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SOYO GROUP INC  
Form 10-K/A  
August 07, 2007

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-K/A

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 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 if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

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

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the past 90 days. Yes [X] No [ ]

Check if disclosure of delinquent filers in response to Item 405 of Regulation S-K (ss.229.405 of this chapter) is not contained in this form, and no disclosure will be contained to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [X]

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 " in Rule 12b-2 of the. (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

The aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was sold, or the average bid and asked price of such common equity, as of March 30, 2007 was \$27,454,286, based on the closing bid price of \$0.56 per share on March 30, 2007.

As of August 6, 2007, there were 49,039,156 shares Outstanding.

Documents Incorporated by Reference: None

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### Explanatory Note

Soyo Group, Inc. (the "Company") is filing this Amendment No. 1 to its Annual Report on Form 10-K for the year ended December 31 2006 (the "December 31, 2006 10-K"), which was originally filed on March 30, 2007. This Amendment No. 1 is being filed to restate the Company's financial statements for the year ended December 31 2006, which understated current liabilities and current assets.

The Company is restating its previously issued 2006 consolidated financial statements for the following reasons: error in recognition of accounts receivable sold with recourse and change in classification of deferred income tax assets and deposits.

In 2006, the Company sold its accounts receivable to Accord Financial Services with recourse. In accordance with generally accepted accounting principles, the transaction should be accounted for as a secured borrowing. During the year, the Company received proceeds of \$15,611,928 from the sale of accounts receivable of which \$12,023,525 had been paid as of yearend. As of December 31, 2006, the outstanding balance of \$3,588,,403 is reported as business loan in the restated consolidated balance sheet.

The Company also reclassified its deferred income tax assets and deposits to current assets as the deferred income tax assets relate to temporary differences arising from current assets, and the deposits pertain to deposits on inventory in transit.

This Amendment No. 1 does not reflect events occurring after the original filing of the Company's December 31, 2006 10-KSB, and does not update or modify the disclosures therein in any way other than as required to reflect the amendment described above.

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## PART I

### ITEM 1. BUSINESS.

When used in this Form 10-K, the words "expects," "anticipates," "estimates" and similar expressions are intended to identify forward-looking statements. Such statements are subject to risks and uncertainties, including those set forth below under "Risks and Uncertainties," that could cause actual results to differ materially from those projected. These forward-looking statements speak only as of the date hereof. We expressly disclaim any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained herein to reflect any change in our expectations with regard thereto or any change in events, conditions or circumstances on which any statement is based. This discussion should be read together with the financial statements and other financial information included in this Form 10-K.

#### Company History

SOYO Group, Inc. formerly Vermont Witch Hazel Company, Inc., a Nevada corporation (the "Company"), was incorporated on August 3, 1994 in the State of Vermont. For seven years, the Company created and marketed skin care and pet care products. The Company manufactured and distributed a line of witch hazel

based natural, hypoallergenic soaps, cleansers and other skin aids.

On December 3, 2001, the Company transferred all its net assets and business to its wholly owned subsidiary, The Vermont Witch Hazel Co., LLC, a California limited liability company which had been formed in October 2001. Also, the Company's board of directors declared a dividend of all of the Company's interest in the LLC to be distributed to the Company's shareholders of record on December 10, 2001. Each shareholder received one member unit in the LLC for each share of common stock held of record by the shareholder.

On December 27, 2001, pursuant to a stock purchase agreement dated December 27, 2001, Kevin Halter Jr. purchased 6,027,000 shares of the Company's common stock from Deborah Duffy representing approximately 51% of the Company's issued and outstanding shares of common stock. Simultaneously with the purchase, the current officers and directors of the Company, namely, Deborah Duffy, Rachel Braun and Peter C. Cullen, resigned and the following three persons were elected to replace them: Kevin Halter Jr., President and Director, Kevin B. Halter, Secretary, Treasurer and Director and Pam Halter, a Director.

On October 8, 2002, the Company changed its domicile from the State of Vermont to the State of Nevada.

On October 24, 2002, pursuant to the terms of a Reorganization and Stock Purchase Agreement ("Reorganization Agreement") dated as of October 15, 2002, the Company acquired (the "Acquisition") all of the equity interest of SOYO, Inc., a Nevada corporation ("SOYO Nevada" or "SOYO Group"), which was a whollyowned subsidiary of SOYO Computer, Inc., a Taiwan company ("SOYO Taiwan"). The Acquisition involved several simultaneous transactions which are set forth below.

1. Mr. Ming Tung Chok ("Ming") and Ms. Nancy Chu ("Nancy") purchased jointly 6,026,798 shares of the Company's common stock for \$300,000 from Kevin Halter Jr., a controlling shareholder of the Company, thereby making Ming and Nancy the majority shareholders of the Company.

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2. The Company issued 1,000,000 shares of Class A Convertible Preferred Stock, par value \$0.001, with a \$1.00 per share stated liquidation value to SOYO Taiwan in exchange for all of the outstanding equity interest in SOYO Group, Inc.
3. The Company issued 28,182,750 shares of common stock, par value \$0.001, to Ming and Nancy as part of the acquisition.
4. Kevin Halter Jr. resigned from his position as President and Director, Kevin B Halter resigned from his position as Secretary, Treasurer and Director and Pam Halter resigned from her position as Director. Effective October 25, 2002, Nancy, Ming and Bruce Nien Fang Lin began serving their terms as directors of the Company. These newly elected directors then appointed the following persons as officers:

| Name           | Title                              |
|----------------|------------------------------------|
| Ming Tung Chok | President, Chief Executive Officer |
| Nancy Chu      | Chief Financial Officer            |
| Nancy Chu      | Secretary                          |

Bruce Nien Fang Lin resigned and left the Company in July 2003.

The consideration for the Acquisition was determined through arms length negotiations and a Form 8-K was filed on October 30, 2002, as amended by a Form 8-K/A filed on December 20, 2002. On November 15, 2002, the Company changed its name from Vermont Witch Hazel Company, Inc. to SOYO Group, Inc.

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

Through October 24, 2002, the Company had only nominal assets and liabilities and no current business operations. As a result of the Acquisition, the Company continued the business operations of SOYO Nevada, which are described here.

SOYO Inc. was incorporated in Nevada on October 22, 1998.

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 the small office and home office (SOHO) market segment.

In 2004, the Company expanded its product offerings into new and higher margin segments. The offerings were divided into three areas: Computer Components and 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). SOYO's distribution network also includes product sales through major retailers, mail-order catalogs and e-tailers to the consumers

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throughout North America and Latin America.

In 2006, SOYO embarked on many new marketing and product programs including the launch of its Specialty Displays Division to focus effort on display sales and distribution and to promote the newly acquired GoVideo™ brand license integration into the SOYO product portfolio. SOYO was also able to expand its presence through distribution in the retail channels of Walmart.com, Samsclub.com, ShopNBC.com, Target.com, eCOST.com, direct2own.com and BDILaguna which now carry various SOYO product lines. In parallel with these efforts, SOYO has continued development on its own direct to consumer eStores with the goal of having all of SOYO's products available for direct purchase.

The company also had several new product introductions including dual screen 17" and 19" monitors, the "FreeStyler" Bluetooth Stereo Headphone and Transmitter Combo and the U201 USB Phone.

### PRODUCTS

SOYO Group, Inc. is the exclusive provider of SOYO branded products in the US and Latin America and actively promotes the SOYO brand in these regions. In addition, SOYO distributes many other electronic products and brands; some of these are licensed such as Go Video and others created by SOYO. On April 5, 2006, SOYO announced that it entered into a two year agreement with Opta Corporation for the use of the GoVideo(R) brand for distribution of SOYO LCD and plasma TV, computer monitors and rear and front screen projectors in the United States and Canada. SOYO is continually exploring branding opportunities with other potential partners. Some brands that SOYO currently distributes include the following:

|            |            |         |
|------------|------------|---------|
| SOYO       | SlimEX     | Bay One |
| GoVideo(R) | Cigar      | Atlas   |
| Sage       | FreeStyler | Dymond  |
| z-Connect  | Dragon     |         |

SOYO pays GoVideo a \$75,000 royalty per quarter for use of the GoVideo name and trademark. There are no licensing fees associated with any of the other brands listed above.

All of the products available to SOYO customers fall into three major product groups: Consumer Electronics, Computer Peripherals and Communications.

#### Consumer Electronics Products

In 2005, SOYO Group, Inc. entered the consumer electronics market which then accounted for over 30% of its sales. In 2006, this product category accounted for nearly 46% of sales.

#### Home Entertainment Flat Screen Televisions

SOYO's Ultra Slim flat-panel, HD-Ready LCD TV's range in size from 20-inch at 640 x 480 resolution to 47-inch at 1920 x 1080 resolution and are promoted under the SOYO and GoVideo brand names. The products offer a wide range of multimedia entertainment options, including broadcast, cable and satellite television programming, as well as DVD and VHS movies, video and online gaming, and the capability of surfing the Internet or acting as a display for a PC. Incorporating advanced imaging technology features such as 3:2 pull down, progressive scan and a digital 3D comb filter that bring you larger, clearer pictures, the Atlas LCD TV features two removable 10-watt speakers that deliver

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stereo surround sound. SOYO offers these products under the Dymond, Onyx, Crystal, and Atlas product lines.

### Bluetooth Wireless Headphone

The FreeStyler Bluetooth Headset product line is available in stereo and single ear versions. Supported by Bluetooth 1.1V with 2402~2480MHz frequency range, FreeStyler provides up to 10 meter operation range hands free, and its auto pairing and authentication function allows users to connect to their cellular phone and PDA wirelessly. With 4~6 hours talk time and 200 hours standby time, the 120mA 3.7V rechargeable battery requires 1.5~2.0 hours charging time.

### Furniture and Cabling

Most of SOYO's large flat panel TV screens will need to either be wall mounted or stood on pedestal furniture. To that end, SOYO designed the Pro-Series line

of TV wall mounting hardware. Measuring 2-5/8" thick the UL listed mountings are an ultra-slim, commercial grade system that can support screen sizes up to 60" with a 15(degree) tilt. SOYO also offers a new line of pedestal furniture offerings under the Le Vello series.

For connectivity to flat panel TV's, SOYO offers cabling solutions under the Dragon branded product line featuring 24 Karat gold contacts.

### Computer Components and Peripherals

#### Motherboards/Bare Bones Systems

The motherboard, which is the physical arrangement in a computer that contains the computer's basic circuitry and components, has been an integral part of most personal computers for more than twenty years. SOYO's Bare Bones System product solution is the basis for any computer system and is offered in AMD and Intel platform configurations. Of the more than 300 motherboard products that SOYO has sold in the past there remain a few active products in this category as well as ongoing support for the install base. SOYO now focuses on specialty markets for its motherboard systems.

#### Portable Storage Devices and Connectivity

The SlimEx 20GB and 40GB USB 2.0 Hard Drives are designed for desktop and laptop users who need high capacity portable storage in an ultra-small package. Large graphics and audio files are quickly displayed, copied or transported to any USB Ported computer. Incorporating a 1.8-inch hard disk from Toshiba, the Slim Drives measure just 3.9" x 2.4" x 0.4" (LWH) and weigh only 2.85 oz. The Slim Drives fit easily into a pocket, purse or briefcase for convenient travel and leave a small footprint on the desktop. Compatible with both PC and Macintosh operating systems, the SlimEx's USB 2.0 cable delivers fast transfer rates of up to 480Mbps and does not require any external power supplies or batteries.

Flash memory is a specialized type of memory component used to store user data and program code. It retains such information even when the power is off. Although flash memory is currently used predominantly in mobile phones and PDAs, it is also found in common consumer products, including MP3 music players, handheld voice recorders and digital answering machines, as well as industrial products. Portable flash memory has assumed many various forms over time. To address this growing product segment, SOYO currently offers a 12-in-1, 9-in-1 and 6-in-1 flash media reader / writer system under the SOYO and BayOne(R) product lines. With both internal and external system configurations available,

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these products allow for connectivity of multiple devices to computers and the ability to download digital photos, video, MP3 music or synchronize with handheld devices all at the same time. The multiple memory reader/writer slots can be used simultaneously. The systems are designed to be universally compatible with all CPU systems and external devices.

Other connectivity devices contained in this product category include TechAID hardware debug cards and PlayStation to PC joystick game pad converters.

### LCD Monitors

Under the Dymond, SOYO and GoVideo brand names, SOYO offers a complete line of LCD monitors for the PC market. From dual screen 19" to single screen 15.4" systems, SOYO products incorporate TFT (Thin Film Transistor) display technology

in a compact design that frees up desk space. Designed to provide a display solution for a wide variety of applications at the office, home or school, the SXGA (Super Extended Graphics Array) technology delivers text and images to assist in creating spreadsheets and reports, writing emails, preparing presentations, watching movies, playing games, or surfing the Internet.

### Communications Equipment

Launched in November 2004, the Soyo "Z-Connect" family of Voice over IP products and services includes an IP phone, a USB Skype phone, routers, adapters and two versions of the gateway, delivering VoIP capabilities with zero set-up fees, zero monthly fees, zero service contracts, zero configuration and zero hidden charges. All hardware is SOYO branded.

The company is also offering DID numbers for the Z-Connect family of products, allowing calls to be received from any other phone over any IP network or through the PSTN, and also offers the SOYO SAGE Smart Calling Card which offers consumers cost savings on long-distance calls. Through a strategic agreement with China Unicom USA Corporation, a division of China Unicom Ltd. (NYSE: CHU), SOYO uses its Public Service Telephone Network and Voice over Internet Protocol network to give users the ability to dial and receive local, long distance, and international calls.

Due to other opportunities in other key product sectors, relative profitability indicators and alternate strategic direction of the business in general, SOYO is decreasing its focus on the communication equipment market.

### PRODUCTION

SOYO Group does not produce the components that it distributes. Approximately 80% of SOYO Group, Inc.'s products are supplied by companies located in Taiwan and China. During 2006, no more than 44% of the products distributed by the SOYO Group were supplied by a third party vendor. SOYO Group, Inc is establishing new partnerships with other OEM manufacturers in the North America and Asia Pacific Regions in order to provide innovative products for consumers.

### TRANSPORTATION AND DISTRIBUTION

SOYO is primarily an electronics importer and distributor. As the majority of SOYO products originate in the Far East (Taiwan and China) SOYO adds value to the product chain by connecting these products with numerous distributors and retailers across North America. Products are bulk shipped via sea cargo carriers through US ports, cleared through customs and are freighted in to SOYO



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distribution centers to be ultimately sent on to distributors and retailers.

This process usually takes 6 to 8 weeks. To this end, SOYO has built up a logistics team that is able to provide product through this channel. Any deviation from this planned routine will typically increase product costs. Deviations from the normal course of transit such as dock worker strikes, increases in fuel costs, expedited delivery times, customs delays, shipment damage, lost cargo and other unforeseen issues can result in unsatisfied customers.

As all product transportation and movement activities are dependent on fuel this commodity can significantly affect the costs of SOYO's goods from origination through to final destination and continuing with shipping on returned goods under the S.A.F.E. program. It is unlikely that any short run increase in fuel prices can be passed along to consumers. Long term increases in fuel costs

eventually will be passed along to distributors and consumers in the form of increased prices or transportation surcharges.

### MARKETING AND SALES

SOYO Group, Inc. has a network of sales offices to service its customers' needs, from prompt order processing to after-sales customer care. SOYO Group, Inc.'s primary markets are North and Latin America. SOYO Group, Inc. also sells products in other markets such as the United Kingdom, Europe, Far East Asia and South Africa, through local preferred distributors and resellers.

SOYO Group, Inc.'s principal sales strategy targets three main markets: (1) end-user consumers; (2) small business users; and (3) small office / home users or SOHO's. To reach target customers, SOYO Group, Inc. sells its products through a wide range of sales channels including national distributors, such as A.S.I. and D&H Distributing, along with regional distributors that specialize in promoting our products to resellers, e-tailers, system builders and other small retailers. To reach end-user consumers and small business users, SOYO Group, Inc. partners with major electronic chain retail stores and mail-order catalogs throughout the continental U.S.A. and Canada including Best Buy Co., Inc., CompUSA, Office Depot, Fry's Electronics, MicroCenter and TigerDirect (a subsidiary of Systemax, Inc.). In 2006, SOYO substantially increased its presence in Canada through the addition of Wal-Mart Canada as a reseller of the SOYO product line.

For the Latin American market, system builders and value-added resellers (VAR) are the primary targets. To reach these customers, SOYO Group, Inc. uses an extensive network of international, national and regional distributors. There are sales offices in Sao Paulo, Brazil, which offer local technical support and return authorization to better service customers in both Brazil and Argentina. As of December 31, 2006, approximately 18% of the SOYO Group's sales and revenues were generated from the Latin American market.

Within the three segments that SOYO distributes product in, namely, communications, consumer electronics and computer peripherals, both B2B (business to business) marketing tactics (such as computer motherboards) and B2C (business to consumer) marketing tactics (such as LCD TV's) are required. In the past, product promotion was primarily done at the retailer level and not at SOYO's level (the distributor level). Typically, big box retailers will hold back some of the product price to cover these marketing costs at their level. This is commonly referred to as Market Development Funding (MDF) or Marketing Cooperation Fees (COOP).

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Moving forward, SOYO is altering its marketing strategy for its brands to assume a more direct level in the promotion role. Many of the consumer electronic products distributed by SOYO are targeted at the young male demographic. Specifically, the 18-34 year old males, who are early adopters of technology and are likely to convey their opinions on products to others and influence subsequent purchase decisions in other parties. In the past, common effective roads to this demographic were in television commercials and print advertising. Recently, technological progressions which allow for the avoidance of advertisements and the internet has caused this demographic to become much more challenging to reach. Because of this, embedded marketing techniques are now being employed to reach this sought after demographic. These techniques include sports sponsorships whereby the message or brand is advertised in the action such as wearing a brand name or product identifier on clothing. Other techniques include placing advertisements in video games, placing product and brand names in movies and programming, advertising on key web sites, etc.

In pursuit of this alternative strategy with respect to brand promotion, SOYO has recently begun to sponsor Mixed Martial Arts Athletes. On October 2, 2006, SOYO sponsored Eric "Big E" Pele in his Bodog fight against Antonio Silva. SOYO has seen benefits from this activity in the form of increased traffic on its web sites. Mixed Martial Arts is unique in that it is now starting to move into mainstream sports in North and Latin America and is becoming as popular as or more popular than boxing by some estimates. Due to its relative infancy however, sponsorship in the MMA arena is currently very cost favorable to the sponsors. The fan base falls well within one of SOYO's target demographics and responds positively to brand promotions. SOYO has chosen a variable approach to sponsorship to mitigate the risks associated with sponsoring a single athlete.

These actions mark a substantial change in SOYO's role with respect to marketing and brand promotion yet is in line with a new strategic direction of building stronger brand recognition and building the quality of the SOYO product portfolio. SOYO intends to build on these early promotional experiences in the years to come and create a name and product line that can compete effectively at a higher level in the competitive hierarchy.

Other advertising outlets that SOYO will engage in for the consumer side include internet, periodicals and other sports related advertising. On the resale side, the internet, trade journals, and trade show attendance will be utilized to promote the brand and acquire key industry contacts.

SOYO currently also engages in some trade show activity. The largest of these events is the Consumer Electronics Show. Some others include the Custom Electronics Design and Installation Association [www.cedia.net](http://www.cedia.net) and Retail Vision [www.retailvision.com](http://www.retailvision.com). CUSTOMERS

The primary customer base is in North America, where the products have long been recognized for premium quality and competitive prices. SOYO Group, Inc. also has a broad customer base in Latin America.

SOYO Group, Inc. also has an ancillary base of customers in the United Kingdom, Europe, Asia and South Africa, which are serviced through preferred relationships with independent distributors local to those markets.

SOYO is continually evolving to meet the needs of its customer base and to resonate well with them. SOYO has recognized the 18-34 year old demographic as one such key group that we are reaching out to.

The following table shows all customers that accounted for more than 10% of

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Company sales in a given year:

| Year end | Key Customer                                  | Revenues      | % of Net Revenue |
|----------|---|---------------|------------------|
| 2006     | Not applicable                                | \$ -          | -                |
| 2005     | E23   | \$ 13,552,324 | 35%              |
| 2004     | SYX Distribution, Inc.<br>a.k.a. Tiger Direct | \$ 8,591,711  | 26%              |
| 2003     | SYX Distribution, Inc.<br>a.k.a. Tiger Direct | \$ 9,943,855  | 32%              |

### SUPPLIERS

From the Company's inception through December 31, 2003, over 80% of the products sold were produced by SOYO Taiwan. In 2004, the Company went through a partial reorganization, changing the sales mix. The decision was made to focus more on peripherals, VoIP, and other products, while deemphasizing sales of hardware and motherboards, which are much more mature markets. As a result, the Company significantly reduced its reliance on SOYO Taiwan.

During 2006, no more than 44% of the products distributed by the SOYO Group were supplied by a third party vendor. SOYO Group, Inc is establishing new partnerships with other OEM manufacturers in the North America and Asia Pacific Regions in order to provide innovative products for consumers.

In continuing efforts to work with and leverage its supply base, SOYO entered into an agreement with GE Capital in 2006 whereby GE guarantees payment to GE approved vendors thereby facilitating larger orders, decreasing risk and allowing SOYO to seamlessly finance these transactions.

### REGULATIONS

SOYO Group, Inc. is subject, to various laws and regulations administered by various state, local and international government bodies relating to the operation of its distribution facilities. SOYO Group, Inc. believes that it is in compliance with all governmental laws and regulations related to its products and facilities, and it does not expect to make any material expenditure in 2007 with respect to compliance with any such regulations.

### COMPETITION

With the wide range of product offerings, SOYO Group, Inc. competes with a large number of small and well-established companies that produce and distribute products in all categories.

SOYO competes with many companies that import, distribute and act as OEM's. However, there are few companies that follow SOYO's business methods overall as most of the companies acting as OEM's spend significantly on R&D whereas SOYO relies upon its suppliers for such services.

Among those that SOYO competes with directly in the marketplace in the consumer electronics industry include AU Optronics, LG.Philips LCD, Syntax Brilliant, JVC, LG Electronics, Panasonic, Philips, Samsung, Sharp, Sony, Thompson, and Toshiba. The primary product offering common among this group is LCD TV's which account for a substantial portion of SOYO sales. Most of the competition in this product line pivots around price point and brand identity and to a lesser extent, features. Because of this, industry gross margins experience downward pressure.

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Secondary product offerings such as furniture are substantially less competitive and offer the opportunity for product differentiation and better margins.

Some computer component competitors include Dell, Hewlett-Packard, Gateway, and ViewSonic, which can compete in multiple product categories including the motherboard and computer monitors. Unlike LCD TV's however, computer monitors offer more favorable margins. Some other computer component competitors include Abit, Asus, Gigabyte, MSI, Daewoo, SanDisk, Lexar Media and SimpleTech which

compete in the other product categories.

Some communications competitors include Vonage, Packet8 and Net2Phone which offer communications packages, services and equipment in the VoIP and or calling card arenas. Competition in this sector is also very robust as it is very difficult to differentiate products or services.

### EMPLOYEES

As of March 31, 2007, the Company employed thirty six (36) people at its headquarters in Ontario, California. The Company also employs outside consultants as needed to meet business objectives.

### ITEM 1A. RISK FACTORS

In addition to the other information set forth in this report, you should carefully consider the following factors which could materially affect our business, financial condition or future results. The risks described below 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.

Our inability to finance future growth could hurt our business.

Our revenues and profit margins are based on our ability to supply substantial amounts of inventory to our customers at a very rapid pace. If we are unable to obtain sufficient inventory from our distributors, our customers will be affected, which could harm our long term ability to sell products through those sales channels.

Increased competition could hurt our business.

There are many manufacturers and distributors of many of the products we sell. Since consumer electronics and communications equipment have traditionally been high volume/high profit areas, increased competition could enter the market and adversely affect our sales and profitability.

We rely on our distributors for a significant portion of our business. If we are unable to maintain good relationships with our distributors, our business could suffer.

Segments of our business, particularly the LCD television business, are subject to rapidly changing prices. As a result, we must often negotiate new pricing, discounts and price protection issues with customers while inventory is either in transit or just landed. If our distributors do not negotiate in good faith, or there is any damage to the products we ship, it could damage our relationship with our distributors and customers, which will adversely affect our sales and profitability.

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We rely on a single supplier for a significant portion of our business. If the supplier is unable to produce the necessary amount of merchandise, our business could suffer.

In 2006, 44% of the SOYO Group's net revenue resulted from products purchased from a single supplier. If that supplier is unable to produce and sell merchandise to us in the quantities ordered, our revenue would be affected while we found other sources of merchandise. The Company is currently negotiating with different suppliers to reduce our dependence on one supplier.

Increases in cost or disruption of supply could harm our business.

Our business and profitability is reliant on our ability to order and obtain product within specified timelines. Any shortages of materials, such as LCD panels, could affect our ability to obtain merchandise and harm our business.

Increases in the cost of energy could affect our profitability.

We were adversely affected in 2005 and 2006 by the skyrocketing price of fuel, which led to higher freight costs. If the price of shipping merchandise continues to climb, it will affect our future profitability.

Litigation or legal proceedings could expose us to significant liabilities and thus negatively affect our financial results.

We are party to several different legal proceedings, which are described in Item 2 of this report. We evaluate these litigation claims and legal proceedings to assess the likelihood of unfavorable outcomes and to estimate, if possible, the amount of potential losses. Based on these assessments and estimates, we establish reserves as required. These assessments and estimates are based on the information available to management at the time and involve management's best judgment. It is possible that actual outcomes or losses may differ materially from those envisioned by our current assessments and estimates. In addition, new or adverse developments in existing litigation claims or legal proceedings involving our Company could require us to establish or increase litigation reserves or enter into unfavorable settlements or satisfy judgments for monetary damages for amounts significantly in excess of current reserves, which could adversely affect our financial results for future periods.

Changes in accounting standards and taxation requirements could affect our financial results.

New accounting standards or pronouncements that may become applicable to our Company from time to time, or changes in the interpretation of existing standards and pronouncements, could have a significant effect on our reported results for the affected periods.

If we are not able to achieve our overall long term goals, the value of an investment in our Company could be negatively affected.

We have established and publicly announced certain long-term growth objectives. These objectives were based on our evaluation of our growth prospects, which are generally based on volume and sales potential of many product types, some of which are more profitable than others, and on an assessment of potential level or mix of product sales. There can be no assurance that we will achieve the required volume or revenue growth or mix of products necessary to achieve our growth objectives.

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### ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

### ITEM 2. PROPERTIES

The Company's corporate headquarter is located at 1420 S. Vintage Ave. Ontario, California, 91761. The property is under a lease agreement expiring November 30, 2008 with terms and conditions as stipulated below:

| Facility                | Address                             | Lease<br>Inception | Lease<br>Expiration | Area          |
|-------------------------|-------------------------------------|--------------------|---------------------|---------------|
| -----                   | -----                               | -----              | -----               | -----         |
| Office and<br>warehouse | 1420 S. Vintage Ave.<br>Ontario, CA | 9/01/2003          | 11/30/2008          | 42,723 sq.ft. |

#### Rent Schedule:

| Start Date      | End Date          | Base Rent (NNN) |
|-----------------|-------------------|-----------------|
| -----           | -----             | -----           |
| October 1, 2004 | February 28, 2006 | \$ 16,869.84    |
| March 1, 2006   | November 30, 2008 | \$ 17,724.30    |

The Company owns an option to extend the term of the leased property for an additional five ( 5) years that can be exercised by providing written notice to the lessor at least six (6) months but not more than 12 months prior to the date that the option period would commence. The Company also maintains a sales representation office in Brazil, located at Rua Andre Ampere 153 andar 17 sala171/172, Brooklin Novo, Sao Paulo, SP, Brazil.

### ITEM 3. LEGAL PROCEEDINGS.

Pourvajdi v. Soyo Group, Inc., et al. On April 14, 2005, Afshin "Andy" Pourvajdi filed a civil Complaint in the Superior Court of the State of California for the County of San Bernardino against the Company, Nancy Chu and DOES 1 through 50. Pourvajdi asserted four causes of action in his Complaint: (1) Double Damages for Violation of Labor Code Section 970; (2) Misrepresentation; (3) Intentional Infliction of Emotional Distress and (4) Breach of Contract. On each of the first two causes of action, Pourvajdi prayed for an award of damages of no less than \$200,000, or according to proof, plus an unspecified amount of punitive damages, his costs of suit and for such other and further relief as the Court deemed just and proper. On the third cause of action, Pourvajdi sought general damages, medical and related expenses, lost earnings (both past and future), punitive damages, costs of suit and for such other and further relief as the Court deemed just and proper. No damage amount was identified for any of the damage elements associated with the third cause of action. On his fourth cause of action, Pourvajdi sought an unspecified amount he claimed was due under the alleged contract with Soyo, plus unspecified amounts of attorneys fees, costs and such other and further relief as the Court deemed just and proper. This action was settled, and the entire action was dismissed with prejudice in the last quarter of 2006.

Soyo Inc. v. XtraPlus, etc, et al. On or about September 27, 2004, Soyo, Inc. ("Soyo") sold computer components to XtraPlus Corporation, dba ZipZoomFly.com ("XtraPlus"), a computer retailer. Soyo invoiced XtraPlus for \$183,600, but XtraPlus failed to pay the invoice and, on March 4, 2005, Soyo filed a civil complaint against XtraPlus in the Superior Court of the State of California for the County of San Bernardino ("Court"). XtraPlus thereafter filed a

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Cross-Complaint against Soyo on May 11, 2005 in which it alleged claims for: (1) Breach of Contract; (2) Breach of Warranty; (3) Breach of the Implied Covenant of Good Faith and Fair Dealing; and (4) Violation of Business & Professions Code ss. 17200. In its prayer in the Cross-Complaint, XtraPlus sought special and general damages in excess of \$100,000, attorneys' fees and costs, and such other relief as the Court might determine to be just and proper. After it filed its

Complaint, Soyo also sought an attachment of \$183,600, plus interest and costs. Ultimately, XtraPlus paid Soyo \$40,000 of the amount sought, and deposited into the registry of the Court the sum of \$140,000 until the action was concluded.

On January 12, 2007, the Court ordered that summary adjudication be granted in favor of Soyo on two of the four claims in Soyo's Complaint against XtraPlus (Soyo voluntarily dismissed the other two claims), and that Soyo recover the remaining balance due on its claim. The Court also ordered that summary judgment be granted in favor of Soyo and against XtraPlus on all of the claims against Soyo that were contained in the XtraPlus Cross-Complaint. The formal order and the proposed judgment reflecting this disposition were entered on February 14, 2007. XtraPlus has the right to appeal this judgment; however, it must do so by approximately May 1, 2007. We cannot predict the outcome, nor whether XtraPlus will file an appeal or otherwise challenge the Court's decision.

Normandin v. Soyo Group, Inc. et al. On August 2, 2004, Gerry Normandin, individually and on behalf of a proposed nationwide class of consumers, filed a Complaint in the Superior Court of the State of California for the County of San Bernardino against the Company and DOES 1 through 100. Normandin asserted three causes of action in his Complaint: (1) Violation of the Consumer Legal Remedies Act, Civil Code Section 1750 et seq.; (2) Violation of Business and Professions Code Section 17200 et seq.; and (3) Violation of Business and Professions Code Section 17500 et seq. Normandin prayed for an order certifying the case as a class action, an award of actual damages suffered by plaintiff and the class in an amount not less than \$1,000 per person, an order for restitution and disgorgement of monies wrongfully acquired by defendants through the sales of motherboards having defective capacitors, an order enjoining the Company from further sales of motherboards with defective capacitors, an award of punitive damages, attorneys' fees and costs, pre-judgment interest and such other relief as the Court may deem just and proper.

The parties have reached a tentative settlement in principle of the action. However, the tentative agreement must be reduced into a formal settlement agreement, and must also be approved by the Court. Notice must also be given to members of the class whom Normandin represents, and any objections to the settlement considered and addressed by the Court. We cannot predict the outcome of these pending matters, nor whether the settlement agreement will ultimately be approved and the case dismissed.

Soyo v. Hartford: Soyo tendered a claim to Hartford Insurance Company of the Midwest ("Hartford") under which it sought a defense and indemnity for the claims asserted in the Normandin action. Hartford rejected that claim, and on May 1, 2006, Soyo Group Inc. filed an action for: (1) Declaratory Relief; (2) Breach of Contract; and (3) Bad Faith against Hartford. Soyo, Inc. was subsequently added as a Plaintiff in a First Amended Complaint ("FAC") that was filed in the action. In the Prayer in the FAC, Soyo sought general, special and punitive damages in amounts that were unspecified, as well as interest costs and attorneys fees.

The dispute was mediated, and an agreement in principle to resolve it was reached on December 21, 2006. The formal settlement agreement is being prepared

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and has not yet been executed by any of the parties. We cannot predict whether a formal agreement will be executed, or the outcome of this action if it is not.

On June 30, 2006, a lawsuit was filed in the United States District Court, Central District of California, Eastern Division, entitled Robert Lewis, Jr. v. Soyo Group, Inc., et al., Case No. EDCV 06-699 VAP (JWJx). The case seeks class

action status and alleges failures to timely pay rebates to purchasers of Soyo products allegedly in violation of unfair competition laws, the California Consumer Legal Remedies Act and contracts with purchasers. The plaintiff seeks disgorgement of all amounts obtained by the Company as a result of the alleged misconduct, plus actual damages, punitive damages and attorneys' fees and costs. The Company has vigorously defended the lawsuit, is currently involved in settlement discussions, and believes that the case will be resolved with no material adverse effect on the Company.

On May 22, 2005, the Company received notice of an investigation by the Attorney General of the State of California (the "AG") regarding the Company's alleged failures to timely pay rebates to purchasers of Soyo products. The Company has cooperated with the investigation and has agreed to the terms of a stipulation for entry of final judgment and permanent injunction (the "Injunction") to be filed by the AG relating to the Company's administration of rebate claims. The Company believes that compliance with the terms of the Injunction will have no material adverse effect on the Company.

On February 15, 2006, the Company received notice of an investigation by counsel for the Federal Trade Commission (the "FTC") regarding the Company's alleged failures to timely pay rebates to purchasers of Soyo products. The Company has cooperated with the investigation and has agreed to the terms of an agreement containing a consent order (the "Consent Order") to be filed by the FTC relating to the Company's administration of rebate claims, which is currently before the FTC for approval. The Company believes that compliance with the terms of the Consent Order will have no material adverse effect on the Company.

On January 26, 2007, the Company filed a lawsuit against Astar Electronics USA, Inc., KXD Technology, Inc. and Does 1 - 25 in the Superior Court of California for the County of Los Angeles, Central District (Case No. BC365349). The Company alleges claims for Breach of Contract, Fraud, and Tortious Interference with Economic Relations and seeks compensatory and punitive damages. Both named defendants were served on January 26, 2007. No trial date has been set. The Company is vigorously asserting its claims against the defendants. No counterclaims have been asserted against the Company in the action to date.

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

During the fourth quarter of the fiscal year ended December 31, 2006, there were no matters submitted to the shareholders for approval.

## PART II

#### ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.



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### (a) Market Prices of Common Stock

The Company's common stock is traded on the Over the Counter Bulletin Board under the symbol "SOYO." The high and low bid intra-day prices of the common stock were not reported on the OTCBB for the time periods indicated on the table below. Accordingly, the Company has set forth the high and low closing prices of our common stock as reported on the OTCBB over the last two years. Further, the sales prices listed below represent prices between dealers without adjustments for retail markups, breakdown or commissions and they may not represent actual transactions.

|                                     | Price Range |         |
|-------------------------------------|-------------|---------|
|                                     | High        | Low     |
| Fiscal Year Ended December 31, 2005 |             |         |
| First Quarter                       | \$ 0.98     | \$ 0.37 |
| Second Quarter                      | 0.88        | 0.60    |
| Third Quarter                       | 0.93        | 0.66    |
| Fourth Quarter                      | 0.89        | 0.55    |
| Fiscal Year Ended December 31, 2006 |             |         |
| First Quarter                       | \$0.74      | \$ 0.50 |
| Second Quarter                      | 0.62        | 0.31    |
| Third Quarter                       | 0.40        | 0.28    |
| Fourth Quarter                      | 0.40        | 0.27    |

### (b) Shareholders

The Company's common shares are issued in registered form. Securities Transfer Corporation, Dallas, Texas, is the registrar and transfer agent for the Company's common stock. As of December 31, 2006 there were 49,025,511 shares of the Company's common stock outstanding and the Company had over 85 shareholders of record.

### (c) Dividends

The Company has never declared or paid any cash dividends on our common stock and it does not anticipate paying any cash dividends in the foreseeable future. The Company currently intends to retain future earnings, if any, to finance operations and the expansion of its business. Any future determination to pay cash dividends will be at the discretion of the board of directors and will be based upon the Company's financial condition, operating results, capital requirements, plans for expansion, restrictions imposed by any financing arrangements and any other factors that the board of directors deems relevant.

During 2006 we declared no dividends on the Class B Preferred Stock outstanding. The dividends recognized and booked in 2006 were the accreted dividends resulting from the valuation of the Series B Preferred Stock at issuance. See "Recent Sales of Unregistered Securities." for more information.

### (d) Penny Stock

Until the Company's shares qualify for inclusion in the NASDAQ system, the public trading, if any, of the Company's common stock will be on the OTC Bulletin Board or the Pink Sheets. As a result, an investor may find it more difficult to dispose of, or to obtain accurate quotations as to the price of, the common stock offered. The Company's common stock is subject to provisions of

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Section 15(g) and Rule 15g-9 of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), commonly referred to as the "penny stock rule." Section 15(g) sets forth certain requirements for transactions in penny stocks, and Rule 15g-9(d) incorporates the definition of "penny stock" that is found in Rule 3a51-1 of the Exchange Act. The SEC generally defines a "penny stock" to be any equity security that has a market price less than \$5.00 per share, subject to certain exceptions. If the Company's common stock is deemed to be a penny stock, trading in the shares will be subject to additional sales practice requirements on broker-dealers who sell penny stock to persons other than established customers and accredited investors. "Accredited investors" are persons with assets in excess of \$1,000,000 or annual income exceeding \$200,000 or \$300,000 together with their spouse. For transactions covered by these rules, broker-dealers must make a special suitability determination for the purchase of such security and must have the purchaser's written consent to the transaction prior to the purchase. Additionally, for any transaction involving a penny stock, unless exempt, the rules require the delivery, prior to the first transaction, of a risk disclosure document, prepared by the SEC, relating to the penny stock market. A broker-dealer also must disclose the commissions payable to both the broker-dealer and the registered representative, and current quotations for the securities. Finally, monthly statements must be sent disclosing recent price information for the penny stocks held in an account and information on the limited market in penny stocks. Consequently, these rules restrict the ability of broker-dealers to trade and/or maintain a market in the Company's common stock and may affect the ability of the Company's shareholders to sell their shares.

### (e) Recent Sales of Unregistered Securities

During the calendar year 2006, the Company issued an aggregate of 344,000 unregistered shares of its common stock to various entities for various reasons.

Through the year, 57,000 unregistered shares were issued to one of our directors, Paul Risberg, for services performed on the Company's behalf.

Through the year, an additional 287,000 unregistered shares were issued to various consultants, contractors and vendors for services performed on the Company's behalf. No single Company or individual received more than 75,000 of the unregistered shares.

### (f) Equity Compensation Plan Information

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 \$0.75. 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. The grants will expire if unused on July 22, 2010.

The Company did not grant any stock options to employees, officers or directors in 2006. As of December 31, 2006, 13 individuals had left the Company, resulting in the forfeiture of 510,000 options. As of December 31, 2006, 2,379,000 of the

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2,889,000 options granted were still outstanding, and 793,000 had vested. As of December 31, 2006, none of the options outstanding had been exercised.

### ITEM 6. SELECTED FINANCIAL DATA

The following selected consolidated financial data of the Company is presented as of and for each of the five years ended December 31, 2006, 2005, 2004, 2003 and 2002. The selected financial data should be read in conjunction with the Company's audited consolidated financial statements and the notes thereto, and "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations".

#### Selected Consolidated Statements of Operations Data:

|   | Year Ended December 31 |               |               |               |
|---|------------------------|---------------|---------------|---------------|
|   | 2006                   | 2005          | 2004          | 2003          |
|   | ----                   | ----          | ----          | ----          |
| Net revenue   | \$ 56,758,688          | \$ 38,263,032 | \$ 32,426,414 | \$ 31,034,239 |
| Income (loss) from operations                         | 1,519,271              | 514,920       | (3,913,683)   | (980,347)     |
| Net income (loss) attributable to common shareholders | 462,049                | (633,443)     | (4,143,978)   | (984,588)     |
| Net income (loss) per common share                    | \$ 0.01                | (\$ 0.01)     | (\$ 0.10)     | (\$ 0.02)     |

#### Selected Consolidated Balance Sheet Data:

|  | December 31   |               |              |               |
|--|---------------|---------------|--------------|---------------|
|  | 2006          | 2005          | 2004         | 2003          |
|  | ----          | ----          | ----         | ----          |
| Total assets                             | \$ 26,769,416 | \$ 16,907,390 | \$ 7,500,437 | \$ 12,729.453 |
| Long-term payable to Soyo                |               |               |              |               |
| Taiwan                                   | 3,735,198     | --            | --           | 12,000,000    |
| Shareholders' Equity (Deficit)           | (2,732,431)   | 1,477,703     | (4,057,028)  | (12,136,783)  |
| Cash dividends declared per common share | N/A           | N/A           | N/A          | N/A           |

### ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with the Company's consolidated financial statements and the notes thereto appearing elsewhere in this Annual Report on Form 10-K for the fiscal year ended December 31, 2006.

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This Annual Report on Form 10-K for the fiscal year ended December 31, 2006 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 may include, among others, statements concerning the Company's expectations regarding its business, growth prospects, revenue trends,

operating costs, working capital requirements, facility expansion plans, competition, results of operations 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 Annual Report on Form 10-K for the fiscal year ended December 31, 2006 involve known and unknown risks, uncertainties and other factors that could cause actual results, performance or achievements of the Company to differ materially from those expressed in or implied by the forward-looking statements contained herein.

Each forward-looking statement should be read in context with, and with an understanding of, the various disclosures concerning the Company and its business made elsewhere in this annual Report on Form 10-K for the fiscal year ended December 31, 2006, as well as other public reports filed with the United States Securities and Exchange Commission. You should not place undue reliance on any forward-looking statement as a prediction of actual results or developments. The Company does not intend to update or revise any forward-looking statement contained in this Annual Report on Form 10-K for the fiscal year ended December 31, 2006 to reflect new events or circumstances except to the extent required by applicable law.

### Background and Overview:

Incorporated in Nevada on October 22, 1998, SOYO Group, Inc. is a distributor of consumer electronics, communications and computer parts. A substantial portion of the products are manufactured in Taiwan and China. Through SOYO Group, Inc. the Company offers a line of LCD televisions and computer monitors, wireless headset devices, motherboards and related peripherals for intensive multimedia applications, telecommunications services and equipment. The product line also includes Bare Bone 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 any home and office (SOHO) users.

SOYO Group's products are sold through an extensive network of authorized distributors to resellers, system integrators, value-added resellers (VARs). These products are also sold through major retailers, distributors and e-tailers to the consumers throughout North America and Latin America.

The Company sells to distributors, retailers and directly to consumers. Revenues through such distribution channels for each of the three years ended December 31, 2006, 2005 and 2004 are summarized as follows:

#### Year Ended December 31

| 2006 | %   | 2005 | %   | 2004 | %   |
|------|-----|------|-----|------|-----|
| ---- | --- | ---- | --- | ---- | --- |

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|              |                     |              |                     |              |                     |              |
|--------------|---------------------|--------------|---------------------|--------------|---------------------|--------------|
| Revenues     |                     |              |                     |              |                     |              |
| Distributors | \$35,510,804        | 62.6         | \$22,312,488        | 58.3         | \$14,704,452        | 45.3         |
| Retailers    | 15,187,152          | 26.8         | 15,742,332          | 41.2         | 17,721,962          | 54.7         |
| Others       | 6,060,732           | 10.6         | 208,212             | 0.5          | N/A                 | N/A          |
| <b>Total</b> | <b>\$56,758,688</b> | <b>100.0</b> | <b>\$38,263,032</b> | <b>100.0</b> | <b>\$32,426,414</b> | <b>100.0</b> |

During the year ended December 31, 2006, no customer accounted for more than 8% of sales.

During the year ended December 31, 2005, the Company had one customer (E23) that accounted for revenues of \$13,552,324, equivalent to 35% of net revenues.

Revenues by geographic segment are summarized as follows:

|                           | Year Ended December 31 |              |                     |              |                     |
|---------------------------|------------------------|--------------|---------------------|--------------|---------------------|
|                           | 2006                   | %            | 2005                | %            | 2004                |
|                           | ----                   | ---          | ----                | ---          | ----                |
| Revenues                  |                        |              |                     |              |                     |
| United States             | \$42,628,547           | 75.2         | \$20,686,944        | 54.1         | \$25,936,978        |
| Other N. America          | 2,472,209              | 4.4          | 983,606             | 2.6          | N/A                 |
| Central and South America | 10,253,665             | 18.0         | 2,993,532           | 7.8          | 6,317,907           |
| Hong Kong                 | 139,490                | 0.2          | 13,598,950          | 35.4         | 171,529             |
| Other locations           | 1,264,777              | 2.2          | N/A                 | N/A          | N/A                 |
| <b>Total</b>              | <b>\$56,758,688</b>    | <b>100.0</b> | <b>\$38,263,032</b> | <b>100.0</b> | <b>\$32,426,414</b> |

During the year 2004 segment data on the "Other N. America Business" segment was not kept as it was very small in relation to the size of the United States business at that time, no compilations of the data were made as there were no internal decision process that would have been governed by such information and the compilation of this information would have been impractical and offered no value to the organization.

During the first part of 2005, the Company had made a commitment to its new product lines, but did not have much inventory to sell. While waiting for the initial inventory shipments, the Company entered into a short term agreement to make sales of computer components to a vendor in Hong Kong (E23). The sales had relatively low margin, and not a business that the Company planned to be in long term. Nevertheless, the sales of such products in 2005 represented a significant portion of the Company's business.

Revenues by product line are summarized as follows:

Year Ended December 31

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|                                   | 2006<br>---- | %     | 2005<br>---- | %     | 2004<br>---- | %    |
|-----------------------------------|--------------|-------|--------------|-------|--------------|------|
| Revenues                          |              |       |              |       |              |      |
| Consumer electronics              | \$27,543,873 | 48.5  | \$18,739,719 | 49.0  | N/A          | N/A  |
| Computer parts and<br>peripherals | 29,204,792   | 51.5  | 18,906,367   | 49.4  | N/A          | N/A  |
| Voice and communication           | 10,023       | --    | 616,946      | 1.6   | N/A          | N/A  |
| Total                             | \$56,758,688 | 100.0 | \$38,263,032 | 100.0 | \$32,426,414 | 100. |

The breakdowns to segregate sales by product line is not available for years prior to 2005. During the years prior to 2005, the Company sold primarily computer parts and peripherals. The dollar volume of sales of both consumer electronics and voice and communication products were very small and immaterial in the scope of the Company's business. As sales of consumer electronics and voice and communication products prior to 2005 have grown, the Company has begun recognizing the sales in each category, and will continue to segregate the sales for reporting purposes in the future.

### Financial Outlook:

In 2006, the Company earned \$678,537, or \$0.01 per share before dividends on preferred stock. The large increases in sales of LCD televisions and LCD monitors were primarily responsible for the large increase in net revenues.

In 2005, the Company earned \$540,310 or \$0.01 cents per share, before preferred dividends, and revamped its core product offerings. As a result, the consumer electronics division, featuring LCD televisions and monitors, was responsible for over 30% of the Company's sales, a number that was expected to grow in the coming years.

In 2004, the Company incurred a net loss before preferred dividends of (\$3,920,245).

As a general rule, the Company has been totally reliant upon the cash flows from its operations to fund future growth. In the last few years, the Company has begun and continues to implement the following steps to increase its financial position, liquidity, and long term financial health:

In 2005, The Company completed a small private placement, began factoring invoices to improve cash flows, and converted several million dollars of debt to equity, all of which improved the Company's financial condition.

In 2006, the Company changed factors to a more beneficial arrangement, and entered into a Trade Finance Flow facility with GE Capital to fund "Star" transactions. The agreement provided for GE Capital to guarantee payment, on the Company's behalf, for merchandise ordered from GE Capital approved manufacturers in Asia. GE Capital guarantees the payment subject to a purchase order from one of our customers. The Company accepts delivery of the goods in the US, and then has the option to either pay for the goods or sell the receivable (from the customer) to our factor, who pays GE Capital.

In March 2007, the Company announced that it had secured a \$12 MM Asset Based Credit Facility from a California bank to provide funding for future growth.

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

### Critical Accounting Policies:

The Company prepared its 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 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. In 2006, the Company booked price protection, co-op marketing fees and sales incentives as expenses under these programs. In 2005, the Company booked over \$1.3 million received from such programs to prior years' purchase discounts and allowances settled in 2005.

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

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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.

### Prior Year's Purchases and Discounts:

There were no amounts related to prior years booked in 2006. However, in early 2005 the company negotiated with its suppliers for discounts and allowances related to purchases made in 2004. The company and its suppliers settled their differences in 2005. The company accounted in 2005 for the settlement as a gain contingency, in accordance with FAS 5, Accounting for Contingencies.

The company also accounted in 2005 for its settlement with suppliers of discounts and allowances as a reduction of cost of goods sold because purchase discounts and allowances are of a "character typical of the customary business activities of the entity" in accordance with APB 9, as amended by APB 30, Reporting the Results of Operations-Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions.

### 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.

### 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.

### Sales Incentives

The Company offers sales incentives to our customers in the form of co-op advertising, price protection and sales discounts. All costs associated with sales incentives are classified as a reduction to net revenues. The following is a summary of the different types of sales incentives: Co-operative advertising allowances are offered to customers as a reimbursement towards their costs for advertising in which our product is featured on its own or in conjunction with other companies' products. The amount offered is either a fixed amount or is based upon a fixed percentage of sales revenue during a specified time period.

Price protection is a concession given by the Company to compensate for the



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difference between the price of the product paid by the customer and a subsequent price reduction of the product by the Company.

Sales discounts are offered to customers at various times based on management's discretion. Discounts could be used to increase sales of a certain model, move stale inventory out of the warehouse, introduce new products, or for another reason that management finds attractive.

### Allowance for Doubtful Accounts

The Company regularly analyzes customer balances, and, when it becomes evident a specific customer will be unable to meet its financial obligations to the Company, such as in the case of the deterioration in the customer's operating results or financial position, a specific allowance for doubtful account is recorded to reduce the related receivable to the amount that is believed reasonably collectible. The Company also records allowances for doubtful accounts for all other customers based on a variety of factors including the length of time the receivables are past due, the financial health of the customer and historical experience. If circumstances related to specific customers change, estimates of the recoverability of receivables could be further adjusted.

### 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 based method, compensation cost is the excess, if any, of the quoted market price of the stock at grant date or other measurement date over the amount an employee must pay to acquire the stock. Under the intrinsic value method, the Company has recognized stock-based compensation common stock on the date of grant.

Effective January 1, 2006 the Company adopted SFAS 123(R) using the modified prospective approach and accordingly prior periods have not been restated to reflect the impact of SFAS 123(R). Under SFAS 123(R), 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 straight-line 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 three years.

SFAS 123(R) 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 has been recorded net of estimated forfeitures for the year ended December 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.

SFAS 123 requires the Company to provide pro-forma information regarding net loss as if compensation cost for the stock options granted to the Company's

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employees had been determined in accordance with the fair value based method prescribed in SFAS 123. Options granted to non-employees are recognized in these financial statements as compensation expense under SFAS 123 (See Note 11) using the Black-Scholes option-pricing model.

If the fair value based method under FAS 123 had been applied in measuring stock-based compensation expense for the year ended December 31, 2005, the pro forma on net income (loss) and net income (loss) per share would have been as follows:

|   | Year Ended<br>December 31,<br>2005 |
|---|------------------------------------|
|   |                                    |
| Net income (loss) attributable to common shareholders, as reported  | \$ (633,443)                       |
| Add: Stock-based employee compensation expense included in reported net income, net of related tax effect   | -                                  |
| Deduct: Total stock-based employee compensation expense determined under fair-value based method for all awards not included in net income (loss_ | (224,919)                          |
|   |                                    |
| Pro forma net income (loss) attributable to common shareholders   | \$ (858,362)                       |
|   |                                    |
| Income (loss) per share:  |                                    |
| Basic/diluted - as reported   | (\$0.01)/(\$0.01)                  |
| Basic/diluted - pro forma   | (\$0.02)/(\$0.02)                  |

### Results of Operations:

Years Ended December 31, 2006 and 2005-

**Net Revenues.** Net revenues increased by \$18,495,656 or 48.3% to \$56,758,688 in 2006 as compared to \$38,263,032 in 2005. The increase in net revenues was primarily attributable to the strong sales of LCD TVs and LCD monitors, as well as the success of our sales force in opening new markets and developing new business opportunities New customers that purchased products from the Company in 2006 that had never before purchased products from the Company included Staples, the Home Depot and Wal Mart Canada.

During the years ended December 31, 2006 and 2005, the Company offered price protection to certain customers under specific programs aggregating \$70,119 and \$140,828 respectively, which reduced net revenues and accounts receivable accordingly.

**Gross Margin.** Gross margin was \$9,224,439 or 16.3% in 2006, as compared to \$4,692,970 or 12.3 % in 2005. Gross margin increased in 2006 as compared to 2005, both on an absolute and percentage of revenue basis, as the Company completed the changed in its core sales offerings from primarily hardware, motherboards and barebones systems to a greater emphasis on computer peripherals and consumer electronics. The Company was able to earn high margins throughout most of the year on LCD monitors, and LCD televisions. Margins were also helped by lower than expected RMA claims and returns of the Company's LCD monitors.

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Sales and Marketing Expenses. Selling and marketing expenses increased by \$232,436 or 25.5 %, to \$1,143,475 in 2006, as compared to \$911,039 in 2005. The increase was entirely due to payments to outside sales reps during the year. The Company began to employ outside sales reps to assist in obtaining new clients. The program was successful, as the outside reps were primarily responsible for the Company obtaining Staples, Home Depot and other big box retailers as customers.

General and Administrative Expenses. General and administrative expenses increased by \$1,951,472 or 53.3 %, to \$5,610,810 in 2006, as compared to \$3,659,338 in 2005. There were several reasons for the increase.

The biggest factor in the increased G&A costs was the Company's mandatory implementation of SFAS No. 123(R). 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) was effective for public companies at the beginning of the first fiscal year that begins after June 15, 2005.

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, \$121,573 for the three months ended June 30, 2006, \$126,924 for the three months ended September 30, 2006, and \$122,773 for the three months ended December 31, 2006. The complete effect of the adoption was a non cash charge against earnings of approximately \$506,222 over the twelve month period.

The next element contributing to the increase in the S,G&A expenses was the Company's use of consultants during the year. The Company was actively searching for new financing throughout the year, culminating in the completion of the UCB \$12 million revolving loan commitment (see Form 8-K filed March 1, 2007). The Company employed several high cost consultants to identify and negotiate with potential financial partners. All together, the Company spent over \$600,000 to pay consultants during the year. The cost of the consultants will not be repeated in 2007, as the Company has terminated their services.

The final element contributing to the increased SG&A costs in 2006 were the legal fees. The Company defended itself against several lawsuits during 2006 and negotiated settlements with both the California Attorney General and the Federal Trade Commission in regard to charges that the Company did not process and pay customer rebate claims properly (see Item 3- Legal Proceedings). The costs associated with the Company's defense of the lawsuits stemming from the rebate issues, and the administrative penalty totalled almost \$600,000.

Taken together, the costs of adapting SFAS No. 123(R) , the business consultants and the increase in legal fees over 2005 totaled approximately \$1.7 million, which accounts for substantially all of the increased costs over 2005.

Provision for Bad Debts. The provision for bad debts was increased to \$907,065 in 2006, as compared to \$34,513 in 2005. Since 2004, the Company has used three

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different factors to increase cash flow. As a result, credit policies and requirements have changed frequently in the last few years. When the Company was prepared to sign the agreement for the \$12 million finance line (see Form 8-K file March 2, 2007), it reexamined the receivables and wrote off all balances over 90 days, and wrote down to present value all balances over 90 days that were making monthly payments. This resulted in a large write off taken in the fourth quarter. As a result, any balances with even a small question about collectivity have been written off. Because of this aggressive stance, the allowance for bad debts has decreased, even though the accounts receivables balance has increased by over \$5 million.

Depreciation and Amortization. Depreciation and amortization of property and equipment was \$43,818 in 2006 as compared to \$35,394 in 2005.

Income (Loss) from Operations. The income from operations was \$1,519,271 for the year ended December 31, 2006, as compared to income from operations of \$514,920 for the year ended December 31, 2005.

Interest Expense. Interest expense increased substantially to \$901,900 in 2006, as compared to \$129,567 in 2005. The increase is due to the Company factoring all receivables in 2006 to improve cash flow, and paying penalties twice during the year for failing to meet the factor's minimum volume requirements. As a result of these penalties, the Company terminated the contract with the factor in February 2007.

Interest Income. Interest income was \$10,561 in 2006 as compared to \$5,301 in 2005. The increase was due to the Company's increased cash flow throughout the year.

Other Income (Expense). Other income/miscellaneous revenue (expense) was a loss of (\$106,262) as compared to a profit of \$150,456 in 2005.

Income Tax Expense. The Company calculated its income tax expense at \$20,310 for 2006 after using net operating loss carryforwards to offset most of its taxable income. The provision for income taxes was \$800 in 2005.

Deferred Income Tax Gain: The Company recognized a deferred income tax gain of \$177,177 in 2006 as an offset to booking the compensation expense required by the adoption of FASB 123R.

Net Income/Loss. The net income before preferred dividends was \$678,537 for the year ended December 31, 2006, as compared to \$540,310 for the year ended December 31, 2005. The reasons for the turnaround are discussed in detail in the above paragraphs.

Preferred Stock Dividends. Accreted and deemed preferred stock dividends were \$216,488 in 2006, as compared to accreted and declared dividends of \$1,173,753 in 2005. The accreted dividends were actually \$174,753 during 2005. Additionally, the Company made a \$999,000 adjustment to the carrying value of the Class A preferred stock during the year. From the Company's inception, the Class A preferred stock was carried on the books at its basis of \$1,000. Prior to the conditional redemption of the Class A preferred stock to common stock on October 24, 2005, the carrying value was adjusted to the face value of \$1,000,000. This resulted in an adjustment to the preferred stock account of \$999,000, and the offsetting journal entry to preferred stock dividends raised the amount recorded during the year to \$1,173,753. No such adjustments were required in 2006.

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### Results of Operations:

Years Ended December 31, 2005 and 2004-

**Net Revenues.** Net revenues increased by \$5,836,618 or 18.0% to \$38,263,032 in 2005 as compared to \$32,426,414 in 2004. The increase in net revenues was primarily attributable to the birth of the consumer products division, which changed the core offerings for sale. The Company sold over \$18.8 million in LCD monitors and televisions in 2005.

On a comparable basis, revenues declined in N. America and Central America in 2005 vs. 2004. There were several reasons for this. During the first part of 2005, the Company had made a commitment to its new product lines, but did not have much inventory to sell. While waiting for the initial inventory shipments, the Company entered into a short term agreement to make sales of computer components to a vendor in Hong Kong (E23). The sales had relatively low margin, and not a business that the Company planned to be in long term. Nevertheless, the sales of such products in 2005 represented a significant portion of the Company's business. For this reason, sales to Hong Kong were very strong in 2005, where they had never been before. When the initial inventory of the consumer electronics products began to arrive, the Company put its efforts into selling those products and establishing those markets, which led to increased sales throughout the rest 2005 and through the present. However, when taken on a comparable basis, due to that period of inactivity, sales in 2005 decreased in 2005 vs. 2004 for the N. American and Central American markets.

During the years ended December 31, 2005 and 2004, the Company offered price protection to certain customers under specific programs aggregating \$140,828 and \$295,998 respectively, which reduced net revenues and accounts receivable accordingly. Price protection offered to customers was significantly decreased in 2005, as the new products did not require the same level of price protection since the sales cycle was much quicker for the Company's customers.

**Gross Margin.** Gross margin was \$4,692,970 or 12.3 % in 2005, as compared to \$2,216,372 or 6.8 % in 2004. Gross margin increased in 2005 as compared to 2004, both on an absolute and percentage of revenue basis, as the Company changed its core sales offerings from hardware, motherboards and barebones systems to a greater emphasis on computer peripherals and consumer electronics. The demand for the new products, specifically the LCD monitors and televisions, was great enough that the Company was able to earn higher margins than in past years sales of computer peripherals.

At the start of the year, the Company was holding inventory that had been purchased during 2004 that was significantly different in appearance and functionality than the products the Company had sought to purchase. For this reason, the Company could not sell the products through normal sales channels. The Company thus continued to negotiate with suppliers to return the products. Subsequently, the negotiations were completed, and the Company booked the results as prior years' purchase discounts and allowances. This decreased the cost of revenues, thereby, increasing the gross margin.

The gross margin was a little over 4% before taking into account the settlement of the prior year's purchase discounts and allowances. The Company believes that gross margin increased by about 4% due to the settlement of the prior year's purchase discounts and allowances, and that gross margin was over 8% because the settlement was included in the calculation.

**Sales and Marketing Expenses.** Selling and marketing expenses decreased by

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\$666,570 or 42.2 %, to \$911,039 in 2005, as compared to \$1,577,609 in 2004. The decrease was entirely due to an expensive Co-op marketing campaign run in 2004 that was not repeated in 2005.

**General and Administrative Expenses.** General and administrative expenses increased by \$98,628 or 2.8%, to \$3,659,338 in 2005, as compared to \$3,560,710 in 2004. There were several reasons for the increase. First, the problems associated with the 2003 audit resulted in a cost of over \$400,000 in legal and accounting fees in 2004 that were not repeated. However, the Company did spend over \$150,000 in legal fees to defend itself against the two legal cases filed against it, and described in section 4 of this report. Additionally, the Company created an Employee Stock Option Plan in 2005 at a cost exceeding \$25,000. The Company began factoring invoices to improve cash flow in 2005. That resulted in higher expenses, but the Company obtained the services of experts in evaluating customer credit, which led to a huge reduction in bad debt expense. The set up and approval of the program cost the Company over \$25,000. As the Company redesigned itself primarily as a distributor of electronics rather than consumer peripherals, the "launch costs" of the new products, especially travel and entertainment, increased significantly in 2005. The Company's travel and entertainment expenses for 2005 increased by over \$100,000. Finally, the Company had a large turnover in personnel relative to the new product offerings. By bringing in specialists to manage the different departments and sell the new products, the Company substantially upgraded its management and sales staffs, at an incremental cost of approximately \$90,000.

**Provision for Bad Debts.** The provision for bad debts was decreased to \$34,513 in 2005, as compared to \$956,738 in 2004. The decrease is due to the improved quality of the Company's credit accounts, and the increased use of experts in evaluating customer credit applications.

**Depreciation and Amortization.** Depreciation and amortization of property and equipment was \$35,394 in 2005 as compared to \$34,998 in 2004.

**Income (Loss) from Operations.** The income from operations was \$52,686 for the year ended December 31, 2005, as compared to a loss from operations of (\$3,913,683) for the year ended December 31, 2004. The income from operations in 2005 was due to the Company's improved operations, successful new product lines and streamlined expenses. In addition, the Company booked over \$1.3 million of offsets to purchases from vendors for price protection and product returns as prior years' purchase discounts and allowances settled in 2005.

**Interest Expense.** Interest expense increased substantially to \$129,567 in 2005, as compared to \$23,371 in 2004. The 454% increase is due to the Company factoring receivables in 2005 to improve cash flow. There was no such activity in 2004.

**Interest Income.** Interest income was \$5,301 in 2005. There was no interest income in 2004.

**Other Income.** Other income/miscellaneous revenue was \$150,456 in 2005, as compared to \$17,609 in 2004.

**Provision for Income Taxes.** Provision for income taxes of \$800 was booked for both 2005 and 2004.

**Net Income/(Loss).** The net income before preferred dividends was \$540,310 for the year ended December 31, 2005, as compared to a net loss of (\$3,920,245) for the year ended December 31, 2004. The reasons for the turnaround are discussed

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in detail in the above paragraphs.

Preferred Stock Dividends. Accreted and deemed preferred stock dividends were \$1,173,753 in 2005, as compared to accreted and declared dividends of \$223,733 in 2004. The accreted dividends were \$174,753 during the year. Additionally, the Company made a \$999,000 adjustment to the carrying value of the Class A preferred stock during the year. From the Company's inception, the Class A preferred stock was carried on the books at its basis of \$1,000. Prior to the conditional redemption of the Class A preferred stock to common stock on October 24, 2005, the carrying value was adjusted to the face value of \$1,000,000. This resulted in an adjustment to the preferred stock account of \$999,000, and the offsetting journal entry to preferred stock dividends raised the amount recorded during the year to \$1,173,753.

### Net Operating Loss Carryforwards:

As of December 31, 2006, the Company had federal operating loss carryforwards of approximately \$4,195,130 expiring in various years through 2024, which can be used to offset future taxable income, if any. No deferred tax benefit for these operating losses has been recognized in the consolidated financial statements due to the uncertainty as to their realizability in future periods. As of December 31, 2006, there were no state operating loss carryforwards available to the Company.

Net deferred tax assets of \$1,570,000 at December 31, 2004 resulting from net operating losses and other temporary differences have been offset by a 100% valuation allowance since management cannot determine whether it is more likely than not that such assets will be realized.

### Liquidity and Capital Resources - December 31, 2006:

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. SOYO Taiwan forgave debt in an amount equal to the difference between \$12,000,000 and the value of the preferred stock. This forgiveness was treated as a capital transaction. Payment was received by SOYO Taiwan in February and March 2004. An agreement was reached in the first quarter of 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 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

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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-transferrable. Based on the terms of the agreement between SOYO Taiwan and the third party, and specifically the limitation on the purchaser not collecting more than \$1,630,000 of the \$12,000,000 from the Company without the prior consent of SOYO Taiwan, the Company has determined that this transaction was in substance a capital transaction. 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 an increase in the loss attributable to common stockholders, and is being accreted from April 1, 2004 through December 31, 2008.

For the year ended December 31, 2006, the Company recorded aggregate dividends of \$216,488, based on the accretion of the discount on the Class B Convertible Preferred Stock. The Company did not declare or accrue any additional dividends on the Class B Preferred Stock.

For the year ended December 31, 2005, the Company recorded aggregate dividends of \$1,173,753, based on the accretion of the discount on the Class B Convertible Preferred Stock of \$174,753, and the adjustment of \$999,000 to the carrying value of the Class A preferred stock, which is described above. The Company did not declare or accrue any additional dividends on the Class B Preferred Stock.

Through March 31, 2007, none of the Class B preferred stock had been converted to common stock, and the Company had not repurchased any of the shares of Class B preferred stock.

Operating Activities. The Company utilized cash of \$2,941,820 from operating activities during the year ended December 31, 2006, compared to utilizing cash of \$178,088 from operating activities during the year ended December 31, 2004, and utilizing cash of \$183,925 from operating activities during the year ended December 31, 2004.

The use of cash in 2006 was due primarily to the Company's large increase in receivables in 2006. As the Company used factors to assist in credit decisions, the Company extended credit to more customers, resulting in large receivable balances. The reasons for the usage of cash in 2005 were the large increases in inventories and receivables, partially offset by the decrease in payables, which were settled with common stock. The primary reasons for the usage of cash in 2004 were the Company's large operating loss and the paydown of the balance due to SOYO Taiwan.

At December 31, 2006 the Company's cash and cash equivalents had increased by \$672,746 to \$1,501,040, as compared to \$828,294 at December 31, 2005.

The Company had working capital of \$5,915,914 at December 31, 2006, as compared to working capital of \$726,061 at December 31, 2005, resulting in current ratios of 1.33 to 1 and 1.04:1 at December 31, 2006 and 2005, respectively.

Accounts receivable increased to \$16,467,135 at December 31, 2006, as compared to \$7,278,520 at December 31, 2005, an increase of \$9,188,615, or 76.9%. The large increase was due to several factors. Most importantly, net revenues



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increased by \$18,495,656 during the year. Another factor is the increased diversity of the Company's customer list. The Company used a factor throughout the year to increase cash flow, and the factor approved all customers for credit lines and limits. As a result of the Company's faith in the ability of the factor's credit analysis, credit lines were approved for a larger number of customers, resulting in larger credit sales and receivables balances.

Inventories decreased to \$7,792,621 at December 31, 2006, as compared to \$7,991,030 at December 31, 2005, a decrease of \$198,409 or 2.4%. The inventory balances included inventory in transit of \$4,005,265 at December 31, 2006 and \$2,686,298 at December 31, 2005. Those figures indicate that inventory in the warehouse was under \$4,000,000 at December 31, 2006. The physical inventory on hand was very low due to high sales volume in the 4th quarter, and correspondingly, the inventory in transit was very high as the Company fills orders for products and attempts to stock products for future sales.

Accounts payable increased by \$2,096,038 to \$16,073,617 at December 31, 2006 as compared to \$13,977,579 at December 31, 2005. The reason for the increase is the increased business volume. The increase corresponds to an increase in receivables for the same time period. The increase would have been larger, but the Company came to an agreement in 2006 with a supplier to pay a balance due over time, resulting in that being reclassified to a long term payable. For more information, see the Form 8-K filed by the Company on December 27, 2006.

Accrued liabilities decreased to \$539,767 at December 31, 2006, as compared to \$1,287,108 at December 31, 2005, a decrease of \$747,341 or 58.1%. The decrease is primarily due to the Company having a better understanding of the amount of RMA accruals that were needed at year end. In 2005, the Company had been selling LCD televisions and monitors for only a short time. As a result, there was no historical data available to determine the amount of the accrual necessary to cover repairs and returns. In keeping with the Company's conservative policy, the Company reserved a large amount for those future expenses. With another year

of data to analyze, the Company believes that the current accrual is adequate, although smaller than the 2005 accrual.

Business Loan increased to \$3,588,403 in 2006 from \$0 in 2005 since receivables were sold with recourse in 2006 to Accord Financial Services.

Long Term Debt increased to \$1,735,198 in 2006 from \$0 in 2005.

The Form 8-K dated December 27, 2006 was intended to document two unusual events that resulted in the Company expanding payment terms for two vendors. The situations were independent, but were reported together on a single Form 8-K.

On December 15, 2006, the Company entered into a Forebearance and Debt Payment Agreement with Eastech Electronics Inc., a Taiwan Company. The Company had purchased consumer electronics products from Eastech in 2006 which failed the Company's quality control inspections. Some of the products contained mold, some of the products did not work properly, and some of the parts were damaged. When the Company received the products, it notified Eastech of the problems, and refused to pay for the shipment. The Company was going to return a majority of the products to Eastech, which would have caused a substantial hardship for Eastech. Eventually, the two companies reached an agreement whereby SOYO would not return the products, but would keep the shipment. Eastech agreed to furnish at least \$50,000 worth of spare parts to repair damaged products, and SOYO agreed to pay for the shipment over time, thereby allowing itself time to find any other damaged goods, account for sales and returns, and make sure that it would not be stuck with unsellable or returned merchandise that could not be

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liquidated.

On October 19, 2006, the Company entered into an agreement with Corion Industrial Corp. governing SOYO's repayment of debt. The debt arose from inventory SOYO purchased from Corion during the period from January to March 2006.

There were several problems with the inventory. First, a substantial portion of the inventory was being purchased to be sold on QVC. As such, these products required that the QVC bar code be affixed to each piece. That process was not completed correctly by Corion, forcing QVC to hire contractors to affix the proper documentation to each piece of inventory. These problems led to delays, and the "product window" during which the TV's were to be sold by QVC was missed. As a result, QVC ended up returning almost \$1 million worth of products.

The second problem with one of the inventory models was that the casing for the TV's was not made according to specifications. As a result, the televisions could not be wall mounted with the external tuner attached. These televisions could not be sold through the retail chains, and were instead deeply discounted to the Shop at Home television network, causing losses of over \$600,000.

The third and final problem with a portion of the inventory was due to the LCD panel itself. Although SOYO purchased a certain level of panel, some of the inventory was delivered with inferior panels. This led to high return rates, discounted products, and revenue shortfalls.

All of the problems with the shipments could be traced back to the manufacturer. As such, SOYO refused to pay for the products until the exact worth of the inventory and the true losses from the subpar inventory could be determined. Eventually, the Companies agreed on a reduced price for the inventory, with SOYO

paying for the products in installments through October 2008. The portion of the debt not due to be paid in 2007 is listed on the balance sheet as long term debt.

**Investing Activities** The Company expended \$48,891, \$621,970 and \$158,670 in 2006, 2005 and 2004 respectively, for the purchase of property and equipment. The large expenditure in 2005 is for the purchase of telephone lines and equipment in China to support the VoIP division, while the amount in 2004 is due to the move to Ontario, California and the resulting leasehold improvements.

**Financing Activities** The Company began factoring its invoices in 2005 to improve cash flow. The Company's initial factor was Wells Fargo PLC. In February 2006, the Company signed a one year contract with Accord Financial Services of North Carolina for factoring services. The agreement expired in February 2007 and was not renewed. During 2006, the Company received \$15,611,928 as proceeds from factoring with Accord Financial Services of which \$3,588,403 remains unpaid as of December 31, 2006.

Under the Accord agreement, all of our receivables were sold with recourse. As such, the Company continues to evaluate each of these receivables monthly in regard to its allowance for bad debts. The original factor, Wells Fargo, bought all accounts without recourse. When the switch over to Accord occurred, those transactions were "with recourse". For more information, please see the contract, which is included as exhibit 10.3 to this report.

In 2006, the Company entered into a Trade Finance Flow facility with GE Capital to fund "Star" transactions. The agreement provided for GE Capital to guarantee payment, on the Company's behalf, for merchandise ordered from GE Capital

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approved manufacturers in Asia. GE Capital guarantees the payment subject to a purchase order from one of our customers. The Company accepts delivery of the goods in the US, then has the option to either pay for the goods or sell the receivable (from the customer) to our factor, who paid GE Capital. For more information, please see the contract, which is included as exhibit 10.4 to this report.

In March 2007, the Company announced that it had secured a \$12 MM Asset Based Credit Facility from a California bank to provide funding for future growth. For more information, please see the form 8-K, filed by company on March 2, 2007.

In October 2005, the Company borrowed \$165,000 from an individual for working capital purposes. The Company repaid \$65,000 of the loan during the year. The balance at the end of 2006 was \$100,000.

On March 29, 2004, LGT Computer, Inc. loaned the Company \$213,750 pursuant to an unsecured note payable due March 28, 2005, with interest at 4% per annum. On May 29, 2004, LGT Computer, Inc. loaned the Company an additional \$700,000 pursuant to an unsecured note payable due May 29, 2005, with interest at 4% per annum. On March 28, 2005, by mutual agreement of the parties, the due dates of the notes were extended one year at the same interest rate. On September 2, 2005, the two loans and accrued interest of \$51,251 were repaid through the issuance of 1,286,669 shares of our restricted common stock. On that date, the market price of the stock was \$0.75.

On March 28, 2005 Ever-Green Technology (Hong Kong) Co., Ltd., purchased 500,000 unregistered shares of our common stock, \$0.001 par value per share (the

"Shares") and common stock purchase warrants to purchase 100,000 shares of our 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.

During March 2003, Nancy Chu, the Company's Chief Financial Officer, director and major shareholder, made short-term advances to the Company of \$360,000 for working capital purposes, of which \$120,000 was repaid during September 2003. The remaining \$240,000 was paid during 2005.

### Principal Commitments:

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

| Contractual Cash Obligations   | Less than 1<br>year | 2-3 years          | 4-5 years          | Over      |
|--------------------------------|---------------------|--------------------|--------------------|-----------|
| Operating Leases               | \$212,692           | \$194,967          | N/A                |           |
| Advances from Directors        | N/A                 | N/A                | N/A                |           |
| Notes Payable/ Short Term Loan | \$100,000           | N/A                | N/A                |           |
| Purchase Commitments           | \$4,005,265         | N/A                |                    |           |
| Royalty Payments Due           | \$353,000           | \$1,047,000        | \$1,480,000        | \$        |
| Long Term Debt                 | -                   | \$3,735,198        | -                  |           |
| <b>Total</b>                   | <b>\$4,670,957</b>  | <b>\$4,977,165</b> | <b>\$1,480,000</b> | <b>\$</b> |

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At December 31, 2006, the Company did not have any long term purchase commitment contracts to honor. The only purchase commitments were for inventory already purchased and in transit of \$4,005,265.

At December 31, 2006, the Company had trade payables to Corion and Eastech. By prior agreement of the companies (see explanation above) the payment of those balances was stretched so that the balances were to be paid in equal installments through October 2008. As a result, balances totaling \$3,735,198 were to be paid by the Company during the time period from January 2008 through October 2008, and have been classified as long term debt as of December 31, 2006.

At December 31, 2006, the Company did not have any material commitments for capital expenditures or have any transactions, obligations or relationships that could be considered off-balance sheet arrangements.

On February 8, 2007, SOYO Group announced that the Company had entered into a licensing agreement with Honeywell International Properties Inc. and Honeywell International Inc., effective January 1st 2007, under which SOYO will supply and market certain consumer electronics products under the Honeywell Brand.

The agreement is for a minimum period of 6.5 (six point five) years and calls for the payment of MINIMUM royalties by SOYO to Honeywell totaling \$3,840,000 (Three Million, Eight Hundred and Forty Thousand Dollars U.S.). Sales levels in excess of minimum agreed targets will result in associated increases in the royalty payments due. Minimum royalty payments due under the agreement are \$184,000 through December 31, 2007, and \$424,000 in 2008.

### ITEM 7A. 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 December 31, 2006 and 2005 were primarily short-term in nature, and since any interest bearing debt was at a pre-arranged rate, the Company had only minimal risk from an increase in interest rates. The Company has factored some of its accounts receivable during 2006, and any increase in the prime lending rate would lead to a higher rate charged on future advances. 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 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

#### (a) Financial Statements

The following financial statements are set forth at the end hereof.

1. Report of Independent Registered Public Accounting Firm

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2. Consolidated Balance Sheets as of December 31, 2006 and 2005
3. Consolidated Statements of Operations for the years ended December 31, 2006, 2005 and 2004
4. Consolidated Statements of Shareholders' Equity (Deficit) for the years ended December 31, 2006, 2005 and 2004
5. Consolidated Statements of Cash Flows for the years ended December 31, 2006, 2005 and 2004
6. Notes to Consolidated Financial Statements.

### SOYO Group, Inc. and Subsidiary Index to Consolidated Financial Statements

|   | Page        |
|---|-------------|
|   | ----        |
| Report of Independent Registered Public Accounting Firm -<br>Vasquez & Company LLP                | F-2         |
| Consolidated Balance Sheets - December 31, 2006 and 2005  | F-3 - F-4   |
| Consolidated Statements of Operations -<br>Years Ended December 31, 2006, 2005 and 2004           | F-5 - F-6   |
| Consolidated Statements of Shareholders' Equity -<br>Years Ended December 31, 2006, 2005 and 2004 | F-7         |
| Consolidated Statements of Cash Flows -<br>Years Ended December 31, 2006, 2005 and 2004           | F-8 - F-10  |
| Notes to Consolidated Financial Statements -<br>Years Ended December 31, 2006, 2005 and 2004      | F-11 - F-33 |

#### REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders  
Soyo Group, Inc. and Subsidiary  
Ontario, California

We have audited the accompanying consolidated balance sheets of Soyo Group, Inc. and Subsidiary as of December 31, 2006 and 2005, and the related consolidated statements of operations, shareholders' equity and cash flows for the years ended December 31, 2006. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over

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financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 11, the accompanying consolidated financial statements have been restated.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Soyo Group, Inc. and Subsidiary as of December 31, 2006 and 2005, and the consolidated results of its operations and its cash flows for the years ended December 31, 2006 in conformity with accounting principles generally accepted in the United States of America.

/s/ Vasquez and Company

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Vasquez and Company, L.P

Los Angeles, California

March 30, 2007 (except for Note 11 as to which the date is August 2, 2007)

### SOYO Group, Inc. and Subsidiary Consolidated Balance Sheets

|   | December 31, |            |
|---|--------------|------------|
|   | 2006         | 2005       |
|   | (Restated)   |            |
| <b>ASSETS</b>   |              |            |
| Current Assets  |              |            |
| Cash and cash equivalents   | \$ 1,501,040 | \$ 828,294 |
| Accounts receivable, net of allowance for doubtful accounts of<br>388,958 and \$589,224 at December 31, 2006 and 2005, respectively | 16,467,135   | 7,278,520  |
| Inventories   | 7,792,621    | 7,991,030  |
| Prepaid expenses  | 36,633       | 20,984     |
| Deferred income tax assets  | 177,177      | --         |

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|   |               |               |
|---|---------------|---------------|
| Deposits  | 243,095       | 36,920        |
|   | -----         | -----         |
| Total current assets  | 26,217,701    | 16,155,748    |
|   | -----         | -----         |
| Property and equipment  | 711,015       | 867,122       |
| Less: accumulated depreciation and amortization   | (159,300)     | (115,480)     |
|   | -----         | -----         |
|   | 551,715       | 751,642       |
|   | -----         | -----         |
| Total Assets  | \$ 26,769,416 | \$ 16,907,390 |
|   | =====         | =====         |
| LIABILITIES   |               |               |
| Current Liabilities   |               |               |
| Accounts payable  | \$ 16,073,617 | \$ 13,977,579 |
| Accrued liabilities   | 539,767       | 1,287,108     |
| Business loan   | 3,588,403     | --            |
| Short term loan   | 100,000       | 165,000       |
|   | -----         | -----         |
| Total current liabilities   | 20,301,787    | 15,429,687    |
|   | -----         | -----         |
| Long term payable   | 3,735,198     | --            |
|   | -----         | -----         |
| Total liabilities   | 24,036,985    | 15,429,687    |
|   | -----         | -----         |
| EQUITY  |               |               |
| Class B Preferred stock, \$0.001 par value,<br>authorized - 10,000,000 shares, Issued<br>and outstanding - 2,797,738 shares in 2006<br>and 2005 | 1,918,974     | 1,702,486     |
| Preferred stock backup withholding  | (149,945)     | (84,999)      |
| Common stock, \$0.001 par value.<br>Authorized - 75,000,000 shares, Issued and<br>outstanding - 49,025,511 shares (48,681,511 shares - 2005)    | 49,026        | 48,682        |
| Additional paid-in capital  | 17,866,531    | 17,225,738    |
| Accumulated deficit   | (16,952,155)  | (17,414,204)  |
|   | -----         | -----         |
| Total shareholders' equity  | 2,732,431     | 1,477,703     |
|   | -----         | -----         |
| Total Liabilities and Shareholders' Equity  | \$ 26,769,416 | \$ 16,907,390 |
|   | =====         | =====         |

See accompanying notes to consolidated financial statements.

SOYO Group, Inc. and Subsidiary  
Consolidated Statements of Operations

Year Ended December 31

-----  
2006

2005

20

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|  |                           |                           |                |
|--|---------------------------|---------------------------|----------------|
|  | -----                     | -----                     | -----          |
| Net revenues   | \$ 6,758,688              | \$ 38,263,032             | \$ 32,4        |
|  | -----                     | -----                     | -----          |
| Cost of revenues, including inventory purchased from<br>Soyo Computer, Inc. of \$0, \$0, and \$14,0004,259 in<br>2006, 2005 and 2004, respectively | 47,534,249                | 34,905,874                | 30,2           |
| Prior years' purchase discounts and allowances settled<br>In 2005  | --                        | (1,335,812)               |                |
|  | -----                     | -----                     | -----          |
| Cost of revenues - net   | 47,534,249                | 33,570,062                | 30,2           |
|  | -----                     | -----                     | -----          |
| Gross margin   | 9,224,439                 | 4,692,970                 | 2,2            |
|  | -----                     | -----                     | -----          |
| Costs and expenses:  |                           |                           |                |
| Sales and marketing  | 1,143,475                 | 911,039                   | 1,5            |
| General and administrative   | 5,610,810                 | 3,659,338                 | 3,5            |
| Bad debts  | 907,065                   | 34,513                    | 9              |
| Adjustment of allowance  | --                        | (462,234)                 |                |
| Depreciation and amortization  | 43,818                    | 35,394                    |                |
|  | -----                     | -----                     | -----          |
| Total cost and expenses  | 7,705,168                 | 4,178,050                 | 6,1            |
|  | -----                     | -----                     | -----          |
| Income (loss) from operations  | 1,519,271                 | 514,920                   | (3,9           |
|  | -----                     | -----                     | -----          |
| Other income (expenses):   |                           |                           |                |
| Interest income  | 10,561                    | 5,301                     |                |
| Interest expense   | (901,900)                 | (129,567)                 | (              |
| Other income (expenses)  | (106,262)                 | 150,456                   |                |
|  | -----                     | -----                     | -----          |
| Other income (expenses) - net  | (997,601)                 | 26,190                    |                |
|  | -----                     | -----                     | -----          |
| Income(loss) before provision (benefit) for income taxes   |                           |                           |                |
| Provision (benefit) for income taxes   |                           |                           |                |
| Current income tax   | (20,310)                  | 800                       |                |
| Deferred income tax  | 177,177                   | --                        |                |
|  | -----                     | -----                     | -----          |
| Net income (loss)  | 678,537                   | 540,310                   | (3,9           |
| Less: Dividends on Convertible Preferred Stock   | (216,488)                 | (1,173,753)               | (2             |
|  | -----                     | -----                     | -----          |
| Net income (loss) attributable to<br>common shareholders   | \$ 462,049                | \$ (633,443)              | \$ (4,1        |
|  | =====                     | =====                     | =====          |
|  |                           |                           |                |
| Net loss per common share - basic and diluted  | \$0.01/\$0.01             | (\$0.01)/\$0.01)          | (\$0.10        |
|  |                           |                           |                |
| Weighted average number of shares of<br>common stock outstanding - basic and diluted   | 49,025,511/<br>59,786,042 | 48,511,681/<br>52,868,673 | 40,00<br>40,00 |

See accompanying notes to consolidated financial statements.



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SOYO Group, Inc. and Subsidiary  
 Consolidated Statements of Shareholders' Equity (Deficit)  
 Years Ended December 31, 2006, 2005 and 2004

|   | Common Stock |             | Preferred Stock |             |
|---|--------------|-------------|-----------------|-------------|
|   | Shares       | Par Value   | Shares          | Par Value   |
| Balance, December 31, 2001  | 28,182,750   | 28,183      | 1,000,000       | 1,000,000   |
| Shares of common stock retained by shareholders in October 2002 transaction | 11,817,250   | 11,817      | (11,817)        |             |
| Net loss for the year ended December 31, 2002                               | --           | --          | --              | --          |
| Balance, December 31, 2002  | 40,000,000   | 40,000      | 1,000,000       | 1,000,000   |
| Net loss for the year ended December 31, 2003                               | --           | --          | --              | --          |
| Balance, December 31, 2003  | 40,000,000   | 40,000      | 1,000,000       | 1,000,000   |
| Issuance of Preferred Stock for Long Term Debt                              | 2,500,000    | 1,304,000   | 10,696,000      | 12,000,000  |
| Dividends   | 114,195      | 114,195     | 114,195         |             |
| Accretion of Discount   | 109,538      | 109,538     |                 |             |
| Net loss for the year ended December 31, 2004                               | --           | --          | (4,143,978)     | (4,143,978) |
| Balance, December 31, 2004  | 40,000,000   | 40,000      | 3,614,195       | 1,528,730   |
| Issuance of Common Stock for Private Placement                              | 500,000      | 500         | 499,500         | 500,000     |
| Issuance of Common Stock for Payment of Services                            | 30,000       | 30          | 30              |             |
| Issuance of Common Stock for Payment of Accounts Payable                    | 5,645,330    | 5,645       | 3,608,744       | 3,614,380   |
| Issuance of Common Stock for Payment of Loan                                | 1,286,669    | 1,287       | 963,714         | 965,000     |
| Issuance of Common Stock for Conversion of Preferred Stock                  | 1,219,512    | 1,220       | (1,000,000)     | (1,000,000) |
| Accretion of Discount   | 174,753      | 174,753     |                 |             |
| Preferred Stock Backup Withholding  | (84,999)     | (84,999)    |                 |             |
| Net Income  | 540,310      | 540,310     |                 |             |
| Preferred Stock Dividends   | (1,173,753)  | (1,173,753) |                 |             |
| Balance, December 31, 2005  | 48,681,511   | 48,682      | 2,614,195       | 1,617,480   |
| Issuance of Common Stock  | 39,000       | 39          | 24,531          | 24,570      |
| Issuance of Common Stock  | 267,000      | 267         | 80,100          | 80,360      |
| Issuance of Common Stock  | 38,000       | 38          | 12,502          | 12,540      |
| Accretion of Discount   | 216,488      | 216,488     |                 |             |

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|                                    |            |          |           |          |
|------------------------------------|------------|----------|-----------|----------|
| Preferred Stock Backup Withholding | (64,946)   | (64,946) |           |          |
| Employee Stock Based Compensation  | 506,221    | 506,221  |           |          |
| Misc. Adjustment                   | 17,439     | 17,439   |           |          |
| Net Income                         | 462,049    | 462,049  |           |          |
|                                    | 49,025,511 | 49,026   | 2,614,195 | 1,769,02 |

|   | Total<br>Accumulated<br>Deficit | Shareholders<br>Deficiency |
|---|---------------------------------|----------------------------|
| Balance, December 31, 2001  | (918,737)                       | (418,737)                  |
| -----   |                                 |                            |
| Shares of common stock<br>retained by<br>shareholders<br>in October 2002<br>transaction   |                                 |                            |
| Net loss for the year<br>ended December 31, 2002  | (10,733,458)                    |                            |
| Balance, December 31, 2002  | (11,652,195)                    | (11,152,195)               |
| -----   |                                 |                            |
| Net loss for the year<br>ended December 31, 2003  | (984,588)                       |                            |
| Balance, December 31, 2003  | (12,636,783)                    | (12,136,783)               |
| -----   |                                 |                            |
| Issuance of Preferred<br>Stock for Long Term Debt<br>Dividends<br>Accretion of Discount<br>Net loss for the year<br>ended December 31, 2004   |                                 |                            |
| Balance, December 31, 2004  | (16,780,761)                    | (4,057,028)                |
| -----   |                                 |                            |
| Issuance of Common<br>Stock for Private Placement<br>Issuance of Common<br>Stock for Payment of Services<br>Issuance of Common<br>Stock for Payment of Accounts Payable<br>Issuance of Common<br>Stock for Payment of Loan<br>Issuance of Common<br>Stock for Conversion of Preferred Stock | 999,000                         |                            |
| Accretion of Discount<br>Preferred Stock Backup Withholding<br>Net Income<br>Preferred Stock Dividends  |                                 |                            |
| Balance, December 31, 2005  | (17,414,204)                    | 1,477,703                  |
| =====   |                                 |                            |
| Issuance of Common Stock<br>Issuance of Common Stock<br>Issuance of Common Stock<br>Accretion of Discount   |                                 |                            |

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Preferred Stock Backup Withholding  
 To book FAS 123 adjustment  
 Misc. Adjustment  
 Net Income

|              |           |
|--------------|-----------|
|              | -----     |
| (16,952,155) | 2,732,431 |
|              | =====     |

See accompanying notes to consolidated financial statements.

SOYO Group, Inc. and Subsidiary  
 Consolidated Statements of Cash Flows

|   | Years Ended December 31, |             |             |
|---|--------------------------|-------------|-------------|
|   | 2006                     | 2005        | 2004        |
|   | -----                    | -----       | -----       |
| OPERATING ACTIVITIES  |                          |             |             |
| Net Income (loss)   | \$ 678,537               | 540,310     | \$ (3,920)  |
| Adjustments to reconcile net<br>income(loss) to net cash provided<br>by (used in) operating activities: |                          |             |             |
| Depreciation  | 43,818                   | 35,394      | 34,818      |
| Provision for doubtful accounts   | 907,065                  | 34,513      | 956,000     |
| Conversion of accounts payable to long-term debt  | 3,735,198                | --          | --          |
| Stock compensation for employees  | 506,222                  | --          | --          |
| Stock compensation paid for<br>professional services  | 134,915                  | --          | --          |
| Changes in operating assets<br>and liabilities:   |                          |             |             |
| (Increase) decrease in:   |                          |             |             |
| Accounts receivable   | (10,095,680)             | (5,236,151) | 3,785,000   |
| Inventories   | 198,409                  | (4,128,119) | 1,173,000   |
| Prepaid expenses  | (15,649)                 | 51,432      | 18,000      |
| Deferred Income Tax Asset   | (177,177)                | --          | --          |
| Deposits  | (206,175)                | (2,109)     | (9,000)     |
| Increase (decrease) in:   |                          |             |             |
| Accounts payable trade & others   | 2,096,038                | 8,017,326   | (2,458,000) |
| Accrued liabilities   | (747,341)                | 509,316     | 236,000     |
| Net cash provided by (used in) operating activities   | (2,941,820)              | (178,088)   | (183,000)   |
| INVESTING ACTIVITIES  |                          |             |             |
| Purchase of property and equipment  | (48,891)                 | (621,970)   | (158,000)   |
| Disposal of Fixed Assets  | 205,000                  | --          | --          |
| Net cash Supplied (used) in investing activities  | 156,109                  | (621,970)   | (158,000)   |

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FINANCING ACTIVITIES

|  |              |           |       |
|--|--------------|-----------|-------|
| Advances from officer, directors and major shareholder             | --           | 165,000   |       |
| Proceeds from accounts receivable discounting                      | 15,611,928   | --        | 913   |
| Repayments of accounts receivable discounting                      | (12,023,525) | --        |       |
| Repayment of advances from officer, director and major shareholder | (65,000)     | (240,000) |       |
|  | --           | 500,000   |       |
| Payment of backup withholding                                      |              |           |       |
| taxes on accreted dividends on preferred stock                     | (64,946)     | (84,999)  |       |
|  | -----        | -----     | ----- |
| Net cash provided by financing activities                          | 3,458,457    | 340,001   | 913   |
|  | -----        | -----     | ----- |

CASH AND CASH EQUIVALENTS:

|                         |           |           |       |
|-------------------------|-----------|-----------|-------|
| Net increase (decrease) | 672,746   | (460,057) | 571   |
| At beginning of year    | 828,294   | 1,288,351 | 717   |
|                         | -----     | -----     | ----- |
| At end of year          | 1,501,040 | 828,294   | 1,288 |
|                         | =====     | =====     | ===== |

SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:

|                            |         |        |     |
|----------------------------|---------|--------|-----|
| Cash paid for interest     | 901,900 | 97,783 | 23, |
| Cash paid for income taxes | 20,310  | 800    |     |

NON-CASH INVESTING AND FINANCING ACTIVITIES

|  |         |           |      |
|--|---------|-----------|------|
| Settlement of business loan of \$913,750 and accrued interest of \$51,251 through issuance of common stock | --      | 965,001   |      |
| Settlement of accounts payable through issuance of common stock  | --      | 3,614,419 |      |
| Conversion of Class A preferred stock to common stock  | --      | 1,000     |      |
| Accretion of discount on Class B preferred stock   | 216,488 | 174,753   | 109, |
| Deemed dividend on Class A preferred stock   | --      | 999,000   |      |

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Noncash dividend on Class B  
preferred stock

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114,

See accompanying notes to consolidated financial statements.

### SOYO Group, Inc. and Subsidiary Notes to Consolidated Financial Statements Years Ended December 31, 2006, 2005 and 2004

#### 1. Organization and Business

##### a. 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 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 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, and pro forma information has not been presented, as this transaction is not a business combination.

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 MingTung Chok, the Company's President, Chief Executive Officer and Director, and Nancy Chu, the Company's Chief Financial Officer, Secretary and Director. 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".

##### b. Nature of Business

SOYO Group, Inc. is a distributor of consumer electronics, computer products and

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communications services and products. The Company radically changed its core offerings for sale in 2004. Through the consumer electronics division, SOYO offers a full line of LCD display televisions and monitors, as well as Bluetooth wireless devices. Through the communications division, SOYO offers discount telephone service through VoIP protocol. The services can be purchased through different types of plans and rates, making the service very flexible for the user. The hardware to create and run VoIP services is also available for sale. Lastly, the Company offers a full line of designer motherboards and related peripherals for intensive multimedia applications, corporate alliances, telecommunications and specialty market requirements. The breadth of the product line also includes Bare Bone 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 any home and office (SOHO) users.

SOYO Group's products are 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 consumers throughout North America and Latin America.

During the years that the Company operated through October 24, 2002, SOYO Nevada was a wholly-owned subsidiary of SOYO Taiwan.

As a general rule, the Company has been totally reliant upon the cash flows from its operations to fund future growth. In the last few years, the Company has begun and continues to implement the following steps to increase its financial position, liquidity, and long term financial health:

In 2005, The Company completed a small private placement, began factoring invoices to improve cash flows, and converted several million dollars of debt to equity, all of which improved the Company's financial condition.

In 2006, the Company changed factors to a more beneficial arrangement, and entered into a Trade Finance Flow facility with GE Capital to fund "Star" transactions. The agreement provided for GE Capital to guarantee payment, on the Company's behalf, for merchandise ordered from GE Capital approved manufacturers in Asia. GE Capital guarantees the payment subject to a purchase order from one of our customers. The Company accepts delivery of the goods in the US, then has the option to either pay for the goods or sell the receivable (from the customer) to our factor, who pays GE Capital. For more information, please see the contract, which is included as exhibit 10.4 to this report.

In March 2007, the Company announced that it had secured a \$12 MM Asset Based Credit Facility from a California bank to provide funding for future growth. For more informaiton, please see the Form 8-K filed by the company on March 2,2007.

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

## 2. Basis of Presentation and Summary of Significant Accounting Policies

### a. Presentation

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

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America.

### b. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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.

### c. Cash and Cash Equivalents

Cash and cash equivalents include all highly-liquid investments with an original maturity of three months or less at the date of purchase. The Company minimizes its credit risk by investing its cash and cash equivalents with major banks and financial institutions located primarily in the United States.

### d. 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 will reduce the computed average cost if it exceeds the component's marketvalue.

During the years ended December 31, 2006, 2005 and 2004, the Company wrote-down the value of its inventory by \$0, \$0 and \$47,084 respectively.

### e. Property and Equipment

Property and equipment are stated at cost. Major renewals and improvements are capitalized; minor replacements and maintenance and repairs are charged to operations. Depreciation is provided on the straight-line method over the estimated useful lives of the respective assets (three to seven years).

Leasehold improvements are amortized over the shorter of the useful life of the improvement or the life of the related lease.

### f. Impairment or Disposal of Long-Lived Assets

Effective January 1, 2002, the Company adopted the provisions of Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets". The Company assesses potential impairments to its long-lived assets when events or changes in circumstances indicate that the carrying amount of an asset may not be fully recoverable. If required, an impairment loss is recognized as the difference between the carrying value and the fair value of the assets. No impairment losses associated with the Company's long-lived assets were recognized during the years ended December 31, 2006 and 2005.

### g. Revenue Recognition

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.

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The Company recognizes product sales generally at the time the product is shipped, although under certain circumstances the Company recognizes product sales at the time the product reaches its destination. Concurrent with the recognition of revenue, the Company provides for the estimated cost of product warranties and reduces revenue for estimated product returns. Sales incentives are generally classified as a reduction of revenue and are recognized at the later of when revenue is recognized or when the incentive is offered. When other significant obligations remain after products are delivered, revenue is recognized only after such obligations are fulfilled. Shipping and handling costs are included in cost of goods sold.

### h. 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.

### i. Warranties

The Company's suppliers generally warrant the products distributed by the Company and allow returns of defective products, including those that have been returned to the Company by its customers. The Company does not independently warrant the products that it distributes, but it does provide warranty services on behalf of the supplier.

### j. Concentration of Cash and Credit Risk

The Company maintains its cash in bank accounts which, at times, may exceed federally insured limits. The Company has not experienced any losses in such accounts to date. Management believes that the Company is not exposed to any significant risk on the Company's cash balances.

Financial instruments that potentially subject the Company to significant concentrations of credit risk consist primarily of trade accounts receivable. The Company performs ongoing credit evaluations with respect to the financial condition of its debtors, but does not require collateral. The Company maintains credit insurance for a portion of this credit risk.

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.

### k. Advertising

Advertising costs are charged to expense as incurred. The Company has not incurred direct advertising costs. However, the Company may participate in cooperative advertising programs with certain of its customers by paying a stipulated percentage of the sales invoice price. Cooperative advertising costs paid for the years ended December 31, 2006, 2005, and 2004 were \$834,616,



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\$849,897, and \$1,481,441 respectively, and are presented under sales and marketing costs in the accompanying consolidated statements of operations.

### l. Income Taxes

The Company accounts for income taxes using the asset and liability method whereby deferred income taxes are recognized for the tax consequences of temporary differences by applying statutory tax rates applicable to future years to differences between the financial statement carrying amounts and the tax bases of certain assets and liabilities. Changes in deferred tax assets and liabilities include the impact of any tax rate changes enacted during the year. A valuation allowance is provided for the amount of deferred tax assets that, based on available evidence, are not expected to be realized.

### m. Income (Loss) Per Common 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 (loss) per share is computed by dividing net income (loss) 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, and stock options granted to employees in 2005. The stock options were not included in the calculation of fully diluted EPS for the year ended December 31, 2006, since the strike price of the outstanding options is below the market price of the Company's common stock. None of the potentially dilutive securities were included in the calculation of loss per share for the years ended December 31, 2005, and 2004 because the Company incurred a loss attributable to common shareholders during such periods and their effect would have been anti-dilutive. Accordingly, basic and diluted loss per share is the same for the years ended December 31, 2006, 2005 and 2004.

### n. Comprehensive Income

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 or loss for the years ended December 31, 2006, 2005 and 2004.

### o. Fair Value of Financial Instruments

The Company believes that the carrying value of its cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities as of December 31, 2006 and 2005 approximate their respective fair values due to the short-term nature of those instruments.

### p. 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

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based method, compensation cost is the excess, if any, of the quoted market price of the stock at grant date or other measurement date over the amount an employee must pay to acquire the stock. Under the intrinsic value method, the Company has recognized stock-based compensation common stock on the date of grant.

Effective January 1, 2006 the Company adopted SFAS 123(R) using the modified prospective approach and accordingly prior periods have not been restated to reflect the impact of SFAS 123(R). Under SFAS 123(R), 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 straight-line 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 three years.

SFAS 123(R) 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 has been recorded net of estimated forfeitures for the year ended December 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.

SFAS 123 requires the Company to provide pro-forma information regarding net loss as if compensation cost for the stock options granted to the Company's employees had been determined in accordance with the fair value based method prescribed in SFAS 123. Options granted to non-employees are recognized in these financial statements as compensation expense under SFAS 123 (See Note 11) using the Black-Scholes option-pricing model.

If the fair value based method under FAS 123 had been applied in measuring stock-based compensation expense for the year ended December 31, 2005, the pro forma on net income (loss) and net income (loss) per share would have been as follows:

|   | Year Ended<br>December 31<br>2005<br>----- |
|---|--|
| Net income (loss) attributable to common shareholders, as reported  | \$ (633,443)                               |
| Add: Stock-based employee compensation expense included in reported net income, net of related tax effect   | -  |
| Deduct: Total stock-based employee compensation expense determined under fair-value based method for all awards not included in net income (loss) | (224,919)                                  |
| Pro forma net income (loss) attributable to common shareholders   | \$ (858,362)<br>=====                      |
| Income (loss) per share:  |  |
| Basic/diluted - as reported   | (\$0.01) / (\$0.0                          |
| Basic/diluted - pro forma   | (\$0.02) / (\$0.0                          |

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### q. 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.

### r. Recent Accounting Pronouncements

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" ("SFAS 159") which permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. SFAS 159 will be effective for the Company on January 1, 2008. The Company is currently evaluating the impact of adopting SFAS 159 on its financial position, cash flows, and results of operations.

In October 2006, the Emerging Issues Task Force ("EITF") issued EITF 06-3, "How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (that is, Gross versus Net Presentation)" to clarify diversity in practice on the presentation of different types of taxes in the financial statements. The Task Force concluded that, for taxes within the scope of the issue, a company may adopt a policy of presenting taxes either gross within revenue or net. That is, it may include charges to customers for taxes within revenues and the charge for the taxes from the taxing authority within cost of sales, or, alternatively, it may net the charge to the customer and the charge from the taxing authority. If taxes subject to EITF 06-3 are significant, a company is required to disclose its accounting policy for presenting taxes and the amounts of such taxes that are recognized on a gross basis. The guidance in this consensus is effective for the first interim reporting period beginning after December 15, 2006 (the first quarter of the Company's fiscal year 2007). The Company does not expect the adoption of EITF 06-3 to have a material impact on our results of operations, financial position or cash flow.

In September 2006, the United States Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" ("SAB 108"). This SAB provides guidance on the consideration of the effects of prior year misstatements in quantifying current year misstatements for the purpose of a materiality assessment. SAB 108 establishes an approach that requires quantification of financial statement errors based on the effects on each of the company's balance sheets, statements of operations and related financial statement disclosures. The SAB permits existing public companies to record the cumulative effect of initially applying this approach in the first year ending after November 15, 2006 by recording the necessary correcting adjustments to the carrying values of assets and liabilities as of the beginning of that year with the offsetting adjustment recorded to the opening balance of retained earnings. Additionally, the use of the cumulative effect transition

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method requires detailed disclosure of the nature and amount of each individual error being corrected through the cumulative adjustment and how and when it arose. The Company is currently evaluating the impact SAB 108 may have on its results of operations and financial condition.

In September 2006, the FASB issued SFAS No. 158, "Employer's accounting for Defined Benefit Pension and Other Post Retirement Plans". SFAS No. 158 requires

employers to recognize in its statement of financial position an asset or liability based on the retirement plan's over or under funded status. SFAS No. 158 is effective for fiscal years ending after December 15, 2006. The Company is currently evaluating the effect that the application of SFAS No. 158 will have on its results of operations and financial condition.

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Issues No. 157, "Fair Value Measurements" ("SFAS 157"), which defines the fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Early adoption is encouraged, provided that the Company has not yet issued financial statements for that fiscal year, including any financial statements for an interim period within that fiscal year. The Company is currently evaluating the impact SFAS 157 may have on its financial condition or results of operations.

In July 2006, the FASB released FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109 (FIN 48). FIN 48 clarifies the accounting and reporting for uncertainties in income tax law. This interpretation prescribes a comprehensive model for the financial statement recognition, measurement, presentation and disclosure of uncertain tax positions taken or expected to be taken in income tax returns. This statement is effective for fiscal years beginning after December 15, 2006. The Company is currently evaluating the impact FIN 48 may have on its financial condition or results of operations.

In March 2006, the FASB issued SFAS No. 156, "Accounting for Servicing of Financial Assets" ("SFAS NO. 156"), which provides an approach to simplify efforts to obtain hedge-like (offset) accounting. This Statement amends FASB Statement No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities", with respect to the accounting for separately recognized servicing assets and servicing liabilities. The Statement (1) requires an entity to recognize a servicing asset or servicing liability each time it undertakes an obligation to service a financial asset by entering into a servicing contract in certain situations; (2) requires that a separately recognized servicing asset or servicing liability be initially measured at fair value, if practicable; (3) permits an entity to choose either the amortization method or the fair value method for subsequent measurement for each class of separately recognized servicing assets or servicing liabilities; (4) permits at initial adoption a one-time reclassification of available-for-sale securities to trading securities by an entity with recognized servicing rights, provided the securities reclassified offset the entity's exposure to changes in the fair value of the servicing assets or liabilities; and (5) requires separate presentation of servicing assets and servicing liabilities subsequently measured at fair value in the balance sheet and additional disclosures for all separately recognized servicing assets and servicing liabilities. SFAS No. 156 is effective for all separately recognized servicing assets and liabilities as of the beginning of an entity's fiscal year that begins after September 15, 2006, with earlier adoption permitted in certain circumstances. The Statement also

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describes the manner in which it should be initially applied. This Statement does not affect the Company's financial statements.

In February 2006, the FASB issued SFAS No. 155, "Accounting for Certain Hybrid Financial Instruments", which amends SFAS No. 133, "Accounting for Derivatives Instruments and Hedging Activities" and SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities". SFAS No. 155 amends SFAS No. 133 to narrow the scope exception for interest-only and principal-only strips on debt instruments to include only such strips

representing rights to receive a specified portion of the contractual interest or principle cash flows. SFAS No. 155 also amends SFAS No. 140 to allow qualifying special-purpose entities to hold a passive derivative financial instrument pertaining to beneficial interests that itself is a derivative instrument. This Statement does not affect the Company's financial statements.

In November 2005, the FASB issued FSP FAS 115-1 and FAS 124-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments" ("FSP 115-1 and 124-1"), which clarifies when an investment is considered impaired, whether the impairment is other-than-temporary, and the measurement of an impairment loss. It also includes accounting considerations subsequent to the recognition of the other-than-temporary impairment and requires certain disclosures about unrealized losses that have not been recognized as other-than-temporary impairments. FSP 115-1 and 124-1 are effective for all reporting periods beginning after December 15, 2005. The Company does not anticipate that the implementation of these statements will have a significant impact on its financial position, results of operations or cash flows.

In May 2005, the FASB issued SFAS No. 154, "Accounting Changes and Error Corrections" ("SFAS No. 154"). SFAS No. 154 is a replacement of Accounting Principles Board Opinion No. 20 and SFAS No. 3. SFAS No. 154 provides guidance on the accounting for and reporting of accounting changes and error corrections. It establishes retrospective application as the required method for reporting a change in accounting principle. SFAS No. 154 provides guidance for determining whether retrospective application of a change in accounting principle is impracticable and for reporting a change when retrospective application is impracticable. SFAS No. 154 also addresses the reporting of a correction of an error by restating previously issued financial statements. SFAS No 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. The Company does not believe that it will have a material impact on its financial position, results of operations or cash flows.

In December 2004, the Financial Accounting Standards Board ("FASB") issued SFAS No. 153, "Exchanges of Nonmonetary Assets, an amendment of APB Opinion No. 29, Accounting for Nonmonetary Transactions." The amendments made by Statement 153 are based on the principle that exchanges of nonmonetary assets should be measured based on the fair value of the assets exchanged. Further, the amendments eliminate the narrow exception for nonmonetary exchanges of similar productive assets and replace it with a broader exception for exchanges of nonmonetary assets that do not have commercial substance. Previously, Opinion 29 required that the accounting for an exchange of a productive asset for a similar productive asset or an equivalent interest in the same or similar productive asset should be based on the recorded amount of the asset relinquished. Opinion 29 provided an exception to its basic measurement principle (fair value) for exchanges of similar productive assets. The FASB believes that exception required that some nonmonetary exchanges, although commercially substantive, be recorded on a carryover basis. By focusing the exception on exchanges that lack commercial substance, the FASB believes this statement produces financial

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reporting that more faithfully represents the economics of the transactions. SFAS 153 is effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. Earlier application is permitted for nonmonetary asset exchanges occurring in fiscal periods beginning after the date of issuance. The provisions of SFAS 153 shall be applied prospectively. The Company has evaluated the impact of the adoption of SFAS 153, and does not believe the impact will be significant to the Company's overall results of operations or financial position.

In November 2004, the FASB issued SFAS No. 151, "Inventory Costs, an amendment of ARB No. 43, Chapter 4". The amendments made by Statement 151 clarify that abnormal amounts of idle facility expense, freight, handling costs, and wasted materials (spoilage) should be recognized as current period charges and require the allocation of fixed production overheads to inventory based on the normal capacity of the production facilities. The guidance is effective for inventory costs incurred during fiscal years beginning after June 15, 2005. Earlier application is permitted for inventory costs incurred during fiscal years beginning after November 23, 2004. This Statement does not affect the Company's financial statements.

### 3. Accounts Receivable

The Company's accounts receivable at December 31, 2006 and 2005 are summarized as follows:

|                                       | 2006          | 2005         |
|---------------------------------------|---------------|--------------|
|                                       | -----         | -----        |
| Accounts receivable                   | \$ 589,224    | \$ 1,074,550 |
| Less: Allowance for doubtful accounts | (388,958)     | (589,224)    |
|                                       | -----         | -----        |
| Balance, end of year                  | \$ 12,878,732 | \$ 7,278,520 |
|                                       | =====         | =====        |

Changes in the allowance for doubtful accounts for the years ended December 31, 2006 and 2005 are summarized as follows:

|   | 2006       | 2005         |
|---|------------|--------------|
|   | -----      | -----        |
| Balance, beginning of year                | \$ 589,224 | \$ 1,074,550 |
| Add: Amounts provided during the year     | 235,939    | (427,721)    |
| Less: Amounts written off during the year | (436,205)  | (57,605)     |
|   | -----      | -----        |
| Balance, end of year                      | \$ 388,958 | \$ 589,224   |
|   | =====      | =====        |

In 2006, there was a direct write off of \$671,126 for sales transactions during the year which turned out to be uncollectible.

Since 2004, the Company has used three different factors to increase cash flow. As a result, credit policies and requirements have changed frequently in the last few years. When the Company was prepared to sign the agreement for the \$12 million finance line (see Form 8-K file March 2, 2007), it reexamined the receivables and wrote off all balances over 90 days, and wrote down to present value all balances over 90 days that were making monthly payments. This resulted in a large write off taken in the fourth quarter. As a result, any balances with even a small question about collectivity have been written off. Because of

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this aggressive stance, the allowance for bad debts has decreased, even though the accounts receivables balance has increased by over \$5 million.

The Company began factoring its invoices in 2005 to improve cash flow. The Company's initial factor was Wells Fargo PLC. In February 2006, the Company signed a one year contract with Accord Financial Services of North Carolina for factoring services. The agreement expired in February 2007 and was not renewed.

Under the Accord agreement, all of our receivables were sold with recourse. As such, the Company continues to evaluate each of these receivables monthly in

regard to its allowance for bad debts. The original factor, Wells Fargo, bought all accounts without recourse. When the switch over to Accord occurred, those transactions were "with recourse".

In 2006, the Company entered into a Trade Finance Flow facility with GE Capital to fund "Star" transactions. The agreement provided for GE Capital to guarantee payment, on the Company's behalf, for merchandise ordered from GE Capital approved manufacturers in Asia. GE Capital guarantees the payment subject to a purchase order from one of our customers. The Company accepts delivery of the goods in the US, then has the option to either pay for the goods or sell the receivable (from the customer) to our factor, who paid GE Capital. The terms and conditions of each advance vary according to current market conditions. At December 31, 2006, certain of the Company's receivables had been bought with recourse by Accord Financial Services. At December 31, 2005, \$580,363 of the Company's receivables had been factored and were owned by Wells Fargo.

#### 4. Property and Equipment

At December 31, 2006 and 2005, property and equipment consisted of the following:

|                                | December 31, |           |
|--------------------------------|--------------|-----------|
|                                | 2006         | 2005      |
| Computer and Equipment         | \$567,642    | \$744,176 |
| Furniture and Fixtures         | 40,357       | 27,943    |
| Leasehold Improvements         | 91,941       | 83,928    |
| Automobiles                    | 11,075       | 11,075    |
| Less: Accumulated Depreciation | (159,300)    | (115,480) |
| Total                          | \$551,715    | \$751,642 |

For the years ended December 31, 2006, 2005 and 2004, depreciation and amortization expense related to property and equipment was \$43,818, \$35,394 and \$34,998, respectively.

#### 5. Advances from Officer, Director and Major Shareholder

During March 2003, Nancy Chu, the Company's Chief Financial Officer, director and major shareholder, made short-term advances to the Company of \$360,000 for

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working capital purposes, of which \$120,000 was repaid during September 2003. The remaining \$240,000 was paid during 2005.

In October 2005, the Company borrowed \$165,000 from an individual for working capital purposes. During 2006, \$65,000 of the loan was repaid. At December 31, 2006, the loan balance stands at \$100,000.

### 6. Business Loan

On March 29, 2004, LGT Computer, Inc. loaned the Company \$213,750 pursuant to an unsecured note payable due March 28, 2005, with interest at 4% per annum. On May 28, 2004, LGT Computer, Inc. loaned the Company an additional \$700,000 pursuant to an unsecured note payable due May 27, 2005, with interest at 4% per annum. On March 28, 2005, by mutual agreement of the parties, the due dates of the notes were extended one year at the same interest rate. On September 2, 2005, the two loans and accrued interest of \$51,251 were repaid through the issuance of 1,286,669 shares of our restricted common stock. On that date, the market price of the stock was \$0.75.

### 7. Long Term Debt

Soyo is indebted to Corion for products purchased between January 2006 and March 2006.

On October 19, 2006, the Parties reached a mutually beneficial settlement relating to the outstanding balance as of that date amounting to \$4,252,682, whereby Soyo agrees to pay Corion the sum of Fifty Thousand dollars (\$50,000) each week until fully paid. Notwithstanding the foregoing, Soyo shall have the right, at its sole discretion, to defer four (4) payments during each calendar quarter. Two (2) of these payments shall be deferred until the calendar quarter following their deferral on a date selected by Soyo, and the remaining two (2) payments shall be paid in weekly installments following all regularly scheduled payments, but in any event not later than October 1, 2008.

No interest shall be charged on the Debt. Soyo shall pay the Debt in full by no later than October 1, 2008.

Until the Debt is paid in full, Soyo agrees not to give any other supplier a consensual lien with priority senior than that of Corion, except for purchase money liens and other similar interests.

### 8. Shareholders' Equity

#### a. Common Stock

As of December 31, 2002, the Company had authorized 75,000,000 shares of common stock with a par value of \$0.001 per share.

Effective October 24, 2002, the Company issued 28,182,750 shares of common stock to Ming Tung Chok and Nancy Chu, who are members of SOYO Nevada management (see Note 1). The shares of common stock were valued at par value, since the transaction was deemed to be a recapitalization of SOYO Nevada. During October 2002, 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 common stock. When the transaction was complete, and control of the Company was transferred, SOYO Nevada management owned 34,209,548 shares of the 40,000,000 outstanding shares of the Company's



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common stock. Subsequent to the transaction, management distributed 8,000,000 shares of common stock to various brokers, bankers and other individuals that assisted with the transaction. No one individual or corporation other than those named in Item 12 of this report ever owned more than 5% of the common shares

outstanding. As a result of this transaction, SOYO Group management currently owns 26,209,548 of the 49,025,511 shares outstanding as of December 31, 2006.

### b. Preferred Stock

As of December 31, 2005, the Company had authorized 10,000,000 shares of preferred stock with a par value \$0.001 per share.

The Board of Directors is vested with the authority to divide the authorized shares of preferred stock into series and to determine the relative rights and preferences at the time of issuance of the series.

Effective October 24, 2002, the Company issued 1,000,000 shares of Class A convertible preferred stock to SOYO Taiwan (see Note 1) with a stated liquidation value of \$1.00 per share. The shares of Class A preferred stock were valued at par value, since the transaction was deemed to be a recapitalization of SOYO Nevada. Each share of Class A preferred stock has one vote per share.

The Class A preferred stock has no stated dividend rate. The shares of Class A preferred stock are convertible, in whole or in part, into common stock at any time during the three-year period subsequent to their issuance, based on the average closing bid price of the common stock for a period of five business days prior to conversion. On October 24, 2005, the one million shares of preferred stock were converted to 1,219,512 shares of common stock. The price of our common stock on that day was \$0.82.

During the first quarter of 2004, 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. SOYO Taiwan forgave debt in an amount equal to the difference between \$12,000,000 and the value of the preferred stock. This forgiveness will be treated as a capital transaction.

Payment was received by SOYO Taiwan in February and March 2004. An agreement was reached 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 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

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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-transferrable.

For the year ended December 31, 2006, the Company recorded accreted dividends of \$216,488. For the year ended December 31, 2005, the Company recorded aggregate dividends of \$1,173,753, based on the accretion of the discount on the Class B Convertible Preferred Stock of \$174,753, and the adjustment of \$999,000 to the carrying value of the Class A preferred stock, which is described above. The Company did not declare or accrue any additional dividends on the Class B Preferred Stock.

### c. Stock Options and Warrants

As of December 31, 2006, the Company had both warrants and options outstanding. The outstanding warrants were those issued to Evergreen Technology as part of the private placement completed in March 2005, and described above.

On July 22, 2005, the Company issued 2,889,000 option grants to employees at a strike price of \$0.75. One third of those options vested and were available for purchase on July 22, 2006, one third will vest on July 22, 2007, and one third will vest on July 22, 2008. The grants will expire if unused on July 22, 2010.

The Company did not grant any stock options to employees, officers or directors in 2006. As of December 31, 2006, 13 individuals had left the Company, resulting in the forfeiture of 510,000 options. As of December 31, 2006, 2,379,000 of the 2,889,000 options granted were still outstanding, and 793,000 had vested. As of December 31, 2006, none of the options outstanding had been exercised.

### Stock Based Compensation

Upon the adoption of SFAS123(R), the Company recorded \$506,222 in compensation costs relating to stock options granted to employees. The amounts recorded represent equity-based compensation expense related to options that were issued in 2005. The compensation costs are based on the fair value at the grant date. There was no such expense recorded during our fiscal year 2005.

The fair value of the options expensed during the year ended December 31, 2006 was estimated using the Black-Scholes option-pricing model with the following assumptions: risk free interest rate of 4.04 %, expected life of five (5) years and expected volatility 147%. The weighted average fair value of the options granted during the year was approximately \$1.5 million.

### 9. Income Taxes

Income before taxes and provision for taxes for each of the three years December 31, 2006, 2005 and 2004 consist of the following:

|                                   | Year Ended December 31 |            |               |
|-----------------------------------|------------------------|------------|---------------|
|                                   | 2006                   | 2005       | 2004          |
| Income (loss) before income taxes | \$ 521,670             | \$ 541,110 | \$(3,919,445) |

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|                            |              |        |        |
|----------------------------|--------------|--------|--------|
| Provision for income taxes |              |        |        |
| Federal                    |              |        |        |
| Current                    | 68           | --     | --     |
| Deferred                   | (132,427)    | --     | --     |
| State                      |              |        |        |
| Current                    | 20,242       | 800    | 800    |
| Deferred                   | (44,750)     | --     | --     |
|                            | -----        | -----  | -----  |
| Total income tax expense   | \$ (156.867) | \$ 800 | \$ 800 |
|                            | =====        | =====  | =====  |

Income taxes amounted to \$ 20,310, \$800, and \$800 for the years ended December 31, 2006, 2005 and 2004, respectively.

The provision for income tax differed from the amount computed by applying the U.S. federal statutory tax rate to income before income taxes due to the effects of the following:

|  | -----<br>Year Ended December 31<br>----- |       |       |
|--|--|-------|-------|
|  | 2006                                     | 2005  | 2004  |
|  | ----                                     | ----  | ----  |
| Statutory federal income tax rate                      | 34%                                      | 34%   | 34%   |
| Increase (reduction) in rate resulting from:           |  |       |       |
| State and foreign taxes, net of federal benefit        | 9%                                       | 9%    | 9%    |
| Stock-based compensation                               | (34%)                                    | --    | --    |
| Net operating loss and net operating loss carryforward | (39%)                                    | (43%) | (43%) |
|  | ---                                      | ---   | ---   |
| Total income tax expense                               | (30%)                                    | 0%    | 0%    |
|  | ===                                      | ===   | ===   |

The deferred tax assets consists of temporary tax difference from stock-based compensation of \$177,177 as of December 31, 2006. There were no deferred tax assets and liabilities recognized through December 31, 2005.

As of December 31, 2006, the Company had federal and state net operating loss carryforwards of \$4,195,130 and \$0, respectively, expiring in various years through 2024, which can be used to offset future taxable income, if any. No deferred tax benefit for these operating losses has been recognized in the consolidated financial statements due to the uncertainty as to their realizability in future periods.

10. Commitments and Contingencies

a. Operating Lease

The Company leases its office and warehouse premises under a five-year non-cancelable operating lease that expires on November 30, 2008, with a five year renewal option. The lease provides for monthly payments of base rent and an unallocated portion of building operating costs. The minimum future lease payments are as follows:

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Years Ending December 31,  
-----

|      |         |
|------|---------|
| 2007 | 212,692 |
| 2008 | 194,967 |

Rent expense for the years ended December 31, 2006, 2005 and 2004 was \$229,540, \$238,836 and \$229,718 respectively.

### 11. Restatement and Reclassification

The Company is restating its previously issued 2006 consolidated financial statements for the following reasons: error in recognition of accounts receivable sold with recourse and change in classification of deferred income tax assets and deposits.

The effect on the Company's previously issued 2006 financial statements is summarized as follows:

|  | As Previously<br>Reported<br>----- | Increase<br>(Decrease)<br>----- | Restated<br>----- |
|--|------------------------------------|---------------------------------|-------------------|
| <b>Balance Sheet Data</b>              |                                    |                                 |                   |
| Accounts receivable                    | \$12,878,732                       | \$ 3,588,403                    | \$16,467,135      |
| Deferred income tax assets             | --                                 | 177,177                         | 177,177           |
| Deposits                               | --                                 | 243,095                         | 243,095           |
| Total current assets                   | 22,209,026                         | 4,008,675                       | 26,217,701        |
| Deferred income tax assets (long-term) | 177,177                            | (177,177)                       | --                |
| Deposits (long-term)                   | 243,095                            | (243,095)                       | --                |
| Total Assets                           | \$23,181,013                       | \$ 3,588,403                    | \$26,769,416      |
| <br>                                   |                                    |                                 |                   |
| Business loan                          | \$ --                              | \$ 3,588,403                    | \$ 3,588,403      |
| Total current liabilities              | 16,713,384                         | 3,588,403                       | 20,301,787        |
| Total Liabilities                      | \$20,448,582                       | \$ 3,588,403                    | \$24,036,985      |
| <br>                                   |                                    |                                 |                   |
| Total Shareholders' Equity             | \$ 2,732,431                       | \$ --                           | \$ 2,732,431      |
| <br>                                   |                                    |                                 |                   |
| <b>Statement of Operations Data</b>    |                                    |                                 |                   |
| Net Income                             | \$ 678,537                         | \$ --                           | \$ 678,537        |

### 12. Significant Concentrations

#### a. Customers

The Company sells to both distributors and retailers. Revenues through such distribution channels for the years ended December 31, 2006, 2005 and 2004 are summarized as follows:

| Year Ended December 31 |       |       |       |       |       |
|------------------------|-------|-------|-------|-------|-------|
|                        | 2006  | %     | 2005  | %     | 2004  |
|                        | ----- | ----- | ----- | ----- | ----- |

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|              |                     |              |                     |              |                     |              |
|--------------|---------------------|--------------|---------------------|--------------|---------------------|--------------|
| Revenues     |                     |              |                     |              |                     |              |
| Distributors | \$35,510,804        | 62.6         | \$22,312,488        | 58.3         | \$14,704,452        | 45.3         |
| Retailers    | 15,187,152          | 26.8         | 15,742,332          | 41.2         | 17,721,962          | 54.7         |
| Others       | 6,060,732           | 10.6         | 208,212             | 0.5          | N/A                 | N/A          |
| <b>Total</b> | <b>\$56,758,688</b> | <b>100.0</b> | <b>\$38,263,032</b> | <b>100.0</b> | <b>\$32,426,414</b> | <b>100.0</b> |

During the year ended December 31, 2006, no customer accounted for more than 8% of sales.

During the year ended December 31, 2005, the Company had one customer (E23) that accounted for revenues of \$13,552,324, equivalent to 35% of net revenues.

### b. Geographic Segments

Revenues by geographic segment are summarized as follows:

|                           | Year Ended December 31 |              |                     |              |                     |
|---------------------------|------------------------|--------------|---------------------|--------------|---------------------|
|                           | 2006<br>-----          | %            | 2005<br>-----       | %            | 2004<br>-----       |
| Revenues                  |                        |              |                     |              |                     |
| United States             | \$42,628,547           | 75.2         | \$20,686,944        | 54.1         | \$25,936,978        |
| Other N. America          | 2,472,209              | 4.4          | 983,606             | 2.6          | N/A                 |
| Central and South America | 10,253,665             | 18.0         | 2,993,532           | 7.8          | 6,317,907           |
| Hong Kong                 | 139,490                | 0.2          | 13,598,950          | 35.4         | 171,529             |
| Other locations           | 1,264,777              | 2.2          | N/A                 | N/A          | N/A                 |
| <b>Total</b>              | <b>\$56,758,688</b>    | <b>100.0</b> | <b>\$38,263,032</b> | <b>100.0</b> | <b>\$32,426,414</b> |

During the year 2004 segment data on the "Other N. America Business" segment was not kept as it was very small in relation to the size of the United States business at that time, no compilations of the data were made as there were no internal decision process that would have been governed by such information and the compilation of this information would have been impractical and offered no value to the organization.

During the first part of 2005, the Company had made a commitment to its new product lines, but did not have much inventory to sell. While waiting for the initial inventory shipments, the Company entered into a short term agreement to make sales of computer components to a vendor in Hong Kong (E23). The sales had relatively low margin, and not a business that the Company planned to be in long term. Nevertheless, the sales of such products in 2005 represented a significant

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portion of the Company's business.

Revenues by product line are summarized as follows:

|                                   | Year Ended December 31 |              |                     |              |                     |
|-----------------------------------|------------------------|--------------|---------------------|--------------|---------------------|
|                                   | 2006                   | %            | 2005                | %            | 2004                |
|                                   | -----                  | -----        | -----               | -----        | -----               |
| Revenues                          |                        |              |                     |              |                     |
| Consumer electronics              | \$27,543,873           | 48.5         | \$18,739,719        | 49.0         | N/A                 |
| Computer parts and<br>peripherals | 29,204,792             | 51.5         | 18,906,367          | 49.4         | N/A                 |
| Voice and communication           | 10,023                 | --           | 616,946             | 1.6          | N/A                 |
| <b>Total</b>                      | <b>\$56,758,688</b>    | <b>100.0</b> | <b>\$38,263,032</b> | <b>100.0</b> | <b>\$32,426,414</b> |

The breakdowns to segregate sales by product line is not available for years prior to 2005. During the years prior to 2005, the Company sold primarily computer parts and peripherals. The dollar volume of sales of both consumer electronics and voice and communication products were very small and immaterial in the scope of the Company's business. As sales of consumer electronics and voice and communication products have grown, the Company has begun recognizing the sales in each category, and will continue to segregate the sales for reporting purposes in the future.

### c. Suppliers

From the Company's inception through December 31, 2003, over 80% of the products sold were produced by SOYO Taiwan. In 2004, the Company went through a partial reorganization, changing the sales mix. The decision was made to focus more on peripherals, VoIP, and other products, while deemphasizing sales of hardware and motherboards, which are much more mature markets. As a result, the Company significantly reduced its reliance on SOYO Taiwan.

During the years ended December 31, 2006 and 2005, the Company did not purchase any products from SOYO Taiwan. During 2006, no more than 44% of the products distributed by the SOYO Group were supplied by any one supplier. As

started in 2004, SOYO Group, Inc. is aggressively establishing new partnerships with other OEM manufacturers in the North America and Asia Pacific Regions in order to provide innovative products for consumers.

The following is a summary of the Company's transactions and balances with SOYO Taiwan as of and for the years ended December 31, 2006, 2005 and 2004:

|                                  | December 31, |       |             |
|----------------------------------|--------------|-------|-------------|
|                                  | 2006         | 2005  | 2004        |
|                                  | -----        | ----- | -----       |
| Accounts payable to SOYO Taiwan  | \$0          | \$0   | \$1,314,910 |
| Long-term payable to SOYO Taiwan | \$0          | \$0   | \$0         |

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|                            | Years Ended December 31, |           |              |
|----------------------------|--------------------------|-----------|--------------|
|                            | 2006                     | 2005      | 2004         |
| Purchases from SOYO Taiwan | \$0                      | \$0       | \$14,004,259 |
| Payments to SOYO Taiwan    | \$0                      | \$873,050 | \$19,154,603 |

During 2006, no more than 44% of the products distributed by the SOYO Group were supplied by any one supplier. SOYO Group, Inc. is establishing new partnerships with other OEM manufacturers in the North America and Asia Pacific Regions in order to provide innovative products for consumers.

In continuing efforts to work with and leverage its supply base, SOYO entered into an agreement with GE Capital in 2006 whereby GE guarantees payment to GE approved vendors thereby facilitating larger orders, decreasing risk and allowing SOYO to seamlessly finance these transactions.

13. Quarterly Results (Unaudited)

Presented below is a summary of the quarterly results of operations for the years ended December 31, 2006 and 2005.

|                                    | Three months ended: |               |               |               |               |
|------------------------------------|---------------------|---------------|---------------|---------------|---------------|
|                                    | March 31, 2006      | June 30, 2006 | Sept 30, 2006 | Dec 31, 2006  | Total         |
| Net revenues                       | \$ 11,548,187       | \$ 10,787,515 | \$ 10,005,084 | \$ 24,417,902 | \$ 56,758,688 |
| Gross margin                       | 1,651,088           | 2,306,753     | 2,233,361     | 3,033,237     | 9,224,439     |
| Income (loss) from Operations      | (209,526)           | 635,182       | 526,909       | 566,706       | 1,518,271     |
| Other Income (Expense), Net        | (64,609)            | (73,968)      | (207,338)     | (651,686)     | (997,591)     |
| Income (loss) before taxes         | (274,135)           | 561,214       | 319,568       | (84,977)      | 522,670       |
| Income taxes                       | 0                   | 0             | 0             | (20,310)      | (20,310)      |
| Deferred Income Tax Gain (Expense) | 0                   | 0             | 0             | 177,177       | 177,177       |
| Net Income (loss)                  | (274,135)           | 561,214       | 319,568       | 71,890        | 678,537       |
| Dividends                          | (49,856)            | (52,598)      | (55,491)      | (58,543)      | (216,488)     |

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|   |            |            |            |            |       |
|---|------------|------------|------------|------------|-------|
| Net Income (Loss)<br>Attributable to<br>Common Shareholders                 | (323,991)  | 508,616    | 264,077    | 13,347     | 46    |
| -----   |            |            |            |            |       |
| Net income<br>(loss) per<br>common share -<br>Basic                         |            |            |            |            |       |
| Diluted   | (.01)      | .01        | (.00)      | (.01)      |       |
|   | (.01)      | .01        | (.00)      | (.01)      |       |
| -----   |            |            |            |            |       |
| Weighted average<br>number of<br>common<br>shares<br>outstanding -<br>Basic | 48,834,511 | 48,834,511 | 48,853,511 | 48,853,511 | 49,02 |
| Diluted   | 51,857,043 | 55,342,474 | 55,515,583 | 57,238,826 | 59,78 |
| -----   |            |            |            |            |       |

Three months ended:

|   | March 31, 2005 | June 30, 2005 | Sept 30, 2005 | Dec 31, 2005  | Total    |
|---|----------------|---------------|---------------|---------------|----------|
| Net revenues  | \$ 3,962,520   | \$ 8,494,311  | \$ 9,233,430  | \$ 16,572,771 | \$ 38,26 |
| Gross margin  | \$ 1,522,035   | \$ 1,054,872  | \$ 206,771    | \$ 1,909,292  | \$ 4,69  |
| Income (loss) from<br>Operations                            | \$ 308,724     | \$ 36,760     | (\$ 482,407)  | \$ 651,843    | \$ 51    |
| Other Income<br>(Expense), Net                              | \$ 77,951      | \$ 65,359     | \$ 120,215    | (\$ 237,335)  | \$ 2     |
| Income (loss) before<br>taxes                               | \$ 386,675     | \$ 102,119    | (\$ 362,192)  | \$ 414,508    | \$ 54    |
| Income taxes  | (800)          | (800)         |               |               |          |
| Net Income (loss)   | \$ 386,675     | \$ 102,119    | (\$ 362,192)  | \$ 413,708    | \$ 54    |
| Dividends   | \$ 39,213      | \$ 42,458     | \$ 42,935     | \$ 1,049,147  | \$ 1,17  |
| Net Income (Loss)<br>Attributable to<br>Common Shareholders | \$ 347,462     | \$ 59,661     | (\$ 405,127)  | (\$ 635,439)  | (\$ 63   |
| -----   |                |               |               |               |          |
| Net income<br>(loss) per<br>common share -<br>Basic         |                |               |               |               |          |
| Diluted   | .01            | --            | (.01)         | (.01)         |          |
|   | .01            | --            | (.01)         | (.01)         |          |
| -----   |                |               |               |               |          |
| Weighted average  |                |               |               |               |          |



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|  |            |            |            |            |        |
|--|------------|------------|------------|------------|--------|
| number of<br>common<br>shares<br>outstanding - |            |            |            |            |        |
| Basic  | 48,681,511 | 48,681,511 | 48,681,511 | 48,681,511 | 48,511 |
| Diluted  | 52,736,204 | 52,736,204 | 48,681,511 | 48,681,511 | 48,511 |
| -----  | -----      | -----      | -----      | -----      | -----  |

During the year 2005, the Company booked approximately \$1,000,000 in the first quarter and \$300,000 in the second quarter to miscellaneous income. During the fourth quarter, the Company determined that the correct classification of the amounts was as a reduction to cost of sales, and not to miscellaneous income. The amounts are placed above as they should have been booked, which will not agree with the 10Q reports issued as of March 31, June 30, and September 30, 2005.

### ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

None.

### ITEM 9A. CONTROLS AND PROCEDURES

#### (a) Evaluation of Disclosure Controls and Procedures:

In conjunction with the audit of the Company's financial statements for the year ended December 31, 2006, 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 date, the Company's disclosure controls and procedures were not effective. 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 2006 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 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. 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, 2006.

In view of the fact that the financial information presented in the 2006 annual

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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 2006 annual report.

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

Each month, the Company's Accounting Manager supervises the reconciliation of the accounts payable subsidiary ledgers with the general ledger, and approves adjustments to inventory based on reconciliation of the general ledger to physical inventory counts. Each quarter, the Accounting Manager records inventory adjustments to the lower of cost or market.

Every month, the Accounting Manager reconciles the bank accounts and compares the bank reconciliation with the balance per general ledger and the daily cash report, reviews the recording of accounts payable to vendors for purchases of inventory, and prepares financial statements with a complete set of adjustments. These tasks will be supervised by the financial consultant until the new Accounting Manager is hired.

During the quarter ended September 30, 2004, the Company implemented a cycle count of its inventory, with the fifty fastest-moving items of "Type A" inventory physically counted and reconciled every morning with the recorded quantities and amounts. All "Type A" inventory is physically counted and reconciled every Monday.

A complete inventory is physically counted and reconciled at the end of every month.

### (b) Changes in internal control over financial reporting:

In light of the foregoing, in 2006, 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 will be installed and operational during the second quarter of fiscal year 2007.

The Company believes that once the new software is installed and operational, all significant deficiencies will have been addressed and corrected.

ITEM 9B. OTHER INFORMATION- NONE

## PART III

### ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The following table and text sets forth the names and ages of all the Company's directors and executive officers and the key management personnel as of March 31, 2007. The Company's Board of Directors is comprised of only one class. All

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of the directors serve until the next annual meeting of stockholders and until their successors are elected and qualified, or until their earlier death, retirement, resignation or removal. Executive officers serve at the discretion of the Board of Directors, and are appointed to serve until the first Board of Directors meeting following the annual meeting of stockholders. Also provided is a brief description of the business experience of each director and executive officer and the key management personnel during the past five years and an indication of directorships held by each director in other companies subject to the reporting requirements under the Federal securities laws.

| Name             | Age | Position Held                                   |
|------------------|-----|---|
| Ming Tung Chok   | 46  | Chief Executive Officer and Director            |
| Nancy Chu        | 50  | Chief Financial Officer, Secretary and Director |
| Paul F. Risberg  | 46  | Director  |
| Chung Chin Keung | 41  | Director  |
| Zhi Yang Wu      | 38  | Director  |

Ming Tung Chok has served as the President, Chief Executive Officer and Director of the Company since October 25, 2002. Prior to serving in this capacity, Mr. Chok was the Vice President of Engineering of SOYO Group, Inc. for the past five years. Mr. Chok received his Bachelor Degree in Electrical Engineering from the California State University, Long Beach. Mr. Chok is married to Ms. Nancy Chu who is a Director, the Chief Financial Officer and the Secretary of the Company.

Nancy Chu has served as the Chief Financial Officer, the Secretary and Director of the Company since October 25, 2002. Prior to serving in this capacity, Ms. Chu was the Vice President of Operations of SOYO Group, Inc. for the past 5 years. Ms. Chu holds a Bachelor Degree in Accounting & Statistics from the Sji Jiang College, Taiwan R.O.C. Ms. Chu is married to Mr. Chok who is the President, Chief Executive Officer and a Director of the Company.

Paul F. Risberg was appointed in October 2005 as an independent non-executive director and audit committee member. Mr. Risberg has more than 13 years of investment banking and securities market expertise. He is currently the president of Altenergy Inc., an alternative energy service company that retails and installs energy Equipment. From 1998 until 2002, Mr. Risberg served as divisional vice president of Fahnstock & Co. Inc. (now known as Oppenheimer & Co.), one of the oldest New York Stock Exchange firms.

Chung Chin Keung was appointed in October 2005 as an independent non-executive director, audit committee member and compensation committee member. Mr. Chung has more than 14 years commercial experience, including more than 10 years in accounting and finance for publicly listed companies in various countries. Mr. Chung is currently the chief finance officer of KPI Co. Ltd. (0605, Hong Kong Stock Exchange), a listed company in Hong Kong. Mr. Chung holds a Master of Business Administration from the University of Manchester, England.

Zhi Yang Wu was appointed in October 2005 as an independent non-executive director and compensation committee member. Mr. Wu is the vice chairman of Qiao Xing Universal Telephone Inc. (Nasdaq: XING), one of China's largest manufacturers and distributors of telecommunication products. Mr. Wu currently

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also serves as chairman & CEO of CEC Telecom, one of the largest mobile phone manufacturers in China and a subsidiary of Qiao Xing. Mr. Wu currently oversees CEC Telecom with annual sales in excess of \$200 million. Mr. Wu received a Diploma in Business Management from Huizhou University of China, and has completed graduate studies in business management at Beijing University.

Each Director received 10,000 unregistered shares of the Company's common stock in 2005. The Directors receive no other compensation for serving on the Board of Directors, but are reimbursed for any out-of-pocket expenses incurred in attending board meetings, and may be compensated for other work done on the Company's behalf.

### Family Relationships.

Ming Tung Chok, President and CEO, and Nancy Chu, CFO and Secretary, are husband and wife. Andy Chu, the President and majority shareholder of SOYO Taiwan, is the brother of Nancy Chu.

### Involvement in Legal Proceedings.

To the best of the Company's knowledge, during the past five years, none of the following occurred with respect to a present or former director or executive officer of the Company: (1) any bankruptcy petition filed by or against any business of which such person was a general partner or executive officer either at the time of the bankruptcy or within two years prior to that time; (2) any conviction in a criminal proceeding or being subject to a pending criminal proceeding (excluding traffic violations and other minor offenses); (3) being subject to any order, judgment or decree, not subsequently reversed, suspended or vacated, of any court of competent jurisdiction, permanently or temporarily enjoining, barring, suspending or otherwise limiting his involvement in any type of business, securities or banking activities; and (4) being found by a court of competent jurisdiction (in a civil action), the SEC or the Commodities Futures Trading Commission to have violated a federal or state securities or commodities law, and the judgment has not been reversed, suspended or vacated.

### Section 16(a) Beneficial Ownership Compliance.

The Company does not have any shares registered under Section 12 of the Securities Act and therefore the owners of the Company's equity securities are not required to report their beneficial ownership under Section 16(a) of the Exchange Act.

### Audit Committee

The Audit Committee of the Board of Directors is comprised of Mr. Risberg and Mr. Keung. The first Audit Committee meeting is scheduled to coincide with the Company's 2007 Annual meeting, the date of which has not yet been set. None of the directors is an Audit Committee Financial Expert.

### Communications with the Board

Any shareholder may communicate directly with the Board of Directors. The Board of Directors has established the following system to receive, track and respond to communications from shareholders addressed to the Company's Board of Directors and its committees and members. Any shareholder may address his or her communication to the Board of Directors, or an individual Board member and send the communication addressed to the recipient group or individual, care of SOYO Group, Inc., Corporate Secretary, 1420 South Vintage Ave., Ontario, CA 91761. The Corporate Secretary will review all communications and deliver the

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communications to the appropriate party in the Corporate Secretary's discretion. The Corporate Secretary may take additional action or respond to communications in accordance with instructions from the recipient of the communication.

### Code of Ethics

We believe that good corporate governance practices promote the principles of fairness, transparency, accountability and responsibility and will ensure that our Company is managed for the long-term benefit of its shareholders. During the past year, we have continued to review our corporate governance policies and practices and to compare them to those suggested by various authorities in corporate governance and the practices of other public companies. Accordingly, in March 2004, the Board adopted a Code of Ethics and Conduct. You may obtain a copy of the Code of Ethics and Conduct and other information regarding our corporate governance practices by writing to the Corporate Secretary, 1420 South Vintage Ave., Ontario, CA 91761.

### ITEM 11. EXECUTIVE COMPENSATION

#### COMPENSATION DISCUSSION AND ANALYSIS

The Compensation Committee of our board of directors and our CEO, CFO and head of Human Resources are collectively responsible for implementing and administering all aspects of our benefit and compensation plans and programs, as well as developing specific policies regarding compensation of our executive officers. Both of the members of our Compensation Committee, Chung Chin Keung and Zhi Yang Wu are independent directors.

#### Compensation Objectives

The stated goal of our compensation committee with respect to executive compensation has been to set compensation at levels that attract and retain the most talented and dedicated executives possible. We attempt to set individual executive compensation levels comparable with executives in other companies of similar size and stage of development. We attempt to reward employees for strong Company performance through the use of stock options. Our Executive Officers, Ming Tung Chok and Nancy Chu, are husband and wife, and are also our founders and largest shareholders.

#### Elements of Compensation

**Base Salary.** All full time executives are paid a base salary. In all cases, the Committee establishes a minimum base salary for our executive officers. Base salaries for our executives are established based on the scope of their responsibilities and the current financial situation of the Company. We also try to take into account competitive market compensation paid by other companies in our industry for similar positions, professional qualifications, academic background, and the other elements of the executive's compensation, namely stock-based compensation.

**Equity Compensation.** We believe that long-term performance is achieved through an ownership culture participated in by our executive officers through the use of stock-based awards. Currently, we do not maintain any incentive compensation plans based on pre-defined performance criteria. The Compensation Committee has the general authority, however, to award equity incentive compensation, i.e. stock options, to our executive officers in such amounts and on such terms as the committee determines in its sole discretion. The Committee does not have a determined formula for determining the number of options available to be granted, subject to the number of options available through our Employee Stock

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Ownership Program. Incentive compensation is intended to compensate officers for accomplishing strategic goals such as meeting defined revenue goals, profitability, and fund raising in accordance with the Company's needs for future growth. The Compensation Committee awarded stock options to executive officers, employees and consultants upon the filing of our Employee Stock Ownership Program in 2005, and expects to award stock options to executive officers, employees and consultants in 2007. No stock options were granted in 2006. Our Compensation Committee grants equity compensation only at times when we do not have material non-public information to avoid timing issues and the appearance that such awards are made based on any such information.

### Determination of Compensation

Our CEO, CFO and head of Human Resources meet annually to evaluate each non-executive employee's performance. A meeting is held towards the end of the fiscal year to determine each employee's compensation for the following year. In the case of our executive officers, the Compensation Committee similarly evaluates the executive's performance and the objectives set forth above at or about the end of our fiscal year to determine executive compensation.

The following table sets forth the cash and other compensation paid by us in 2004, 2005 and 2006 to the individuals who served as our chief executive officer and chief financial officer. No other executives received total compensation greater than \$100,000 in 2006.

### Summary Compensation Table

| Name  | Year | Salary    | Options Granted |
|---|------|-----------|-----------------|
| Ming Tung Chok (i)<br>President, Chief Executive<br>Officer<br>and Director | 2004 | \$144,000 | 0               |
|   | 2005 | \$144,000 | 600,000         |
|   | 2006 | \$144,000 | 0               |
| Nancy Chu (ii)<br>Chief Financial Officer and<br>Seretary                   | 2004 | \$120,000 | 0               |
|   | 2005 | \$120,000 | 600,000         |
|   | 2006 | \$120,000 | 0               |

(i) Ming Tung Chok has served as the President, Chief Executive Officer and Director of the Company since October 25, 2002. Prior to serving in this capacity, Mr. Chok was the Vice President of Engineering of SOYO Group, Inc. for the past five years. Mr. Chok received his Bachelor Degree in Electrical Engineering from the California State University, Long Beach. Mr. Chok is married to Ms. Nancy Chu who is a Director, the Chief Financial Officer and the Secretary of the Company.

(ii) Nancy Chu has served as the Chief Financial Officer, the Secretary and Director of the Company since October 25, 2002. Prior to serving in this capacity, Ms. Chu was the Vice President of Operations of SOYO Group, Inc. for the past 5 years. Ms. Chu holds a Bachelor Degree in Accounting & Statistics from the Sji Jiang College, Taiwan R.O.C. Ms. Chu is married to Mr. Chok who is the President, Chief Executive Officer and a Director of the Company.

### Outstanding Stock Options At December 31, 2006

| Name | Number of<br>Exercisable | Exercise<br>Price | Vesting Date | Option Expiration<br>Date |
|------|--------------------------|-------------------|--------------|---------------------------|
|------|--------------------------|-------------------|--------------|---------------------------|

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### Options

| Name           | Number of Shares | Exercise Price | Grant Date    | Expiration Date |
|----------------|------------------|----------------|---------------|-----------------|
| Ming Tung Chok | 200,000          | \$.75          | July 22, 2006 | July 22, 2010   |
|                | 200,000          | \$.75          | July 22, 2007 | July 22, 2010   |
|                | 200,000          | \$.75          | July 22, 2008 | July 22, 2010   |
| Nancy Chu      | 200,000          | \$.75          | July 22, 2006 | July 22, 2010   |
|                | 200,000          | \$.75          | July 22, 2007 | July 22, 2010   |
|                | 200,000          | \$.75          | July 22, 2008 | July 22, 2010   |

### Pension Benefits

We do not sponsor any qualified or non-qualified defined benefit plans.

### Nonqualified Deferred Compensation

We do not maintain any non-qualified defined contribution or deferred compensation plans. Our Compensation Committee, which is comprised solely of "outside directors" as defined for purposes of Section 162(m) of the Code, may elect to provide our officers and other employees with non-qualified defined contribution or deferred compensation benefits if the Compensation Committee determines that doing so is in our best interests.

### Compensation of Directors

Each Director received 10,000 unregistered shares of the Company's common stock in 2005. The Directors receive no other compensation for serving on the Board of

Directors, but are reimbursed for any out-of-pocket expenses incurred in attending board meetings, and may be compensated for other work done on the Company's behalf.

### COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION

None of the members of the Compensation Committee have any relationship with the Company or any of its officers or employees other than in connection with their role as a director. None of the members of the Compensation Committee have participated in any related party transactions with the Company since the beginning of the Company's last fiscal year.

### EMPLOYMENT CONTRACTS

We do not currently have employment contracts with any of our executive officers. We may enter into employment contracts with our executive officers, employees or consultants at any time if we deem it to be in the best interests of the company.

### ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The following table sets forth the number of shares of common stock beneficially owned as of March 31, 2007 by (i) those persons or groups known to the Company who beneficially own more than 5% of the Company's common stock; (ii) each director and director nominee; (iii) each executive officer whose compensation exceeded \$100,000 in the fiscal year ended December 31, 2006; and, (iv) all directors and executive officers as a group. The information is determined in accordance with Rule 13(d)-3 promulgated under the Exchange Act based upon information furnished by persons listed or contained in filings made by them

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with the Securities and Exchange Commission by information provided by such persons directly to the Company. Except as indicated below, the stockholders listed possess sole voting and investment power with respect to their shares.

| Name/Title/Address(1)                     | Total Number of Shares | Percentage Ownership(2) |
|---|------------------------|-------------------------|
| Ming Tung Chok                            | 12,000,000             | 24.48%                  |
| Nancy Chu                                 | 14,209,548             | 28.98%                  |
| Paul F. Risberg                           | 57,000                 | .02%                    |
| Chung Chin Keung                          | 10,000                 | .01%                    |
| Zhi Yang Wu                               | 10,000                 | .01%                    |
| All officers and directors as a group (3) | 26,248,548             | 53.50%                  |
| Urmston Capital (4)                       | 10,054,596             | 20.50%                  |

(1) Unless otherwise provided, the addresses of these holders is 1420 S. Vintage Ave. Ontario California 91761.

(2) The percentage ownership is based upon 49,025,511 shares outstanding on March 30, 2007.

(3) Since Ming Tung Chok and Nancy Chu are husband and wife, they are considered beneficial owners of each others common stock. Collectively, they own 26,209,548 shares and are each considered beneficial owners of 26,209,548 shares.

(4) The address for Urmston Capital is 148 Xinglung Road, Sec. 3, WenShan District, Taipei, Taiwan R.O.C.

As the result of an agreement between SOYO Taiwan and an unrelated third party in 2004 2,500,000 shares of Class B preferred stock were issued by the Company to the unrelated third party in exchange for the forgiveness of a \$12,000,000 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 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. If the Class B Preferred Stock were converted at the closing bid price of \$0.26 per share on December 31, 2006, the holder would have 10,054,596 shares of the Company's common stock.

### ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.

Ming Tung Chok, the President and Chief Executive Officer of the Company, is married to Nancy Chu, the Chief Financial Officer of the Company. Andy Chu, the President and majority shareholder of SOYO Taiwan, is the brother of Nancy Chu.



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The following is a summary of the Company's transactions and balances with SOYO Taiwan as of and for the years ended December 31, 2005, 2004 and 2003:

December 31,

|                                  | 2006 | 2005 |
|----------------------------------|------|------|
| Accounts payable to SOYO Taiwan  | \$0  | \$0  |
| Long-term payable to SOYO Taiwan | \$0  | \$0  |

Years Ended December 31,

|                            | 2004 | 2003 | 2004      |
|----------------------------|------|------|-----------|
| Purchases from SOYO Taiwan | \$0  | \$0  | \$0       |
| Payments to SOYO Taiwan    | \$0  | \$0  | \$873,050 |

### ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

#### Independent Accountant Fees

The following table sets forth the fees for professional audit services rendered by Vasquez & Company LLP for the audit of the Company's annual financial statements for the fiscal years 2006 and 2005.

|                | 2006      | 2005      |
|----------------|-----------|-----------|
| Audit Fees (1) | \$122,500 | \$121,580 |
| Tax Fees       | 15,000    | 13,000    |
| All Other Fees |           |           |
| Total Fees     | \$137,500 | \$134,580 |

(1) Includes annual audit fees and fees for preissuance review of quarterly filings.

In 2006, Grobstein, Horwath & Company, the Company's predecessor auditors, charged \$6,000 for a review and reissuance of the Company's 2003 audit report.

### ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a) Exhibits.

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The following is a list of exhibits filed as part of this Annual Report on Form 10-K. Where so indicated by footnote, exhibits which were previously filed are incorporated by reference.

| Exhibit Number | Description  |
|----------------|--|
| 3.1            | Articles of Incorporation, Incorporated herein by reference to the Definitive Schedule 14A File No. 333-42036, filed on September 27, 2002.  |
| 3.2            | Bylaws, Incorporated herein by reference to the Definitive Schedule 14A File No. 333-42036, filed on September 27, 2002.   |
| 10.1           | SOYO Group Agreement with China Unicom dated February 1, 2004, Incorporated herein by reference to the Form 10-K for the fiscal year ended December 31, 2004, File No. 333-42036, filed on March 31, 2005          |
| 10.2           | Office Lease at 140 S. Vintage Ave., Ontario, CA dated August 21, 2003, Incorporated herein by reference to the Form 10-K for the fiscal year ended December 31, 2004, File No. 333-42036, filed on March 31, 2005 |
| 10.3           | SOYO Group Agreement with Accord Financial Services, dated February 6, 2006  |
| 10.4           | SOYO Group Agreement with GE Capital, dated August 3, 2006   |
| 21.1           | Subsidiaries of the Company, Incorporated herein by reference to the Form 10-K, File No. 333-42036, filed on April 15, 2003  |
| 23.1           | Consent of Independent Registered Public Accounting Firm, Vasquez & Company LLP  |
| 31.1           | CERTIFICATION REQUIRED BY RULE 13a-14(a) OR RULE 15d-14(d) AND UNDER SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002*  |
| 31.2           | CERTIFICATION REQUIRED BY RULE 13a-14(a) OR RULE 15d-14(d) AND UNDER SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002   |
| 32.1           | CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002   |
| 32.2           | CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002   |

\*Filed herein

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SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

SOYO GROUP, INC.

Dated: August 7, 2007 By /s/ Ming Tung Chok  
-----  
Name: Ming Tung Chok  
Title: President and Chief Executive Officer

In accordance with the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Dated: August 7, 2007 By /s/ Ming Tung Chok  
-----  
Name: Ming Tung Chok  
Title: President, Chief Executive Officer and Director

Dated: August 7, 2007 By /s/ Nancy Chu  
-----  
Name: Nancy Chu  
Title: Chief Financial Officer, Secretary and

Dated: August 7, 2007 By /s/ Paul F. Risberg  
-----  
Name: Paul F. Risberg  
Title: Director

Dated: August 7, 2007 By /s/ Chung Chin Keung  
-----  
Name: Chung Chin Keung  
Title: Director

Dated: August 7, 2007 By /s/ Zhi Yang Wu  
-----  
Name: Zhi Yang Wu  
Title: Director