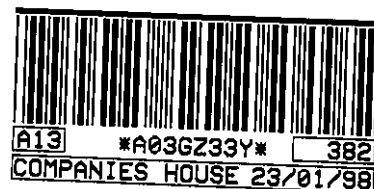


AEC Holdings (UK) Limited

Financial Statements
for the year ended 31 December 1996

Registered no: 2915494



AEC Holdings (UK) Limited

	Pages
Directors' report	1-3
Report of the auditors	4-5
Consolidated profit and loss account	6
Statement of total recognised gains and losses	7
Consolidated balance sheet	8
Company balance sheet	9
Reconciliation of movement in shareholders' funds	10
Consolidated cashflow statement	11
Notes to consolidated cashflow statement	12
Principal accounting policies	13-16
Notes to the financial statements	17-33

Directors' report

The directors present their report together with the group financial statements for the year ended 31 December 1996.

Principal activities

The group operates in the entertainment industry worldwide, acquiring music, video and film rights and marketing these by the release of its own label records, cassettes, compact discs and video-cassettes and by the sub-licensing, direct sale or other exploitation of the rights.

Review of business

The company operates as a parent company of the Castle Communications group of companies.

Future developments

The group will continue to exploit its audio rights through the manufacture and sale of finished product in the form of CDs, LPs, cassettes and other new media and by licensing.

During the year to 31 December 1996, the group continued to exploit its visual rights in much the same way, the finished product in this case being in the form of videos and other new media.

At 31 December 1996 the group reassessed its strategy with regard to visual rights. As a consequence it ceased to sell video finished product as of 31 March 1997 and instead will exploit these rights solely via licensing arrangements in the future. The costs associated with this decision of £11,494,000 are detailed under note 9 to the financial statements as Fundamental Group Reorganisation.

On 13 July 1997 Alliance Entertainment Corporation, the company's ultimate parent company, filed to reorganise under Chapter 11 of the United States bankruptcy code in order to reorganise its core business and to restructure its long term debt, revolving credit facilities and trade creditor obligations.

The company itself was specifically excluded from the filing due to its status as a non-domestic entity in the US and continues to trade normally.

Results and dividends

The consolidated loss for the year after taxation amounted to £8,919,000 (1995: profit £1,391,000).

The deficit of £8,919,000 has been transferred to reserves from the profit and loss account.

The directors do not recommend the payment of a dividend.

Directors and directors' interests

The directors serving during the period or appointed subsequent to year end were as follows:

E B Newman	(USA) (resigned 30 May 1997)
A K Narang	(USA) (resigned 15 November 1997)
J J Bianco	(USA) (resigned 15 November 1997)
J Cokell	(appointed 1 February 1997)
C Joyce	(USA) (appointed 14 July 1997)

Messrs Newman, Narang and Bianco are officers of the ultimate parent company, Alliance Entertainment Corporation and their interests in the shares and options in the ultimate holding company are disclosed in the financial information of the US parent Alliance Entertainment Corporation, submitted to the Securities Exchange Commission.

There were no contracts of significance existing during the period or at the year end in which a director of the company was materially interested.

None of the directors had a beneficial interest in the shares of the company and other group companies at 31 December 1996. The directors' interests in the shares and options of the ultimate parent company, Alliance Entertainment Corporation have not been disclosed as provided for by Statutory Instrument No 802, 1995.

Fixed assets

Changes in fixed assets are summarised in Notes 12, 13 and 14 to the financial statements.

Charitable donations

Charitable donations made by the group during the year amounted to £21,000 (1995: £4,000).

Creditor payment policy

The company's current policy concerning the payment of the majority of its trade creditors is to follow the CBI's Prompt Payers Code (copies are available from the CBI, Centre Point, 103 New Oxford Street, London WC1A 1DU). For other suppliers, the company's policy is to:

- (a) settle the terms of payment with those suppliers when agreeing the terms of each transaction;
- (b) ensure that those suppliers are made aware of the terms of payment by inclusion of the relevant terms in contracts; and
- (c) pay in accordance with its contractual and other legal obligations.

The payment policy applies to all payments to creditors for revenue and capital supplies of goods and services without exception. Wherever possible UK subsidiaries follow the same policy and overseas subsidiaries are encouraged to adopt similar policies, by applying local best practices.

Directors' responsibilities

The directors are required by UK Company law to prepare financial statements for each financial period that give a true and fair view of the state of affairs of the company and the group as at the end of the financial period and of the profit or loss of the group for that period.

The directors confirm that suitable accounting policies have been used and applied consistently and reasonable and prudent judgements and estimate have been made in the preparation of the financial statements for the period ended 31 December 1996. The directors also confirm that applicable accounting standards have been followed and that the financial statements have been prepared on the going concern basis.

The directors are responsible for keeping proper accounting records, for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Auditors

A resolution to re-appoint Coopers & Lybrand as auditors will be proposed at the Annual General Meeting.

By order of the Board



E J N Cook

Secretary

19 December 1997

Report of the auditors to the members of AEC Holdings (UK) Limited

We have audited the financial statements on pages 6 to 33.

Respective responsibilities of directors and auditors

As described on page 3, the company's directors are responsible for the preparation of financial statements. It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

Basis of opinion

We conducted our audit in accordance with 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.

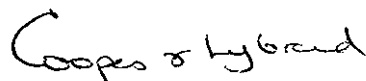
We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity 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 on pages 13 and 14 of the accounts concerning the basis of preparation. As stated therein the company has guaranteed certain debt obligations of the company's ultimate parent company Alliance Entertainment Corporation ("parent company") which on 13 July 1997 filed to reorganise under Chapter 11 of the United States bankruptcy code. The accounts have been prepared on a going concern basis and the validity of this depends on the successful completion of the financial restructuring of the immediate and ultimate parent company, a company incorporated in the USA; on the parent company and the group's banks and other lenders continuing their support by providing adequate facilities pending the successful completion of the financial restructuring; and on Chase Manhattan Bank N.A not seeking to enforce their security pending the successful completion of the financial restructuring. The accounts do not include any adjustments that would result should the group be unable to continue in operational existence. Our opinion is not qualified in this respect.

Opinion

In our opinion the accounts give a true and fair view of the state of affairs of the company and the group at 31 December 1996 and the loss, total recognised losses and cash flows of the group for the year then ended and have been prepared in accordance with the Companies Act 1985.

A handwritten signature in cursive script that reads "Coopers & Lybrand".

Coopers & Lybrand

Chartered Accountants and Registered Auditors

1 Embankment Place
London
WC2N 6NN

19 December 1997

Consolidated profit and loss account for the year ended 31 December 1996

	Notes	Year ended 31 December 1996 £'000	18 months ended 31 December 1995 £'000
Turnover	2	39,738	50,850
Cost of sales		(25,695)	(32,300)
Gross profit		14,043	18,550
Administrative expenses		(11,977)	(13,526)
Other operating income	4	1,977	82
Operating profit		4,043	5,106
Profit on disposal of subsidiaries	6	-	97
Profit on ordinary activities before interest	5	4,043	5,203
Interest receivable and similar income	7	24	46
Interest payable	8	(2,564)	(3,043)
Exceptional item - Fundamental Group Reorganisation	9	(11,494)	-
Loss/profit on ordinary activities before taxation		(9,991)	2,206
Tax on profit on ordinary activities	10	1,081	(815)
Loss/profit on ordinary activities after taxation		(8,910)	1,391
Minority interests		(9)	-
Loss/profit for the financial year		(8,919)	1,391
Dividends (including dividends and other appropriations in respect of non-equity shares)	11	-	-
Retained loss/profit for the year		(8,919)	1,391

There is no difference between the (loss)/profit on ordinary activities before taxation and the retained (loss)/profit for the year stated above, and their historical cost equivalents.

The (loss)/profit on ordinary activities before taxation is derived from continuing operations.

**Statement of total recognised gains and losses
for the year ended 31 December 1996**

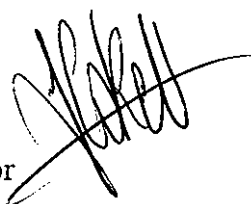
	Year ended 31 December 1996 £'000	18 months ended 31 December 1995 £'000
Loss/profit for the financial year	(8,919)	1,391
Dividends	-	
Currency translation differences on foreign currency net investments	(38)	7
Total gains and losses recognised	<u>(8,957)</u>	<u>1,398</u>

Consolidated balance sheet at 31 December 1996

	Notes	31 December 1996 £'000	31 December 1995 £'000
Fixed assets			
Intangible assets	12	32,436	35,550
Tangible assets	13	1,560	1,444
		<u>33,996</u>	<u>36,994</u>
Current assets			
Stocks	15	3,154	2,838
Debtors	16	20,198	26,609
Cash at bank and in hand		488	1
		<u>23,840</u>	<u>29,448</u>
Creditors: amounts falling due within one year	17	(45,737)	(41,080)
Net current liabilities		<u>(21,897)</u>	<u>(11,632)</u>
Total assets less current liabilities		<u>12,099</u>	<u>25,362</u>
Creditors: amounts falling due after more than one year	17	(9,022)	(12,116)
Provisions for liabilities and charges	18	(631)	(1,801)
		<u>2,446</u>	<u>11,445</u>
Capital and reserves			
Called up share capital	19	9,695	9,695
Capital reserve	20	363	363
Profit and loss account	20	(7,612)	1,387
Equity shareholders' funds		<u>2,446</u>	<u>11,445</u>

The financial statements on pages 6 to 33 were approved by the Board of Directors on *19th December* 1997 and were signed on its behalf by:

Director



Company balance sheet at 31 December 1996

	Notes	31 December 1996 £'000	31 December 1995 £'000
Fixed assets			
Intangible assets		-	-
Tangible assets		-	-
Investments	14	24,984	24,984
		<u>24,984</u>	<u>24,984</u>
Current assets			
Stocks		-	-
Debtors	16	1,561	1,858
Cash at bank and in hand		-	-
		<u>1,561</u>	<u>1,858</u>
Creditors: amounts falling due within one year	17	(7,444)	(5,063)
Net current liabilities		<u>(5,883)</u>	<u>(3,205)</u>
Total assets less current liabilities		<u>19,101</u>	<u>21,779</u>
Creditors: amounts falling due after more than one year	17	(8,940)	(11,903)
Provisions for liabilities and charges	18	-	-
		<u>10,161</u>	<u>9,876</u>
Capital and reserves			
Called up share capital	19	9,695	9,695
Profit and loss account	20	466	181
Equity shareholders' funds		<u>10,161</u>	<u>9,876</u>

The financial statements on pages 6 to 33 were approved by the Board of Directors on 19th December 1997 and were signed on its behalf by:



Director

Reconciliation of movements in shareholders' funds

	Year ended 31 December 1996 £'000	18 months ended 31 December 1995 £'000
Total gains and losses recognised since last annual report	(8,957)	1,398
New share capital issued	-	9,695
Goodwill on acquisitions in the year written-off	(42)	(11)
Negative goodwill transferred to capital reserve	-	363
Net addition to shareholders' funds	(8,999)	11,445
Opening shareholders' funds	11,445	-
Closing shareholders' funds	2,446	11,445

Consolidated cashflow statement for the year ended 31 December 1996

	Notes	Year ended 31 December 1996 £'000	18 months ended 31 December 1995 £'000
Net cash inflow from operating activities (i)		9,068	10,293
Returns on investments and servicing of finance			
Interest received		24	46
Interest paid		(2,594)	(2,896)
Dividends paid		-	-
Net cash outflow from returns on investments and servicing of finance		(2,570)	(2,850)
Taxation			
Corporation tax (payments)/repayments		(79)	-
Overseas tax paid		-	-
Net cash (outflow)/inflow from taxation		(79)	-
Investing activities			
Sale of tangible fixed assets		105	-
Purchase of tangible fixed assets		(775)	(779)
Net addition to intangible fixed assets		(2,763)	(10,627)
Purchase of subsidiary (net of cash acquired)	23	-	(23,639)
Sale of subsidiary		-	97
Net cash outflow from investing activities		(3,433)	(34,948)
Net cash outflow before financing		2,986	(27,505)
Financing			
Redemption of debt	20	-	9,695
Secured loans		(2,863)	7,925
Other loans and capital leases		(508)	(272)
Net cash inflow from financing	22	(3,371)	17,348
Decrease in cash and cash equivalents	21	(385)	(10,157)

Notes to consolidated cashflow statement for the year ended 31 December 1996

(i) Reconciliation of operating profit to net cash inflow from operating activities

	Year ended 31 December 1996 £'000	18 months ended 31 December 1995 £'000
Operating profit	4,043	5,106
Depreciation and amortisation	6,558	1,020
Provisions against royalty advances	7,392	2,585
Provision for bad and doubtful debts	2,429	670
Decrease in stocks	(316)	296
(Increase) in debtors	(3,382)	(10,164)
Increase in creditors	3,824	10,791
Fundamental Restructuring	(11,494)	-
Loss on sale of fixed assets	56	-
Write-back of goodwill	(42)	(11)
Net cash inflow from operating activities	<u>9,068</u>	<u>10,293</u>

Principal accounting policies

Basis of accounting

The financial statements have been prepared on the historic cost basis of accounting, and in accordance with applicable Accounting Standards in the United Kingdom.

Going Concern

The accounts have been prepared on the going concern basis which assumes that the company and all its subsidiary undertakings will continue in operational existence for the foreseeable future having adequate funds to meet their obligations as they fall due.

As set out in note 26 to these financial statements, the company has guaranteed certain debt obligations of the company's ultimate parent undertaking Alliance Entertainment Corporation. On 13 July 1997 Alliance Entertainment Corporation filed to reorganise under Chapter 11 of the United States bankruptcy code (see below). Accordingly the validity of the going concern assumption depends on:

- the successful completion of the financial restructuring of the company's immediate and ultimate holding company Alliance Entertainment Corporation ("parent company") which is referred to below;
- the continued provision of adequate facilities by the parent company and the group's banks and other lenders pending the successful completion of the financial restructuring; and
- Chase Manhattan Bank N.A not seeking to enforce their security over the assets of the company and certain subsidiary undertakings of the company pending the successful completion of the financial restructuring.

If the group were unable to continue in operational existence, adjustments would have to be made to reduce the balance sheet values of assets to their recoverable amounts and to provide for further liabilities which might arise. Additionally, further adjustments would have to be made to reclassify fixed assets and long term liabilities as current assets and current liabilities, respectively. While the outcome of the matters set out above is uncertain for the reasons explained in this note, the directors have considered the proposed financial restructuring and are satisfied that it is appropriate for the accounts to be prepared on the going concern basis at this time.

Financial restructuring

On 13 July 1996 Alliance Entertainment Corporation, the company's immediate and ultimate parent company filed to reorganise under Chapter 11 of the United States bankruptcy code in order to reorganise its core business and to restructure its long debt, revolving credit facilities and trade creditor obligations.

The company itself was specifically excluded from the filing due to its status as a non-domestic entity in the United States and continues to trade normally.

As part of the financial restructuring agreements, the parent company's lenders have agreed to provide lender support to the parent company and its subsidiaries until the financial restructuring becomes effective. In addition Chase Manhattan Bank N.A have agreed not to enforce their security over the group and certain subsidiary undertakings (as described in note 26) pending the successful completion of the financial restructuring.

Basis of consolidation

The consolidated financial statements incorporate the assets and liabilities of the company and all its subsidiary undertakings at 31 December 1996 and the results for the year ended on that date. The results of subsidiary undertakings acquired or disposed of are brought into account up to, or from, the date control passes. Intra-group sales and profits are eliminated fully on consolidation.

On acquisition of a subsidiary, all of the subsidiary's assets and liabilities that exist at the date of acquisition are recorded at their full values reflecting their condition at that date. All changes to those assets and liabilities, and the resulting gains and losses, that arise after the group has gained control of the subsidiary are charged to the post acquisition profit and loss account.

Turnover

Turnover comprises the invoiced value of sales of records, compact discs and audio and video cassettes and the sale of distribution rights, excluding value added tax. Sales of copyrights and other media rights are also included in turnover.

Foreign currencies

Assets and liabilities of subsidiaries in foreign currencies are translated into sterling at rates of exchange ruling at the end of the financial year and the results of foreign subsidiaries are translated at the average rate of exchange for the year. Differences on exchange arising from the retranslation of the opening net investment in subsidiary companies, and from the translation of the results of those companies at average rate, are taken to reserves and are reported in the statement of total recognised gains and losses. All other foreign exchange differences are taken to the profit and loss account in the year in which they arise.

Intangible assets (copyrights)

Audio copyrights as at 31 December 1996 are included at cost. No amortisation is charged, but the valuation is reviewed annually and provision made for any permanent diminution in value.

Visual copyrights are carried at cost, less amortisation. The costs of such copyrights are amortised on a straight line basis over their useful lives. Under normal circumstances the useful life is estimated at the lesser of 20 years or the actual period of copyright. In certain instances, where the directors consider such a policy is inappropriate, the period may be reduced to 5 years to reflect the fact that the useful life of the copyright can be prudently estimated to be only this long. Where the directors anticipate that the future sales revenue from individual copyrights will be insufficient to recover any unamortised costs, such costs are written off immediately.

Intangible assets (trademarks)

Trademarks are valued at cost and are amortised over ten years.

Tangible fixed assets

Depreciation is provided on tangible fixed assets at rates calculated to write off the cost of each asset evenly over its expected useful life as follows:

Short leasehold premises	over the period of lease
Equipment, fixtures and motor vehicles	between 2 and 5 years

In the event of a permanent diminution in value, immediate provision is made.

Stocks

Stocks comprise finished goods, which are valued at the lower of cost and net realisable value, and freehold properties held for resale, which are held at estimated realisable value where this is less than cost.

Advance royalty payments

Advance royalty payments for rights for records, compact discs, audio cassettes and sell-through videos are written off on the basis of units sold, in line with the terms specified in the licence agreement. Where the directors anticipate that future sales will be insufficient to recoup advance royalty payments, the amount considered to be irrecoverable is written off immediately.

Sale of rights

Where media rights are licensed for a fixed or guaranteed sum, turnover is recognised at the point the sale agreement is concluded and the master tapes are delivered and profit is calculated by matching the guaranteed sum with the associated costs of the rights.

Pensions

The group contributes towards personal pension schemes in respect of certain senior employees, the costs of which are charged in the profit and loss account as incurred.

Deferred taxation

Deferred taxation arising from timing differences between profits as computed for taxation purposes and profits as stated in the accounts is provided under the liability method to the extent that a liability is likely to arise in the foreseeable future.

Goodwill

Goodwill arising on consolidation represents the excess of the fair value of the consideration given over the fair value of the identifiable net assets acquired. Goodwill arising on the acquisition of subsidiaries and associates is written off immediately against reserves. Negative goodwill is taken to the Capital Reserve.

Finance and operating leases

Costs in respect of operating leases are charged on a straight line basis over the lease term. Leasing agreements which transfer to the group substantially all the benefits and risk of ownership of an asset are treated as if the asset had been purchased outright. The assets are included in fixed assets and the capital element of the leasing commitments is shown as obligations under finance leases. The lease rentals are treated as consisting of capital and interest elements. The capital element is applied to reduce the outstanding obligations and the interest element is charged against profit in proportion to the reducing capital element outstanding. Assets held under finance leases are depreciated over the useful lives of equivalent owned assets.

Notes to the financial statements for the year ended 31 December 1996

1 Profit for the financial year

As permitted by Section 230 of the Companies Act 1985, the parent company's profit and loss account has not been included in these financial statements. The parent company's retained profit for the year was £285,000 (1995: £80,000).

2 Turnover

Segmental analysis by destination:

	Year ended 31 December 1996 £'000	18 months ended 31 December 1995 £'000
United Kingdom	19,887	25,217
Germany	10,939	13,092
Rest of Europe	4,043	6,767
North America	3,573	3,475
Rest of World	1,296	2,299
	<hr/>	<hr/>
Sales to third parties	39,738	50,850
	<hr/>	<hr/>

Segmental analysis by origin:

	Turnover		Profit before taxation	
	Year ended 31 December 1996 £'000	18 months ended 31 December 1995 £'000	Year ended 31 December 1996 £'000	18 months ended 31 December 1995 £'000
United Kingdom	41,373	48,328	(10,077)	2,036
Germany	1,199	6,056	86	170
Less: inter-area sales	(2,834)	(3,534)	-	-
	<hr/>	<hr/>	<hr/>	<hr/>
	39,738	50,850	(9,991)	2,206
	<hr/>	<hr/>	<hr/>	<hr/>

Overseas net assets are not considered significant and are therefore not separately identified.

Further segmental information has not been disclosed as in the opinion of the directors, disclosure would be seriously prejudicial to the interests of the company.

3 Directors and employees

Messrs Newman, Narang and Bianco are officers of the ultimate holding company, Alliance Entertainment Corporation; and their emoluments are disclosed in the financial information of the US parent Alliance Entertainment Corporation, submitted to the Securities Exchange Commission.

None of the directors received any remuneration from the company or its subsidiaries during the period.

The average weekly number of persons (including directors) employed by the group during the year was:

	Group	
	Year ended	18 months ended
	31 December 1996	31 December 1995
	Number	Number
United Kingdom	113	100
Overseas	4	8
	<u>117</u>	<u>108</u>
	<u><u>117</u></u>	<u><u>108</u></u>
By category:		
Administration	63	53
Production	7	8
Promotion	10	5
Sales	23	30
Warehousing	14	12
	<u>117</u>	<u>108</u>
	<u><u>117</u></u>	<u><u>108</u></u>
	£'000	£'000
Staff costs:		
Wages and salaries	4,065	4,227
Social security	340	448
Other pension costs	49	56
	<u>4,454</u>	<u>4,731</u>
	<u><u>4,454</u></u>	<u><u>4,731</u></u>

4 Other operating income

	Year ended 31 December 1996 £'000	18 months ended 31 December 1995 £'000
Rent receivable (net of outgoings)	8	20
Exchange gains	1,956	58
Miscellaneous income	13	4
	<u>1,977</u>	<u>82</u>

5 Profit on ordinary activities before taxation

	Year ended 31 December 1996 £'000	18 months ended 31 December 1995 £'000
Profit on ordinary activities is stated after charging:		
Depreciation for the year:		
Tangible owned fixed assets	430	342
Tangible fixed assets held under finance leases	251	254
Amortisation of intangible fixed assets	5,877	424
Current year expenditure:		
Auditors' remuneration for:		
Audit	127	128
Other services to company and UK subsidiaries	40	184
Hire of leasehold properties	338	332
Hire of other assets - operating leases	35	74

Note: Remuneration of the company's auditors for provision of non-audit services to the company and its UK subsidiary undertakings covers taxation compliance and advisory fees and other non-statutory audit services.

6 Profit on disposal of subsidiaries

	Year ended 31 December 1996 £'000	18 months ended 31 December 1995 £'000
Liquidation of subsidiary	-	97

7 Interest receivable and similar income

	Year ended 31 December 1996 £'000	18 months ended 31 December 1995 £'000
Interest receivable	24	46

8 Interest payable and similar charges

	Year ended 31 December 1996 £'000	18 months ended 31 December 1995 £'000
On bank loans, overdrafts and other loans repayable within five years:		
Finance leases and hire purchase contracts	40	55
Overdrafts and bank loans	2,524	2,988
	<u>2,564</u>	<u>3,043</u>

9 Fundamental Group Reorganisation

At 31 December 1996 the group reassessed its strategy and took the decision to refocus and reduce significantly its operations with regard to visual rights. As a consequence a decision was taken to cease selling video finished product as of 31 March 1997 and instead will exploit these rights solely via licensing arrangements in the future. The financial cost of this fundamental change the focus of the groups' business was as follows:

	£'000
Redundancy provisions	369
Bad debt provisions	692
Stock provisions	251
Video rights provisions	5,368
Video intangible provisions	4,814
	<u>11,494</u>

10 Tax on profit (loss) on ordinary activities

	Year ended 31 December 1996 £'000	18 months ended 31 December 1995 £'000
United Kingdom corporation tax at 33%		
Current	113	858
Deferred	(1,558)	(43)
Underprovision in respect of prior years		
Current	(253)	-
Deferred	510	-
ACT written off	107	-
	<u>(1,081)</u>	<u>815</u>

11 Dividends

No dividends were paid during the year.

The directors have become aware that, although Castle Communications plc had the necessary distributable reserves, the final dividend received from that company on 31 December 1996 had been paid before the necessary filing of final accounts for the period with the Registrar of Companies. Based on the accounts of Castle Communications plc for the period ended 31 December 1994, payments totalling £392,000 were ultra vires the company and could be recoverable. An Extraordinary General Meeting of the shareholders of Castle Communications plc was held on 13 November 1996 rectifying the position.

12 Intangible assets - Copyrights

The company has no intangible fixed assets. Details of those relating to the group are as follows:

	Group £'000
Cost or valuation	
At 1 January 1996	35,974
Additions	2,889
Disposals	(143)
At 31 December 1996	38,720
Amortisation	
At 1 January 1996	424
Charge for the year	5,877
Disposals	(17)
At 31 December 1996	6,284
Net book value	
At 31 December 1996	32,436
At 31 December 1995	35,550

Cost or valuation at 31 December 1996 is represented by:

Cost - audio	29,789
Cost - visual	2,647
	32,436

Audio copyrights were valued by the directors at 31 December 1996. The basis of the valuation was the economic value of the rights in their existing use within the business of the group.

As stated in the accounting policies, audio copyrights are carried at cost and are not amortised. The requirement of the Companies Act 1985 is to amortise intangible fixed assets over their estimated useful economic lives. The directors consider that to amortise such copyrights would not give a true and fair view as it is the group's policy to maintain the copyrights in such condition that the value of the rights taken as a whole is not impaired by the passage of time; as a consequence any amortisation would, in the opinion of the directors, be immaterial.

On acquisition of the subsidiary Castle Communications plc, fair value adjustments amounting to £6,474,000 were made to increase the cost base of the audio intangible assets acquired.

13 Tangible fixed assets

The company has no tangible fixed assets. Details of those relating to the group are as follows:

	Leasehold premises £'000	Equipment, fixtures and motor vehicles £'000	Total £'000
Cost			
At 1 January 1996	25	2,015	2,040
Additions	-	960	960
Disposals	-	(351)	(351)
At 31 December 1996	25	2,624	2,649
Depreciation			
At 1 January 1996	2	594	96
Charge for year	1	680	681
Disposals	-	(188)	(188)
At 31 December 1996	3	1,086	1,089
Net book value			
At 31 December 1996	22	1,538	1,560
At 1 January 1996	23	1,421	1,444

The net book value of tangible fixed assets includes an amount of £332,000 (1995: £485,000) in respect of assets held under finance leases.

The net book value of leasehold premises described above relates to a lease which had less than 50 years to run at the balance sheet date.

14 Investments

	Group		Company	
	31 December 1996 £'000	31 December 1995 £'000	31 December 1996 £'000	31 December 1995 £'000
At 1 January 1996 and at 31 December 1996	-	-	24,984	24,984

The directors consider that to give full particulars of all subsidiary undertakings would lead to a statement of excessive length. The following information relates to those subsidiary undertakings whose results or financial position, in the opinion of the directors, principally affected the figures of the group:

	Percentage of ordinary share capital held at 31 December 1996	Country of incorporation and principal country in which company operates
Castle Communications plc	100%	Great Britain
Subsidiaries of Castle Communications plc:		
Castle Copyrights Limited	100%	Great Britain
Hendring Limited	99.4%	Great Britain
Eastern Light Productions Limited	100%	Great Britain
Castle Music Limited	100%	Great Britain
Dojo Limited	100%	Great Britain
Kaz Records Limited	100%	Great Britain
Big Picture Limited	50%	Great Britain
Subsidiaries of Big Picture Limited:		
Dragon Media Limited	100%	Great Britain
Castle Communications (Deutschland) GmbH	100%	Germany

All group companies incorporated in Great Britain are registered in England and Wales. All group companies operate in the entertainment industry.

During the year, Castle Communications plc acquired the outstanding shares held by the minority shareholder in Eastern Light Productions Limited for £10,000.

On 31 May 1996 the company acquired 50% of the share capital of Big Picture Limited. This investment was subsequently sold on 31 March 1997.

15 Stocks

The company has no stocks. Details of those relating to the group are as follows:

	31 December 1996 £'000	31 December 1995 £'000
Stocks comprise:		
Finished goods	3,154	2,738
Freehold properties held for sale	-	100
	<u>3,154</u>	<u>2,838</u>

16 Debtors

	Group		Company	
	31 December 1996 £'000	31 December 1995 £'000	31 December 1996 £'000	31 December 1995 £'000
Amounts falling due within one year:				
Trade debtors	11,233	13,203	-	-
Other debtors and prepayments	1,143	1,387	37	52
Amounts due from associated undertakings	106	14	-	-
Amount due from subsidiary undertakings	-	-	1,216	1,230
Corporation tax	28	-	-	-
Amounts due from parent or fellow subsidiary's undertakings in respect of group relief	-	-	308	576
	<u>12,510</u>	<u>14,604</u>	<u>1,561</u>	<u>1,858</u>
Advance royalty payments prepaid	7,688	12,005	-	-
	<u>20,198</u>	<u>26,609</u>	<u>1,561</u>	<u>1,858</u>

In the opinion of the directors, advance royalty payments prepaid are recoupable over the unexpired period of the relevant licences, some of which exceed one year. In the directors opinion any allocation between amounts falling due in less than or after one year would not be meaningful.

17 Creditors

	Group		Company	
	31 December 1996 £'000	31 December 1995 £'000	31 December 1996 £'000	31 December 1995 £'000
Amounts falling due within one year:				
Bank overdraft	347	437	-	-
Bank loans	16,841	15,742	1,841	1,742
Other loans	-	185	-	-
Liability under hire purchase agreements (note 25)	210	218	-	-
Trade creditors	11,095	11,061	-	-
Amount owed to parent/commonly controlled undertakings	13,641	9,973	5,594	3,306
Dividends payable	18	9	-	-
Amounts due to parent/commonly controlled undertakings in respect of group relief	101	-	-	-
Corporation tax	267	330	-	5
Other taxation and social security	529	411	-	-
Other creditors	749	526	-	-
Accruals and deferred income	1,003	1,231	9	10
Rights commitments	936	957	-	-
	<u>45,737</u>	<u>41,080</u>	<u>7,444</u>	<u>5,063</u>
Amounts falling due after more than one year:				
Liability under hire purchase agreements (repayable over one and under two years) (note 25)	81	213	-	-
Bank loans	8,941	11,903	8,940	11,903
	<u>9,022</u>	<u>12,116</u>	<u>8,940</u>	<u>11,903</u>

Bank loans can be analysed as follows:

	Current liabilities £'000	Long term liabilities £'000	Total £'000
Cash equivalents	15,000	-	15,000
Non cash equivalents	1,841	8,941	10,782
	<u>16,841</u>	<u>8,941</u>	<u>25,782</u>

Cash equivalent bank loans represent amounts drawn down under a revolving syndicated loan facility with the Chase Manhattan Bank N.A. and others and are repayable on demand. Interest is payable at a variable rate at the time when individual tranches mature and are either rolled over or repaid. Details of the security given in respect of these facilities are disclosed in note 26 to the financial statements.

Non cash equivalent bank loans represent amounts borrowed under a term loan arrangement from Chase Manhattan Bank N.A. and others and are repayable in quarterly instalments with the final instalment being due on 30 September 1999.

18 Provisions for liabilities and charges

	Group		Company	
	31 December 1996	31 December 1995	31 December 1996	31 December 1995
	£'000	£'000	£'000	£'000
Deferred taxation				
Tax effect of timing differences	2,225	1,878	-	-
Advance corporation tax	(122)	(77)	-	-
Tax effect of losses carried forward	(1,472)	-	-	-
	<u>631</u>	<u>1,801</u>	<u>-</u>	<u>-</u>
	<u><u>631</u></u>	<u><u>1,801</u></u>	<u><u>-</u></u>	<u><u>-</u></u>

	Deferred taxation £'000
At 1 January 1996	1,801
Profit and loss account	1,048
Transfer from ACT payable	(122)
	<u>631</u>
At 31 December 1996	<u><u>631</u></u>

There is no unprovided potential liability for deferred taxation for the group or the company. The provision for deferred taxation principally relates to tax relief on advance royalties prepaid. Unprovided deferred tax on tax losses carried forward was £1,495,000 (1995:nil).

19 Share capital

	31 December 1996 £'000	31 December 1995 £'000
Authorised		
15,000,000 ordinary shares of £1 each	<u>15,000</u>	<u>15,000</u>
Allotted, called up and fully paid		
9,694,546 ordinary shares of £1 each	<u>9,695</u>	<u>9,695</u>

20 Share premium account and reserves

Group	Capital reserve £'000	Profit and loss account £'000
At 1 January 1996	363	1,387
Retained loss for the year	-	(8,919)
Goodwill written-off on acquisition	-	(42)
Exchange adjustment	-	(38)
At 31 December 1996	<u>363</u>	<u>(7,612)</u>

The cumulative amount of negative goodwill written back to group reserves at 31 December 1996 was £310,000 (1995: £352,000).

Company	Profit and loss account £'000
At 1 January 1996	181
Retained profit for the year	285
At 31 December 1996	<u>466</u>

21 Cash and cash equivalents

	1996 £'000	1995 £'000
Changes during the year:		
At 1 January 1996/1 July 1994	(14,436)	-
Acquisition of Castle Communications plc	-	(4,286)
Net cash outflow before adjustments for the effects of foreign exchange rate changes	(385)	(10,157)
Effect of foreign exchange rate changes	(38)	7
	<u>(14,859)</u>	<u>(14,436)</u>
At 31 December	<u>(14,859)</u>	<u>(14,436)</u>
Analysis of balances:		
Cash at bank and in hand	488	1
Bank loans and overdrafts	(15,347)	(14,437)
	<u>(14,859)</u>	<u>(14,436)</u>
At 31 December	<u>(14,859)</u>	<u>(14,436)</u>

22 Analysis of changes in financing during the year

	1996		1995	
	Share capital £'000	Secured and other loans £'000	Share capital £'000	Secured and other loans £'000
Balance at 1 January	9,695	8,185	-	-
Cash (outflows)/inflows from financing	-	(3,371)	9,695	7,653
New capital leases	-	183	-	532
	<u>9,695</u>	<u>4,997</u>	<u>9,695</u>	<u>8,185</u>
Balance at 31 December	<u>9,695</u>	<u>4,997</u>	<u>9,695</u>	<u>8,185</u>

23 Acquisition of Castle Communications plc

On 9 September 1994 the Company acquired the whole of the share capital of Castle Communications Plc. The consideration for the purchase was settled in cash. Castle Communication Plc's identifiable assets and its liabilities were as follows:

	£'000
Intangible assets	25,347
Tangible assets	729
Cash	1,345
Stock	3,134
Debtors	7,851
Prepayments	560
Advance royalties	11,289
Loans	(10,006)
Trade creditors	(9,545)
Other creditors	(3,468)
Obligations on capital lease > 1 year	(91)
Deferred income taxes	(1,256)
Rights commitment > 1 year	(542)
Net assets	25,347
Goodwill	(363)
	<hr/> 24,984 <hr/>
Satisfied by	
Cash paid (investment)	24,984
Cash	(1,345)
	<hr/> 23,639 <hr/>
Cash flow	

There were no fair value adjustments other than the revaluation of intangible assets from a book value of £18,873,000 to a fair value of £25,347,000 ie an increase of £6,474,000.

24 Commitments

The company did not have any commitments under operating leases at 31 December 1996. The commitments of the group are as follows:

	Year ended 31 December 1996		18 months ended 31 December 1995	
	Land and buildings £'000	Other £'000	Land and buildings £'000	Other £'000
Operating leases				
Commitments in next financial year from leases expiring:				
Within one year of the balance sheet date	-	1	-	-
Within two to five years of the balance sheet date	-	30	-	13
In more than five years of the balance sheet date	378	-	306	21
	<u>378</u>	<u>31</u>	<u>306</u>	<u>34</u>
	<u><u>378</u></u>	<u><u>31</u></u>	<u><u>306</u></u>	<u><u>34</u></u>

25 Finance leases

The company did not have any finance leases at 31 December 1996. The finance lease commitments of the group are detailed below.

Included in fixed assets are fixtures and equipment held under finance leases. As at 31 December, the gross book value of these assets was £648,000 (1995: £831,000). Associated accumulated depreciation amounted to £316,000 (1995: £346,000) and depreciation of £251,000 (1995: £254,000) has been charged to the profit and loss account for the year.

Amounts repayable by the group under finance leases are analysed as follows:

	31 December 1996 £'000	31 December 1995 £'000
Repayable within one year of balance sheet date (note 17)	210	218
Repayable between two and five years of balance sheet date (note 17)	81	213
	<u>291</u>	<u>431</u>
	<u><u>291</u></u>	<u><u>431</u></u>

26 Contingent liabilities

The company has a number of contingent liabilities arising from third party claims. The directors are of the opinion that, while the outcome of the claims cannot be predicted with any certainty, they do not expect any liability which may arise to have a material impact of the company's results, cashflow or financial condition.

On 25 July 1995 the company entered into certain security documentation with Chase Manhattan Bank N.A. to, inter alia, secure the obligations of the company, its ultimate parent and certain other group companies to the Chase Manhattan N.A. acting as security agents under a loan agreement dated 25 July 1995. As part of these obligations Chase Manhattan N.A. have a first charge over the of the issued ordinary shares of the company and certain subsidiary undertakings.

On 24 July 1995 the company executed an indenture guaranteeing the obligations of the company's ultimate parent, Alliance Entertainment Corporation pursuant to the issue by Alliance Entertainment Corporation of \$125 million senior subordinate notes due 2005 issued for the purposes of meeting the working capital requirements of Alliance Entertainment Corporation and its subsidiaries.

The filing under Chapter 11 of the US bankruptcy code by Alliance Entertainment Corporation, the company's ultimate parent company, does not affect either the security documentation or the indenture described above.

The company has entered a composite cross guarantee with other group companies in order to secure banking facilities. Under the terms of this guarantee the company is jointly and severally liable, with all other group companies, for any liability to the group's bankers, Coutts & Co., which cannot be met by the company in whose name the liability exists.

27 Post balance sheet events

On 13 July 1997 Alliance Entertainment corporation, the company's ultimate parent company, filed to reorganise under Chapter 11 of the United States bankruptcy code in order to reorganise its core business and to restructure its long term debt, revolving credit facilities and trade creditor obligations.

The company itself was specifically excluded from the filing due to its status as a non-domestic entity in the US and continues to trade normally.

28 Ultimate Parent Company

The immediate and ultimate parent company is Alliance Entertainment Corporation, a company incorporated in USA and registered in USA. Copies of the ultimate parent company's Annual Report are available to the public from Alliance Entertainment Corporation, 110 East 59th Street, New York, New York 10022, USA.