SOYO GROUP INC
Form 10-Q
May 17, 2006

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal quarter ended March 31, 2006

[_] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from __________________ to ___________________

Commission File Number 333-42036

SOYO GROUP, INC.

(Exact Name of Registrant as specified in its Charter)

Nevada	95-4502724
(State or other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification Number)

1420 South Vintage Avenue, Ontario, California 91761-3646

(Address of Principal Executive Offices) (Zip Code)

(909) 292-2500

(Issuer's Telephone Number, Including Area Code)

Securities registered under Section 12(b) of the Exchange Act: None

Securities registered under Section 12(g) of the Exchange Act: None

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No [ ]

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes [ ] No [X]

1

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer [ ] Accelerated filer [ ] Non-accelerated filer [X]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). [ ] Yes [X] No

Indicate the number of shares outstanding of each of the Registrant's classes of Common Stock as of the latest practicable date.

As of May 15, 2006, there were 48,720,511 shares Outstanding.

Documents Incorporated by Reference: None

2

SOYO GROUP, INC. AND SUBSIDIARY

INDEX

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Condensed Consolidated Balance Sheets - March 31, 2006 (Unaudited) and December 31, 2005 4

Condensed Consolidated Statements of Operations (Unaudited) - Three Months Ended March 31, 2006 and 2005 6

Condensed Consolidated Statements of Cash Flows (Unaudited) - Three Months Ended March 31, 2006 and 2005 8

Notes to Condensed Consolidated Financial Statements (Unaudited) - Three Months Ended March 31, 2006 and 2005 10

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations 15

Item 3. Quantitative and Qualitative Disclosures about Market Risk 23

Item 4. Controls and Procedures 24

PART II. OTHER INFORMATION

Item 2. Changes in Securities, Use of Proceeds and Issuer Purchases of Equity Securities 26

Item 3. Defaults upon Senior Securities 26

Item 4. Submission of Matters to a vote of security holders 26

Item 5. Other information 27

Item 6. Exhibits and Reports on Form 8-K 27

SIGNATURES 28

3

SOYO Group, Inc. and Subsidiary
Condensed Consolidated Balance Sheets

SOYO Group, Inc. and Subsidiary
Consolidated Balance Sheets

	March 31,	December 31,
	2006 (unaudited)	2005
ASSETS		
CURRENT		
Cash and cash equivalents	$ 54,411	$ 828,294
Accounts receivable, net of allowance for doubtful accounts of $639,224 at March 31, 2006 and December 31, 2005 respectively	6,821,483	7,278,520
Inventories	11,255,016	7,991,030
Prepaid Expenses	2,105	20,984
Income tax refund receivable	0	0
Total Current Assets	18,133,015	16,118,828
Property and Equipment	917,304	867,122

Less: accumulated depreciation and amortization	(141,296)	(115,480)
	776,008	751,642
Deposits	42,445	36,920
Total Assets	18,951,468	16,907,390

(continued)

4

SOYO Group, Inc. and Subsidiary
Condensed Consolidated Balance Sheets

SOYO Group, Inc. and Subsidiary
Consolidated Balance Sheets (continued)

	March 31,	December 31,
	2006	2005
LIABILITIES		
CURRENT		
Accounts payable	16,930,908	13,977,579
Total Accounts Payable	16,930,908	13,977,579
Accrued liabilities	347,509	1,287,108
Advances from officers, directors and major shareholder	0	0
Business Loan	0	0
Short Term Loan	100,000	165,000
Current Liabilities	17,378,417	15,429,687
Total Liabilities	17,378,417	15,429,687
EQUITY		

Class A Preferred stock, $0.001 par value	0	0
Class B Preferred stock, $0.001 par value	1,752,342	1,702,486
Preferred Stock Backup Withholding	(99,956)	(84,999)
Common stock, $0.001 par value Authorized - 75,000,000 shares	48,721	48,682
Additional paid-in capital	17,610,140	17,225,738
Accumulated deficit	(17,738,196)	(17,414,204)
Total Shareholder's Equity (Deficiency)	1,573,051	1,477,703
Total Liabilities plus Shareholders' Equity	$ 18,951,468	$ 16,907,390

See accompanying notes to condensed consolidated financial statements.

SOYO Group, Inc. and Subsidiary
Condensed Consolidated Statements of Operations (unaudited)

	Three months ended March 31,	
	2006	2005
Net revenues	$ 11,548,187	$ 3,962,520
Cost of revenues	9,897,099	3,440,485
Prior Years Purchase Discounts	0	1,089,172
Gross margin	1,651,088	1,611,207
Costs and expenses:		
Sales and marketing	74,886	239,465
General and administrative	1,484,994	933,973
Provision for doubtful accounts	50,000	31,124
Depreciation and amortization:		
Property and equipment	25,815	8,749
Total costs and expenses	1,635,695	1,213,311
Income (Loss) from operations	15,393	397,896

Other income (expense):		
Interest income	3,247	0
Interest expense	(72,387)	(11,221)
Other income (expense)	4,531	0
Other income (expense), net	(64,609)	(11,221)
Income (Loss) before cumulative effect of change in accounting principle	(49,216)	386,675
Cumulative Effect on Prior Years of Changing to Fair Value Method of Accounting for Stock Based Compensation	(224,919)	0
Net Income (loss)	(274,135)	386,675
Less: Dividends on Convertible Preferred Stock	49,856	39,213
Net income (loss) attributable to common shareholders	(323,991)	$ 347,462
Net loss per common share - Basic and diluted	(.01) (.01)	.01 .01
Weighted average number of shares of common stock outstanding - Basic and diluted	48,540,681 53,296,071	40,530,000 44,748,149

(continued)

6

SOYO Group, Inc. and Subsidiary
Condensed Consolidated Statements of Operations (unaudited) (continued)

Earnings per common share		
Income (loss) before cumulative effect of a change in accounting principle and preferred stock dividends	.00	.01
Cumulative effect on prior years of changing to fair value method of accounting for stock-based compensation	(.01)	0
Preferred stock dividends	.00	.00
Net income (loss)	(.01)	.01

Earnings per common share assuming dilution–		
Income (loss) before cumulative effect of a change in accounting principle and preferred stock dividends	.00	.01
Cumulative effect on prior years of changing to fair value method of accounting for stock-based compensation	(.01)	0
Preferred stock dividends	.00	.00
Net income (loss)	(.01)	.01

See accompanying notes to condensed consolidated financial statements.

7

SOYO Group, Inc. and Subsidiary
Condensed Consolidated Statements of Cash Flows (Unaudited)

	Three Months Ended March 31,	
	2006	2005
OPERATING ACTIVITIES		
Net income	$ (274,135)	$ 386,675
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and Amortization	25,815	8,749
Non cash payments for Director's Compensation	24,570	--
Stock based Compensation	359,871	--
Provision for doubtful Accounts	50,000	31,124
Changes in operating assets and liabilities:		
(Increase) decrease in:		
Accounts receivable	407,037	(593,089)
Inventories	(3,263,986)	1,043,196
Prepaid expenses	18,879	(3,503)
Deposits	(5,525)	15,840

Increase (decrease) in:		
Accounts payable -	2,953,329	(1,906,334)
Accrued liabilities	(939,599)	(254,332)
Net cash used in operating activities	(643,744)	(1,271,674)
INVESTING ACTIVITIES		
Purchase of property and equipment	(50,182)	--
Proceeds from sale of equipment	--	56,662
Net cash used in investing activities	(50,182)	56,662

(continued)

8

SOYO Group, Inc. and Subsidiary
Condensed Consolidated Statements of Cash Flows (Unaudited) (continued)

FINANCING ACTIVITIES		
Advances from officer, director and major shareholder	(65,000)	(60,000)
Proceeds from issuance of Common Stock	--	500,000
Payment of backup withholding tax on accreted dividends on preferred stock	(14,957)	--
Net cash provided by financing activities	(79,957)	440,000
CASH AND CASH EQUIVALENTS		
Net decrease	(773,883)	(775,012)
At beginning of period	828,294	1,288,351
At end of period	54,411	$ 513,339
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		

Cash paid for Interest	72,387	0
NON-CASH INVESTING AND FINANCING ACTIVITIES		
Accretion of discount on preferred stock	49,856	39,213
Directors' compensation	24,570	--
Stock option compensation	359,871	--

See accompanying notes to condensed consolidated financial statements.

SOYO Group, Inc. and Subsidiary
Notes to Condensed Consolidated Financial Statements (Unaudited)
Three Months Ended March 31, 2006 and 2005

1. Organization and Basis of Presentation

Organization - Effective October 24, 2002, Vermont Witch Hazel Company, Inc., a Nevada corporation ("VWHC"), acquired SOYO, Inc., a Nevada corporation ("SOYO Nevada"), from SOYO Computer, Inc., a Taiwan corporation ("SOYO Taiwan), in exchange for the issuance of 1,000,000 shares of convertible preferred stock and 28,182,750 shares of common stock, and changed its name to SOYO Group, Inc. ("SOYO"). The 1,000,000 shares of preferred stock were issued to SOYO Taiwan and the 28,182,750 shares of common stock were issued to certain members of SOYO Nevada management.

Subsequent to this transaction, SOYO Taiwan maintained an equity interest in SOYO, continued to be the primary supplier of inventory to SOYO, and was a major creditor. In addition, there was no change in the management of SOYO and no new capital invested, and there was a continuing family relationship between certain members of the management of SOYO and SOYO Taiwan. As a result, this transaction was accounted for as a recapitalization of SOYO Nevada, pursuant to which the accounting basis of SOYO Nevada continued unchanged subsequent to the transaction date. Accordingly, the pre-transaction financial statements of SOYO Nevada are now the historical financial statements of the Company.

In conjunction with this transaction, SOYO Nevada transferred $12,000,000 of accounts payable to SOYO Taiwan to long-term payable, without interest, due December 31, 2005. During the three months ended March 31, 2004, the Company agreed with a third party to convert the long-term payable into convertible preferred stock.

On December 9, 2002, SOYO's Board of Directors elected to change SOYO's fiscal year end from July 31 to December 31 to conform to SOYO Nevada's fiscal year end.

On October 24, 2002, the primary members of SOYO Nevada management were Ming Tung Chok, the Company's President, Chief Executive Officer and Director, and Nancy Chu, the Company's Chief Financial Officer. Ming Tung Chok and Nancy Chu are husband and wife. Andy Chu, the President and major shareholder of SOYO Taiwan, is the brother of Nancy Chu.

Unless the context indicates otherwise, SOYO and its wholly-owned subsidiary, SOYO Nevada, are referred to herein as the "Company".

Basis of Presentation - The accompanying condensed consolidated financial statements include the accounts of SOYO and SOYO Nevada. All significant intercompany accounts and transactions have been eliminated in consolidation. The condensed consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles.

Interim Financial Statements - The accompanying interim condensed consolidated financial statements are unaudited, but in the opinion of management of the Company, contain all adjustments, which include normal recurring adjustments, necessary to present fairly the financial position at March 31, 2006, the results of operations for the three months ended March 31, 2006 and 2005, and cash flows for the three months ended March 31, 2006 and 2005. The condensed consolidated balance sheet as of December 31, 2005 is derived from the Company's audited consolidated financial statements.

Certain information and footnote disclosures normally included in financial statements that have been prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission, although management of the Company believes that the disclosures contained in these condensed consolidated financial statements are adequate to make the information presented therein not misleading. For further information, refer to the consolidated financial statements and the notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2005, as filed with the Securities and Exchange Commission.

The preparation of financial statements in conformity with United States general accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Significant estimates primarily relate to the realizable value of accounts receivable, vendor programs and inventories. Actual results could differ from those estimates.

The results of operations for the three months ended March 31, 2006 is not necessarily indicative of the results of operations to be expected for the full fiscal year ending December 31, 2006.

Business - The Company sells products under three different product lines: 1) Computer Components and Peripherals 2) Consumer Electronics and 3) Communications Equipment and Services. The products are sold to distributors and retailers primarily in North, Central and South America.

Earnings Per Share - Statement of Financial Accounting Standards No. 128, "Earnings Per Share", requires presentation of basic earnings per share ("Basic EPS") and diluted earnings per share ("Diluted EPS"). Basic income per share is computed by dividing net income available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted income per share gives effect to all dilutive potential common shares outstanding during the period. Potentially dilutive securities consist of the outstanding shares of preferred stock.

As of March 31, 2006, potentially dilutive securities consisted of 2,948,342 shares of Class B Convertible Preferred Stock with a stated liquidation value of $1.00 per share that are convertible into common stock at fair market value, but not less than $0.25 per share.

As of March 31, 2006, 4,755,390 shares of common stock were issuable upon conversion of the Class B Convertible Preferred Stock based on the $0.62 per share conversion price.

As of March 31, 2005, potentially dilutive securities consisted of 1,000,000 shares of Class A Convertible Preferred Stock with a stated liquidation value of $1.00 per share that are convertible into common stock at fair market value, and 2,653,408 shares of Class B Convertible Preferred Stock with a stated liquidation value of $1.00 per share that are convertible into common stock at fair market value, but not less than $0.25 per share.

As of March 31, 2005, 4,248,149 shares of common stock were issuable upon conversion of the Class A Convertible Preferred Stock and the Class B Convertible Preferred Stock, consisting of 1,162,791 shares of common stock issuable upon conversion of the Class A Convertible Preferred Stock, based on the closing price of $0.86 per common share at March 31, 2005, and 3,085,358

shares of common stock issuable upon conversion of the Class B Convertible Preferred Stock, based on the $0.86 per share conversion price.

Comprehensive Income (Loss) - The Company displays comprehensive income or loss, its components and accumulated balances in its consolidated financial statements. Comprehensive income or loss includes all changes in equity except those resulting from investments by owners and distributions to owners. The Company did not have any items of comprehensive income (loss) during the three months ended March 31, 2006 and 2005.

Significant Risks and Uncertainties - The Company operates in a highly competitive industry subject to aggressive pricing practices, pressures on gross margins, frequent introductions of new products, rapid technological advances, continual improvement in product price/performance characteristics, and changing consumer demand.

As a result of the dynamic nature of the business, it is possible that the Company's estimates with respect to the realizability of inventories and accounts receivable may be materially different from actual amounts. These differences could result in higher than expected allowance for bad debts or inventory reserve costs, which could have a materially adverse effect on the Company's financial position and results of operations.

Stock-Based Compensation - Prior to January 1, 2006, the Company accounted for employee stock-based compensation using the intrinsic value method supplemented by pro forma disclosures in accordance with APB 25 and SFAS 123 "Accounting for Stock-Based Compensation" ("SFAS 123"), as amended by SFAS No.148 "Accounting for Stock-Based Compensation--Transition and Disclosures." Under the intrinsic value method, compensation cost is measured as the excess of, if any, of the market price of the Company's common stock at the date of grant, or at any subsequent measurement date, over the amount an employee must pay to acquire the stock. Such amounts are amortized as compensation expense over the vesting period of the related stock options. Under the intrinsic value method, the Company was not required to recognize stock-based compensation.

Effective January 1, 2006 the Company adopted SFAS 123R using the modified prospective approach and accordingly prior periods have not been restated to reflect the impact of SFAS 123R. Under SFAS 123R, stock-based awards granted prior to its adoption will be expensed over the remaining portion of their vesting period. These awards will be expensed under the accelerated amortization method using the same fair value measurements which were used in calculating pro forma stock-based compensation expense under SFAS 123. For stock-based awards granted on or after January 1, 2006, the Company will amortize stock-based compensation expense on a straight-line basis over the requisite service period, which is generally a three-four year vesting period.

On March 7, 2005, the Company registered its 2005 Stock Compensation Plan on Form S-8 with the Securities and Exchange Commission, registering on behalf of our employees, officers, directors and advisors up to 5,000,000 shares of our common stock purchasable by them pursuant to common stock options granted under our 2005 Stock Compensation Plan. The plan was approved by shareholder vote during a special meeting of shareholders on February 17, 2006.

On July 22, 2005, the Company issued 2,889,000 option grants to employees at a strike price of $.75. One third of those options will vest and be available for purchase on July 22, 2006, one third on July 22, 2007, and one third on July 22, 2008. As a result, the fair value of the options will be expensed between now and July 22, 2008. The grants will expire if unused on July 22, 2010.

The Company has calculated the fair value of each option granted to employees as sixty three cents (.63) based on the Black Scholes option pricing model.

As of March 31, 2006, employees have left the Company and forfeited 330,000 options. Therefore, the charge against earnings was calculated on the remaining 2,559,000 options.

For the three months ended March 31, 2006, the Company recorded stock-based compensation expense of $134,952 which reduced income from operations and net income. The cumulative effect of the change from intrinsic value to fair value method of accounting for stock-based compensation in the amount of $224,919 was also recognized and reduced net income. The impact on basic and diluted net income per share for the three months ended March 31, 2006 was $(0.01). SFAS 123R requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from initial estimates. Stock-based compensation expense was recorded net of estimated forfeitures for the three months ended March 31, 2006 such that expense was recorded only for those stock-based awards that are expected to vest. Previously under APB 25 to the extent awards were forfeited prior to vesting, the corresponding previously recognized expense was reversed in the period of forfeiture.

For the three month period ended March 31, 2006, the fair value of option grants is estimated on the date of grant utilizing the Black-Scholes option-pricing model with the weighted average assumption for options granted during 2005-2006, expected life of the option is 5 years, expected volatility of 146%, risk free interest rate of 4.04% and a 0% dividend yield on common stock. The weighted average fair value at the grant date for such option is $0.63 per option.

2. Short Term Loan

In October 2005, the Company borrowed $165,000 from an individual for working capital purposes. As of March 31, 2006, $65,000 of the loan had been repaid, and $100,000 was still outstanding.

3. Equity-Based Transactions

Effective December 30, 2003, SOYO Taiwan entered into an agreement with an unrelated third party to sell the $12,000,000 long-term payable due it by the Company. As part of the agreement, SOYO Taiwan required that the purchaser would be limited to collecting a maximum of $1,630,000 of the $12,000,000 from the Company without the prior consent of SOYO Taiwan. In substance, SOYO Taiwan forgave debt in an amount equal to the difference between the $12,000,000 and the value of the preferred stock issued in settlement of this debt. This forgiveness of debt was treated as a capital transaction. Payment from the third party was received by SOYO Taiwan in February and March 2004. An agreement was reached during the three months ended March 31, 2004 whereby 2,500,000 shares of Class B preferred stock would be issued by the Company to the unrelated third party in exchange for the long-term payable.

The Class B preferred stock has a stated liquidation value of $1.00 per share and a 6% dividend, payable quarterly in arrears, in the form of cash, additional shares of preferred stock, or common stock, at the option of the Company. The Class B preferred stock has no voting rights. The shares of Class B preferred stock are convertible, in increments of 100,000 shares, into shares of common stock based on the $1.00 stated value, at any time through December 31, 2008, based on the fair market value of the common stock, subject, however, to a minimum conversion price of $0.25 per share. No more than 500,000 shares of Class B preferred stock may be converted into common stock in any one year. On December 31, 2008, any unconverted shares of Class B preferred stock automatically convert into shares of common stock based on the fair market value of the common stock, subject, however, to a minimum conversion price of $0.25 per share. Beginning one year after issuance, upon ten days written notice, the Company or its designee will have the right to repurchase for cash any portion or all of the outstanding shares of Class B preferred stock at 80% of the liquidation value ($0.80 per share). During such notice period, the holder of the preferred stock will have the continuing right to convert any such preferred shares pursuant to which written notice has been received into common stock

13

without regard to the conversion limitation. The Class B preferred stock has unlimited piggy-back registration rights, and is non-transferrable.

The Company recorded the issuance of the Class B preferred stock at its fair market value on March 31, 2004 of $1,304,000, which was determined by an independent investment banking firm. The $10,696,000 difference between the $12,000,000 long-term payable and the $1,304,000 fair market value of the Class B preferred stock was credited to additional paid-in capital. The difference between the fair market value and the liquidation value of the Class B preferred stock is being recognized as an additional dividend to the Class B preferred stockholder, and as a reduction to earnings available to common stockholders, and will be accreted from April 1, 2004 through December 31, 2008.

5. Significant Concentrations

a. Customers

The Company sells to both distributors and retailers. Revenues through such distribution channels are summarized as follows:

	Three Months Ended March 31,			
	2006		2005	
Revenues				
Distributors	$ 4,479,959	38.8%	$ 2,821,181	71.2%
Retailers	7,068,228	61.2%	1,141,339	28.8%
	$11,548,187	100.0%	$ 3,962,520	100.0%

During the three months ended March 31, 2006 and 2005, the Company offered price protection to certain customers under specific programs aggregating $0 and $99,272, respectively, which reduced net revenues and accounts receivable accordingly.

Information with respect to customers that accounted for 10% or more of the Company's revenues is presented below.

During the three months ended March 31, 2006 and 2005, the Company had two customers that accounted for revenues of $4,213,370 and $1,673,160, equivalent to 36.5% and 42.2% of net revenues, respectively. The two customers were Shop at Home Network, LLC and E23 Inc.

b. Geographic Segments

Financial information by geographic segments is summarized as follows:

	Three Months Ended March 31,			
	2006		2005	
Revenues				
North America	$ 9,114,585	78.9%	$ 1,560,833	39.4%
Central and South America	2,205,222	19.1%	280,623	7.1%
Hong Kong	0		1,945,308	49.1%
Other locations	228,380	2.0%	175,756	4.4%
	$11,548,187	100.0%	$ 3,962,520	100.0%

c. Suppliers

Of the products the Company sold in 2005, no more than 39% of the products were produced by any one vendor. The Company is working to reduce that dependency and expects that no more than 20% of any products sold in 2006 will be produced by one vendor.

Through October 24, 2002, SOYO Nevada was a wholly-owned subsidiary of SOYO Taiwan (see Note 1). Subsequent to that date, SOYO Taiwan agreed to provide inventory to SOYO on an open account basis through December 31, 2005. Despite that commitment, SOYO Group purchased no products from SOYO Taiwan in 2006 or 2005.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Cautionary Statement Pursuant to Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995:

This Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2005 contains "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, including statements that include the words "believes", "expects", "anticipates", or similar expressions. These forward-looking statements include, but are not limited to, statements concerning the Company's expectations regarding its working capital requirements, financing requirements, business prospects, and other statements of expectations, beliefs, future plans and strategies, anticipated events or trends, and similar expressions concerning matters that are not historical facts. The forward-looking statements in this Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2005 involve known and unknown risks, uncertainties and other factors that could cause the actual results, performance or achievements of the Company to differ materially from those expressed in or implied by the forward-looking statements contained herein.

Background and Overview:

Historically, the Company has sold computer components and peripherals to distributors and retailers primarily in North, Central and South America. The Company operated in one business segment. A substantial majority of the Company's products were purchased from SOYO Taiwan pursuant to an exclusive distribution agreement effective through December 31, 2005, and were sold under the "SOYO" brand.

Effective October 24, 2002, Vermont Witch Hazel Company, Inc., a Nevada corporation ("VWHC"), acquired SOYO, Inc., a Nevada corporation ("SOYO Nevada"), from SOYO Computer, Inc., a Taiwan corporation ("SOYO Taiwan), in exchange for the issuance of 1,000,000 shares of convertible preferred stock and 28,182,750 shares of common stock, and changed its name to SOYO Group, Inc. ("SOYO"). The 1,000,000 shares of preferred stock were issued to SOYO Taiwan and the 28,182,750 shares of common stock were issued to certain members of SOYO Nevada

15

management. During October 2002, certain members of the management of SOYO Nevada also separately purchased 6,026,798 shares of the 11,817,250 shares of common stock of VWHC outstanding prior to VWHC's acquisition of SOYO Nevada, for $300,000 in personal funds. The 6,026,798 shares represented 51% of the outstanding shares of VWHC common stock. Accordingly, SOYO Taiwan and SOYO Nevada management currently own 34,209,548 shares of the 40,000,000 shares of the Company's common stock outstanding.

Subsequent to this transaction, SOYO Taiwan maintained an equity interest in SOYO, continued to be the primary supplier of inventory to SOYO, and was a major creditor. In addition, there was no change in the management of SOYO and no new capital invested, and there was a continuing family relationship between certain members of the management of SOYO and SOYO Taiwan. As a result, for financial reporting purposes, this transaction was accounted for as a recapitalization of SOYO Nevada, pursuant to which the accounting basis of SOYO Nevada continued unchanged subsequent to the transaction date. Accordingly, the pre-transaction financial statements of SOYO Nevada are now the historical financial statements of the Company.

Unless the context indicates otherwise, SOYO and its wholly-owned subsidiary, SOYO Nevada, are referred to herein as the "Company".

The Company's is a distributor of Computer Peripherals, Communications Equipment, and Consumer Electronics. SOYO Group's products have always been sold through an extensive network of authorized distributors to resellers, system integrators, and value-added resellers (VARs). These products are also sold through major retailers, mail-order catalogs and e-tailers to the consumers throughout North America, Latin America and around the world.

Through 2004, the Company was a distributor of computer products, a substantial portion of which were manufactured in Taiwan and China. Through SOYO Inc. the Company offered a full line of designer motherboards and related peripherals for intensive multimedia applications, corporate alliances, telecommunications and specialty market requirements. The product line also included basic bare bones PC motherboard systems, flash memory as well as small hard disk drives for corporate and mobile users, internal multimedia reader/writer and wireless networking solutions products for home and office (SOHO) users.

In 2004, the Company expanded its product offerings into new and higher margin segments. The offerings were divided into three areas: Computer, Peripherals, Communications Equipment, and Consumer Electronics. Throughout 2005 and the first quarter of 2006, these were the areas that produced revenues for the Company.

Financial Outlook:

As of March 31, 2006, the Company is reliant upon the cash flows from its operations. The Company does not have any external sources of capital, and no established credit facilities. In the past two years, the Company has borrowed funds from an officer, director, major shareholder and a private lender.

The Company is currently attempting to improve its financial condition and liquidity by exploring the availability of outside debt and equity financing; to the extent such funding is available under reasonable terms and conditions. Additionally, the Company is attempting to secure credit facilities that will

16

reduce the cost of purchasing inventory, provide better and cheaper terms on purchases and improve cash flow.

On March 28, 2005 the Company announced that an accredited investor, Ever-Green Technology (Hong Kong) Co., Ltd., purchased 500,000 unregistered shares of its common stock, $0.001 par value per share (the "Shares") and common stock purchase warrants to purchase 100,000 shares of its common stock exercisable at $1.50 per share at any time until March 22, 2008 (the "Warrants"). The total offering price was $500,000, which was paid in cash.

There can be no assurances that these measures will result in an improvement in the Company's operations or liquidity. To the extent that the Company's operations and liquidity do not improve, the Company may be forced to reduce operations to a level consistent with its available working capital resources. The Company may also have to consider a formal or informal restructuring or reorganization.

Critical Accounting Policies:

The Company prepared its condensed consolidated financial statements in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Management periodically evaluates the estimates and judgments made. Management bases its estimates and judgments on historical experience and on various factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates as a result of different assumptions or conditions.

The Company operates in a highly competitive industry subject to aggressive pricing practices, pressures on gross margins, frequent introductions of new products, rapid technological advances, continual improvement in product price/performance characteristics, and changing consumer demand.

As a result of the dynamic nature of the business, it is possible that the Company's estimates with respect to the realizability of inventories and accounts receivable may be materially different from actual amounts. These differences could result in higher than expected allowance for bad debts or inventory reserve costs, which could have a materially adverse effect on the Company's financial position and results of operations.

The following critical accounting policies affect the more significant judgments and estimates used in the preparation of the Company's condensed consolidated financial statements.

Vendor Programs:

Funds received from vendors for price protection, product rebates, marketing and training, product returns and promotion programs are generally recorded as adjustments to product costs, revenue or sales and marketing expenses according to the nature of the program. The Company records estimated reductions to revenues for incentive offerings and promotions. Depending on market conditions, the Company may implement actions to increase customer incentive offerings, which may result in an incremental reduction of revenue at the time the incentive is offered.

Accounts Receivable:

The Company recognizes revenue when persuasive evidence of an arrangement exists, delivery has occurred, the sales price is fixed or determinable, and collectibility is probable.

The Company records estimated reductions to revenue for incentive offerings and promotions. Depending on market conditions, the Company may implement actions to increase customer incentive offerings, which may result in an incremental reduction of revenue at the time the incentive is offered.

In order to determine the value of the Company's accounts receivable, the Company records a provision for doubtful accounts to cover probable credit losses. Management reviews and adjusts this allowance periodically based on historical experience and its evaluation of the collectibility of outstanding accounts receivable.

Inventories:

Inventories are stated at the lower of cost or market. Cost is determined by using the average cost method. The Company maintains a perpetual inventory system which provides for continuous updating of average costs. The Company evaluates the market value of its inventory components on a regular basis and reduces the computed average cost if it exceeds the component's market value. Inventories consist primarily of computer parts and components purchased from SOYO Taiwan.

Income Taxes:

The Company records a valuation allowance to reduce its deferred tax assets to the amount that is more likely than not to be realized. In the event the Company was to determine that it would be able to realize its deferred tax assets in the future in excess of its recorded amount, an adjustment to the deferred tax assets would be credited to operations in the period such determination was made. Likewise, should the Company determine that it would not be able to realize all or part of its deferred tax assets in the future, an adjustment to the deferred tax assets would be charged to operations in the period such determination was made.

Results of Operations:

Three Months Ended March 31, 2006 and 2005:

Net Revenues. Net revenues increased by $7,585,667 or 191%, to $11,548,187 in 2006, as compared to $3,962,520 in 2005. The increase in net revenues in 2006 as compared to 2005 was simple. During the first quarter of 2005 the Company had not yet begun selling the LCD televisions and monitors. The products had been ordered, but had not yet arrived. With very little inventory to sell, sales were scarce.

Gross Margin. Gross margin was $1,651,088 or 14.3% in 2006, as compared to $1,611,207 or 40.7% in 2005. Comparing the gross margin between the quarters is impractical, as the sales were generated from different products. In 2005, the Company was still selling computer parts only, with a smattering of VOIP sales. Additionally, the gross margin in 2005 contains $1,089,172 of income derived from "Prior Year's Purchases Discounts and Allowances settled in 2005". The gross margin in 2006 represents a mix of sales of all of the Company's product lines, which is relevant for future periods.

Sales and Marketing Expenses. Selling and marketing expenses decreased by $164,579 to $74,886 in 2006, as compared to $239,465 in 2005. The decrease is

due to the large decrease in marketing funds given to customers. In 2005, with the only sales coming from the highly competitive computer peripherals department, many co-op programs were necessary to fuel sales. In 2006, with the more diverse product lines, the Company is not participating in the same types of programs.

General and Administrative Expenses. General and administrative expenses increased by $551,021 to $1,484,994 in 2006, as compared to $933,973 in 2005. The increase is due to three factors: Increased attorney's fees dealing with the two lawsuits the Company is involved in, the costs of purchasing and testing the Company's new accounting software, and the SEC's requirement that the Company change to the fair value method of Accounting for Stock Based Compensation.

Provision for Doubtful Accounts. The Company recorded a provision for doubtful accounts of $50,000 in the three months ended March 31, 2006. The Company recorded a provision for doubtful accounts of $31,124 the three months ended March 31, 2005. The larger provision is due to the increased sales volume, increased receivables, and slightly greater average age of the receivables.

Depreciation and Amortization. Depreciation and amortization of property and equipment was $25,815 in 2006, as compared to $8,749 in 2005. The increase is due to the telephone lines purchased in China in 2005 now being depreciated.

Income from Operations. The income from operations was $15,393 for the three months ended March 31, 2006, as compared to income from operations of $397,896 for the three months ended March 31, 2005. The income from operations in 2006 equalled approximately two percent of gross sales, which the company believes is in line with expectations. The 2005 results included several hundred thousand dollars of prior years purchases and discounts, which inflated the number as compared to sales. Additionally, the 2006 number contains a charge of approximately $135,000 to comply with the requirements of SFAS 123R, Share-Based Payment, that the Company change to the fair value method of Accounting for Stock Based Compensation. Without this charge against earnings, income from operations would have been approximately $150,000.

Miscellaneous Income. Miscellaneous income was $4,531 for the three months ended March 31, 2006. There was no miscellaneous income in the three months ended March 31, 2005.

Interest Income. Interest income was $3,247 for the three months ended March 31, 2006. There was no interest income in 2005.

Interest Expense. Interest expense was $72,387 for the three months ended March 31, 2006. Interest expense was $11,221 in 2005. The large increase is due to the Company beginning to factor receivables to improve cash flow in the middle of 2005, and the switch of financing institutions. The Company paid $40,000 to the old financier to pay off minimum requirements, and has now switched to another financier with better coverage of the receivables.

Provision for Income Taxes. There was no provision for income taxes in 2006 or in 2005.

Net Income (loss). Net loss was $274,135 for the three months ended March 31, 2006, as compared to net income of $386,675 for the three months ended March 31, 2005. The net loss included approximately $360,000 of non cash expenses to comply with the requirements of SFAS 123R, Share-Based Payment, that the Company change to the fair value method of Accounting for Stock Based Compensation. Of

this amount, $224,919 represents cumulative effect of the change in accounting principle. Without this charge, net income would have been almost $90,000.

Financial Condition - March 31, 2006:

Liquidity and Capital Resources:

Effective December 30, 2003, SOYO Taiwan entered into an agreement with an unrelated third party to sell the $12,000,000 long-term payable due it by the Company. As part of the agreement, SOYO Taiwan required that the purchaser would be limited to collecting a maximum of $1,630,000 of the $12,000,000 from the Company without the prior consent of SOYO Taiwan. In substance, SOYO Taiwan forgave debt in an amount equal to the difference between the $12,000,000 and the value of the preferred stock issued in settlement of this debt. This forgiveness of debt was treated as a capital transaction. Payment from the third party was received by SOYO Taiwan in February and March 2004. An agreement was reached during the three months ended March 31, 2004 whereby 2,500,000 shares of Class B preferred stock would be issued by the Company to the unrelated third party in exchange for the long-term payable.

The Class B preferred stock has a stated liquidation value of $1.00 per share and a 6% dividend, payable quarterly in arrears, in the form of cash, additional shares of preferred stock, or common stock, at the option of the Company. The Class B preferred stock has no voting rights. The shares of Class B preferred stock are convertible, in increments of 100,000 shares, into shares of common stock based on the $1.00 stated value, at any time through December 31, 2008, based on the fair market value of the common stock, subject, however, to a minimum conversion price of $0.25 per share. No more than 500,000 shares of Class B preferred stock may be converted into common stock in any one year. On December 31, 2008, any unconverted shares of Class B preferred stock automatically convert into shares of common stock based on the fair market value of the common stock, subject, however, to a minimum conversion price of $0.25 per share. Beginning one year after issuance, upon ten days written notice, the Company or its designee will have the right to repurchase for cash any portion or all of the outstanding shares of Class B preferred stock at 80% of the liquidation value ($0.80 per share). During such notice period, the holder of the preferred stock will have the continuing right to convert any such preferred shares pursuant to which written notice has been received into common stock without regard to the conversion limitation. The Class B preferred stock has unlimited piggy-back registration rights, and is non-transferable.

The Company recorded the issuance of the Class B preferred stock at its fair market value on March 31, 2005 of $1,304,000, which was determined by an independent investment banking firm. The $10,696,000 difference between the $12,000,000 long-term payable and the $1,304,000 fair market value of the Class B preferred stock was credited to additional paid-in capital. The difference between the fair market value and the liquidation value of the Class B preferred stock is being recognized as an additional dividend to the Class B preferred stockholder, and as a reduction to earnings available to common stockholders, and will be accreted from April 1, 2004 through December 31, 2008.

Operating Activities. The Company utilized cash of $643,744 in operating activities during the three months ended March 31, 2006, as compared to $1,271,674 in operating activities during the three months ended March 31, 2005.

At March 31, 2006, the Company had cash and cash equivalents of $54,411 as compared to $828,294 at December 31, 2005. During the final few days of the quarter, the Company was informed that two big shipments totaling approximately $4,000,000 that were to be sent to customers were delayed. The customers needed to delay the receipt of the goods for business reasons. As a result, the Company was unable to sell the products before the end of the quarter, and unable to factor the invoices. This resulted in a severe cash shortage at quarter end.

The Company had working capital of $754,598 at March 31, 2006, as compared to working capital of $689,141 at December 31, 2005, resulting in current ratios of 1.04:1 and 1.04:1 at March 31, 2006 and December 31, 2005, respectively.

Accounts receivable decreased to $6,821,483 at March 31, 2006, as compared to $7,278,520 at December 31, 2005, a decrease of $457,037 or 6.3%. The Company's provision for doubtful accounts stood at $639,224 and $589,224 as of March 31, 2006 and December 31, 2005 respectively.

Inventories increased to $11,255,016 at March 31, 2005, as compared to $7,991,030 at December 31, 2005, an increase of $3,263,986 or 40.8%. During the final few days of the quarter, the Company was informed that two big shipments totaling approximately $4,000,000 that were to be sent to customers were delayed. The customers needed to delay the receipt of the goods for business reasons. As a result, the Company was unable to sell the product before the end of the quarter. The products were sold to customers during the second quarter.

Accounts payable increased to $16,930,908 at March 31, 2006, as compared to $13,977,579 at December 31, 2005, an increase of $2,953,329 or 21.1%, as a result of large inventory purchases during the quarter.

Accrued liabilities decreased to $347,509 at March 31, 2006, as compared to $1,287,108 at December 31, 2005, a decrease of $939,599. The large decrease is due to reductions in accruals for marketing expenses, RMA expenses and other accrued liabilities. The Company had large accruals over the year end, as the Company had very little experience selling the new products, and was unsure of the return or RMA rates. With the additional time that has passed and the additional experience, the Company is satisfied that the current accruals are sufficient.

Financing Activities. In October 2005, the Company borrowed $165,000 from an individual for working capital purposes. As of March 31, 2006, $100,000 is owed to that individual.

Principal Commitments:

A summary of the Company's contractual cash obligations as of March 31, 2006 is as follows:

		Payments Due By Period			
Contractual Cash Obligations	Total	Less than 1 year	Between 1-2 years	Between 3-5 years	After 5 years
Operating leases	$ 567,178	$ 212,692	$ 354,486	$ --	$ --
Short Term Loan	100,000	100,000	--	--	--
Total contractual cash obligations	$ 667,178	$ 312,692	$ 354,486	$ --	$ --

Off-Balance Sheet Arrangements:

At March 31, 2006, the Company did not have any transactions, obligations or relationships that could be considered off-balance sheet arrangements.

Commitments and Contingencies:

At March 31, 2006, the Company did not have any material commitments for capital expenditures.

Recent Accounting Pronouncements:

In May 2005, FASB issued SFAS No. 154, Accounting Changes and Error Corrections, a replacement of APB Opinion No. 20 and FASB Statement No. 3. SFAS 154 applies to all voluntary accounting principle changes as well as the accounting for and reporting of such changes. SFAS 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005.

SFAS 154 requires voluntary changes in accounting principle be retrospectively applied to financial statements from previous periods unless such application is impracticable. Changes in depreciation, amortization, or depletion for long-lived, non-financial assets are accounted for as a change in accounting estimate that is affected by a change in accounting principle, under the newly issued standard.

SFAS 154 replaces APB Opinion No. 20 and SFAS 3. SFAS 154 carries forward many provisions of Opinion 20 and SFAS 3 without change including those provisions related to reporting a change in accounting estimate, a change in reporting entity, correction of an error and reporting accounting changes in interim financial statements. The FASB decided to completely replace Opinion 20 and SFAS 3 rather than amending them in keeping to the goal of simplifying U.S. GAAP. The provisions of SFAS No. 154 are not expected to have a material effect on the Company's consolidated financial position or results of operation.

In December 2004, the FASB issued SFAS No. 153, "Exchanges of Nonmonetary Assets, an amendment of APB Opinion No. 29". SFAS 153 addresses the measurement of exchanges of nonmonetary assets. It eliminates the exception from fair value measurement for nonmonetary exchanges of similar productive assets in paragraph 21(b) of APB Opinion No. 29, Accounting forNonmonetary Transactions, and replaces it with an exception for exchanges that do not have commercial substance. SFAS 153 specifies that a nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange.

The exception under APB 29 required that some nonmonetary exchanges, although commercially substantive, be recorded on a carryover basis. SFAS 153 eliminates the exception to fair value for exchanges of similar productive assets and replaces it with a general exception for exchange transactions that do not have commercial substance--that is, transactions that are not expected to result in significant changes in the cash flows of the reporting entity.

SFAS 153 is effective on January 1, 2006. The adoption of SFAS 153 is not

expected to have an impact on the Company's consolidated financial statements or disclosures.

In December 2004, the FASB issued Statement of Financial Accounting Standards No. 123 (revised 2004), Share-Based Payment ("SFAS No. 123(R)") which replaces SFAS No. 123, Accounting for Stock-Based Compensation and supersedes APB Opinion No. 25, Accounting for Stock Issued to Employees. SFAS No. 123(R) requires that companies recognize all share-based payments to employees, including grants of employee stock options, in the financial statements. The cost will be based on the fair value of the equity or liability instruments issued and recognized over the respective vesting period of the stock option. Pro forma disclosure of this cost will no longer be an alternative under SFAS No. 123(R). SFAS 123(R) is effective for public companies at the beginning of the first fiscal year that begins after June 15, 2005.

Transition methods available to public companies include either the modified prospective or modified retrospective adoption. The modified prospective transition method requires that compensation cost be recognized beginning on the effective date, or date of adoption if earlier, for all share-based payments granted after the date of adoption and for all unvested awards existing on the date of adoption. The modified retrospective transition method, which includes the requirements of the modified prospective transition method, additionally requires the restatement of prior period financial information based on amounts previously recognized under SFAS No. 123 for purposes of pro-forma disclosures. The Company adopted SFAS No. 123(R) effective January 1, 2006.The Company adopted the modified prospective method. As a result, the Company recognized a charge against earnings of $134,952 for the three months ended March 31, 2006, and the cumulative effect on prior years of changing to the fair value method of $224,919.

In November 2004, the FASB issued SFAS No. 151, "Inventory Costs, an amendment of ARB No. 43, Chapter 4." SFAS 151 amends the guidance in ARB No. 43, Chapter 4, "Inventory Pricing," to clarify the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material (spoilage). Paragraph 5 of ARB 43, Chapter 4, previously stated that ". . . under some circumstances, items such as idle facility expense, excessive spoilage, double freight, and rehandling costs may be so abnormal as to require treatment as current period charges. . . ." SFAS 151 requires that those items be recognized as current-period charges regardless of whether they meet the criterion of "so abnormal." In addition, SFAS 151 requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities.

SFAS 151 is effective on January 1, 2006. Earlier application is permitted for inventory costs incurred beginning January 1, 2005. The provisions of SFAS 151 shall be applied prospectively. The adoption of SFAS 151 is not expected to have an impact on the Company's consolidated financial statements or disclosures.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company does not have any market risk with respect to such factors as commodity prices, equity prices, and other market changes that affect market risk sensitive investments.

As the Company's debt obligations at March 31, 2006 are primarily short-term in nature and non-interest bearing, the Company does not have any risk from an

increase in interest rates. However, to the extent that the Company arranges new interest-bearing borrowings in the future, an increase in current interest rates would cause a commensurate increase in the interest expense related to such borrowings.

The Company does not have any foreign currency risk, as its revenues and expenses, as well as its debt obligations, are denominated and settled in United States dollars.

ITEM 4. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures:

In conjunction with the audit of the Company's financial statements for the years ended December 31, 2003 and 2004, the Company's Chief Executive Officer and its Chief Financial Officer reviewed and evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e) and 15d-15(e)), which are designed to ensure that material information the Company must disclose in its reports filed or submitted under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), is recorded, processed, summarized and reported on a timely basis, and have concluded, based on that evaluation, that as of such dates, the Company's disclosure controls and procedures were not adequate. In addition, the Company's automated financial reporting systems are overly complex, poorly integrated and inconsistently implemented.

The Company's Chief Executive Officer and Chief Financial Officer arrived at this conclusion based on a number of factors, including that the Company's system of internal control during 2003 and 2004 did not: (1) properly record accounts payable to vendors for purchases of inventory, (2) did not properly record adjustments to inventory per the general ledger to physical inventory balances, (3) did not properly record inventory adjustments to the lower of cost or market using the average inventory method, (4) did not periodically reconcile the Company's main bank account between August 2003 and December 2003, (5) did not have adequate controls over interim physical inventory procedures, and (6) did not generate timely and accurate financial information to allow for the preparation of timely and complete financial statements. The Company did not have an adequate financial reporting process because of the aforementioned material weaknesses, including the difficulty in identifying and assembling all relevant contemporaneous documentation for ongoing business transactions, and significant turnover in the Company's financial staff. In addition to the foregoing, a former employee withheld information from the auditor during the 2003 audit. Accordingly, the Company's Chief Executive Officer and Chief Financial Officer concluded that there were significant deficiencies, including material weaknesses, in the Company's internal controls over its financial reporting at the end of the fiscal period ended December 31, 2003.

In view of the fact that the financial information presented in the 2003 annual report was prepared in the absence of adequate internal controls over financial reporting, the Company devoted a significant amount of time and resources to the analysis of the financial information and documentation underlying the financial statements contained in this annual report, including the related interim financial statements, resulting in the restatement of certain interim financial statements. In particular, the Company reviewed all significant account balances and transactions underlying the financial statements to verify the accuracy of the financial statements contained in the 2003 annual report.

24

When the Company's senior management realized that there were significant deficiencies, including material weaknesses, in our 2003 internal control over financial reporting, we retained outside advisors to assist the Company's financial staff in preparing the Company's financial statements, including the restated interim periods

To address these weaknesses, the Company took the following corrective actions:

>> The Company hired a new Accounting Manager, then replaced the Accounting Manager with a more qualified candidate. That employee recently left the Company to return overseas for a family emergency. The employee will not be returning to the Company, which means that as of March 31, 2006, the Company was operating without an Accounting Manager or Controller. While the Company searched for a replacement, the Company retained a financial consultant and former CPA to oversee the day to day management of the accounting department. The Company has recently added additional personnel to complete the day to day accounting tasks.

In light of the foregoing, management took the following actions to rectify the deficiencies as described above.

>> Management hired experts to assist with the financial reporting required, and to train Company employees to perform such tasks in the future.

>> Management hired experts to assist in the evaluation and implementation of new accounting software. The evaluation was completed, and the software has been paid for. The software is currently being tested and will be installed and operational during the second quarter of fiscal year 2006.

In conjunction with the audit of the Company's financial statements for the year ended December 31, 2005, the Company's Chief Executive Officer and its Chief Financial Officer reviewed and evaluated the corrective actions listed above. The officers believed that such corrective actions minimize the risk of material misstatement, but the corrective actions continued to have significant deficiencies.

As of May 15, 2006, the Company has hired an Accounting Manager and additional finance personnel. The Chief Executive Officer and the Chief Financial Officer are satisfied that with the personnel in place, and with the additional efforts of the Financial Consultant/ CPA, that the books and records portray a completely accurate picture of the Company's financial position and that all transactions are being captured and reported as required. The Company believes that once the new software is installed and operational, and the new Accounting Manager is trained, all significant deficiencies will have been addressed and corrected.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

On August 2, 2004, a lawsuit was filed in California Superior Court entitled Gerry Normandan. et al, v. SOYO Inc. Case No. RCV 082128. The case seeks class action status and alleges defects in motherboards which Soyo distributes, and that the Company misrepresented and omitted material facts concerning the motherboards. The plaintiff seeks restitution and disgorgement of all amounts

obtained by defendant as a result of alleged misconduct, plus interest, actual damages, punitive damages and attorneys' fees. The Company is vigorously defending the lawsuit and believes that it will be resolved with no material adverse effect on the Company.

On April 14, 2005 a lawsuit was filed in Superior Court of the State of California, County of San Bernardino, entitled Afshin Pourvajdi v. SOYO Group, Inc., Nancy Chu and various Doe defendants. Case RCV 086992. The complaint alleges causes of action for: 1) Double damages for violation of labor code Section 970; 2) Misrepresentation; 3) Intentional Infliction of Emotional Distress; 4) Breach of Contract. The prayer for relief in the Complaint seeks damages of no less than $200,000 on the first and second causes of action, plus an unspecified amount of punitive damages and an unspecified amount of general and punitive damages on the third cause of action and an unspecified amount of general and punitive damages on the fourth cause of action. Plaintiff also seeks to recover all costs and attorney fees. The case arises from a consultant who worked briefly for the Company in 2004 and whose contract was not renewed. The Company expects the case to be settled during the second quarter of 2006. The Company will update shareholders as to the status of the case as soon as a definitive outcome is reached.

There are no other legal proceedings that have been filed against the Company.

None of the Company's directors, officers or affiliates, or owner of record of more than five percent (5%) of its securities, or any associate of any such director, officer or security holder, is a party adverse to the Company or has a material interest adverse to the Company in reference to pending litigation.

ITEM 1A: RISK FACTORS

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, "Item 1A. Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2005, which could materially affect our business, financial condition or future results. The risks described in our Annual Report on Form 10-K are not the only risks facing our Company. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

ITEM 2. CHANGES IN SECURITIES, USE OF PROCEEDS AND ISSUER PURCHASES OF EQUITY SECURITIES

None

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

On March 7, 2005, the Company registered its 2005 Stock Compensation Plan on Form S-8 with the Securities and Exchange Commission, registering on behalf of our employees, officers, directors and advisors up to 5,000,000 shares of our common stock purchasable by them pursuant to common stock options granted under

our 2005 Stock Compensation Plan. The plan was approved by shareholder vote during a special meeting of shareholders on February 17, 2006.

ITEM 5. OTHER INFORMATION

None

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

A list of exhibits required to be filed as part of this report is set forth in the Index to Exhibits, which immediately precedes such exhibits, and is incorporated herein by reference.

(b) Reports on Form 8-K

Three Months Ended March 31, 2006:

None

27

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

SOYO GROUP, INC.

(Registrant)

DATE: May 15, 2006

By: /s/ Ming Tung Chok
Ming Tung Chok
President and Chief Executive Officer

DATE: May 15, 2006

By: /s/ Nancy Chu
Nancy Chu
Chief Financial Officer

DATE: May 15, 2006

By /s/ Paul F. Risberg

	Name: Paul F. Risberg Title: Director
DATE: May 15, 2006	By /s/ Chung Chin Keung

	Name: Chung Chin Keung Title: Director
DATE: May 15, 2006	By /s/ Zhi Yang Wu

	Name: Zhi Yang Wu Title: Director

INDEX TO EXHIBITS

Exhibit Number	Description of Document
31.1	Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 - Ming Tung Chok
31.2	Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 - Nancy Chu
32	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 - Ming Tung Chok and Nancy Chu