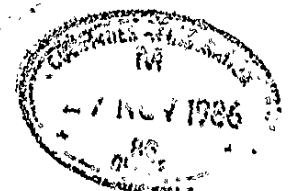


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Phonogram Limited

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**Directors' Report and Accounts
for the year ended 31st December 1985**



PHONOGRAM LIMITED

DIRECTORS' REPORT

The directors submit their report and accounts for the year ended December 31, 1985.

Results and dividends

The Directors recommend that a dividend of £1,650,000 be paid to Polygram Leisure Limited.

The results for the year are set out on page 4.

Review of the business

The company's principal activity during the year was the marketing of gramophone records, musicassettes and compact discs.

Lower sales in the first six months were due in part to a postponement of a number of releases to the latter part of the year. These proved successful and achieved high chart positions, taking turnover to budgeted levels for the year.

Since the year end a proportion of the company's trade has been purchased by an associated company at market value.

Tangible fixed assets

The movements in tangible fixed assets during the year are set out in note 7.

Directors and their interests

The directors of the company during the year were:

J. W. Crane	
J. D. Golembo	(Appointed November 1, 1985)
R. Lopez S	(Resigned April 30, 1985)
M. L. Oberstein	(Appointed July 1, 1985)
A. J. Powell	(Appointed February 25, 1985)
D. I. Simone	(Appointed August 5, 1985)
J. V. Watson	(Appointed February 25, 1985 - Resigned November 1, 1985)

At no time during the year did any director have any interest in shares which is required by Section 324 of the Companies Act 1985, to be notified to the company.

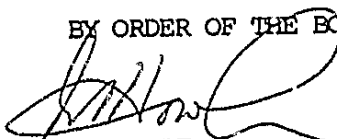
PHONOGRAM LIMITED

DIRECTORS' REPORT
(continued)

Auditors

A resolution to reappoint Arthur Young as auditors will be proposed at the Annual General Meeting.

BY ORDER OF THE BOARD



M. HOWLE
Secretary

P.O Box 2LB
15 Saint George Street,
London W1A 2LB

August 1, 1986



Arthur Young

Chartered Accountants
Rena House, 7 Rensel Building
Fetter Lane, London EC4A 3DF

REPORT OF THE AUDITORS TO THE MEMBERS OF
PHONOGRAM LIMITED

We have audited the accounts on pages 4 to 12 in accordance with approved auditing standards.

In our opinion the accounts, which have been prepared under the historical cost convention, give a true and fair view of the state of the company's affairs at December 31, 1985 and of its profit and source and application of funds for the year then ended and comply with the Companies Act 1985.

Arthur Young
ARTHUR YOUNG

August 1, 1986.

PHOTOGRAM LIMITEDPROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDED DECEMBER 31, 1985

	<u>Notes</u>	£'000	<u>1985</u> <u>£'000</u>	<u>1984</u> <u>£'000</u>
Turnover	3		47,329	35,394
Cost of sales			(31,487)	(24,106)
Gross profit			15,842	11,288
Distribution costs		(2,500)		(2,312)
Administrative expenses		(9,344)		(8,413)
			(12,344)	(10,725)
Profit on ordinary activities before taxation	4		3,498	563
Tax on profit on ordinary activities	6		(1,610)	(40)
Profit on ordinary activities after taxation			1,888	523
Dividend			(1,650)	-
Transfer from revaluation reserve			-	248
Profit for the financial year			238	771
Retained profit/(loss) brought forward			90	(681)
Retained profit carried forward			328	90

The notes on page 7 to 12 form part of these accounts

PHONOGRAM LIMITEDBALANCE SHEET AT DECEMBER 31, 1985

	<u>Notes</u>	<u>£'000</u>	<u>1985</u> <u>£'000</u>	<u>1984</u> <u>£'000</u>
Fixed assets:				
Tangible assets	7	230		202
Investments	8	---		---
			230	202
Current assets:				
Stocks	9	884		546
Debtors	10	21,725		10,971
Cash at bank and in hand		18		556
		22 627		12,073
Creditors: amounts falling due within one year	11	(22,029)		(11,685)
Net current (liabilities)/assets			598	388
Total assets less current liabilities			828	590
Provision for liabilities and charges				
Deferred taxation	12		---	---
			828	590
Capital and reserves				
Called up share capital	13		500	500
Profit and loss account			328	90
			828	590

J W CRANE

D I SIMONE

) Directors

August 1, 1986

The notes on pages 7 to 12 form part of these accounts.

PHONOGRAM LIMITEDSTATEMENT OF SOURCE AND APPLICATION OF FUNDS
FOR THE YEAR ENDED DECEMBER 31, 1985

	£'000	1985 £'000	1984 £'000
Source of funds:			
Profit on ordinary activities before taxation	3,498		563
Adjustment for items not involving the movement of funds:			
Depreciation	79		66
Profit on sale of tangible fixed assets	(10)		-
Total generated from operations		3,567	629
Funds from other sources:			
Proceeds from sale of tangible fixed assets		44	17
		3,611	646
Application of funds:			
Taxation paid	(40)		-
Purchase of tangible fixed assets	(148)		(106)
Transfer of assets to (from) group companies	7		(11)
		(181)	(117)
Increase in working capital		3,430	529
Components of increase in working capital.			
Stocks	338		52
Debtors	10,754		2,392
Creditors	(7,124)		(2,755)
		3,968	(311)
Movement in net liquid funds:			
Bank loans and overdrafts	-		284
Cash and bank balances	(538)		556
		(538)	840
		3,430	529

The notes on page 7 to 12 form part of these accounts

PHONOGRAM LIMITEDNOTES TO THE ACCOUNTS AT DECEMBER 31, 19851 Ultimate holding company

The directors regard Philips Gloeilampenfabrieken N.V. which is incorporated in The Netherlands as the company's ultimate holding company

2 Accounting policies

These accounts are prepared under the historical cost convention modified to include the revaluation of tangible fixed assets as described below.

Tangible fixed assets

Tangible fixed assets and accumulated depreciation were revalued annually up to December 31 1982 in line with price index established for group purposes to reflect the replacement cost of the assets. Thereafter in accordance with the holding company's accounting policy no further revaluations are being made in the accounts.

Depreciation is charged on a straight line basis. Accumulated depreciation includes amounts transferred from revaluation surpluses in earlier years and not charged to the profit and loss account.

Rates of depreciation are:

Plant and equipment - 25%

Post balance sheet events

Events relating to the year ended December 31, 1985, which occurred before the date of approval of the accounts by the board of directors, have been included in the accounts to the extent that this is required by Statement of Standard Accounting Practice No 17

Investments

Investments are stated at cost less amounts written off.

Stocks

Stocks are stated at lower of cost and estimated net realisable value. Cost represents actual cost and consists, in the case of own manufactured products, of direct material and labour cost together with the relevant proportion of factory fixed and variable overheads. Net realisable value is the estimated selling price less estimated costs of disposal

Foreign currencies

Assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the market rate of exchange ruling at that date whilst transactions in foreign currencies are recorded at the rate ruling at the date of the transactions. All differences are taken to the profit and loss account in line with Statement of Standard Accounting Practice No 20.

PHONOGRAM LIMITEDNOTES TO THE ACCOUNTS AT DECEMBER 31, 1985
(continued).2. Accounting policies (continued)Royalties and advances

Royalties are accounted for on an accruals basis.

Advances to artists are written down to the estimated amount that will be recovered from future sales and royalty receipts.

Deferred taxation

Deferred taxation is provided by the liability method on all timing differences which are expected to reverse in the foreseeable future.

3. Turnover

Turnover represents the invoiced value of goods and services excluding value added tax. The geographical area to which turnover relates is as follows:

	1985 £'000	1984 £'000
United Kingdom	33,282	29,502
Europe	5,601	2,550
United States of America	5,160	1,593
Other	3,286	1,749
	<u>47,329</u>	<u>35,394</u>

4. Profit on ordinary activities before taxation

Profit is stated after charging:

	1985 £'000	1984 £'000
Depreciation of tangible fixed assets	79	66
Auditors' remuneration	-	-
Exchange losses	48	45
	<u>---</u>	<u>---</u>

5. Employees

The average weekly number of employees including directors the year was:

	1985 No.	1984 No.
Commercial and administrative	86	77
	<u>---</u>	<u>---</u>

PHOTOGRAM LIMITED

NOTES TO THE ACCOUNTS AT DECEMBER 31, 1985
(continued)

5. Employees

Staff costs, including directors remuneration, during the year amounted to:

	<u>1985</u> <u>£'000</u>	<u>1984</u> <u>£'000</u>
Wages and salaries	1,126	943
Social security costs	81	67
Other pension costs	79	57
	<u>1,286</u>	<u>1,067</u>
Directors' remuneration (including pension contributions)	<u>151</u>	<u>41</u>
Emoluments of the chairman (excluding pension contributions)	<u>-</u>	<u>-</u>
Emoluments (excluding pension contributions) of the highest paid director	<u>53</u>	<u>27</u>
The number of other directors whose emoluments (excluding pension contributions) fell within the ranges below were:		

	<u>1985</u> <u>No.</u>	<u>1984</u> <u>No.</u>
£Nil - £5,000	-	1
£5,001 - £10,000	1	-
£10,001 - £15,000	-	1
£15,001 - £20,000	1	-
£20,001 - £25,000	2	-

There was one employee who earned between £40,000 and £45,000 (excluding pension contributions), during the year (1984 - none).

PHONOGRAM LIMITEDNOTES TO THE ACCOUNTS AT DECEMBER 31, 1985
(continued)6. Taxation

The rates of U.K. corporation tax used are 45% for the period January 1 to March 31, 1985 and 40% for the period April 1 to December 31, 1985.

	<u>1985</u> £'000	<u>1984</u> £'000
Current year:		
Corporation tax	1,639	-
Group relief	-	40
	<u>1,639</u>	<u>40</u>
Prior year:		
Group relief	(29)	-
	<u>1,610</u>	<u>40</u>

7. Tangible fixed assets

	<u>Plant and equipment</u> £'000
Cost or valuation:	
At January 1, 1985	325
Additions	148
Transfers to group companies	(21)
Disposals	(93)
	<u>359</u>
At December 31, 1985	<u>359</u>
Depreciation:	
At January 1, 1985	123
Provided during the year	79
Transfers to group companies	(14)
Disposals	(59)
	<u>129</u>
At December 31, 1985	<u>129</u>
Net book value:	
At December 31, 1985	<u>230</u>
Net book value:	
At January 1, 1985	<u>202</u>

PHONOGRAM LIMITEDNOTES TO THE ACCOUNTS AT DECEMBER 31, 1985
(continued)7. Tangible fixed assets (continued)

The historic cost and related depreciation of fixed tangible assets are shown below:

	<u>Plant and equipment</u> £'000
Cost	359
Depreciation	(129)

Balance December 31, 1985	230

Balance December 31, 1984	202

8. Investments

	<u>Shares in group companies</u> £
Cost at January 1, and December 31, 1985	100
Amounts written off at January 1, and December 31, 1985	100

Net book values at January 1, and December 31, 1985	£ -

The company has the following investments

	<u>Country of incorporation</u>	<u>Holding</u>	<u>Percentage held</u>
Shares in group companies:			
Polygram Musicvideo Limited	England	100 ordinary shares	100%

9. Stocks

	<u>1985</u> £'000	<u>1984</u> £'000
Stocks consist of:		
Finished goods	884	546
	---	---

PHONOGRAM LIMITEDNOTES TO THE ACCOUNTS AT DECEMBER 31, 1985
(continued)10. Debtors

	1985 £'000	1984 £'000
Trade debtors	5,734	4,249
Group companies:		
U.K. holding company	6,712	-
Overseas group companies	7,554	392
U.K. group companies	940	5,799
Other debtors	689	439
Prepayments	96	92
	<u>21,725</u>	<u>10,971</u>

11. Creditors: amounts falling due within one year

	1985 £'000	1984 £'000
Group companies:		
Overseas group companies	785	11
U.K. group companies	487	40
Dividend	1,630	-
Other creditors	729	1,244
Current corporation tax	1,639	-
Accruals	16,739	10,390
	<u>22,029</u>	<u>11,685</u>

12. Deferred taxation

The full potential liability for deferred tax has been provided at the effective rate of UK corporation tax of 36.25% for the year to 31st December 1986. The directors do not consider it is reasonable at present to assume that timing differences will not reverse in the foreseeable future.

	1985 £'000	1984 £'000
Capital allowances in advance of depreciation	2	10
Other timing differences	(2)	(10)
	<u>-</u>	<u>-</u>
	-	-
	<u>-</u>	<u>-</u>

In addition future tax relief not taken up in the accounts should be available on the following item:

Other timing differences which should produce future tax relief on	263	98
	<u>-</u>	<u>-</u>

PHONOGRAM LIMITEDNOTES TO THE ACCOUNTS AT DECEMBER 31, 1985
(continued)13. Share capital

	<u>Authorised</u>		<u>Allotted, issued and fully paid</u>	
	<u>1985 No.</u>	<u>1984 No.</u>	<u>1985 No.</u>	<u>1984 No.</u>
Ordinary shares of £1 each	100	100	100	100
Deferred ordinary shares of £1 each	500,000	500,000	500,000	500,000
	<u>500,100</u>	<u>500,100</u>	<u>500,100</u>	<u>500,100</u>