

Manga Entertainment Limited

Report and Financial Statements

31 December 2001

 ERNST & YOUNG



Manga Entertainment Limited

Registered No: 2202664

Directors

M Gleicher
S Newman
A Norbury

Secretary

R Ramus

Auditors

Ernst & Young LLP
Rolls House
7 Rolls Buildings
Fetter Lane
London EC4A 1NH

Registered Office

Suite 10
500 Chiswick High Street
London
W4 5RG

Directors' report

The directors present their report and financial statements for the year ended 31 December 2001.

Results and dividends

The profit for the year, after taxation amounted to £1,044,324. The directors do not recommend payment of any dividend.

Principal activities

The company's principal activities are the sale of videocassettes and merchandising, and the licensing of video, theatrical, merchandising and television broadcasting rights.

Directors and their interests

The directors who served during the year were as follows:

M Gleicher
S Newman
A Norbury

There are no directors' interests requiring disclosure under the Companies Act 1985.

Auditors

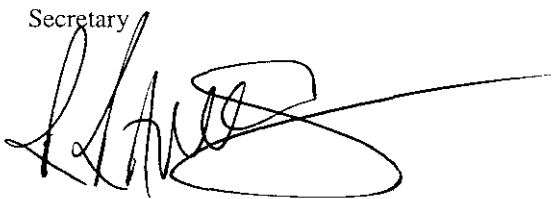
A resolution to re-appoint Ernst & Young LLP as the company's auditor will be put to the forthcoming Annual General Meeting.

Special provision relating to small companies

This report has been prepared in accordance with the special provisions of Part VII of the Companies Act 1985 relating to small companies.

By order of the board

Secretary



1 August 2003

Statement of directors' responsibilities in respect of the financial statements

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company and of its profit or loss for that period. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent; and
- prepare the financial statements on a going concern basis, unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and to enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Independent auditors' report

to the members of Manga Entertainment Limited

We have audited the company's financial statements for the year ended 31 December 2001 which comprise the Profit and Loss Account, Statement of Total Recognised Gains and Losses, Balance Sheet, and the related notes 1 to 20. These accounts have been prepared on the basis of the accounting policies set out therein and with the Financial Reporting Standard for Smaller Entities.

This report is made solely to the company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

As described in the Statement of Directors' Responsibilities the company's directors are responsible for the preparation of the financial statements in accordance with applicable United Kingdom law and accounting standards.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions with the company is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it.

Basis of audit opinion

We conducted our audit in accordance with United Kingdom Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Fundamental uncertainty

In forming our opinion, we have considered the adequacy of the disclosures made in note 1 to the financial statements concerning their preparation on a going concern basis. The validity of this basis depends on the continued financial support of the ultimate parent undertaking which itself has recurring losses from operations, a working capital deficiency and is dependent on the support of its current shareholders and financiers and the raising of additional finance to continue as a going concern. The financial statements do not include any adjustments which would result from continued financial support not being made available to the company. Our audit opinion is not qualified in this respect.

Independent auditors' report

to the members of Manga Entertainment Limited (continued)

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the company as at 31 December 2001 and of its profit for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Ernst & Young LLP

Ernst & Young LLP
Registered Auditor
London

18 August 2003

Profit and loss account

for the year ended 31 December 2001

	Notes	2001 £	2000 £
Turnover	3	2,384,016	1,797,890
Cost of sales		(818,536)	(3,882,879)
Gross profit/(loss)		1,565,480	(2,084,989)
Distribution costs		(186,064)	(172,045)
Administrative expenses		(335,404)	(220,940)
Operating profit/(loss)	4	1,044,012	(2,477,974)
Other interest receivable and similar income	6	609	2,373
Interest payable and similar charges	7	(297)	(846,708)
Profit/(loss) on ordinary activities before taxation		1,044,324	(3,322,309)
Tax on profit/(loss) on ordinary activities	8	—	—
Profit/(loss) for the financial year	18	1,044,324	(3,322,309)

Statement of total recognised gains and losses

There are no recognised gains or losses other than the profit attributable to the shareholders of the company of £1,044,324 for the year ended 31 December 2001 and the loss of £3,322,309 for the year ended 31 December 2000.

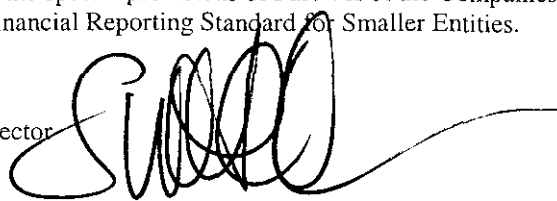
Balance sheet

at 31 December 2001

	Notes	2001 £	2000 £
Fixed assets			
Intangible assets	9	58,120	80,836
Tangible assets	10	23,706	31,609
Investments	11	200,000	200,000
		<u>281,826</u>	<u>312,445</u>
Current assets			
Advances	12	45,567	95,966
Stocks	13	50,547	91,425
Debtors	14	4,192,331	2,410,095
Cash at bank and in hand		3,265	—
		<u>4,291,710</u>	<u>2,597,486</u>
Creditors: amounts falling due within one year	15	(11,360,300)	(10,741,019)
Net current liabilities		<u>(7,068,590)</u>	<u>(8,143,533)</u>
Total assets less current liabilities		<u>(6,786,764)</u>	<u>(7,831,088)</u>
Capital and reserves			
Called up share capital	17	2,576,136	2,576,136
Profit and loss account	18	(9,362,900)	(10,407,224)
Equity shareholders' funds	18	<u>(6,786,764)</u>	<u>(7,831,088)</u>

The accounts have been prepared in accordance with the special provisions of Part VII of the Companies Act 1985 relating to small companies and with the Financial Reporting Standard for Smaller Entities.

Director



1 August 2003

Notes to the financial statements

at 31 December 2001

1. Fundamental accounting concept

The financial statements have been prepared on a going concern basis on the basis that continued financial support will be made available by the ultimate parent undertaking, Palm Entertainment Properties LLC, when required, to enable the company to meet its liabilities as and when they fall due and in particular, that the ultimate parent undertaking will not require repayment of its existing debt of approximately £9m due from the company in the foreseeable future. The ultimate parent undertaking has recurring losses from operations and has a working capital deficiency and is dependent on the support of its current shareholders and financiers. Its continuation as a going concern is dependent upon it raising further funds and working capital. The current options under considerations are: raising additional equity financing, the refinancing or restructuring of its loans or raising proceeds from the sale of assets. There can be no assurance that the ultimate parent undertaking will generate sufficient profits or cash flows in the future and therefore be in a position to provide continued support. However, in view of the company's ability to generate sufficient cash flow to fund its own operations and meet its liabilities, with the exception of the loan with the ultimate parent undertaking, without further support from Palm Entertainment Properties LLC, the directors consider it appropriate to adopt a going concern basis in these financial statements.

However, should the ultimate parent undertaking fail to provide support when or if required, the going concern basis used in preparing the company's financial statements would be invalid and adjustments would have to be made to reduce the value of assets to their realisable amount, to provide for any further liabilities which might arise and to reclassify fixed assets as current assets.

2. Accounting policies

Accounting convention

The financial statements are prepared under the historical cost convention and in accordance with applicable accounting standards.

Consolidated financial statements

The company is exempt by virtue of Section 248 of the Companies Act 1985 from the requirement to prepare group financial statements. These financial statements present information about the company as an individual undertaking and not about its group.

Impairment of fixed assets

The carrying values of fixed assets, including investments, are reviewed for impairment in periods if events or changes in circumstances indicate the carrying value may not be recoverable.

Intangible fixed assets

Intangible fixed assets represent costs incurred in registering the Manga trademark overseas. The cost is amortised over 10 years.

Tangible fixed assets

Depreciation is provided by the company to write off the cost less the estimated residual value of tangible fixed assets by equal instalments over their estimated useful economic lives as follows:

Motor vehicles	-	3 years
Office equipment	-	4 years
Fixtures and fittings	-	5 years

Foreign currencies

Transactions in foreign currencies are recorded using the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated using the rate of exchange ruling at the balance sheet date. All differences are taken to the profit and loss account.

Notes to the financial statements

at 31 December 2001

2. Accounting policies (continued)

Leasing commitments

Rentals payable under operating leases are charged to the profit and loss account on a straight line basis over the lease term.

Stocks

Stocks are stated at the lower of cost and net realisable value.

Advances

Released film and video advances are valued at cost less amortisation which is calculated by applying the royalty rates specified in the contract to the different income streams. Where the directors consider that future income streams are insufficient to write the costs off over the remaining term of the agreement, an immediate write down is made.

Deferred taxation

Deferred taxation is provided using the liability method on all timing differences, which are expected to reverse in the future without being replaced, calculated at the rate at which it is anticipated the timing difference will reverse.

Royalties receivable

Royalties, including non-returnable royalty advances and income from the licensing of distribution rights in overseas territories, are recognised on an accruals basis.

Statement of cash flows

The company has not prepared a statement of cash flows as it is a small company entitled to the filing exemptions under sections 246 and 247 of the Companies Act 1985.

3. Turnover

Turnover is stated net of value added tax, discounts and returns and is derived from the continuing activity of the provision of goods and services to third party customers during the year.

It is the opinion of the directors that, in view of the nature of the company's business, the markets in which it operates do not differ substantially from each other and are, therefore, treated as one market for the purposes of disclosing turnover in these financial statements.

4. Operating loss

This is stated after charging:

	2001	2000
	£	£
Auditors' remuneration	5,000	5,500
Depreciation of tangible fixed assets	7,903	10,197
Amortisation of intangible fixed assets	22,716	20,853

5. Directors' remuneration

	2001	2000
	£	£
Directors' emoluments:		
Remuneration and benefits	—	—

Notes to the financial statements

at 31 December 2001

6. Other interest receivable and similar income

	2001	2000
	£	£
Other interest receivable	609	2,373

7. Interest payable and similar charges

	2001	2000
	£	£
Third party loans	—	240,420
Exchange loss on foreign currency balances	297	606,288
	297	846,708

8. Taxation

	2001	2000
	£	£
UK corporation tax	—	—

Due to the availability of brought forward losses, there is no liability to UK corporation tax for the year. The losses available to carry forward and offset against trading profits of future years are approximately £7.4m (2000 - £8.5m).

9. Intangible fixed assets

	Trademark £
Cost:	
At 1 January 2001 and 31 December 2001	176,049
Amortisation:	
At 1 January 2001	95,213
Charge for the year	22,716
At 31 December 2001	117,929
Net book value:	
At 31 December 2001	58,120
At 1 January 2001	80,836

Notes to the financial statements

at 31 December 2001

10. Tangible fixed assets

	<i>Motor vehicles, computers and office equipment</i>	<i>Fixtures and fittings</i>	<i>Total</i>
	£	£	£
Cost:			
At 1 January 2001 and 31 December 2001	132,333	77,403	209,736
Depreciation:			
At 1 January 2001	122,919	55,208	178,127
Charge for the year	2,354	5,549	7,903
At 31 December 2001	125,273	60,757	186,030
Net book value:			
At 31 December 2001	7,060	16,646	23,706
At 1 January 2001	9,414	22,195	31,609

11. Fixed asset investments

	<i>Shares in group undertakings</i>
	£
Cost:	
At 1 January 2001 and 31 December 2001	386,000
Amounts provided:	
At 1 January 2001 and 31 December 2001	186,000
Net book value:	
At 1 January 2001 and 31 December 2001	200,000

Details of the investments in which the company holds 20% or more of the nominal value of any class of share capital are as follows:

	<i>Holding</i>	<i>Proportion of voting rights and shares held</i>	<i>Principal activity</i>
Manga Publishing Limited	Ordinary shares	100%	Non-trader
Manga Studio Limited	Ordinary shares	100%	Non-trader
Manga Entertainment Inc.	Ordinary shares	100%	Video distribution

Manga Entertainment Inc. is incorporated in the United States of America.

Notes to the financial statements

at 31 December 2001

11. Fixed asset investments (continued)

The results for the year ended 31 December 2001 and the aggregate capital and reserves of these subsidiaries were as follows:

	2001		2000	
	<i>Profit/ (loss) for the year £000</i>	<i>Aggregate capital and reserve £000</i>	<i>Profit/ (loss) for the period £000</i>	<i>Aggregate capital and reserve £000</i>
Manga Publishing Limited	—	(506)	—	(506)
Manga Studio Limited	—	(530)	—	(530)
Manga Entertainment Inc.	210	(737)	(313)	(947)

Manga Entertainment Inc. has a 30 June year end.

12. Advances

	£
Cost:	
At 1 January 2001	12,673,638
Additions	385,981
At 31 December 2001	13,059,619
Amortisation and provisions:	
At 1 January 2001	12,577,672
Written off during the year	436,380
At 31 December 2001	13,014,052
Net book value:	
At 31 December 2001	45,567
At 1 January 2001	95,966

Included within the advances are amounts that will be received after more than one year. Due to the nature of the recoupment it is not possible to estimate the amount.

13. Stocks

	2001 £	2000 £
Finished goods and goods for resale	50,547	91,425

Notes to the financial statements

at 31 December 2001

14. Debtors

	2001	2000
	£	£
Amounts falling due within one year:		
Trade debtors	210,630	–
Amounts owed by subsidiary undertakings	2,727,339	1,591,837
Amounts owed by group undertakings	1,254,274	810,923
Other debtors	–	6,335
Prepayments and accrued income	88	1,000
	<u>4,192,331</u>	<u>2,410,095</u>

15. Creditors: amounts falling due within one year

	2001	2000
	£	£
Bank overdraft	–	2,125
Trade creditors	89,917	110,115
Amounts due to subsidiary undertakings	440,003	375,912
Amounts due to parent undertaking	8,928,060	8,928,060
Other taxes and social security costs	121,502	1,380
Other creditors	–	6,443
Accruals and deferred income	1,780,818	1,316,984
	<u>11,360,300</u>	<u>10,741,019</u>

16. Deferred tax asset

Deferred tax assets not recognised in the financial statements are as follows:

	2001	2000
	£	£
Depreciation in advance of capital allowances	18,849	16,478
Tax losses carried forward	2,231,430	2,555,485
Other short term timing differences	47,125	5,008
	<u>2,297,404</u>	<u>2,576,971</u>

Notes to the financial statements

at 31 December 2001

17. Called up share capital

	2001 £	2000 £
Authorised:		
Ordinary shares of £1 each	150	150
Deferred shares of £1 each	2,755,016	2,755,016
	<u>2,755,166</u>	<u>2,755,166</u>
Allotted, called up and fully paid		
Ordinary shares of £1 each	100	100
Deferred shares of £1 each	2,576,036	2,576,036
	<u>2,576,136</u>	<u>2,576,136</u>

The deferred share were issued on the 1 February 1995 at par. The shares do not carry the rights to any dividend or distribution and are not redeemable.

They carry no votes at any general meeting of the company, however at any separate general meeting of the holders of the Deferred share on a show of hands any shareholder present in person shall have one vote, and on a poll every such holder who is present in person or by proxy shall have one vote for each Deferred share of which he is a holder.

On a winding up of the company, the Deferred shareholders have the right to receive £1 per share, but only after the holders of the Ordinary shares shall have received the nominal amount paid up on their shares plus a further £10 million on aggregate.

18. Reconciliation of shareholders' deficit and movement on reserves

	Share Capital £	Profit and loss account £	Total shareholders' deficit £
At 1 January 2000	2,576,136	(7,084,915)	(4,508,779)
Loss for the year	—	(3,322,309)	(3,322,309)
At 1 January 2001	2,576,136	(10,407,224)	(7,831,088)
Profit for the year	—	1,044,324	1,044,324
At 31 December 2001	<u>2,576,136</u>	<u>(9,362,900)</u>	<u>(6,786,764)</u>

19. Related party transactions

During the year, Manga Entertainment Inc, a subsidiary of Manga Entertainment Limited and incorporated in the United States, paid royalties totalling £584,985 to the company (2000 - £444,574). At 31 December 2001 Manga Entertainment Inc. owed £2,727,339 to the company (2000 - £1,591,837).

At 31 December 2001 the company owed Manga Publishing Limited £127,129 (2000 - £127,129).

During the year Palm Pictures LLC, a company under common ownership, incurred expenses on behalf of Manga Entertainment Limited of £307,316. At 31 December 2001 the company owed Palm Pictures LLC £312,874 (2000 - £5,558).

Notes to the financial statements

at 31 December 2001

19. Related party transactions (continued)

During the year Manga Entertainment Limited loaned Palm Pictures Limited, a company under common ownership, £787,743. At 31 December 2001 Palm Pictures Limited owed £1,254,274 to the company (2000 - £466,531).

During the year Manga Entertainment Limited was repaid £101,167 by Rykodisc Limited, a company that was under common ownership. At 31 December 2001 the company was owed £nil (2000 - £101,167) by Rykodisc Limited.

During the year, Palm Entertainment Properties LLC, a company incorporated in the United States of America, acquired from its subsidiary, Palm Entertainment Properties Limited, the entire share capital of Manga Entertainment Limited. At that date, the intercompany balance of £8,928,060 owed by Manga Entertainment Limited to Palm Entertainment Properties Limited, was transferred to Palm Entertainment Properties LLC. The full balance remains at the year end date.

20. Ultimate parent undertaking

During the year, Palm Entertainment Properties LLC, a company incorporated in the United States of America, acquired from its subsidiary, Palm Entertainment Properties Limited, 100% of the share capital of the company and is now the ultimate parent undertaking.

The parent undertaking of the smallest and largest group of which the company is a member, and for which group accounts are prepared is Palm Entertainment Properties LLC, a company incorporated in the United States of America.