

A copy of this document, which comprises listing particulars relating to The Character Group plc prepared in accordance with the Listing Rules made under section 74 of the Financial Services and Markets Act 2000, has been delivered to the Registrar of Companies in England and Wales for registration, as required by section 83 of that Act.

These listing particulars have been issued in connection with an application which has been made for the 7,500,000 New Ordinary Shares to be admitted to the Official List of the UK Listing Authority and to trading on the London Stock Exchange's market for listed securities. It is expected that such admission will become effective and dealings in the New Ordinary Shares will commence on 23 February 2004. The Ordinary Shares are traded on the London Stock Exchange and no other stock exchange.

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## **The Character Group plc**

*(Incorporated and registered in England and Wales under the Act – No. 3033333)*

### **Listing Particulars**

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The Directors of the Company, whose names appear on page 40 of this document, accept responsibility for the information contained in this document. To the best of the knowledge and belief of the Directors (who have taken all reasonable care to ensure that such is the case), the information contained in this document is in accordance with the facts and does not omit anything likely to affect the import of such information.

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## Definitions

The following definitions apply throughout this document and in the accompanying Form of Proxy unless the context otherwise requires:

"Act"	the Companies Act 1985, as amended;
"Admission"	the admission of the New Ordinary Shares to the Official List becoming effective in accordance with the Listing Rules and admission of the New Ordinary Shares to trading having been granted by the London Stock Exchange to its market for listed securities;
"Approved Scheme"	the Company's Inland Revenue approved 1995 Executive Share Option Scheme, further particulars of which are set out in paragraph 11.1 of Part IV of this document;
"Board" or "Directors"	the directors of the Company, whose names are set out on page 40;
"Circular"	the circular letter from the Company to its Shareholders, comprising listing particulars, dated 22 June 2001, a copy of which will be available for inspection as stated in paragraph 15.8 of Part IV of this document;
"Company" or "Character Group"	The Character Group plc;
"connected persons"	persons as defined by section 346 of the Act;
"Convertible Loan Note"	the £4,600,000 (nominal) unsecured convertible loan note issued by the Company on 16 July 2001, further details of which are set out in Part III of this document;
"CREST"	the system for trading securities, or interests in securities in uncertificated form, operated by CRESTCo;
"CRESTCo"	CRESTCo Limited, the operator (as defined in The Uncertificated Securities Regulations 1995) of CREST;
"EMI Scheme"	the Company's Enterprise Management Incentive Share Option Scheme, further particulars of which are set out in paragraph 11.3 of Part IV of this document;
"Giochi Preziosi"	Giochi Preziosi S.p.A.;
"Group"	the Company and its existing subsidiaries;
"Listing Rules"	the listing rules of the UK Listing Authority made under section 74 of the Financial Services and Markets Act 2000;
"London Stock Exchange"	London Stock Exchange plc;
"Official List"	The Official List of the UK Listing Authority;
"Ordinary Shares"	ordinary shares of 5p each in the capital of the Company;
"New Ordinary Shares"	the 7,500,000 new Ordinary Shares issued and allotted to Valtidone on 8 December 2003 following conversion of the balance outstanding at that date of the Convertible Loan Note;
"Relevant Executive Directors"	together, R. King, K.P. Shah, J.J.P. Kissane and J.J. Diver;
"Shareholders"	holders of Ordinary Shares;
"Share Schemes"	together, the Approved Scheme and Unapproved Scheme;
"TISA"	Toys Investments S.A.;
"UK" or "United Kingdom"	the United Kingdom of Great Britain and Northern Ireland;

"UK Listing Authority"	the Financial Services Authority acting in its capacity as the competent authority for the purposes of Part VI of the Financial Services and Markets Act 2000;
"Unapproved Scheme"	the Company's unapproved 1997 Executive Share Option Scheme, further particulars of which are set out in paragraph 11.2 of Part IV of this document; and
"Valtidone"	Valtidone S.p.A.

## **Part I**

### **Information regarding The Character Group plc**

#### **Introduction**

This document comprises listing particulars relating to the Company and has been prepared in accordance with the Listing Rules. These listing particulars are for lodgement purposes only and have been published in accordance with the requirements of Chapter 5 of the Listing Rules due to the conversion by Valtidone of its remaining interest in the balance outstanding of the Convertible Loan Note into the New Ordinary Shares as announced by the Company on 3 December 2003. This document is not being sent to Shareholders but is available for inspection at the Document Viewing Facility of the UKLA, 25 The North Colonnade, London E14 5HS.

#### **The Business of the Group**

The Group is engaged in the design, development and international distribution of digital cameras, toys, games and giftware. The Group's business is conducted through three divisions:

##### *The Toy and Games Division*

This division comprises Character Options Limited, Character Games Limited, Toy Options (Far East) Limited and Character Games (Far East) Limited. This division is engaged in the design, development, importation, marketing and distribution of toys and games. Traditionally this division has focused principally on the UK market but, following the acquisition of its games business in 2000 and given the recent successful development of its strategy for the origination of its own product lines, the division's market has grown with distribution being achieved, and further developed, in Europe, the United States of America and in other significant territories.

##### *The Digital Products Division*

This division comprises World Wide Licenses Limited ("WWL") and WWL (Europe) Limited. This division is engaged principally in the design and distribution of digital cameras which it started to develop from June 2000.

In addition, WWL provides Group companies with management and other services in relation to their Far Eastern operations, including quality assurance, quality control and local procurement.

The successes of this division in developing and bringing products to market in this new sector has seen a rapid growth in sales and, in real terms, growth of 137% in sales was achieved in the year ended 31 August 2003.

An important development in this division has been the agreement entered into with the Polaroid Corporation in July 2002. This is a licence agreement authorising the use by the division of the Polaroid name and trade mark in relation to a range of newly developed digital camera products. This agreement, which was originally limited to the territories of the United States of America and Canada but has subsequently been extended to include all major territories throughout the world other than the Peoples' Republic of China, is initially for a term of three years expiring in October 2005. The agreement grants exclusive rights to WWL to design, develop, manufacture and sell digital cameras (other than single use digital cameras) under the Polaroid<sup>®</sup> brand in the licensed territories.

##### *The Giftware Division*

This division comprises Downpace Limited and Downpace (Far East) Limited. This division is engaged in business as a gift importer and distributor in the UK.

## Financial information relating to the Group

In the financial year ended 31 August 2003, the Company generated profits before taxation of £5.8 million on sales of £85.3 million.

Your attention is drawn to the financial information relating to the Company which is set out in Part II of this document.

## Current trading and prospects

At the Annual General Meeting of the Company held on 21 January 2004, Richard King (Chairman), commenting on the Group's current trading and prospects, said:

"Sales for the Group for the four months to 31 December 2003 rose by approximately 8.5% over the corresponding period for the previous year. Set against the generally difficult trading conditions in the UK in the run up to Christmas, this increase was satisfactory, although it was nevertheless disappointing with sales of toys, games and gifts not reaching their full potential.

The digital division, however, saw an impressive growth of approximately 145% over the period. This increase was achieved in spite of experiencing certain difficulties with our US distribution which have already been addressed by the recent appointment of a new distributor who has formed a new division to concentrate on the distribution of our digital ranges. We believe that this distributor will take advantage of its extensive customer base in the US, and that we shall see substantial growth in US sales during the second half of the year.

In the UK, our digital sales have grown more than tenfold, and this has firmly put us into the market as a major digital supplier. Sales in other international territories are developing well.

The lower than projected sales in the toys and games, and giftware divisions, the additional costs incurred in changing the US distributor, and as alluded to in the annual report, the costs incurred in our extensive new product development programme, where we are yet to see any material benefit, are likely to cause a drop in profitability at the interim stage when compared to the same period last year.

Following the conversion of the loan stock in December, the Group is today completely ungeared, with no bank overdraft or other borrowings.

The Directors believe that the outcome for the year as a whole will be satisfactory and in line with market expectations."

## Background to and information regarding the Convertible Loan Note

On 22 June 2001, the Company announced that it proposed *inter alia* to issue the £4.6 million (nominal) Convertible Loan Note to TISA as part of its refinancing arrangements announced on the same day. The Circular was dated and dispatched to Shareholders on 22 June 2001. The terms of the Convertible Loan Note provided that the nominal amount outstanding of the Convertible Loan Note would be convertible into Ordinary Shares, at any time from the date of its issue until the third anniversary of its date of issue, at a price of 40p per share. As stated in the Circular, the full conversion of the Convertible Loan Note would result in the issue of 11.5 million new Ordinary Shares. Full details of the Convertible Loan Note were *inter alia* given in the Circular. The issue of the Convertible Loan Note was approved *inter alia* by Shareholders at an Extraordinary General Meeting of the Company convened by the Circular and held on 16 July 2001, immediately following which the Convertible Loan Note was issued to TISA.

As announced on 4 October 2001, the transfer of the Convertible Loan Note by TISA to Valtidone was approved by the Board on 3 October 2001.

On 12 November 2003, it was announced that Valtidone had partially exercised its conversion rights in respect of £1.6 million (nominal) of the Convertible Loan Note with the result that 4 million new Ordinary Shares, representing approximately 9.7 per cent. of the then issued Ordinary Share capital of the Company, was allotted and issued by the Company to Valtidone, representing approximately

8.8 per cent. of the issued Ordinary Share capital of the Company as enlarged by such issue. These 4 million new Ordinary Shares were admitted to the Official List and to trading on the London Stock Exchange's market for listed securities on 17 November 2003.

On 3 December 2003, the Company announced that it had issued and allotted the 7.5 million New Ordinary Shares to Valtidone as a result of the exercise by Valtidone of its conversion rights in respect of the balance of £3 million (nominal) of its remaining interest in the Convertible Loan Note. These 7.5 million New Ordinary Shares represent approximately 14.2 per cent. of the issued Ordinary Share capital of the Company as enlarged by such further issue.

As the New Ordinary Shares represent more than 10 per cent. of the Company's existing issued Ordinary Share capital as at 3 December 2003, the Company is required to issue these listing particulars under the Listing Rules.

Application has been made for the New Ordinary Shares to be admitted to the Official List and to trading on the London Stock Exchange's market for listed securities. Admission is expected to become effective on 23 February 2004. The New Ordinary Shares rank *pari passu* in all respects with the Company's existing issued Ordinary Shares, including in relation to any right to receive any dividend made, paid or declared following the date of allotment. A definitive share certificate in respect of the New Ordinary Shares will be delivered to Valtidone within 7 days of Admission.

Further information relating to the terms of the Convertible Loan Note is set out in Part III of this document.

### **Further Information**

Further information relating to the Company and the Group is set out in Part IV of this document.

## Part II

### Accountants' Report

The following is the full text of a report on the Company from Baker Tilly, (the Reporting Accountants), to the Directors of the Company and Collins Stewart Limited.



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and

The Directors  
Collins Stewart Limited  
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London EC2V 7QR

17 February 2004

Dear Sirs

#### **THE CHARACTER GROUP PLC ("the Company")**

#### **Introduction**

We report in connection with the proposed admission to the Official List of the UK Listing Authority and to trading on the London Stock Exchange's market for listed securities (the "Listing") of the Company's ordinary shares issued and allotted on 3<sup>rd</sup> December 2003. This report has been prepared for inclusion in the related listing particulars (the "Listing Particulars").

#### **Basis of preparation**

The financial information set out below has been extracted from the audited consolidated accounts of the Company and its subsidiaries (the "Group") for the three years ended 31 August 2003, after making such adjustments as we consider necessary. The accounts for the year ended 31 August 2001 were audited by HLB Kidsons who gave an unqualified report thereon. The accounts for the years ended 31 August 2002 and 31 August 2003 were audited by Baker Tilly (formerly HLB Kidsons) who gave unqualified reports thereon.

## **Responsibility**

The consolidated accounts are the responsibility of the directors of the Company (the "Directors"). The Directors are also responsible for the contents of the Listing Particulars dated 17 February 2004 in which this report is included.

It is our responsibility to compile the financial information set out in our report from the Company's financial records, to form an opinion on the financial information and to report our opinion to you.

## **Basis of opinion**

We conducted our work in accordance with the Statements of Investment Circular Reporting Standards issued by the Auditing Practices Board. Our work included an assessment of evidence relevant to the amounts and disclosures in the financial information. The evidence included that previously obtained by us relating to the audit of the accounts underlying the financial information. It also included an assessment of the significant estimates and judgements made by those responsible for the preparation of the financial records and whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our work 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 information is free from material misstatement, whether caused by fraud or other irregularity or error.

## **Opinion**

In our opinion, the financial information set out below gives, for the purpose of the Listing Particulars, a true and fair view of results, cash flows and total recognised gains and losses of the Group for the three years ended 31 August 2003 and of the state of affairs of the Group at the end of each of the three years.

## CONSOLIDATED PROFIT AND LOSS ACCOUNTS

	Note	Year ended 31 August		
		2001 ? 00	2002 ? 00	2003 ? 00
<b>Turnover</b>	2	58,887	58,939	85,308
Cost of sales		(42,809)	(38,933)	(58,610)
<b>Gross profit</b>		16,078	20,006	26,698
<b>Net operating expenses</b>				
Selling and distribution costs		(7,356)	(7,119)	(9,138)
Administration expenses		(13,171)	(11,218)	(11,700)
Other operating income		440	408	526
<b>Operating (loss)/profit</b>	3	(4,009)	2,077	6,386
Interest	5	(866)	(562)	(563)
<b>(Loss)/profit on ordinary activities before taxation</b>		(4,875)	1,515	5,823
Taxation	6	(878)	(262)	(287)
<b>(Loss)/profit on ordinary activities after taxation</b>		(5,753)	1,253	5,536
Dividend	7	-	-	(1,310)
<b>Retained (Loss)/profit for the year</b>	19	(5,753)	1,253	4,226
<b>Earnings per share</b>	8			
? basic		(14.03p)	3.06p	13.50p
? fully diluted		(14.03p)	2.63p	10.60p
? dividend per share	7	-	-	3.00p
<b>EBITDA (earnings before interest, tax, depreciation and amortisation)</b>		(3,243)	2,782	7,395

All activity arose from the Group's continuing operations.

There were no material recognised gains or losses other than items dealt within the profit and loss accounts above.

For exchange rate movements taken to reserves see note 19.

## CONSOLIDATED BALANCE SHEETS

	Note	As at 31 August		
		2001 ? 00	2002 ? 00	2003 ? 00
<b>Fixed assets</b>				
Intangible assets	9	818	773	737
Tangible assets	10	2,012	1,844	1,876
Investments	11	53	74	341
		<u>2,883</u>	<u>2,691</u>	<u>2,954</u>
<b>Current assets</b>				
Stocks	12	7,785	4,982	8,143
Trade debtors subject to finance arrangements		5,957	7,946	7,302
Factor advances		(4,432)	(6,580)	(5,401)
		1,525	1,366	1,901
Debtors ? including non-factored trade debtors	13	6,416	10,117	16,776
Cash at bank and in hand		1,638	3,284	3,932
		<u>17,364</u>	<u>19,749</u>	<u>30,752</u>
Creditors: amounts falling due within one year:	14			
Convertible loan note		-	-	(4,600)
Other creditors		(13,953)	(15,374)	(23,504)
		<u>3,411</u>	<u>4,375</u>	<u>2,648</u>
<b>Net current assets</b>		<u>6,294</u>	<u>7,066</u>	<u>5,602</u>
<b>Total assets less current liabilities</b>				
Creditors: amounts falling due after more than one year:	15			
Convertible loan note		(4,600)	(4,600)	-
Other creditors		(5)	(1)	(4)
		<u>(4,605)</u>	<u>(4,601)</u>	<u>(4)</u>
<b>Provision for liabilities and charges</b>	16			
Investment in joint venture:				
Share of gross assets		-	-	-
Share of gross liabilities		(13)	-	-
		<u>1,676</u>	<u>2,465</u>	<u>5,598</u>
<b>Net assets</b>		<u>1,676</u>	<u>2,465</u>	<u>5,598</u>
<b>Capital and reserves</b>				
Called up share capital	18	2,064	2,064	2,064
Shares to be issued	19, 24	908	908	-
Capital redemption reserve	19	15	15	15
Share premium	19	7,843	7,843	7,843
Merger reserve	19	651	651	651
Profit and loss account	19	(9,805)	(9,016)	(4,975)
		<u>1,676</u>	<u>2,465</u>	<u>5,598</u>
<b>Equity shareholders?funds</b>	17	<u>1,676</u>	<u>2,465</u>	<u>5,598</u>

## CONSOLIDATED CASH FLOW STATEMENTS

	Note	Year ended 31 August		
		2001 ? 00	2002 ? 00	2003 ? 00
<b>Cash (outflow)/inflow from operating activities</b>	21	(6,488)	3,064	3,817
<b>Returns on investment and servicing of finance</b>				
Interest received		70	17	12
Interest paid		(928)	(575)	(574)
Interest element of finance lease rental payments		(8)	(4)	(1)
<b>Net cash (outflow) for returns on investments and servicing of finance</b>		(866)	(562)	(563)
<b>Taxation</b>		474	(155)	(285)
<b>Capital expenditure and financial investment</b>				
Payments to acquire tangible fixed assets		(355)	(770)	(1,038)
Sale of tangible fixed assets		45	200	24
Purchase of business and assets	9	-	-	(902)
<b>Net cash (outflow) for capital expenditure and financial investment</b>		(310)	(570)	(1,916)
Equity dividends paid		-	-	(410)
<b>Cash (outflow)/inflow before use of liquid resources and financing</b>		(7,190)	1,777	643
<b>Financing</b>				
Issue of ordinary share capital		3,278	-	-
Issue of convertible loan note		4,600	-	-
Capital element of finance lease rentals		(49)	(37)	5
Short term bank loan		(259)	(94)	-
<b>Net cash inflow/(outflow) from financing</b>		7,570	(131)	5
<b>Increase in cash in the year</b>	23	380	1,646	648
<b>Decrease in net debt in the year</b>	23	688	1,777	643

## NOTES TO THE FINANCIAL INFORMATION

### 1 PRINCIPAL ACCOUNTING POLICIES

#### Basis of accounting

The accounts have been prepared in accordance with applicable accounting standards and under the historical cost accounting rules. The principal accounting policies of the Group are set out below:

#### Basis of consolidation

The consolidated financial information comprises the accounts of the Group, all of which are made up to the end of the Company's financial year.

Where part of the purchase consideration for an acquisition is dependent on future profits of the acquired company or business, and can be satisfied, at the Group option, by the issue of new shares, provision is made for the estimated future consideration and shown in the balance sheet as shares to be issued in accordance with the requirement of FRS 7.

#### Goodwill

Goodwill arising on acquisitions of businesses and subsidiary undertakings is calculated as the excess of the fair value of the consideration given and costs of acquisition over the fair value of the separable net assets acquired. Goodwill arising on acquisitions before 1 September 1998 was written off against reserves immediately on acquisition. In accordance with FRS 10, goodwill arising on acquisitions on or after 1 September 1998 is capitalised as an intangible fixed asset and amortised over its estimated useful economic life. The goodwill carried in the balance sheet is written off over 20 years. Goodwill previously written off directly to reserves has not been reinstated on the balance sheet, but written off against the profit and loss reserve in accordance with the transitional provisions of FRS 10.

On the subsequent disposal or termination of a previously acquired business, the profit or loss on disposal or termination is calculated after charging the amount of any related goodwill taken directly to reserves on acquisition and the net book value of any related goodwill capitalised in the balance sheet.

#### Investments

Investments are valued at the lower of cost and recoverable amount, where recoverable amount is the higher of net realisable value and value in use. Provision is made against investments where the diminution in value is considered to be permanent. Own shares are valued at the lower of cost and market value.

#### Depreciation

Depreciation is provided on all tangible fixed assets at rates calculated to write off the cost of each asset evenly over its expected useful life. The following principal rates per annum are used:

Freehold buildings	4%
Short leasehold improvements	over the unexpired term of the lease
Tooling	20 ? 100%
Fixtures, fittings and equipment	20 ? 33%
Motor vehicles	20 ? 25%

Impairment write downs are made in accordance with FRS 11 by comparing the net realisable value to the value in use.

#### Stocks

Stocks are stated at the lower of cost and net realisable value. Net realisable value is based on estimated selling price less the estimated cost of disposal.

## NOTES TO THE FINANCIAL INFORMATION

### 1 PRINCIPAL ACCOUNTING POLICIES - continued

#### Factoring arrangements

Certain subsidiaries have factoring agreements under which debts approved by the factor company are assigned to them without recourse. Non-refundable advances are made by the factor company. The directors do not intend that the company will support any losses from factored debts, and the factor company can only seek recourse of funds from the asset financed and can not seek any other recourse. A linked presentation of the relevant balances is therefore shown on the face of the balance sheet in accordance with the requirements of FRS 5. The factor company has a debenture over the assets of the Company and certain subsidiary companies. The factoring charges are charged to the profit and loss account as they accrue. The amount charged to the profit and loss in the year was ? 02,000 (2002: ? 38,000) (2001: ? 49,000). Of this amount ? 22,000 (2002: ? 07,000) (2001: ? 95,000) has been charged as interest (see note 5), with the remainder being charges made by the factor company which have been included within administration expenses.

#### Foreign currencies

In the accounts of individual group undertakings, transactions in foreign currencies are recorded in the local currency using the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated using the rate of exchange ruling at the balance sheet date and the gains and losses on translation are included in the profit and loss account. In the consolidated accounts, the results and the balance sheets of overseas subsidiary undertakings are translated at the year end exchange rates. Exchange differences resulting from the re-translation of opening net assets are dealt with in reserves. All other exchange differences are dealt with in the profit and loss account.

#### Leasing and hire purchase contracts

Assets held under finance leases and hire purchase contracts are capitalised in the balance sheet and are depreciated over their useful lives. The interest element of the rental obligations is charged to the profit and loss account over the period of the lease and represents a constant proportion of the balance of capital repayments outstanding. Rentals paid under operating leases are charged to income as incurred.

#### Financial instruments

Financial assets are recognised on the balance sheet at the lower of cost and net realisable value. Discounts and premia are charged or credited to the profit and loss account over the life of the asset or liability to which they relate. The Group has taken advantage of the exemption available for short term debtors and creditors.

#### Deferred taxation

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events that result in an obligation to pay more tax in the future or a right to pay less tax in the future have occurred at the balance sheet date. Timing differences are differences between the Group taxable profits and its results as stated in the accounts that arise from the inclusion of gains and losses in tax assessments in periods different from those in which they are recognised in the accounts.

Deferred tax is recognised in respect of the retained earnings of overseas subsidiaries and associates only to the extent that, at the balance sheet date, dividends have been accrued as receivable or a binding agreement to distribute past earnings in future has been entered into by the subsidiary or associate.

Deferred tax is measured at the average tax rates that are expected to apply in the periods in which timing differences are expected to reverse, based on tax rates and laws that have been enacted or substantially enacted by the balance sheet date. Deferred tax is measured on a non-discounted basis.

#### Pension contributions

The Group operates defined contribution pension schemes. Contributions are allocated to the profit and loss account when due.

#### Research and development

Research and development costs represent expenditure that is directly attributable to the development of products, and are written off as an expense in the year incurred.

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## 2 TURNOVER

Turnover represents the amount derived from the provision of goods and services which arise from the Group ordinary activities, stated net of value added tax. An analysis of turnover by geographical market is given below:

### Analysis of turnover by geographical market by destination

	12 months to 31 August 2001 ? 00	12 months to 31 August 2002 ? 00	12 months to 31 August 2003 ? 00
United Kingdom	41,465	42,213	51,781
Rest of the world	17,422	16,726	33,527
<b>Total</b>	<b>58,887</b>	<b>58,939</b>	<b>85,308</b>

### Analysis of turnover by division

	12 months to 31 August 2001 ? 00	12 months to 31 August 2002 ? 00	12 months to 31 August 2003 ? 00
Toys and games	32,524	36,097	43,988
Giftware	10,053	8,498	7,387
Digital	16,310	14,344	33,933
<b>Total</b>	<b>58,887</b>	<b>58,939</b>	<b>85,308</b>

All the Group activities during the years ended 31 August 2003, 2002 and 2001 are classed as continuing. The Directors consider that the disclosure of further disaggregated information would be seriously prejudicial to the commercial interests of the Group.

## 3 OPERATING (LOSS)/PROFIT

	Note	12 months to 31 August 2001 ? 00	12 months to 31 August 2002 ? 00	12 months to 31 August 2003 ? 00
Operating (loss)/profit is stated after charging:				
Staff costs	4	6,643	5,846	6,686
Auditors' remuneration	? audit services	90	98	107
	? non audit services	75	35	33
Operating leases	? land and buildings	369	240	291
Research and development costs		-	370	1,023
Depreciation of tangible fixed assets	? owned assets	705	658	975
	? assets held under finance leases and HP contracts	31	2	4
		736	660	979
Goodwill amortisation		30	45	30
Loss/(profit) on disposal of fixed assets		52	78	(3)

#### 4 DIRECTORS AND EMPLOYEES

	12 months to 31 August 2001 ? 00	12 months to 31 August 2002 ? 00	12 months to 31 August 2003 ? 00
Staff costs including Directors' emoluments			
Wages and salaries	5,806	5,196	5,856
Social security costs	583	402	522
Other pension costs	254	248	308
	<b>6,643</b>	<b>5,846</b>	<b>6,686</b>
The average number of employees during the year was:	Number	Number	Number
Management and administration	101	72	73
Selling and distribution	126	100	130
	<b>227</b>	<b>172</b>	<b>203</b>

The amount payable to pension schemes as at the balance sheet date was ? 8,000 (2002: ? 4,000) (2001: ? 3,000).

The following table shows a breakdown of the remuneration of the Directors for the years ended 31 August 2003, 2002 and 2001.

#### Directors' Remuneration

	Salary/fees	Performance bonus	Benefit in Kind	Pension Contribution	Total
	£	£	£	£	£
<b>Year ended 31 August 2003</b>					
R King	149,000	149,000	4,902	52,150	355,052
E Preziosi	-	-	-	-	-
K P Shah	144,000	144,000	3,969	36,000	327,969
J J P Kissane	122,000	122,000	2,582	36,600	283,182
J J Diver	122,000	122,000	6,626	24,400	275,026
I S Fenn (non-executive)	17,033	-	-	-	17,033
Lord Birdwood (non-executive)	17,033	-	-	-	17,033
A G Horvat (non-executive) - appointed 29 November 2002	13,333	-	-	-	13,333
M F V Cellai (non-executive) - resigned 29 November 2002	-	-	-	-	-
	<b>584,399</b>	<b>537,000</b>	<b>18,079</b>	<b>149,150</b>	<b>1,288,628</b>
<b>Year ended 31 August 2002</b>					
R King	140,833	140,833	17,178	47,250	346,094
E Preziosi	-	-	-	-	-
K P Shah	135,833	135,833	9,990	32,500	314,156
J J P Kissane	115,000	115,000	9,209	27,500	266,709
J J Diver	115,000	115,000	9,209	22,000	261,209
I S Fenn (non-executive)	15,000	-	-	-	15,000
Lord Birdwood (non-executive)	15,000	-	-	-	15,000
M F V Cellai (non-executive)	-	-	-	-	-
	<b>536,666</b>	<b>506,666</b>	<b>45,586</b>	<b>129,250</b>	<b>1,218,168</b>

#### 4 DIRECTORS AND EMPLOYEES - continued

Year ended 31 August 2001	Salary/fees	Performance bonus	Benefit in Kind	Pension Contribution	Total
	£	£	£	£	£
R King	135,000	-	24,168	47,250	206,418
E Preziosi	-	-	-	-	-
K P Shah	130,000	-	8,905	32,500	171,405
J J P Kissane	110,000	-	12,761	27,500	150,261
J J Diver	110,000	-	15,912	22,000	147,912
I S Fenn (non-executive)	15,000	-	-	-	15,000
Lord Birdwood (non-executive)	15,000	-	-	-	15,000
M F V Cellai (non-executive)	-	-	-	-	-
	515,000	-	61,746	129,250	705,996

On 28 March 1996, J J P Kissane and J J Diver were each granted options over 100,000 ordinary shares in the Company at an exercise price of 107p per share, exercisable between 28 March 1999 and 27 March 2006. On 4 February 2003, both Messrs Kissane and Diver waived their rights in respect of these options. On 5 February 2003, options over 185,000 new ordinary shares in the Company were granted to each of J J P Kissane and J J Diver. These options have been granted pursuant to the Enterprise Management Incentive Share Option Scheme which was approved by shareholders on 22 January 2003. The options are exercisable at a price of 54 pence per share normally no earlier than three and not later than ten years from the date of the grant, subject to the achievement of a predetermined profit related performance target.

R King, K P Shah, J J P Kissane and J J Diver are the only directors to whom retirement benefits are accruing under a money purchase pension scheme.

At 31 August 2003 the mid-market price of an issued ordinary share in the Company was 119.5 pence (2002: 25 pence) (2001: 17.75pence) and during the year the price ranged from 24 pence to 123.5 pence (2002: 13 pence to 31 pence) (2001: 59.97 pence to 17.75 pence).

#### 5 INTEREST

	12 months to 31 August 2001 ? 00	12 months to 31 August 2002 ? 00	12 months to 31 August 2003 ? 00
Total interest receivable	70	17	12
Total interest payable:			
On bank overdraft and similar charges	(333)	(138)	(222)
Convertible loan note interest	-	(230)	(230)
Finance leases and hire purchase contracts	(8)	(4)	(1)
Factor advances	(595)	(207)	(122)
	(866)	(562)	(563)

## 6 TAXATION

	12 months to 31 August 2001 ? 00	12 months to 31 August 2002 ? 00	12 months to 31 August 2003 ? 00
<b>UK Corporation Tax</b>			
Tax on profit for the period	-	-	-
Adjustments in respect of previous periods	789	-	-
	<u>789</u>	<u>-</u>	<u>-</u>
<b>Foreign Tax</b>			
Tax on profit for the period	89	224	552
Adjustments in respect of previous periods	-	-	-
	<u>89</u>	<u>224</u>	<u>552</u>
Total current tax	<u>878</u>	<u>224</u>	<u>552</u>
<b>Deferred Tax</b>			
Tax losses	-	-	(473)
Origination and reversal of timing differences	-	38	208
Total deferred tax	<u>-</u>	<u>38</u>	<u>(265)</u>
Tax on profit on ordinary activities	<u>878</u>	<u>262</u>	<u>287</u>
<b>Factors affecting tax charge for the period</b>			
(Loss)/Profit on ordinary activities before taxation	(4,875)	1,515	5,823
(Loss)/Profit on ordinary activities multiplied by standard rate of corporation tax in the UK of 30% (2002: 30%) (2001: 30%)	(1,463)	455	1,747
Effects of:			
Expenses not deductible for tax purposes	(6)	160	164
Capital allowances in excess of depreciation	(123)	(194)	(212)
Other temporary differences between taxable and accounting profit	(233)	38	(481)
Lower tax rate on overseas earnings	(259)	(235)	(413)
Utilisation of tax losses	-	-	(445)
Tax losses not utilised	2,173	-	192
Adjustments in respect of prior periods	789	-	-
Current tax charge for the year	<u>878</u>	<u>224</u>	<u>552</u>

The deferred tax credit for the year ended 31 August 2003 includes a value for tax losses previously unrecognised. These losses were previously unrecognised as the Directors did not consider that there was sufficient evidence to support the recognition of a deferred tax asset. Having considered the results of the subsidiary companies for the year ended 31 August 2003, and prepared forecasts for the period ahead, the Directors are of the opinion that some of the tax losses within the Group will be recovered against future taxable profits within a time horizon which they consider to be reasonable.

## 7 DIVIDEND

On equity shares:

Interim dividend paid ? 1p (2002: 0p) (2001: 0p) per share

Final dividend proposed ? 2p (2002: 0p) (2001:0p) per share

12 months to 31 August 2001 ? 00	12 months to 31 August 2002 ? 00	12 months to 31 August 2003 ? 00
-	-	410
-	-	900
-	-	1,310

## 8 EARNINGS PER SHARE

Basic earnings per share

Impact of share option schemes

Impact of convertible loan note

Fully diluted earnings per share

12 months to 31 August 2003		
Profit after taxation	Weighted average number of ordinary shares	Pence per share
5,536,000	41,002,909	13.50
-	1,224,118	(0.39)
161,000	11,500,000	(2.51)
5,697,000	53,727,027	10.60

Basic earnings per share

Impact of share option schemes

Impact of convertible loan note

Fully diluted earnings per share

12 months to 31 August 2002		
Profit after taxation	Weighted average number of ordinary shares	Pence per share
1,253,000	41,002,909	3.06
-	1,224,118	(0.09)
161,000	11,500,000	(0.34)
1,414,000	53,727,027	2.63

Basic earnings per share

Impact of share option schemes

Impact of convertible loan note

Fully diluted earnings per share

12 months to 31 August 2001		
Profit after taxation	Weighted average number of ordinary shares	Pence per share
(5,753,000)	41,002,909	(14.03)
-	-	-
-	-	-
(5,753,000)	41,002,909	(14.03)

## 9 INTANGIBLE ASSETS ? GOODWILL

<b>Cost</b>	<b>? 00</b>
1 September 2000	1,808
Adjustment - 2001 (see note 24)	(900)
	<hr/>
1 September 2001 and 1 September 2002	908
Decrease in deferred consideration from previous year - 2003	(6)
	<hr/>
<b>31 August 2003</b>	<b>902</b>
	<hr/>
<b>Amortisation</b>	
1 September 2000	60
Charge for Year - 2001	30
	<hr/>
1 September 2001	90
Charge for Year - 2002	45
	<hr/>
1 September 2002	135
Charge for Year - 2003	30
	<hr/>
<b>31 August 2003</b>	<b>165</b>
	<hr/>
<b>Net book value</b>	
<b>31 August 2003</b>	<b>737</b>
	<hr/>
31 August 2002	773
	<hr/>
31 August 2001	818
	<hr/>

During the year ended 31 August 2000 the Group acquired the business and assets of The Really Useful Games Company Limited. Character Games Limited, a wholly owned subsidiary of the Company, was formed to carry on the business acquired from The Really Useful Games Company Limited.

The final cost of the acquisition was based on sales and post-tax profits of Character Games Limited for the three years ended 31 December 2002. The consideration could be satisfied in whole or in part at the Company option by the issue of new shares in The Character Group plc at market value.

The value of the consideration for the acquisition was finalised during the year ended 31 August 2003 and the consideration was settled in cash by Character Games Limited, rather than by the issue of shares in the Company. The acquisition of the business and assets of The Really Useful Games Company Limited was originally accounted for in the Company but has now been accounted for in the accounts of Character Games Limited following payment of the consideration.

## 10 TANGIBLE FIXED ASSETS

	Freehold land and buildings	Short leasehold improvements	Tooling	Fixtures fittings and equipment	Motor vehicles	Total
Cost	£ 00	£ 00	£ 00	£ 00	£ 00	£ 00
1 September 2000	1,182	93	1,029	1,671	1,088	5,063
Additions	-	-	124	166	65	355
Disposals	-	(67)	(799)	(221)	(208)	(1,295)
Differences on exchange	-	(3)	1	2	(1)	(1)
1 September 2001	1,182	23	355	1,618	944	4,122
Additions	-	57	342	188	183	770
Disposals	-	-	(190)	(186)	(621)	(997)
Differences on exchange	-	5	(11)	(8)	-	(14)
1 September 2002	1,182	85	496	1,612	506	3,881
Additions	-	13	706	224	95	1,038
Disposals	-	-	-	(15)	(206)	(221)
Differences on exchange	-	(1)	(12)	(8)	-	(21)
<b>31 August 2003</b>	<b>1,182</b>	<b>97</b>	<b>1,190</b>	<b>1,813</b>	<b>395</b>	<b>4,677</b>
<b>Depreciation</b>						
1 September 2000	122	53	894	1,077	426	2,572
Charge for the year	39	18	102	322	255	736
Disposals	-	(57)	(792)	(205)	(144)	(1,198)
1 September 2001	161	14	204	1,194	537	2,110
Charge for the year	39	16	201	290	114	660
Disposals	-	-	(178)	(181)	(379)	(738)
Exchange rate movement	-	5	-	-	-	5
1 September 2002	200	35	227	1,303	272	2,037
Charge for the year	48	25	633	178	95	979
Disposals	-	-	-	(14)	(186)	(200)
Exchange rate movement	-	(1)	(7)	(7)	-	(15)
<b>31 August 2003</b>	<b>248</b>	<b>59</b>	<b>853</b>	<b>1,460</b>	<b>181</b>	<b>2,801</b>
<b>Net book value</b>						
<b>31 August 2003</b>	<b>934</b>	<b>38</b>	<b>337</b>	<b>353</b>	<b>214</b>	<b>1,876</b>
31 August 2002	982	50	269	309	234	1,844
31 August 2001	1,021	9	151	424	407	2,012

The net book value of fixed assets includes £ ,000 (2002: £ ,000) (2001: £ 9,984) in respect of assets held under finance leases and hire purchase contracts, the depreciation of which is shown in note 3.

## 11 FIXED ASSET INVESTMENTS

	Shares listed		Total ? 00
	Own shares ? 00	in the UK ? 00	
<b>Cost</b>			
1 September 2001, 1 September 2002 and 31 August 2003	908	2	910
<b>Amortisation and provisions</b>			
1 September 2000	(757)	-	(757)
Movement in provision	(100)		(100)
1 September 2001	(857)	-	(857)
Movement in provision	21	-	21
1 September 2002	(836)	-	(836)
Movement in provision	267	-	267
<b>31 August 2003</b>	<b>(569)</b>	<b>-</b>	<b>(569)</b>
<b>Net book value</b>			
<b>31 August 2003</b>	<b>339</b>	<b>2</b>	<b>341</b>
31 August 2002	72	2	74
31 August 2001	51	2	53

The market value of the listed investments as at 31 August 2003 is ? ,206 (2002: ? ,897) (2001: ? ,717).

Issued shares in the Company are held by the trustee of the Company's Employee Share Ownership Trust ("the Trust") for the benefit of the Group's employees, former employees and their respective families. At 31 August 2003 the Trust held 285,000 shares (2002: 285,000) (2001: 285,000) which had a market value of ? 39,000 (2002: ? 2,000) (2001: ? 1,000). In accordance with UITF 13 these shares have been stated at the lower of cost and market value. The nominal value of the shares held by the Trust is ? 4,250.

During the three period to and as at 31 August 2003 the Company held more than 10% of the equity of the following principal undertakings:

Subsidiaries	Country of incorporation and operation	Class of share capital held	Proportion held by the parent undertaking	Nature of business
Character Options Limited	United Kingdom	Ordinary	100%	Design and distribution of toys and games
Toy Options (Far East) Limited	Hong Kong	Ordinary	100%	Design and distribution of toys and games
Character Games Limited	United Kingdom	Ordinary	100%	Design and distribution of games and puzzles
Character Games (Far East) Limited	Hong Kong	Ordinary	100%	Design and distribution of games and puzzles
Downpace Limited	United Kingdom	Ordinary	100%	Gift importer and distributor
World Wide Licenses Limited	Hong Kong	Ordinary	100%	Design and distribution of digital cameras
WWL (Europe) Limited (incorporated September 2002)	United Kingdom	Ordinary	100%	Distribution of digital cameras
WWL (UK) Limited	United Kingdom	Ordinary	100%	Non-trading
Universal Concepts (UK) Limited	United Kingdom	Ordinary	100%	Non-trading
Toy Options Group plc	United Kingdom	Ordinary	100%	Non-trading
Prelude Worldwide Limited	United Kingdom	Ordinary	100%	Non-trading
Q-Stat Limited	United Kingdom	Ordinary	100%	Non-trading
Toy Options Limited	United Kingdom	Ordinary	100%	Non-trading
Character.com Limited	United Kingdom	Ordinary	100%	Non-trading
Cool-Cam Limited	United Kingdom	Ordinary	100%	Non-trading
Character Promotions Limited *	United Kingdom	Ordinary	100%	Non-trading
Prelude (Far East) Limited	Hong Kong	Ordinary	100%	Non-trading
On Stretch Limited	Hong Kong	Ordinary	100%	Non-trading

\*Up until 29 August 2002 the Company held 50% of the issued shares. From this date the holding became 100%  
All of the subsidiary undertakings have been included in these consolidated accounts.

**12 STOCKS**

	2001 ? 00	2002 ? 00	2003 ? 00
Raw materials and components	1,245	557	1,237
Finished goods for resale	6,540	4,425	6,906
	7,785	4,982	8,143

**13 DEBTORS**

	2001 ? 00	2002 ? 00	2003 ? 00
Trade debtors (non-factored)	3,891	6,479	13,695
Other debtors	857	1,366	876
Prepayments and accrued income	1,146	1,788	1,456
Deferred tax	522	484	749
	6,416	10,117	16,776

**Deferred Tax**

The elements of deferred tax are as follows:	2001 ? 00	2002 ? 00	2003 ? 00
Difference between accumulated depreciation and tax depreciation	139	104	197
Other timing differences	32	29	(272)
Tax losses	351	351	824
	522	484	749

The movements in deferred tax are as follows:

	2001 ? 00	2002 ? 00	2003 ? 00
At 1 September	522	522	484
Profit and loss account	-	(38)	265
<b>At 31 August</b>	<b>522</b>	<b>484</b>	<b>749</b>

The deferred tax asset of ? 49,000 (2002: ? 84,000) (2001: ? 22,000) is recoverable against future forecast taxable profits within a time horizon that the Directors consider more likely than not to occur.

Deferred tax assets have not been recognised in respect of tax losses of ? ,271,000 (2002: ? 2,793,000) (2001: ? 2,793,000). At a tax rate of 30%, these losses represent a potential tax asset of ? ,581,000 (2002: ? ,838,000) (2001: ? ,838,000). These losses would be recoverable in the event of taxable profits arising in certain subsidiary companies.

**14 CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR**

	2001 ? 00	2002 ? 00	2003 ? 00
Trade creditors	9,218	7,390	17,313
Short-term bank loan	94	-	-
Corporation tax	69	175	712
Other taxation and social security	366	713	803
Accruals and deferred income	4,170	7,093	4,671
Finance leases and hire purchase contracts	36	3	5
Convertible loan note	-	-	4,600
	13,953	15,374	28,104

A bank has a debenture over the assets and undertakings of the Company and certain subsidiary companies. Further, a major trade creditor who offers trade finance is secured by a debenture over the assets and undertakings of a subsidiary company. As at 31 August 2003 the amount outstanding to the secured trade creditor amounted to ? ,487,000 (2002: ? ,225,000) (2001: ? ,523,000)

#### 14 CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR - continued

The short term bank loan in 2001 was secured by a fixed and floating charge over the assets of a subsidiary, and was further guaranteed by the Company.

##### Convertible loan note

On 16 July 2001 the Company issued a convertible loan note.

The earliest redemption date is 16 July 2004. The outstanding, unconverted amount of the loan note is repayable at its nominal value at the option of the Company or the noteholder at any time on or after this date, subject to a notice period of 30 days.

The note is convertible, in whole or in part, into up to 11,500,000 ordinary shares of 5p each at a rate of 40p (nominal) per share at any time prior to 16 July 2004, at the option of the noteholder.

The note will become repayable forthwith in the event of a default, which means any of the following:

- (i) the Company is 14 days late with any payment
- (ii) the Company fails to comply with any term of the loan note agreement, after 30 days notice thereof is given to the Company
- (iii) the Company is wound up or a receiver or administrator is appointed.

Details of the conversion of this loan note are set out in note 29.

#### 15 CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR

	2001 ? 00	2002 ? 00	2003 ? 00
Convertible loan note (see note 14)	4,600	4,600	-
<b>Other creditors</b>			
Finance leases and hire purchase contracts repayable in less than five years	5	1	4
	<u>4,605</u>	<u>4,601</u>	<u>4</u>

#### 16 PROVISION FOR LIABILITIES AND CHARGES

##### Investment in joint venture

The movement in the share of gross assets less the share of gross liabilities in the investment in the joint venture was as follows:

	2001 ? 00	2002 ? 00	2003 ? 00
1 September	191	13	-
Movement in Provision	(178)	(13)	-
31 August	<u>13</u>	<u>-</u>	<u>-</u>

#### 17 RECONCILIATION OF EQUITY SHAREHOLDERS?FUNDS

	12 months to 31 August 2001 ? 00	12 months to 31 August 2002 ? 00	12 months to 31 August 2003 ? 00
(Loss)/profit for the financial year	(5,753)	1,253	4,226
Exchange differences taken to reserves	204	(464)	(185)
Issue of shares	3,278	-	-
Movement in shares to be issued	(900)	-	(908)
Net (subtraction from)/addition to shareholders?funds	<u>(3,171)</u>	<u>789</u>	<u>3,133</u>
Opening shareholders?funds	4,847	1,676	2,465
Closing shareholders?funds	<u>1,676</u>	<u>2,465</u>	<u>5,598</u>

## 18 CALLED UP SHARE CAPITAL (EQUITY)

	2001 ? 00	2002 ? 00	2003 ? 00
<b>Authorised</b>			
110,000,000 (2002: 110,000,000) (2001: 110,000,000) ordinary shares of 5 pence each	5,500	5,500	5,500
<b>Allotted called up and fully paid</b>			
41,287,909 (2002: 41,287,909) (2001: 41,287,909) ordinary shares of 5 pence each	2,064	2,064	2,064

Between 8 and 14 August 2001, 18,168,246 new ordinary shares with an aggregate nominal value of ? 08,412.30 were allotted for cash at a price of 20 pence per share pursuant to a partially underwritten rights issue, full details of which were set out in the prospectus dated 22 June 2001.

### Share options

The Company adopted the rules of an Inland Revenue approved executive share option scheme on 3 May 1995.

As at 31 August 2003, options to acquire up to a total of 522,000 (2002: 798,500) (2001: 247,000) new ordinary shares in the Company remained outstanding under this scheme details of which were as follows:

No. of shares	Date granted	Exercise period	Exercise price
24,000	5 March 1997	5 March 2000 to 4 March 2007	101.0p
18,000	5 December 1997	5 December 2000 to 4 December 2007	136.5p
480,000	15 February 2002	15 February 2005 to 14 February 2012	24.25p

The Company adopted the rules of its unapproved executive share option scheme on 2 June 1997. On 5 February 2003 options over a total of 352,500 new ordinary shares in the Company were granted to Group employees at an exercise price of 54.0p per share. As at 31 August 2003, options to acquire up to a total of 688,000 (2002: 382,500) (2001: 175,500) new ordinary shares in the Company remained outstanding under this scheme, details of which were as follows:

No. of shares	Date granted	Exercise period	Exercise price
128,500	5 December 1997	5 December 2000 to 4 December 2004	136.5p
207,000	15 February 2002	15 February 2005 to 14 February 2009	24.25p
352,500	6 February 2003	6 February 2006 to 5 February 2010	54.0p

The Company adopted the rules of an Inland Revenue qualifying Enterprise Management Incentive share option scheme with the sanction of shareholders following an extraordinary general meeting of the Company on 22 January 2003. On 5 February 2003, options over a total of 1,131,250 new ordinary shares in the Company were granted to Group employees at an exercise price of 54p per share. As at 31 August 2003, options to acquire a total of 1,131,250 new ordinary shares in the Company remained outstanding under this scheme. These options are exercisable during the period from 5 February 2006 until 4 February 2013.

No amount is payable by any grantee of an option at the time of grant under any of the Company executive share option schemes.

## 19 SHARE CAPITAL AND RESERVES

	Called up share capital ? 00	Shares to be issued ? 00	Capital redemption reserve ? 00	Share premium account ? 00	Merger reserve ? 00	Profit and loss account ? 00	Total ? 00
1 September 2000	1,156	1,808	15	5,473	651	(4,256)	4,847
Shares issued	908	-	-	2,370	-	-	3,278
Movement in shares to be issued	-	(900)	-	-	-	-	(900)
Exchange differences	-	-	-	-	-	204	204
Loss retained	-	-	-	-	-	(5,753)	(5,753)
1 September 2001	2,064	908	15	7,843	651	(9,805)	1,676
Exchange differences	-	-	-	-	-	(464)	(464)
Profit retained	-	-	-	-	-	1,253	1,253
1 September 2002	2,064	908	15	7,843	651	(9,016)	2,465
Exchange differences	-	-	-	-	-	(185)	(185)
Profit retained	-	-	-	-	-	4,226	4,226
Movement	-	(908)	-	-	-	-	(908)
<b>31 August 2003</b>	<b>2,064</b>	<b>-</b>	<b>15</b>	<b>7,843</b>	<b>651</b>	<b>(4,975)</b>	<b>5,598</b>

In accordance with FRS 10, goodwill previously written off against reserves has not been reinstated and the goodwill has been offset against the profit and loss account reserve. The cumulative amount of positive goodwill written off against reserves is ? ,645,000 (31 August 2002: ? ,645,000) (31 August 2001: ? ,645,000). The goodwill has been eliminated as a matter of accounting policy and would be charged to the profit and loss account on the subsequent disposal of the business to which it related.

## 20 GUARANTEES AND OTHER FINANCIAL COMMITMENTS

a. At each year end the Company was committed under non-cancellable operating leases to making the following payments during the next year

	2001 Land and buildings ? 00	2002 Land and buildings ? 00	2003 Land and buildings ? 00
Expiring within one year	202	217	241
Expiring between one and five years	125	271	225
Expiring after five years or more	121	245	-
	448	733	466

b. The Group has entered into contracts for minimum royalties in the amounts set out below which are contracted to be paid to licensors irrespective of sales and are not provided for in the accounts as the directors believe that the required level of future sales will be achieved:

	2001 ? 00	2002 ? 00	2003 ? 00
Within one year	330	928	1,843
Between one and two years*	296	1,008	1,632
Between two and five years	-	968	-
	626	2,904	3,475

\* A subsidiary has an option to terminate one of these contracts in which event a substantial part of these amounts would not be payable.

## 20 GUARANTEES AND OTHER FINANCIAL COMMITMENTS - continued

c. The future minimum hire purchase and finance lease payments to which the Group was committed at 31 August are:

	2001 ? 00	2002 ? 00	2003 ? 00
Net amounts payable within one year	36	3	5
Net amount payable between two and five years	5	1	4
	41	4	9

## 21 RECONCILIATION OF OPERATING (LOSS)/PROFIT TO NET CASH (OUTFLOW)/INFLOW FROM OPERATING ACTIVITIES

	12 months to 31 August 2001 ? 00	12 months to 31 August 2002 ? 00	12 months to 31 August 2003 ? 00
Operating (loss)/profit	(4,009)	2,077	6,386
Depreciation, impairment and amortisation	766	705	1,009
Movement in respect of own shares	100	(21)	(267)
Loss/(profit) on disposal of fixed assets	52	78	(3)
Decrease/(increase) in stocks	3,745	2,803	(3,161)
Increase in debtors	(1,398)	(3,632)	(6,659)
(Decrease)/increase in creditors	(5,948)	1,518	6,697
Exchange movement	204	(464)	(185)
Net cash (outflow)/inflow from operating activities	(6,488)	3,064	3,817

## 22 RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET DEBT

	12 months to 31 August 2001 ? 00	12 months to 31 August 2002 ? 00	12 months to 31 August 2003 ? 00
Increase in cash in the period	380	1,646	648
Cash inflow/(outflow) from movement in debt and lease financing	308	131	(5)
Movement in net debt resulting from cash flows	688	1,777	643
Net debt at 1 September	815	1,503	3,280
Net debt at 31 August	1,503	3,280	3,923

## 23 ANALYSIS OF NET DEBT

	Cash at bank and in hand ? 00	Short-term bank loan ? 00	Lease finance ? 00	Total ? 00
31 August 2000	1,258	(353)	(90)	815
Cash flow	380	259	49	688
31 August 2001	1,638	(94)	(41)	1,503
Cash flow	1,646	94	37	1,777
31 August 2002	3,284	-	(4)	3,280
Cash flow	648	-	(5)	643
31 August 2003	3,932	-	(9)	3,923

## 24 SHARES TO BE ISSUED

	? 00
1 September 2000	1,808
Adjustment in relation to an acquisition in 2000	(900)
	<hr/>
1 September 2001 and 1 September 2002	908
Movement	(908)
	<hr/>
31 August 2003	-
	<hr/>

The final part of the consideration in respect of the acquisition of the business and assets of The Really Useful Games Company Limited was agreed on 10 July 2003 to be paid in cash. Further details of this transaction are set out in note 9.

## 25 FINANCIAL INSTRUMENTS

The Group's use of financial instruments is explained below.

### Liquidity Risk

The Group finances itself through a combination of equity and short term debt. The Group satisfied its liquidity requirements during the period under review. The Group's main working capital facility is provided by factoring. There was also continued use of short term bank facilities during the period under review. Details of the borrowing facilities are set out in note 25d.

### Foreign currency risk

The Group faces foreign currency exposures on translation of the net assets and results of its overseas subsidiaries and on trading transactions undertaken mainly in US dollars. The Group seeks to mitigate the effect of its currency exposures by buying currency forward when appropriate. The Group does not hedge its resulting translation exposures as these are accounting rather than cash exposures.

As permitted by FRS13 short term debtors and creditors have been excluded from all financial instrument disclosures.

### a. Exchange risk

The tables below show the Group's currency exposures; in other words those transactional exposures that give rise to the net currency gains and losses recognised in the profit and loss account. Such exposures comprise the monetary assets and monetary liabilities of the Group that are not denominated in the operating currency of the operating company involved.

These currency exposures were as follows:

#### Net foreign currency monetary assets

	At 31 August 2003		
	Functional currency of group operation		
	Sterling ? 00	HK\$ ? 00	Total ? 00
Sterling	-	7	7
US\$	(117)	988	871
Euro	15	-	15
	<hr/>		
Total	(102)	995	893
	<hr/>		
	At 31 August 2002		
	Functional currency of group operation		
	Sterling ? 00	HK\$ ? 00	Total ? 00
Sterling	-	1	1
US\$	(76)	877	801
Euro	97	1	98
	<hr/>		
Total	21	879	900
	<hr/>		

## 25 FINANCIAL INSTRUMENTS - continued

### Net foreign currency monetary assets

	At 31 August 2001		
	Functional currency of group operation		
	Sterling ? 00	HK\$ ? 00	Total ? 00
Sterling	-	-	-
US\$	395	683	1,078
Euro	-	-	-
Total	395	683	1,078

### b. Fair values

The fair value of all financial instruments at 31 August 2003, 31 August 2002 and 31 August 2001 was not materially different from their book value.

### c. Maturity of financial liabilities

The maturity profile of the Group financial liabilities at 31 August were as follows:

	At 31 August		
	2001 ? 00	2002 ? 00	2003 ? 00
In one year or less, or on demand	130	3	4,600
In more than one year, but not more than two years	5	4,601	4
In more than two years, but not more than five years	4,600	-	-
In more than five years	-	-	-
Total	4,735	4,604	4,604

### d. Borrowing facilities

The Group has various available borrowing facilities. The undrawn committed facilities available in respect of which all conditions had been met at 31 August, were as follows:

	At 31 August		
	2001 ? 00	2002 ? 00	2003 ? 00
Expiring within one year	1,406	2,156	1,860
Expiring between one year, but not more than two years	-	-	-
Expiring in more than two years	-	-	-
Total	1,406	2,156	1,860
Committed borrowing facilities	1,500	2,250	2,750

25 FINANCIAL INSTRUMENTS - continued

e. Interest rate risk profile of financial assets and financial liabilities

Financial assets

Financial assets comprise cash at bank.

		At 31 August 2003			
		Floating rate financial assets ? 00	Fixed rate financial assets ? 00	Financial assets on which no interest received ? 00	Total ? 00
Currency					
Sterling		2,043	-	-	2,043
US\$		871	-	-	871
Euro		15	-	-	15
HK\$		1,003	-	-	1,003
Total		3,932	-	-	3,932
		At 31 August 2002			
		Floating rate financial assets ? 00	Fixed rate financial assets ? 00	Financial assets on which no interest received ? 00	Total ? 00
Currency					
Sterling		2,337	-	-	2,337
US\$		801	-	-	801
Euro		98	-	-	98
HK\$		48	-	-	48
Total		3,284	-	-	3,284
		At 31 August 2001			
		Floating rate financial assets ? 00	Fixed rate financial assets ? 00	Financial assets on which no interest received ? 00	Total ? 00
Currency					
Sterling		554	-	-	554
US\$		1,072	-	-	1,072
HK\$		12	-	-	12
Total		1,638	-	-	1,638

## 25 FINANCIAL INSTRUMENTS - continued

### e. Interest rate risk profile of financial assets and financial liabilities

#### Financial liabilities

	At 31 August 2003			
	Floating rate financial liabilities ? 00	Fixed rate financial liabilities ? 00	Financial liabilities on which no interest received ? 00	Total ? 00
Currency				
Sterling	-	4,600	-	4,600
US\$	-	-	-	-
HK\$	-	4	-	4
<b>Total</b>	<b>-</b>	<b>4,604</b>	<b>-</b>	<b>4,604</b>

  

	At 31 August 2002			
	Floating rate financial liabilities ? 00	Fixed rate financial liabilities ? 00	Financial liabilities on which no interest received ? 00	Total ? 00
Currency				
Sterling	4	4,600	-	4,604
US\$	-	-	-	-
HK\$	-	-	-	-
<b>Total</b>	<b>4</b>	<b>4,600</b>	<b>-</b>	<b>4,604</b>

  

	At 31 August 2001			
	Floating rate financial liabilities ? 00	Fixed rate financial liabilities ? 00	Financial liabilities on which no interest received ? 00	Total ? 00
Currency				
Sterling	135	4,600	-	4,735
US\$	-	-	-	-
HK\$	-	-	-	-
<b>Total</b>	<b>135</b>	<b>4,600</b>	<b>-</b>	<b>4,735</b>

The floating rate financial liabilities comprise:

sterling denominated bank borrowings and overdrafts that bear interest at rates based on LIBOR or NatWest bank base rates. Obligations under finance leases and hire purchase contracts.

The fixed rate financial liability comprises the convertible loan note. Interest is payable at the rate of 5% per annum.

Further details regarding the convertible loan note are set out in note 14.

#### 26 THE CHARACTER GROUP PLC EMPLOYEE SHARE OWNERSHIP TRUST

The Company Employee Share Ownership Trust (the Trust) is governed by a Trust Deed dated 19 June 1998. The Trustees may grant options over such shares in the Company acquired by them or otherwise provide benefits to the beneficiaries, as defined in the Trust Deed. The Trust is required to meet its own costs, and has waived its right to dividend income. At 31 August 2003, 31 August 2002 and 31 August 2001 no options had been granted by the Trust. Details of the shares held by the Trust are set out in note 11.

#### 27 CONTINGENT LIABILITIES

The Company has guaranteed the obligations of certain subsidiary companies to their factor companies, trade finance companies, certain banks and others in the normal course of business. The factor company has a fixed and floating charge over the assets of the Company and some subsidiaries. The Company is a member of a Group registration for Value Added Tax purposes.

## 28 RELATED PARTY TRANSACTIONS

During the three years ended 31 August 2003 the Company entered into transactions with Giochi Preziosi S.p.A., a company of which E Preziosi and M Cellai are directors. Further, Toys Investment S.A., a company in which E Preziosi is interested and of which M Cellai is a director held approximately 28.8% of the issued share capital of The Character Group plc until such shares were transferred to Giochi Preziosi S.p.A. on 19 July 2002. At 31 August 2003, G Preziosi S.p.A. continued to hold such shares in the Company.

Trade was carried out on an arms length basis and is summarised below:

	2001 ? 00	2002 ? 00	2003 ? 00
Total net sales to Giochi Preziosi S.p.A.	1,987	479	1,374
Total net purchases from Giochi Preziosi S.p.A.	189	2,148	2,862
Balance due from/(due to) Giochi Preziosi S.p.A.	338	(90)	175

During the year ended 31 August 2002, Lord Birdwood received a fee of ? 0,000 in relation to the provision of search, selection and related recruitment services. Such fee was in addition to his fee as a non-executive director of the Company.

There were no other material related party transactions.

## 29 POST BALANCE SHEET EVENT

On 11 November 2003, Valtidone S.p.A., the holder of the ? ,600,000 (nominal) convertible loan note in The Character Group plc, converted ? ,600,000 (nominal) of the loan note into new ordinary shares, at a conversion price of 40 pence per ordinary share. This resulted in the allotment of 4,000,000 ordinary shares with a nominal value of ? 00,000, representing approximately 8.8% of the Company issued share capital as enlarged by the issue of the new ordinary shares. The new ordinary shares were allotted on 11 November 2003 and admitted to the Official List on 17 November 2003. The Company received a notification from Valtidone S.p.A. on 24 November 2003 of its sale of the 4,000,000 new ordinary shares.

On 3 December 2003 the Company issued and allotted a further 7,500,000 new ordinary shares of 5p each to Valtidone S.p.A. following the due exercise by Valtidone S.p.A. of the remainder of its rights of conversion in respect of the outstanding ? ,000,000 (nominal) of the loan note at the conversion price.

Following the loan note conversion, Valtidone S.p.A. has an interest in 7,500,000 new ordinary shares which represents approximately 14.2per cent of the issued ordinary share capital of the Company as enlarged by the issue of the new ordinary shares.

## 30 NATURE OF FINANCIAL INFORMATION

The financial information presented above in respect of the three years ended 31 August 2003 does not constitute statutory accounts for each of the years. Statutory accounts for the three years ended 31 August 2003 have been delivered to the Registrar of Companies. In respect of the statutory accounts for the two years ended 31 August 2003, Baker Tilly (formerly HLB Kidsons) have made an unqualified report under Section 235 of the Companies Act 1985 and such report did not contain any statement under section 237(2) or (3) of that Act. In respect of the statutory accounts for the year ended 31 August 2001, HLB Kidsons have made an unqualified report under Section 235 of the Companies Act 1985 and such report did not contain any statement under section 237(2) or (3) of that Act.

## 31 CONSENT

We consent to the inclusion of this report in the listing particulars dated 17 February 2004 and accept responsibility for this report for the purposes of Chapter 6 of the Rules of the UK Listing Authority.

Yours faithfully

**Baker Tilly**  
Registered Auditor  
Chartered Accountants

## Part III

### Principal terms and conditions of the Convertible Loan Note

At an Extraordinary General Meeting of the Company held on 16 July 2001:-

- (a) an ordinary resolution was passed pursuant to the terms of which the constitution and issue of the Convertible Loan Note was approved by shareholders; and
- (b) a special resolution was passed authorising the dis-application of Section 89(1) of the Act (relating to shareholders' pre-emption rights) to allow the allotment of up to 11,500,000 new Ordinary Shares following a due exercise of the conversion rights attaching to the Convertible Loan Note (further details of which are given below).

The Convertible Loan Note was issued by the Company on 16 July 2001 to TISA. The principal monies subscribed for the Convertible Loan Note amounted in total to £4,600,000 and were paid by TISA to, and received by, the Company on 16 July 2001. On 3 October 2001, the Convertible Loan Note was transferred by TISA to Valtidone.

The following constitutes a summary of the principal provisions of the Convertible Loan Note:

1. interest is payable upon the balance outstanding and remaining unconverted from time to time of the principal monies at a rate of 5 per cent. per annum. Such interest is payable quarterly in arrears on 30 September, 31 December, 31 March and 30 June in every year (or if not a business day on the next business day following), with the first such payment having been made on 1 October 2001;
2. conversion rights are granted to the holder of the Convertible Loan Note (the "**Noteholder**") under the Convertible Loan Note entitling the Noteholder to convert the principal monies into fully paid Ordinary Shares on the basis of a subscription price of 40 pence per Ordinary Share. On full conversion of the principal monies in this manner, a maximum of 11,500,000 Ordinary Shares will be issued by the Company. The conversion rights are exercisable at any time during the period from the date of issue of the Convertible Loan Note until the third anniversary of the date of issue of the Loan Note. Such rights are exercisable in whole or in part or by instalment throughout such period provided that the minimum amount of the principal monies that may be converted (other than where the same shall represent the outstanding balance of the principle monies) is £400,000 (i.e. 1,000,000 Ordinary Shares);
3. the conversion rights described in paragraph 2 above are not exercisable by TISA and are not exercisable by any person, firm or corporation that shall be acting in concert with TISA within the meaning of the City Code on Takeovers and Mergers (the "**City Code**"). The determination of whether or not any person shall be acting in concert with TISA shall be made by the Company's brokers at the relevant time, in consultation with the Panel on Takeover and Mergers (the "**Panel**"). The Panel's determination in such regard shall be final and conclusive;
4. a restriction on the exercise of the conversion rights attaching to the Convertible Loan Note applies where or to the extent that the exercise of the conversion rights results in the number of shares in public hands falling below the level prescribed by the Listing Rules as being the minimum level that must remain in public hands for the Company to retain its listing. At the present time this percentage is 25 per cent. In such circumstances the Company will notify the Noteholder of the maximum number of Ordinary Shares in respect of which the conversion rights may be exercised at that time and the conversion rights will be restricted accordingly unless or until the position pertaining shall have changed;
5. in the event of any consolidation or sub-division affecting the Ordinary shares whilst the conversion rights remain exercisable, adjustments will be made to the number of Ordinary Shares and/or the applicable subscription price if and to the extent determined to be appropriate by the Company's auditors, whose determination shall (in the absence of manifesto) be final and binding;

6. where the Noteholder shall not be TISA or a person acting in concert with it, in the event of an offer to Shareholders of new Ordinary Shares for subscription or purchase by way of rights or the offer of options or rights or warrants to purchase new Ordinary Shares (including convertible securities) at a price that is less than the prevailing market price, then the Company will offer or procure an offer on equivalent terms to the Noteholder, the Noteholder being treated for such purpose as the registered holder of all Ordinary Shares remaining capable of being issued upon exercise of the conversion rights attaching to the Convertible Loan Note;
7. following the expiry of not less than 30 days' written notice at any time on or after the third anniversary of the date of issue of the Convertible Loan Note, either the Company or the Noteholder may require the repayment of the outstanding principal monies due in respect thereof. Repayment obligations also apply in the event of certain defaults by the Company (e.g. default in paying interest, having a receiver or similar office holder appointed over it, the Company being wound up or failing to procure a remedial breach within 30 days of being required to do so by the Noteholder);
8. the conversion rights are exercisable by the service of a prescribed form of notice of conversion and the relative Ordinary Shares must be issued and allotted within 7 days of receipt of the same by the Company. A certificate for the balance of the Convertible Loan Note entitlement (if any) will be issued to the Noteholder together with a certificate representing the Ordinary Shares arising on conversion. The Company is obliged to use its reasonable endeavours to obtain listing for the Ordinary Shares so allotted within a reasonable time of such allotment if at such time the Company remains listed;
9. the Company is obliged to maintain sufficient authorised share capital to satisfy the allotment requirements arising upon full conversion of the outstanding principle monies under the Convertible Loan Note. In addition the Company is required to give the Noteholder notice of any offer made to Shareholders to acquire all or a proportion of the issued Ordinary Shares and is obliged to use its reasonable endeavours to procure that an equivalent offer is extended to the Noteholder in respect of any Ordinary Shares issued to it in exercise of its conversion rights during the period of the offer;
10. a register of the Noteholder is to be maintained by the Company. No transfer of the Convertible Loan Note will be approved by the directors of the Company if it is not in respect of the whole principal amount thereof or if it is to a person treated as acting in concert (within the meaning of the City Code) with the Noteholder;
11. the provisions of the Convertible Loan Note are governed and construed in accordance with the laws of England and the courts of England have exclusive jurisdiction in connection therewith.

On 11 November 2003, the Company allotted 4,000,000 new Ordinary Shares to Valtidone following the due exercise by Valtidone of the rights of conversion attaching to the Convertible Loan Note in respect of £1,600,000 million (nominal) of the Convertible Loan Note. Such new Ordinary Shares were admitted to the Official List to trading on the London Stock Exchange's market for listed securities on 17 November 2003. On 3 December 2003, the Company allotted the New Ordinary Shares to Valtidone following the due exercise in by Valtidone of the rights of conversion attaching to the Convertible Loan Note in respect of £3,000,000 million (nominal) of the Convertible Loan Note. Such latter exercise was in respect of the balance outstanding at such date of the Convertible Loan Note. At the date of this document, the Convertible Loan Note has been fully converted and no amount thereof remains outstanding or is capable of reissue.

## Part IV

### Additional information

#### 1. Incorporation and registered office

- 1.1 The Company was incorporated in England and Wales on 15 March 1995 with registered number 3033333 under the Act as a private company limited by shares with the name Bluechart Limited. The Company was re-registered as a public limited company on 4 May 1995 under the name Toy Options Group plc. On 17 September 1997 the Company changed its name to The Character Group plc.
- 1.2 The Group's head office is at 86-88 Coombe Road New Malden Surrey KT3 4QS and the registered office of the Company is situated at 5<sup>th</sup> Floor, 4 Chiswell Street, London EC1Y 4UP.
- 1.3 The principal legislation under which the Company operates is the Act and the regulations made thereunder.

#### 2. Share Capital

- 2.1 As at the date of this document, options over a total of 2,150,050 unissued Ordinary Shares had been granted for nil consideration to qualifying employees of the Group and remained unexercised under the Share Schemes as follows:

Scheme	Date of grant	No. of unissued Ordinary Shares under option	Exercise price	Exercise period
Approved Scheme	05.03.97	20,000	101p	05.03.00 to 04.03.07
	05.12.97	13,500	136.5p	05.12.00 to 04.12.07
	15.02.02	402,000	24.25p	15.02.05 to 14.02.12
Unapproved Scheme	05.12.97	128,500	136.5p	05.12.00 to 04.12.04
	15.02.02	166,300	24.25p	15.02.05 to 14.02.09
	06.02.03	341,250	54p	06.02.06 to 05.02.10
EMI Scheme	05.02.03	1,078,500	54p	05.02.06 to 04.02.13

- 2.2 There have been no changes in the amount of the Company's issued share capital in the three years preceding the date of this document other than those set out in this paragraph 2.2:
- 2.2.1 on 8 August 2001, 13,218,246 new Ordinary Shares were issued to certain of the then existing Shareholders by way of a 1 for 1 rights issue at a price of 20p per Ordinary Share;
- 2.2.2 on 8 August 2001, 4,950,000 new Ordinary Shares were issued to TISA in furtherance of its underwriting obligations in respect of the rights issue referred to in paragraph 2.2.1 pursuant to its obligations under the agreement referred to in paragraph 8.3 below at a price of 20p per Ordinary Share;
- 2.2.3 on 11 November 2003, 4,000,000 new Ordinary Shares were issued to Valtidone upon due exercise of its conversion rights in respect of £1,600,000 (nominal) of the Convertible Loan Note; the effective conversion price being 40p per Ordinary Share;
- 2.2.4 on 3 December 2003, 7,500,000 new Ordinary Shares were issued to Valtidone upon due exercise of its conversion rights in respect of £3,000,000 (nominal), being the balance outstanding, of the Convertible Loan Note; the effective conversion price being 40p per Ordinary Share.
- 2.3 The authorised and issued share capital of the Company, as at 16 February 2004 (the latest practicable date prior to the publication of this document) and as it will be immediately following the Admission is set out in the table below:

Authorised		Issued fully paid or credited as fully paid	
£'s	Number	£'s	Number
5,500,000	110,000,000	2,639,395.45	52,787,909

2.4 Pursuant to resolutions passed at the Company's annual general meeting held on 21 January 2004, presently:

2.4.1 the directors of the Company are authorised (for a period expiring at the conclusion of the next annual general meeting of the Company or, if earlier, 21 April 2005) to allot relevant securities (as defined in the Act) up to a maximum nominal amount of £688,132, representing 13,762,640 Ordinary Shares, being approximately 26.1 per cent. of the current issued ordinary share capital of the Company;

2.4.2 the directors of the Company are authorised, for the purposes of the articles of association of the Company (for a period expiring at the conclusion of the annual general meeting of the Company next following the passing of such resolution), to offer Shareholders the entitlement to receive Ordinary Shares, credited as fully paid, in whole or in part instead of cash in respect of dividends declared or paid by the Company during such period;

2.4.3 the Company is generally and unconditionally authorised to make market purchases of Ordinary Shares up to a maximum number of 6,790,000 at a price of not less than the nominal value of an Ordinary Share nor greater than 105 per cent. of the average middle market prices of an issued Ordinary Share as derived from the Daily Official List of the London Stock Exchange on the five business days immediately preceding the date on which the Company shall contract to purchase any such Ordinary Share; and

2.4.4 the directors of the Company are empowered (such power to expire at the same time as the authority referred to in paragraph 2.4.1 above) to:

(a) allot equity securities (as defined in the Act) up to the maximum of the amount of the authority referred to in paragraph 2.4.1 above for cash, other than pro-rata to existing holdings, in connection with any rights issue;

(b) allot Ordinary Shares to Shareholders in lieu of cash dividend entitlements; and

(c) allot equity securities for cash otherwise than as referred to in paragraphs 2.4.4(a) and (b) above up to an aggregate nominal amount of £103,220, representing 2,064,400 Ordinary Shares (being approximately 3.9 per cent. of the current issued ordinary share capital of the Company)

as if Section 89(1) of the Act (relating to Shareholders rights of pre-emption in respect of the allotment of equity securities by the Company) did not apply to any such allotment or offer.

2.5 Save as disclosed in paragraph 2.1 above, no share or loan capital of the Company, or of any other company within the Group, is under option or has been agreed, conditionally or unconditionally, to be put under option.

2.6 The provisions of section 89 of the Act, which confer on Shareholders rights of pre-emption in respect of the allotment of equity securities which are or are to be paid up in cash (other than by way of allotment to employees under an employee share scheme defined in section 743 of the Act), apply to the authorised but unissued share capital of the Company except to the extent disapplied by the resolution of 21 January 2004 referred to in paragraph 2.4.4 above.

2.7 The authorised but unissued share capital of the Company at the date of this document is 2,860,604.55 divided into 57,212,091 Ordinary Shares (representing approximately 52 per cent. of the authorised share capital of the Company).

- 2.8 The issued Ordinary Shares are in registered form and are capable of being held in certificated and uncertificated form.
- 2.9 As at 16 February 2004 (being the latest practicable date prior to the publication of this document), the Company held no Ordinary Shares in treasury.

### 3. Subsidiaries

3.1 The Company is the ultimate holding company of the Group. The Group is engaged in the design, development and international distribution of toys, games and digital cameras.

3.2 The Company has the following subsidiaries, all of which are, directly or indirectly, wholly owned private companies incorporated in England and Wales, each having its registered office at 5<sup>th</sup> Floor, 4 Chiswell Street, London EC1Y 4UP:

Name	Date of Incorporation	Issued share capital (fully paid or credited as fully paid save where otherwise indicated)	Nature of business
Character Options Limited	1 March 1991	100,000 ordinary shares of £1 each	Design and distribution of toys and games
Downpace Limited	23 March 1981	1,000 ordinary shares of £1 each	Gift importer and Distributor
WWL (UK) Limited	3 September 1997	2 ordinary shares of £1 each	Non-trading
Universal Concepts (UK) Limited	15 April 1996	5,000 "A" ordinary shares of £1 each; and 20,000 "B" ordinary shares of £1 each	Non-trading
Character Games Limited	14 December 1999	801 ordinary shares of £1 each	Design and distribution of games and puzzles
Toy Options Group plc	30 July 1997	50,000 ordinary shares of £1 each (paid up as to 25% of the nominal value thereof)	Non-trading
Prelude Worldwide Limited	21 November 1997	2 ordinary shares of £1 each	Non-trading
Q-Stat Limited	11 August 1999	2 ordinary shares of £1 each	Non-trading
Toy Options Limited	9 November 2000	1 ordinary share of £1	Non-trading
Character.com Limited	11 February 2000	1 ordinary share of £1	Non-trading
Cool-Cam Limited	3 February 2000	1 ordinary share of £1	Non-trading
WWL (Europe) Limited	26 September 2002	1 ordinary share of £1	Distribution of digital cameras
Character Promotions Limited	1 March 1999	100 ordinary shares of £1 each	Non-trading

3.3 The Company has the following further subsidiaries, all of which are, directly or indirectly, wholly owned private companies incorporated in Hong Kong, each having its registered office at 6F, Wheelock House, 20 Pedder Street, Central, Hong Kong.

Name	Date of Incorporation	Issued share capital (fully paid or credited as fully paid)	Nature of business
Toy Options (Far East) Limited	4 December 1990	3,000,000 ordinary shares of HK\$1 each	design and distribution of toys and games
World Wide Licenses Limited	3 October 1996	5,000,000 ordinary	Design and distribution of

		shares of HK\$1 each	digital cameras
Prelude (Far East) Limited	20 March 1998	2 ordinary shares of HK\$1 each	Non-trading
On Stretch Limited	7 September 1998	2 ordinary shares of HK\$1 each	Non-trading
Character Games (Far East) Limited	12 October 1998	2 ordinary shares of HK\$1 each	Distribution of games and puzzles

#### 4. Memorandum and Articles of Association

4.1 The Company's objects are set out in clause 4 of its Memorandum of Association (the "**Memorandum**"). A copy of the Memorandum is available for inspection as stated in paragraph 15.1 below.

The Company's principal objects, as stated in clause 4 of the Memorandum, are *inter alia*, to carry on:-

4.1.1 all of any of the businesses of manufacturers, wholesalers, importers, exporters, retailers, distributors, transporters, general merchants and dealers in all and every type of merchandise and commodity whether as principals, managers, agents or otherwise and to buy, sell, alter, repair, exchange, deal, hire, let out on rental and finance goods and articles of all descriptions including, without limitation, toys, games and playthings and all other activities and things capable of being carried on in connection with the foregoing businesses or any of them;

4.1.2 business as a holding company and to control and co-ordinate the administration and operation of any companies for the time being directly or indirectly controlled by the Company; and

4.1.3 any other trade or business which may seem to the Company capable of being conveniently carried on in connection with the aforesaid objects or calculated directly or indirectly to enhance the value of or render profitable any of the property or rights of the Company and otherwise to do all such things as are incidental or conducive to the above mentioned objects or any of them.

4.2 The Articles of Association of the Company (the "**Articles**"), a copy of which is available for inspection as stated in paragraph 15.1 below, contain provisions, *inter alia*, as summarised below:

##### 4.2.1 *Rights attaching to Ordinary Shares*

The rights attaching to Ordinary Shares are, *inter alia*, as follows:

###### (a) Voting

Subject to any disenfranchisement effected pursuant to paragraph 4.5 below, and to any special rights or restrictions as to voting attached to any class of shares, on a show of hands every member who is present in person or by proxy and who is entitled to vote shall have one vote and, upon a poll, every member present in person or by proxy and who is entitled to vote shall have one vote for every Ordinary Share held by him provided that no member shall, unless the directors otherwise determine, be entitled to vote at any general meeting unless all calls or other sums payable by him in respect of his Ordinary Shares have been paid.

###### (b) Dividends

Subject to the Act, the Company may, in general meeting, declare dividends to be paid to members of the Company, but no dividends may be declared in excess of the amount recommended by the directors. Except insofar as the rights attaching to, or the terms of issue of any shares otherwise provide (no

such shares presently being in issue), all dividends shall be apportioned and paid *pro rata* according to the amounts paid or credited as paid up (other than in advance of calls) on the Ordinary Shares during any portion or portions of the period in respect of which the dividend is paid. The directors may from time to time pay to the members of the Company such interim dividends as appear to the directors to be justified by the financial position of the Company.

The directors may, subject to the Act and with the prior sanction of an ordinary resolution of the Company, offer to members the right to elect to receive further Ordinary Shares, credited as fully paid, in lieu of all or any part of such cash dividend entitlements.

Any dividend unclaimed after a period of twelve years from its due date for payment will be forfeited and shall revert to the Company.

(c) Liquidation

On a winding up or other return of capital, the holders of Ordinary Shares are entitled to share in any surplus assets *pro rata* to the amount paid up on their Ordinary Shares. A liquidator of the Company may, with the sanction of an extraordinary resolution of the Company, divide *in specie* amongst the members the whole or any part of the assets of the Company in such manner as he shall think fair and may with like sanction vest the whole or any part of the assets in trustees upon such trusts for the benefit of the members as the liquidator shall with like sanction think fit.

4.2.2 *Alteration of capital*

Subject to the provisions of the Act and any other applicable statutes or regulations:

- (a) the Company may by special resolution issue redeemable shares;
- (b) subject to any special rights previously conferred on the holders of any existing shares, any share may be issued with such rights or restrictions as the Company may determine by ordinary resolution or, if no such resolution has been passed or so far as the resolution does not make specific provision, as the directors may decide;
- (c) the Company may, by ordinary resolution, increase, consolidate and subdivide its share capital and cancel any shares which have not at the date of the ordinary resolution been taken or agreed to be taken by any person;
- (d) the Company may purchase its own shares; and
- (e) by special resolution the Company may reduce its share capital and any capital redemption reserve, share premium account or other undistributable reserve.

4.2.3 *Variation of rights*

Whenever the capital of the Company is divided into different classes of share, the rights or privileges attached to any class may, subject to the Act and the special rights attaching to any class of share in the Company, be varied or abrogated, whether or not the Company is being wound up, either with the consent in writing of the holders of three-quarters in nominal amount of the issued shares of the affected class or with the sanction of an extraordinary resolution passed at a separate general meeting of the holders of the shares of that class. At any such general meeting (other than an adjourned meeting) the necessary quorum is two persons holding or representing by proxy not less than one-third in nominal amount of the issued shares of the class in question.

4.2.4 *Transfer of shares*

The instrument of transfer of a share shall be in any usual form or in any other form approved by the directors and shall be signed by or on behalf of the transferor and, if

the share is partly paid, by the transferee. The directors may decline to recognise any instrument of transfer of a share which is not fully paid. Subject to the provisions referred to in paragraph 4.2.5(b) below, the Articles do not contain any restriction on the free transferability of fully paid shares on which the Company does not have a lien, provided that the instrument of transfer is in favour of not more than four transferees and is in respect of only one class of share and the provisions in the Articles relating to the deposit of instruments of transfer have been complied with.

By resolution of the board dated 14 November 1996, the Company determined that the Ordinary Shares may be held in uncertificated form and that they may be transferred by means of a "relevant system" (as such term is defined in the Uncertificated Securities Regulations 1995) including CREST.

#### 4.2.5 *Suspension of rights*

- (a) If the directors are satisfied that any shareholder or any other person appearing to be interested in shares held by such shareholder has been duly served with notice under section 212 of the Act and is in default of such notice for the prescribed period, then they may by notice (a "**default notice**") to such shareholder direct that, in respect of such shares and any further shares which are issued in respect of such shares (the "**default shares**"), the shareholder shall not be entitled to be present or to vote either personally or by proxy at any general or class meeting of the Company or to exercise any other rights conferred by his shareholding in relation to general or class meetings of the Company.
- (b) Where the default shares represent at least 0.25 per cent. of the class of shares concerned, the default notice may in addition direct that any dividend or part thereof or other money which would otherwise be payable in respect of the default shares shall be retained by the Company without any liability to pay interest thereon when such money is finally paid and that (subject to certain exceptions) no transfer of any shares held by the shareholder shall be registered.

## 5. **Directors' and other interests**

5.1 The names and functions of the Directors are as follows:

Richard King	Executive Chairman (Chairman of the Nominations Committee and a member of the Audit Committee)
Enrico Preziosi	Chief Executive and Managing Director
Kirankumar Premchand Shah FCCA	Group Finance Director
Joseph John Patrick Kissane	Managing Director – Character Options Limited
Jonathan James Diver	Group Marketing Director
Ian Stanley Fenn	Senior Independent Non-Executive Director (Chairman of the Audit Committee and a member of the Remuneration and Nominations Committees)
Mark William Ogilvie Birdwood, The Lord	Independent Non-Executive Director (Chairman of the Remuneration Committee and a member of the Audit and Nominations Committees)
Aldo (otherwise known as "Gianfranco") Horvat	Non-Executive Director

Details of the Directors' management expertise and experience are as follows:

**Richard King** (58) Executive Chairman, has extensive experience in the toy industry and has been involved in importing consumer products from the Far East since 1969. He established the original business of The Character Group plc jointly with Mr Kissane and Mr Shah in 1991 and works in close association with the management of each division to develop and implement Group strategies.

**Enrico Preziosi** (55) Chief Executive Officer and Managing Director, was appointed to the Board as a Non-Executive Director in August 2000 and as Chief Executive and Managing Director in May 2001. He is the Chairman of, and is interested in a majority of the issued shares of, Giochi Preziosi S.p.A. He founded Giochi Preziosi S.p.A. in 1984 and has since been instrumental in growing its business.

**Kirankumar Premchand Shah** (49), Group Finance Director, is a member of the Chartered Association of Certified Accountants. After initially working in private accountancy practice, he moved into industry and since 1978 has been involved extensively in the toy industry, notably in his role in jointly heading up a successful management buyout of Merit Toys Limited in 1981 and its subsequent sale to Bluebird Toys plc in 1988. He jointly established the original business of The Character Group plc with Mr King and Mr Kissane in April 1991.

**Joseph John Patrick Kissane** (51), Managing Director of Character Options Limited, has considerable sales expertise in and outside of the toy industry, gained over a period of 30 years, notably with such companies as Nabisco, Lego and Tonka. He is one of the founders of the Group.

**Jonathan James Diver** (39), Group Marketing Director, joined the Group in September 1991 from Rainbow Toys Limited, where he was Senior Marketing Executive. He became Group Marketing Director in August 1994, and has developed close working relationships with the Group's suppliers. He has played a key role in the development and implementation of the Group's marketing strategy.

**Ian Stanley Fenn** (60), Senior Independent Non-Executive Director, joined the Board in May 1995. He has extensive experience in corporate finance gained over many years in stockbroking and merchant banking in the City of London. He is a Director of ARM Corporate Finance Limited which is authorised and regulated by the Financial Services Authority.

**Mark William Ogilvie Birdwood, The Lord** (65), Independent Non-Executive Director, was appointed to the Board in September 1995. He has experience as a Director of quoted and private companies. He has particular interests in executive placement and recruitment.

**Aldo "Gianfranco" Horvat** (61), Non-Executive Director, was appointed to the Board in November 2002. He is a consultant to Giochi Preziosi S.p.A. and has over 30 years experience in the toy industry.

5.2 The business address of the Directors is 86-88 Coombe Road, 2nd Floor, New Malden, Surrey KT3 4QS which is the head office of the Company.

5.3 The following table shows, in respect of each of the Directors, the names of all companies and partnerships outside the Group, of which he has, at any time in the five years prior to the date of this document, been a director or (as appropriate) a partner (excluding subsidiaries of any such companies).

Each directorship or partnership is currently held unless otherwise stated.

Director	Company or Partnership Name	Status
Richard King	Trading Offers Limited Clearmark Group plc Trading Options Limited	resigned 31/1/2001 (dissolved 20 April 1999)
Enrico Preziosi	Giochi Preziosi SPA Calcio Como SPA Fingiochi SPA	resigned 18/10/2003
Kirankumar Premchand Shah	Deancraft Limited Key Vehicle Holdings Limited Megashire Limited	(dissolved) resigned 30/7/1999 (dissolved) resigned 30/7/1999 (dissolved) resigned 30/7/1999
Joseph John Patrick Kissane	J. Squared Properties Limited	(dissolved 10/10/2000)
Jonathan James Diver	British Toy & Hobby Association Limited	
Lord Birdwood	Fiortho Limited Martlet Limited	

	North Star Consortium (Kings Waterfront) Limited	
	IMS Group plc	resigned 25/7/2000
	Jasmin plc	resigned 03/02/00
Ian Stanley Fenn	ARM Corporate Finance Limited	
	Oakleigh Renown Limited	
Aldo "Gianfranco" Horvat	HG Sviluppo SRL	resigned 6 May 2003
	Linea Gig SpA	resigned 8 January 1999
	Gig Distribuzione SpA	resigned 8 January 1999
	Giochi e Giocattoli SpA	resigned 18 October 1998
	Publikids SRL	resigned 27 January 1999
	Toy Service SpA	resigned 18 October 1998

5.4 R. King was a non-executive director of Clearmark Group plc when it went into administrative receivership on 20 August 1991. He had ceased, within 12 months prior to that time, to be an executive director of that company and of a number of its subsidiary companies which also went into administrative receivership on or about 20 August 1991. K. P. Shah, whilst not a director at the time of entry of Clearmark Group plc into administrative receivership in August 1991, had, within 12 months prior to that time, been an executive director of that company. The statement of affairs of Clearmark Group plc stated that the total deficiency as regards its creditors was £7.828 million.

5.5 A.G. Horvat was a director of Toy Service SpA ('TSS'), an Italian corporation, which operated a business as a toy retailer from a number of premises in and around Turin, Italy, up until 1995. In 1995, TSS commenced the implementation of an ambitious expansion plan to extend its operations throughout Italy. A combination of high costs associated with the expansion, vigorous competition from the existing toy retailers and the difficult trading conditions in the Italian toy market, particularly in 1998, resulted in TSS sustaining substantial and unanticipated losses. As a consequence, TSS became insolvent in or about late 1998, when the its administration passed into the hands of an official appointed under the applicable Italian insolvency legislation (broadly similar in function to a liquidator in the UK).

TSS was, at that time, a wholly owned subsidiary of Linea Gig SpA. Gig Distribuzione SpA and Publikids SRL were also subsidiaries (the 'Subsidiaries') of Linea Gig SpA. Linea Gig SpA had guaranteed a number of the obligations and liabilities of TSS and, as a consequence of the TSS insolvency and the demands of its creditors, was found itself, notwithstanding its profitable trading to that time, to be insolvent along with the Subsidiaries.

Formal deeds of arrangement, pursuant to which the claims of the creditors of Linea Gig SpA, TSS and each of the Subsidiaries were compromised in a manner binding on all of the creditors and the relevant companies, were approved by the official court in Florence, Italy between November 1999 and July 2002. As a consequence, it is believed that the preferential creditors of these companies received or will receive payment of all indebtedness due to them and other creditors received or will receive approximately 40% of the amounts due to them. The total shortfall in meeting in full the claims of the creditors of these various companies has been estimated to be approximately £55 million.

Aldo Horvat was not engaged in relation to the day to day management of the business of TSS and was, in effect, a non-executive director of TSS at all relevant times. Mr Horvat was the Chief Executive Officer of the other companies referred to above at all material times.

5.6 Save as set out above in paragraphs 5.4 and 5.5 above, none of the Directors has been involved in any company as a director with an executive function at the time or within 12 months preceding the receivership, compulsory liquidation, administration, company voluntary arrangement or any composition or arrangement with its creditors generally or any class of its creditors in respect of that company.

5.7 Save as set out in this paragraph 5, none of the Directors has:

5.7.1 been the subject of any bankruptcy or individual voluntary arrangement;

- 5.7.2 been a director with an executive function of any company at the time of, or within 12 months preceding, any receivership, compulsory liquidation, creditor's voluntary liquidation, administration, company voluntary arrangement or any composition or arrangement with creditors generally or any class of creditors of such company;
- 5.7.3 any outstanding judgment against him;
- 5.7.4 any unspent convictions in relation to indictable offences;
- 5.7.5 been involved in any partnership as a partner at any time or within 12 months preceding the compulsory liquidation, administration or partnership voluntary arrangement in respect of that partnership;
- 5.7.6 been involved in any receivership of his own assets or as a partner of a partnership at the time or within 12 months preceding the receivership of any assets of that partnership;
- 5.7.7 received any public criticisms by statutory or regulatory authorities (including designated professional bodies) nor been disqualified by a court from acting as a director of a company or from acting in the management or conduct of the affairs of a company.

There is no other information material to the Directors' directorships of the Company, the omission of which might affect the import of the information contained herein.

- 5.8 The interests in the share capital of the Company of the Directors (all of which are beneficial), as notified to the Company pursuant to sections 324 or 328 of the Act or which are required to be entered on the register to be maintained under the provisions of section 325 of the Act or which are the interests of a person connected with a Director (within the meaning of Section 346 of the Act), which interests, if such connected persons were directors of the Company would be required to be disclosed pursuant to sections 324 or 328 of the Act and the existence of which is known or could, with reasonable diligence, be ascertained by the Directors as at 16 February 2004 (being the latest practicable date prior to the publication of this document) are as follows:

Director	Number of Ordinary Shares	% of issued ordinary share capital
R. King	5,270,428	9.98
E. Preziosi	11,885,898	22.52
K.P. Shah	5,620,000	10.65
J.J.P. Kissane	1,462,300	2.77
J.J. Diver	1,690,640	3.2
I.S. Fenn	9,000	0.02
Lord Birdwood	8,750	0.02
A.G. Horvat	-	-
The Trustees of the TOPS pension fund <sup>1</sup>	1,600,000	3.03
Orbis Pension Trustees Limited <sup>2</sup>	285,000	0.54

Notes:

1. Each of R. King, K.P. Shah and J.J. Diver are beneficiaries under these pension scheme arrangements and are each, accordingly, interested in the pension scheme's holding of Ordinary Shares;

2. Orbis Pension Trustees Limited is the Trustee of the Company's Employee Share Ownership Trust. Each of R. King, K.P. Shah, J.J.P. Kissane and J.J. Diver is deemed to be interested in such Ordinary Shares by virtue of being within the class of beneficiaries defined by such Trust.

ncluded in the interests of R. King are his interests in 1,885,428 Ordinary Shares held by Cedarberg Investments Limited and 320,000 Ordinary Shares held by Mrs M.H. King (the spouse of Mr King). Included in the interests of K.P. Shah are the interests of Sarissa Holdings Limited in 5,620,000 Ordinary Shares. Included in the interests of E. Preziosi are the interests of Giochi Preziosi in 11,885,898 Ordinary Shares.

- 5.9 As at 16 February 2004 (being the latest practicable date prior to publication of this document), the following Directors have been granted options for nil consideration to subscribe for Ordinary Shares under the Approved Scheme, all of which remain unexercised:

Director	Date of grant	No. of Ordinary Shares under option	Exercise Price	Exercise Period
J.J.P. Kissane	05.02.03	185,000	54p	05.02.06 to 04.02.13
J.J. Diver	05.02.03	185,000	54p	05.02.06 to 04.02.13

- 5.10 As at 16 February 2004 (being the latest practicable date prior to publication of this document), other than the persons listed below and the relevant Directors as stated in paragraph 5.8 above, the Directors are not aware of any person who (directly or indirectly) is interested in three per cent. or more of the issued share capital of the Company:

	Number of Ordinary Shares	% of issued ordinary share capital
Valtidone	7,500,000	14.21
Sweet Briar Investments Limited	1,875,000	3.55

- 5.11 None of the Directors is or has been involved in any transaction with the Company or any member of the Group which is or was unusual in its nature or conditions, significant to the business of the Group and which was effected by the Company or any member of the Group during the current or immediately preceding financial year or which was effected by the Company or any member of the Group during an earlier financial year and remains in any respect outstanding or unperformed.
- 5.12 No loans or guarantees have been granted or provided to, or for the benefit of, any of the Directors by any member of the Group.
- 5.13 The Directors are not aware of any person who, either directly or indirectly, jointly or severally, exercises as at the date of this document or could exercise, following Admission, control over the Company.

## 6. Directors' service agreements and other information

- 6.1 The services of certain of the Executive Directors are retained pursuant to service agreements entered into by each of them with the Company on 9 May 1995. The following are particulars of such service agreements (as amended from time to time since execution):

	R. King	K.P. Shah	J.J.P. Kissane	J.J. Diver
Basic Salary	£167,625	£165,600	£145,180	£145,180
Pension Contribution	currently 35% (rising to 40%) of basic salary *	Currently 25% (rising to 40%) of basic salary *	currently 30% (rising to 40%) of basic salary *	currently 20% (rising to 40%) of basic salary *
Notice	12 months either way			

\* this entitlement rises (as appropriate) from 20% to 25% on attaining the age of 46, from 25% to 30% on attaining the age of 51, from 30% to 35% on attaining the age of 56 and from 35% to 40% on attaining the age of 61.

Each of the above-mentioned Executive Directors is entitled, under the terms of his service contract, to a bonus equal to his basic salary in the event that specified performance targets

are met or exceeded. These targets require increases in earnings per Ordinary Share in each financial year of the Group, adjusted to exclude certain exceptional non-trading items. The adjustments to be made are intended to eliminate from the calculation of earnings per share, for the purposes only of calculating directors' bonuses, certain exceptional and non-recurring items which in the opinion of the Board ought not to be taken account in the calculation of such bonuses. The items to be excluded are profits and/or losses on disposal of property, leases, goodwill, investments or any other substantial fixed asset not disposed of in the ordinary course of business; write-offs of goodwill; surpluses or deficits on re-valuation of fixed assets; costs of an abortive acquisition; exceptional write-offs associated with an acquisition of another company's business and any other exceptional items which shall be considered by the remuneration committee of the Board, in consultation with the auditors of the Company, to be appropriate.

The basic salaries referred to above will be reviewed with effect from 1 September 2004 and thereafter annually with effect from 1 September in every year by the remuneration committee of the Board. In addition to the remuneration payable in accordance with the above particulars, each of the Relevant Executive Directors is entitled to the option of the use of a company car and participation in any medical health scheme operated by or on behalf of the Company. There are no provisions in the Relevant Executive Directors' service agreements for compensation to be payable to any of the Relevant Executive Directors for early termination thereof.

- 6.2 Lord Birdwood, I.S. Fenn, E. Preziosi and A.G. Horvat each have letters of appointment relating to their positions as directors of the Company. Each of Lord Birdwood, I.S. Fenn and A.G. Horvat receive a director's fee at a rate of £20,000 per annum which is subject to review on 31 March in every year. Mr. Preziosi does not receive a fee for the discharge of his office as a director of the Company. The appointments of each of Lord Birdwood, I.S. Fenn and A.G. Horvat is for a period until the next annual general meeting of the Company when each will retire and will be eligible to offer himself for re-election. Subject to his re-election at that time it is anticipated that each of these appointments will be renewed until the following Annual General Meeting of the Company. Pursuant to the terms of the undertakings given by the Executive Directors other than E. Preziosi the appointment of E. Preziosi as an executive director of the Company may at the present time only be terminated upon the unanimous vote of the other members of the board of directors of the Company.
- 6.3 Save as set out in paragraphs 6.1 and 6.2 above, there are no service agreements existing between any of the Directors and the Company or any of its subsidiaries.
- 6.4 The total aggregate of the remuneration paid (including pension contributions) and benefits in kind granted to the Directors by members of the Group during the year ended 31 August 2003 was £1,288,628.

## **7. Litigation**

- 7.1 A claim for £142,336.90 was issued on 23 March 2001 by DSK Supplies Limited against Universal Concepts ((UK) Limited in respect of alleged non-payment for goods that it claims to have supplied. The claim is disputed and a defence was filed and served on 2 May 2001. No formal steps have been taken in these proceedings since that date and there has been no contact from or communication with the claimant in these proceedings since 2002..
- 7.2 Notice dated 11 December 2002 has been received by K Mart Corporation, a multiple retail organisation in the United States of America ("USA"), from a patent holder alleging that certain of the own brand digital camera products of World Wide Licenses Limited ("WWL") infringe the patent holder's registered patent in the USA. No supplies of WWL's products have been made to this retailer directly or through its authorised distributor and no formal intimation of claim has been made against WWL and/or its authorised distributors in the USA. No detailed investigation has been made at this time into the assertions of patent infringement by WWL to date. The position will continue to be monitored by the Directors and, as appropriate, professional advice sought regarding WWL's position if any formal intimation of claim is made in relation to any allegations of infringement against WWL.

7.3 Save as disclosed above, there are no, nor have there been any, legal or arbitration proceedings nor, so far as the Company is aware, are any such proceedings pending or threatened by or against the Company or any other company within the Group which may have (or which have had during the last twelve months) a significant effect on the financial position of the Group.

## **8. Material Contracts**

The following contracts (not being contracts entered into in the ordinary course of business) have been entered into by members of the Group within the period of two years immediately preceding the date of this document and are, or may be, material or contain a provision under which any member of the Group has an obligation or entitlement which is material to the Group as at the date of this document:

- 8.1 an agreement dated 21 June 2001, between the Company, the Relevant Executive Directors, E. Preziosi, Collins Stewart Limited and TISA relating to the arrangements agreed by and between the parties in relation to the offer by way of rights made by the Company on 16 July 2001 and the associated underwriting arrangements. The Company paid Collins Stewart Limited a fee of £150,000 in relation to the performance of its obligations in relation to such arrangements and also bore all costs, charges and expenses of and incidental to the arrangements put in place by such agreement, including the fees of the UK Listing Authority, the London Stock Exchange and associated legal and accountancy expenses. The obligations of all parties under this agreement were substantially discharged following the admission to the Official List and to trading on the London Stock Exchange's market for listed securities of the Ordinary Shares referred to in paragraph 2.2.1 and 2.2.2 of this Part IV. The only material provisions that continue to have effect under this agreement are certain representations, warranties and indemnities given by the Company and by the Relevant Executive Directors and E. Preziosi to Collins Stewart Limited. Such representations, warranties and indemnities are conventional for an agreement of this kind;
- 8.2 the Convertible Loan Note, the principal terms and conditions of which are summarised in Part III of this document.

## **9. Consent**

Baker Tilly have given and not withdrawn their written consent to the inclusion in this document, in the form and context in which it is included, of their report set out in Part II of this document and have authorised the contents of that part of this document for the purposes of Regulation 6(1)(e) of The Financial Services and Markets Act 2000 (Official Listing of Securities) Regulations 2001.

## **10. Working Capital**

The Company is of the opinion that, taking into account existing bank facilities available to the Group, the Group has sufficient working capital for its present requirements, that is for at least the next twelve months from the date of this document.

## **11. The Share Schemes**

### *11.1 The Approved Scheme*

The Company adopted the rules constituting the Approved Scheme by resolution passed on 3 May 1995, and obtained Inland Revenue approval therefor under Schedule 9 to the Taxes Act on 9 May 1995.

The main features of the rules of the Approved Scheme are summarised below:

#### **11.1.1 Eligibility**

Directors and employees of the Company and its subsidiaries working more than 25 hours and 20 hours respectively (exclusive of meal breaks) are eligible to participate unless they are within two years of retirement or hold a material interest in the Company, being ten per cent. or more of the share capital of the Company if at the relevant time the Company is a close company within section 414(1) Taxes Act. No eligible executive may participate as of right and the extent of each individual's

participation is at the discretion of the directors, subject always to the limits described in paragraphs 11.2 and 11.3 below.

#### 11.1.2 Individual participation limits

No option will be granted to an eligible employee if the aggregate exercise price for that option, when added to the aggregate exercise price of all rights which, within the previous ten years, have been granted to that employee under the Approved Scheme or any other Inland Revenue approved share option scheme of the Company (other than a savings related scheme) for employees of the Group and which in every case remain outstanding would exceed £30,000

#### 11.1.3 Overall limits

The Company may not grant an option under the Approved Scheme if, as a result, the aggregate number of Ordinary Shares issued or issuable in respect of all options granted under the Share Schemes or any other share option scheme for employees of the Group adopted or entered into on or after the date of adoption of the Approved Scheme would, in the ten years immediately preceding the date upon which the option is granted, exceed ten per cent. of the issued ordinary share capital of the Company.

#### 11.1.4 Subscription price

The price per Ordinary Share at which an option may be exercised under the Approved Scheme will be determined by the Directors but will be not less than the higher of its nominal value and its market value on the day of grant, which shall be either as determined in accordance with the provisions of sections 272 and 273 of the Taxation of Chargeable Gains Act 1992 and agreed with the Inland Revenue Shares Valuation Division (if the option is granted at a time when the Ordinary Shares have not been admitted to the Official List) or (if the Ordinary Shares are then listed) the average of the middle market quotations of an Ordinary Share as shown in the Daily Official List of the London Stock Exchange for the three dealing days immediately preceding the day upon which the option is granted.

#### 11.1.5 Grant of options

An option granted under the Approved Scheme will be granted free of charge. An option may only be granted under the Approved Scheme:

- (a) within the period of 42 days after the date upon which the Approved Scheme is approved by the Inland Revenue;
- (b) within the periods of 42 days immediately after the publication by the Company of each of its interim results and the preliminary announcement of its final results in each financial year;
- (c) at other times in exceptional circumstances.

#### 11.1.6 Option share rights

The Ordinary Shares issued upon the exercise of an option granted under the Approved Scheme will rank *pari passu* in all respects with the Ordinary Shares then in issue save as regards any dividend payable by reference to a record date prior to such issue.

#### 11.1.7 Exercise of options

An option granted under the Approved Scheme cannot be exercised more than ten years after the date on which it was granted nor, normally, can it be exercised less than three years after its grant. However, options may be exercised (whether the initial three year period has expired or not) in the following circumstances:

- (a) the personal representatives of a deceased participant may exercise the participant's options within one year after the date of death of the relevant

participant, failing which they will lapse;

- (b) if a participant ceases to be employed by reason of injury, disability, redundancy, retirement or as a result of the sale of his employing company or the transfer of the business in which he is employed, he may exercise his option before the later of six months from the date of such termination of employment or 42 months from the date of grant of the option, failing which it will lapse;
- (c) on the termination of a participant's employment for any other reason the directors may, in their absolute discretion, notify the participant in writing that his option may be exercised on the expiry of the later of six months from the date of such termination of employment or 42 months from the date of grant of the option failing which it will lapse;
- (d) if another company acquires control of the Company following any amalgamation or reconstruction and if the acquiring company so agrees, an option may be exchanged for an option to subscribe for shares in the acquiring company on terms equivalent to the option granted to a participant under the Approved Scheme. Alternatively, a participant may exercise an option granted under the Approved Scheme within six months after being notified by the Company of such a change of control, failing which it will lapse; or
- (e) if the Company passes a resolution for voluntary winding-up, any subsisting option may be exercised within six months after the date upon which the resolution is passed.

#### 11.1.8 Performance conditions

The directors may impose objective conditions on the exercise of options and it is proposed by them that such conditions will be imposed as reflect the guidelines of the investor protector committees, including the Association of British Insurers, from time to time. The Directors intend to impose targets of sustained improvement in the underlying performance of the Company as a pre-condition of the exercise of options granted under the Approved Scheme. Initially, the Directors considered that growth in earnings per share was a suitable measurement of the Company's performance and options were granted subject to a condition that they would only be exercisable if, over a three year period following the grant of the option, the Company achieved growth in its earnings per share which exceeded the growth in the Retail Prices Index by an average of two per cent. per year. At present time the Remuneration Committee is of the view that it is more appropriate that options granted under the Approved Scheme will be subject to the condition that they may not in normal circumstances be exercised unless:

- (a) predetermined targets for profit before tax and interest (adjusted to eliminate certain intra-group charges); or
- (b) predetermined targeted increases in the consolidated, fully diluted earnings per share of the Group

are met or exceeded.

#### 11.1.9 General

- (a) The Approved Scheme is administered by the Remuneration Committee of Board which is made up wholly of non-executive directors.
- (b) An option may be renounced within 28 days after the date upon which it was granted in which case it will be deemed never to have been granted.
- (c) An option is not transferable other than by transmission upon death to a participant's personal representatives in accordance with the rules of the

Approved Scheme. An option will lapse if a participant purports to deal with it.

- (d) No option may be granted under the Approved Scheme after 3 May 2005, being the tenth anniversary of the date upon which the Approved Scheme was adopted, or such earlier date as may be determined by the Board. The termination of the Unapproved Scheme will not affect options previously granted..
- (e) If the Company undertakes a capitalisation or rights issue or any consolidation, sub-division or reduction of its ordinary share capital, the number of Ordinary Shares available under the Approved Scheme, the option price and the number of Ordinary Shares comprised in each option may be adjusted, with the prior written approval of the Inland Revenue, as the auditors confirm in writing to be in their opinion fair and reasonable.
- (f) The Company shall at all times ensure that sufficient Ordinary Shares are kept available to satisfy all outstanding options.
- (g) Save for amendments designed to address requirements necessary for the Approved Scheme to satisfy and to continue to satisfy the requirements for approval by the Commissioners of the Inland Revenue, the rules of the Approved Scheme cannot be amended to the advantage of the participants without the prior approval of shareholders in general meeting.
- (h) Participation in the Approved Scheme does not afford to any participant any additional right to compensation on the termination of his employment.
- (i) No option shall be granted to an individual to whom the London Stock Exchange's Model Code on transactions in securities by listed companies (the "**Model Code**") applies if he is aware that such grant would be in breach of the Model Code nor shall any option be exercised in such circumstances.

## 11.2 *The Unapproved Scheme*

The Company adopted the rules constituting the Unapproved Scheme by resolution passed on 2 June 1997. The Unapproved Scheme has not been approved by the Inland Revenue.

The provisions of the rules of the Unapproved Scheme are substantially similar to the rules constituting the Approved Scheme as regards grant, exercise, adjustment and administration. The principal differences between the rules for the two schemes are as follows:

### 11.2.1 Individual participation limits

No option will be granted to an eligible employee if the aggregate exercise price for that option, when added to the aggregate exercise price of all rights which, within the previous ten years, have been granted to that employee under the Share Schemes or any other share option scheme of the Company (other than a savings related share option scheme) shall exceed four times the eligible employee's annual basic salary and the value of fluctuating emoluments (if any) paid over the prior twelve months.

### 11.2.2 Overall limits

The overall limits specified in paragraph 11.1.3 above in relation to the Approved Scheme apply in like fashion to the Unapproved Scheme.

### 11.2.3 Grant of Options

An option may be granted under the Unapproved Scheme in much the same way as specified under paragraph 11.1.5 in relation to the Approved Scheme except that, given that no approval will be given by the Inland Revenue in relation to the Unapproved Scheme, the provisions of paragraph 11.1.5(a) do not apply to the Unapproved Scheme and instead options were capable of being granted under the

Unapproved Scheme within a period of 42 days after the date upon which the Unapproved Scheme was adopted by the Company.

#### 11.2.4 Exercise of Options

Under the Unapproved Scheme an option cannot be exercised more than seven years after the date on which it was granted. Further, options may be exercised (whether the initial three year period has expired or not) in the circumstances outlined in paragraphs 11.1.7(d) and (e) above and otherwise on the cessation of a participant's employment for any reason if the directors, in their absolute discretion, notify the participant in writing within 42 days of such cessation that his option may be exercised for a period not exceeding the shorter of six months from the date of such cessation of employment and the unexpired term of the option.

#### 11.2.5 Termination

No option may be granted under the Approved Scheme after 2 June 2007, being the tenth anniversary of the date upon which the Approved Scheme was adopted, or such earlier date as may be determined by the Board. The termination of the Unapproved Scheme will not affect options previously granted.

#### 11.2.6 Other Differences

As the Unapproved Scheme is not by the Inland Revenue, amendments to the its rules, in the manner contemplated under paragraph 11.1.9(g) above in relation to the Approved Scheme, and adjustments to options, in the manner contemplated under paragraph 11.1.9(e) above in relation to the Approved Scheme, do not apply in relation to the Unapproved Scheme.

### 11.3 *EMI Scheme*

The Company adopted the rules constituting the EMI Scheme pursuant to a resolution passed on 22 January 2003. Option agreements entered into pursuant to the EMI Scheme are intended to qualify as Enterprise management Incentives for the purposes of section 62 of, and Schedule 14 to, the Finance Act 2000.

The provisions of the rules of the EMI Scheme are substantially similar to the rules constituting the Approved Scheme as regards grant, exercise, adjustment and administration. The principal differences between the rules for the two schemes are as follows:

#### 11.3.1 Eligibility

All employees and Directors of the Company or any of its subsidiaries, whose committed time to the business of the Group constitutes at least 25 hours per week or 75% of his/her working time, will be eligible to participate in the EMI Scheme.

#### 11.3.2 Limits on participation by employees

Participation by employees of the Group will be limited under the rules of the EMI Scheme such that no option will be granted to an eligible employee to the extent that the aggregate market value of the Ordinary Shares to be subject to the new option to be granted to him/her on the relevant date of grant:

- (a) when added to the aggregate market values (at their respective dates of grant) of all rights which, within the previous ten years, have been granted to that employee under the EMI Scheme and/or the other Share Schemes shall exceed the aggregate of four times his/her current or previous year annual basic salary and the value of any bonus or commission arrangements not exceeding an amount equal to the applicable basic salary ("**applicable remuneration**");
- (b) when added to the aggregate market values (at their respective dates of grant) of all rights which have been granted under the EMI Scheme and are outstanding at the relevant date of grant shall exceed £3,000,000;

- (c) when added to the aggregate market values (at their respective dates of grant) of all rights which have been granted to that employee under the EMI Scheme and the other Share Schemes in the previous 12 months shall exceed 1½ times his/her applicable remuneration;
- (d) whether alone or when added to the aggregate market values (at their respective dates of grant) of all rights which have within the previous three years been granted to him/her (whether exercised or not) under the EMI Scheme or the Approved Scheme shall exceed £100,000.

#### 11.3.3 Overall limits

The total number of unissued Ordinary Shares over which options may be granted when aggregated with the total number of Ordinary Shares issued or issuable following an exercise of any such options under the Share Schemes:

- (a) in the ten years immediately preceding the date upon which an option is granted, shall not exceed ten per cent of the issued Ordinary Shares at such time; or
- (b) in the three year period following the adoption of the EMI Scheme, shall not exceed 3 per cent of the issued Ordinary Shares at such time.

#### 11.3.4 Grant of options

Options may only be granted during the 42 day period following:

- (a) the date of formal adoption of the EMI Scheme; and subsequently
- (b) the expiry of three dealing days after the preliminary announcement of the Group's final results, or the announcement of the Group's interim results, for any financial period

and at other times in exceptional circumstances.

The foregoing is subject to the proviso that no option shall be granted to an individual to whom the Model Code applies if the Directors are aware that such grant would be in breach of the Model Code. Options will not be transferable or assignable but may, at the discretion of the Directors, be exercised by the personal representatives of a deceased optionholder within 6 months of the date of death of the optionholder. The number of Ordinary Shares subject to an option may be adjusted in substantially the same circumstances as apply in relation to the Approved Scheme.

#### 11.3.5 Exercise of options

An option may usually only be exercised during the period commencing on the third, and ending on the business day prior to the tenth, anniversary of the date of grant. Earlier exercise is permitted in the following circumstances:

- (a) in the event of a takeover, reconstruction or winding-up of the Company, the options may be exercised; or
- (b) if a participant ceases to be employed within the Group for any reason the Directors have a discretion to allow its exercise within six months of his employment so ceasing, or, if shorter, for the unexpired term of the option.

An option will lapse to the extent that it is not exercised in accordance with these entitlements. Notwithstanding the foregoing provisions regarding exercise, no exercise of an option shall be effective if the Directors are aware that such exercise and/or the subsequent allotment and issue or transfer of Ordinary Shares to the relevant individual would be in breach of the Model Code, or any other provisions of the listing rules of the UK Listing Authority.

#### 11.3.6 Performance conditions

Performance conditions may be imposed upon options granted under the EMI Scheme and the Remuneration Committee's approach in relation to the imposition of performance conditions on options granted under the Approved Scheme is applied in like fashion to option granted under the EMI Scheme.

#### 11.3.7 Amendments

The Directors may amend the rules of the EMI Scheme provided that no such amendment shall:

- (a) have effect in relation to options granted under the EMI Scheme prior to such amendment taking effect;
- (b) have the effect of giving an advantage to any existing optionholder, or shall be made to the following matters, without the prior approval of the Company in general meeting:
  - (c) eligibility to participate in the EMI Scheme;
  - (d) the calculation of the option price;
  - (e) the limits on the grant of options;
  - (f) the periods during which, and in the manner in which, options may be granted and exercised on the takeover, reconstruction or winding-up of the Company; and
- (g) any other provision of the EMI Scheme where such amendment would enhance the benefits of participants.

Subject to the above, the Directors may make such minor amendments to the Scheme as are necessary or desirable to benefit the administration of the Scheme or to take account of a change in legislation or to obtain or maintain favourable tax, exchange control or regulatory treatment for optionholders or the Company or any member of the Group.

#### 11.3.8 Pensionable benefit status

Under present tax legislation, no benefits derived from the grant of an option under the EMI Scheme (whether arising out of the right to acquire Ordinary Shares or from the acquisition or disposal of Ordinary Shares upon an exercise of any such option) constitute income included as "relevant earnings" for the purposes of determining pensionable entitlements.

#### 11.3.9 Termination

The EMI Scheme will automatically terminate on 22 January 2013 or earlier if determined by the Board. The termination of the EMI Scheme will not affect options previously granted.

## 12. United Kingdom Taxation - Taxation of dividends paid on New Ordinary Shares

This section is intended only as a general guide to current United Kingdom tax law and practice for Shareholders who are resident or ordinarily resident in the United Kingdom for tax purposes, who are the beneficial owners of Ordinary Shares and who hold them as investments. **Shareholders who are in any doubt about their tax position, or who are subject to taxation in a jurisdiction other than the UK, should consult their own professional adviser.**

Under current UK taxation legislation, no tax is withheld from dividend payments by the Company.

A Shareholder who is an individual resident in the UK for tax purposes will generally be entitled to a tax credit in respect of any dividend received from the Company and will be taxed on the aggregate of that net cash dividend and the tax credit (the gross dividend) which will be regarded as the top slice of the Shareholder's income. The value of the tax credit is equal to 10 per cent of the gross

dividend received, which is also equal to one-ninth of the amount of the net cash dividend. The gross dividend is included in computing the income of such an individual holder for UK tax purposes.

In the case of a UK resident individual who is liable to income tax at the starting, lower or basic rate, the tax credit will in each case match his income tax liability in respect of the dividend and there will be no further tax to pay. Higher rate taxpayers will be liable to tax on the gross dividend at a rate of 32.5 per cent; the tax credit will be set against but will not fully match their tax liability on the gross dividend and they will have to pay additional income tax equal to 25 per cent of the net cash dividend.

A Shareholder within the charge to corporation tax and resident for tax purposes in the UK will not normally be liable to UK tax on the receipt of a dividend but cannot reclaim from the Inland

Revenue any tax credit attaching to the dividend payment.

Tax credits on dividends received from the Company in respect of shares held in Personal Equity Plans or Individual Savings Accounts will be repayable in respect of dividends paid before 6 April 2004.

Registered charities may reclaim the credits from the Inland Revenue on a reducing balance basis until 5 April 2004.

### **13. Property**

13.1 The Group's principal establishment in the UK is at Lees Brook Mill, Lees Road, Oldham, Lancashire, OL4 5JL. The freehold of these premises is owned by the Company. The premises comprise a converted mill building, originally built in the late 1880's. Considerable work has been undertaken to modernise the premises and adapt them to the Group's use. The floor area provided by the building is approximately 240,000 square feet. The principal use of these premises is as warehousing, fulfilment and as administrative offices.

13.2 The Group's principal establishment in Hong Kong is at Room 816-817 AIA Tower New World Centre 20 Salisbury Road Tsim Sha Tsui Kowloon, Hong Kong. The premises are occupied pursuant to the terms of a lease for a term that commenced on 1 July 2001 and ends on 31 December 2004. These premises comprise approximately 5,730 square feet. The current monthly rent is HK\$114,620. The principal use of these premises is as administrative offices.

### **14. General**

14.1 Save as disclosed in the section entitled "Current trading and prospects" in Part I hereof, there has been no significant change in the trading or financial position of the Group since 31 August 2003, being the date to which the last audited consolidated accounts of the Group were made up.

14.2 The costs, charges, expenses and fees of, and incidental to, the application for the Admission are payable by the Company and are estimated to amount to £37,696.16 (excluding any applicable Value Added Tax payable thereon). No remuneration is payable to financial intermediaries whether by way of underwriting commission or margin, guarantee commission, placing commission or selling agent's commission in respect of the New Ordinary Shares.

14.3 Save for the information set out in paragraph 3 of this Part IV, the Company has no subsidiaries.

14.4 The New Ordinary Shares for which application has been made for admission to the Official List and to trading on the London Stock Exchange have not been sold nor are they available, in whole or in part, to the public in conjunction with such application.

14.5 The financial information contained in this document does not constitute statutory accounts within the meaning of section 240 of the Act. Baker Tilly (formerly known as HLB Kidsons), Registered Auditors and Chartered Accountants, of Marlborough House, Victoria Road South, Chelmsford, Essex, CM1 1LN have audited the Group's accounts for the three financial years ended 31 August 2003 and have duly made reports under section 235 of the Act upon the statutory accounts of the Group in respect of each of such years and such accounts, together with such reports, have been delivered to the Registrar of Companies in England and Wales

in accordance with the applicable provisions of the Act. Each such report was unqualified and did not contain any statements under sections 237(2) or (3) of the Act.

- 14.6 The New Ordinary Shares have been issued at a premium of 35p per share over their nominal value of 5p based on the conversion price prescribed by the Convertible Loan Note.
- 14.7 The Company's registrars are Neville Registrars Limited, 18 Laurel Lane, Halesowen, West Midlands, B63 3DA.

#### **15. Documents for Inspection**

Copies of the following documents may be inspected at the Company's registered office, 5th Floor, 4 Chiswell Street, London EC1Y 4UP, during normal business hours on weekdays (except Saturdays and Public Holidays) for a period of 14 days from the date of this document:

- 15.1 the memorandum and articles of association of the Company;
- 15.2 the audited consolidated statutory accounts of the Company and its subsidiaries for each of the financial years ended 31 August 2002 and 31 August 2003;
- 15.3 the report of Baker Tilly reproduced in Part II of this document together with their statement of adjustments relating thereto;
- 15.4 the service agreements and letters of appointment referred to in paragraph 6.1 above;
- 15.5 the rules of each of the Share Schemes;
- 15.6 the material contracts referred to in paragraph 8 above;
- 15.7 the written consent referred to in paragraph 9 above;
- 15.8 the Circular;
- 15.9 the Convertible Loan Note; and
- 15.10 this document.

17 February 2004.