

Edgar Filing: SOYO GROUP INC - Form 10-K/A

SOYO GROUP INC  
Form 10-K/A  
February 26, 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, 2005

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

1

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

Edgar Filing: SOYO GROUP INC - Form 10-K/A

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 an accelerated filer (as defined in Rule 12b-2 of the Act). Yes [ ] No [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 large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

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

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

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 31, 2006 was \$29,392,507, based on the closing bid price of \$0.60 per share on March 31, 2006.

As of March 31, 2006, there were 48,987,511 shares Outstanding.

Documents Incorporated by Reference: None

2

SOYO GROUP, INC.  
FORM 10-K  
INDEX

Page  
----

PART I

Item 1. Business.....	4
Item 2. Properties.....	15
Item 3. Legal Proceedings.....	16
Item 4. Submission of Matters to a Vote of Security Holders.....	16

# Edgar Filing: SOYO GROUP INC - Form 10-K/A

## PART II

Item 5.	Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.....	17
Item 6.	Selected Financial Data.....	20
Item 7	Management's Discussion and Analysis of Financial Condition and Results of Operations.....	21
Item 7A	Quantitative and Qualitative Disclosures About Market Risk.....	38
Item 8.	Financial Statements and Supplementary Data.....	39
Item 9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.....	72
Item 9A.	Controls and Procedures.....	74
Item 9B.	Other Information.....	76

## PART III

Item 10.	Directors and Executive Officers of the Registrant.....	76
Item 11	Executive Compensation.....	79
Item 12.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.....	80
Item 13.	Certain Relationships and Related Transactions.....	81
Item 14.	Principal Accountant Fees and Services.....	82

## PART IV

Item 15.	Exhibits, Financial Statement Schedules .....	83
	Signatures.....	84

3

## 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

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

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 & 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.

4

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 wholly owned 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.
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.

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

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.

5

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 home and office (SOHO) users.

SOYO Group's products have always been sold through an extensive network of authorized distributors to resellers, system integrators, and value-added resellers (VARs).

These products are also sold through major retailers, mail-order catalogs and e-tailers to the consumers throughout North America and Latin America.

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. Throughout 2005, these were the areas that produced revenues for the Company.

PRODUCTS

Computer Components and Peripherals

Motherboards/Bare Bones Systems

-----

The motherboard has been an integral part of most personal computers for more than twenty years. Actually, a carryover from architecture used for years in mainframe computers, a motherboard is the physical arrangement in a computer that contains the computer's basic circuitry and components. It is the data and power infrastructure for the entire computer.

SOYO Group Inc.'s Bare Bones System product solution is the basis for any computer system. The All-in-One (Audio, Video and LAN onboard) contains our motherboard in AMD as well as Intel platforms, case, power supply, keyboard, mouse and speakers. The 4-in-1 includes the Bare Bones case, power supply, mouse

6

and keyboard. Consumer demand for this product is very high since the majority of components are integrated in the box.

Portable Storage Devices

The CIGAR 20GB and 40GB USB 2.0 Hard Drives are ideal for desktop and laptop users who need high capacity in an ultra-small package. One of the smallest harddrives available today, large graphics and audio files are quickly and easily displayed, copied or transported to any USB Ported computer. Incorporating a 1.8-inch hard disk from Toshiba, the SlimDrive measures just 4.02" x 2.36" x 0.43" (LWH) and weighs only 3.5 oz. The SlimDrive fits easily into a pocket, purse or briefcase for convenient travel and leaves a small footprint on the desktop. Compatible with both PC and Macintosh operating systems, the SlimDrive's USB 2.0 cable delivers fast transfer rates of up to 480Mbps and does not require any external power supplies or batteries. The magnesium alloy casing provides superior shock resistance. Additional capacities are expected to be available later this year.

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.

The BayOne(R) Flash Media Reader/Writer is a unique 6-in-1 breakout box that can be installed in a 3.5" or 5.25" drive bay for easy front panel access, featuring combination reader/writer for 6 flash media standards and two (2) front USB 2.0 ports. The BayOne(R) internal multimedia reader/writer conveniently fits into the front of the PC. With the BayOne(R), SOYO Group, Inc.'s customers can now connect multiple devices to their computers and download digital photos, video, MP3 music or hot sync their handheld devices all at the same time. The multiple memory reader/writer slots also can be used simultaneously, enabling SOYO Group, Inc.'s customers to take full advantage of this compact all-in-one solution. The BayOne(R) was designed to be universally

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

compatible with all systems and external devices, making it easy to install and also very user-friendly.

The Compact Hub Reader/Writer is a combination USB 2.0 Hub and 12-in-1 flash media card reader/writer that expands the functionality of computers. It offers three USB 2.0 hubs for convenient connection between a computer and digital camera, PDA, hand-held computer, USB phone, MP3 player, keyboard, mouse or printer. The flash memory card slots can all be used at the same time for data download, exchange and storage. The Compact Hub Reader/Writer is hot-swappable, which means that external devices can be added or removed while the computer is on, offers automatic plug-n-play convenience and is backward compatible to USB 1.1.

7

### Consumer Electronics Products

-----

SOYO Group, Inc. entered the consumer electronics market in 2005 with a strong line of entertainment products that includes docking stations, LCD and plasma TVs, wireless headphones and USB speakers. Although this is the newest group in the product line, it accounted for over 30% of sales in 2005.

SOYO entered the LCD market in the 2nd quarter of 2005. The Company began by selling 17 and 19 inch LCD computer monitors, and 32" and 37" LCD televisions, and will soon ship 42" sets.

### MONITORS

-----

The Dymond series LCD monitor incorporates TFT (Thin Film Transistor) display technology in a compact design that frees up valuable desk space, with a wide-angle flat screen that offers a view of the screen from various angles without compromising image quality. Featuring high brightness, sharp contrast and vivid colors, the Dymond's built-in speakers deliver stereo-quality sound. Designed to provide a display solution for a wide variety of applications at the office, home or school, the Dymond's 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. The Dymond series monitors are available in black or silver and are currently manufactured in the 17 inch and 19 inch sizes.

### HOME ENTERTAINMENT FLAT SCREEN TELEVISIONS

-----

SOYO's Ultra Slim flat-panel, HD-Ready 32-inch and 37 inch LCD TV delivers stunning picture quality to home entertainment. The product offers 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. Incorporating advanced imaging technology features such as 3:2 pull down, progressive scan and digital 3D comb filter that bring you larger, clearer pictures, the Atlas LCD TV features two powerful, removable 10-watt speakers that deliver stereo surround sound.

8

Bluetooth Wireless Headphone  
-----

FreeStyler Bluetooth Headset  
-----

FreeStyler is a simple, straightforward Bluetooth headset with excellent sound quality. The headset can be connected to your mobile phone and PDA wirelessly. 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. It provides 4~6 Hrs. talk time and 200 Hrs. standby time by the rechargeable battery at 120mA 3.7v. with only 1.5~2.0 Hrs. charging time. The headset is now available through SOYO's exclusive launch partner Fry's Electronics, and will also be sold through SOYO's network of dealers, distributors and online retailers.

Communications Equipment  
-----

The Telecommunications Industry Association forecast that spending on VoIP systems would rise to \$3.5 billion in 2005. VOIP protocols have evolved to offer a richer set of features, scalability and standardization than was available only a few years ago, and In November 2004, Soyo introduced our "Z-Connect" family of Voice over IP products and services. The Z-Connect product line includes the Z-Connect phone, Z-Connect router, and two versions of the Z-Connect gateway, delivering VoIP capabilities with zero set-up fees, zero monthly fees, zero service contracts, zero configuration and zero hidden charges. Users simply plug the Z-Connect phone into a broadband connection for instant VoIP service. The Z-Connect router combines a voice gateway and a broadband router, enabling users to plug their traditional telephones for VoIP service, and up to four computers can also share Internet access. Z-Connect customers immediately begin saving money on long-distance and international calls, using the free call time of up to 150 minutes included with the phone or router. Additional call time can be purchased on our web site. SOYO Group's VoIP service is based on a flexible pay-as-you go strategy, enabling users to prepay for minutes, and make international and long-distance calls at extremely low rates. "Peer-to-peer" calls between Z-Connect telephones and routers within the Z-Connect Network are always free, anywhere in the world.

In November 2004, we introduced our "Z-Connect" family of Voice over IP products and services. The Z-Connect product line includes the Z-Connect phone, Z-Connect router, and two versions of the Z-Connect gateway, delivering VoIP capabilities with zero set-up fees, zero monthly fees, zero service contracts, zero configuration and zero hidden charges. Users simply plug the Z-Connect phone into a broadband connection for instant VoIP service. The Z-Connect router combines a voice gateway and a broadband router, enabling users to plug their traditional telephones for VoIP service, and up to four computers can also share Internet access. Z-Connect customers immediately begin saving money on long-distance and international calls, using the free call time of up to 150 minutes included with the phone or router. Additional call time can be purchased on our web site. SOYO Group's VoIP service is based on a flexible pay-as-you go



strategy, enabling users to prepay for minutes, and make international and long-distance calls at extremely low rates. "Peer-to-peer" calls between Z-Connect telephones and routers within the Z-Connect Network are always free, anywhere in the world.

The Z-Connect Single Mode Gateway is the ideal IP telephony solution for small businesses to save money on long-distance and international phone calls and faxes. Up to four analog telephones or a PBX can be connected to the Single-Mode Gateway, which provides the option for users to choose separate DID (Direct Inbound Dial) number for each phone line for inbound calls, and also determine the order in which inbound calls are received.

The Z-Connect Dual Mode Gateway supports any IP network and the PSTN. It features an intelligent switching function that determines which network - the IP or PSTN - to make for using calls, without changing the user's familiar dialing interaction with the phone system. The Dual Mode Gateway seamlessly integrates into the office environment, easily connecting to the PBX, and is compatible with a variety of networks, broadband access devices and system configurations. All local calls, as well as emergency and toll-free numbers, are routed through the PSTN, while long-distance and international calls are routed through the IP, for maximum cost savings.

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 is also entering the calling card market, to offer consumers cost savings on long-distance calls.

In February 2005, SOYO announced a very important development for the Z-Connect product line in the form of an agreement with China Unicom USA Corporation, a division of China Unicom Ltd. (NYSE: CHU), to use its Public Service Telephone Network and Voice over Internet Protocol network (the largest in the world), to give users the ability to dial and receive local, long distance, and international calls. China Unicom is one of the largest telecommunication companies in the world and its choice of SOYO Group for a partnership agreement is an extremely important and strategic development opportunity.

#### 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. As of December 31, 2005, no single supplier is

10

supplying more than 39% of the products distributed and sold by the SOYO Group. Aside from this one vendor, no other company supplies more than ten percent of the products that the Company sells.

#### TRANSPORTATION AND DISTRIBUTION

SOYO Group, Inc. is the exclusive provider for SOYO(R) branded products in

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

the United States and Latin America. SOYO Group, Inc. has facilities in the U.S. and worldwide. The logistics team members play a key role by providing product through this channel. Through their efforts, SOYO Group, Inc. is able to achieve a high level of efficiency and exceed customer expectations by maintaining a swift and reliable delivery system.

### 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) home/small office 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.).

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, 2005, approximately 20% of the SOYO Group's sales and revenues were generated from the Latin American market.

### 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.

11

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.

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. During the year ended December 31, 2004, the Company had one customer (SYX Distribution, Inc., otherwise known as Tiger Direct) that accounted for revenues of \$8,591,711, equivalent to 26% of net revenues. During the year ended December 31, 2003, the same customer accounted for revenues of \$9,943,855, equivalent to 32% of net revenues.

### SUPPLIERS

From the Company's inception through December 31, 2003, over 80% of the

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

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.

As of December 31, 2005, no more than 39% of the products distributed by the SOYO Group are being supplied by any one supplier. Other than that single supplier, no other Vendor supplied more than ten percent of the Company's inventory available for sale. Notwithstanding the reduced emphasis on distributing SOYO Taiwan products, SOYO Group had a supply Commitment Agreement with SOYO Taiwan which provided that SOYO Taiwan would continue to supply SOYO Group at current levels on an open account basis through 2005. The agreement expired on December 31, 2005. In 2005, SOYO Group did not purchase any goods from SOYO Taiwan.

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

### 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 expenditures in 2006 with respect to compliance with any such regulations.

12

### STRATEGY

SOYO Group, Inc.'s strategy is to capitalize on its market position as a leading provider of consumer electronics, communications, and networking products by increasing its penetrations of existing markets through acquisitions and expanding into new markets.

### 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. The following is a list of competitors by category:

- >> Computer Components and Peripherals - Abit, Asus, Gigabyte, MSI, ViewSonic, Daewoo, Dell, SanDisk, Lexar Media and SimpleTech
- >> Consumer Electronics - Panasonic, ViewSonic, Samsung
- >> Communications - Vonage, Packet8, Net2Phone

### EMPLOYEES

As of March 31, 2006, the Company employed thirty six (36) people at its headquarters in Ontario, California.

### ITEM 1A. RISK FACTORS

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

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.

13

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.

We were forced to sue a customer (Xtraplus, d.b.a. ZipZoomFly last year for non payment of invoices resulting from a dispute. The customer felt that we did not pay rebates to our end users buying our products through this distributor on a timely basis. The dispute led to a lawsuit that is currently pending in California Superior Court. If that scenario is repeated, or if we are unable to maintain relationships with our distributors, the business could suffer.

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.

Last year, 39% 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 the cost of energy could affect our profitability.

We were adversely affected in 2005 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

Edgar Filing: SOYO GROUP INC - Form 10-K/A

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.

14

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.

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 Inception	Lease Expiration	Area
Office and Warehouse	1420 S. Vintage Ave, Ontario C	9/1/2003	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

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

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

15

that the option period would commence. The Company also maintains a sales representation office in Brazil, located at Rua Andre Ampere 153 andar 17 sala 171/172, Brooklin Novo, Sao Paulo, SP, Brazil.

### ITEM 3. LEGAL PROCEEDINGS.

On August 2, 2004, a lawsuit was filed in California Superior Court entitled Gerry Normandan. et al, v. SOYO Inc. Case No. RCV 082128. The case seeks class action status and alleges defects in motherboards which Soyo distributes, and that the Company misrepresented and omitted material facts concerning the motherboards. The plaintiff seeks restitution and disgorgement of all amounts obtained by defendant as a result of alleged misconduct, plus interest, actual damages, punitive damages and attorneys' fees. The Company is vigorously defending the lawsuit and believes that it will be resolved with no material adverse effect on the Company.

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

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 fiscal year ended December 31, 2005, there were no matters submitted to the shareholders for approval.

16

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

On February 17, 2006, the Company held a special meeting to vote on the 2005 Employee Stock Option Compensation Plan. The record date for the determination of shareholders entitled to vote was January 27, 2006. The plan was approved by shareholder vote.

### PART II

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

##### (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, 2004:		
First Quarter	\$0.19	\$0.11
Second Quarter	0.19	0.12
Third Quarter	0.26	0.12
Fourth Quarter	0.43	0.31
Fiscal Year Ended December 31, 2005:		
First Quarter	\$ .98	\$0.37
Second Quarter	0.88	0.60
Third Quarter	0.93	0.66
Fourth Quarter	0.89	0.55

17

##### (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, 2005 there were 48,681,511 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

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

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 2005 we declared no dividends on either the Class A or Class B Preferred Stock outstanding. The dividends recognized and booked in 2005 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 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

18

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 2005, the Company issued an aggregate of 8,681,511 unregistered shares of its common stock to various entities for various reasons.

On March 28, 2005 the Company announced that an accredited investor, 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.



## Edgar Filing: SOYO GROUP INC - Form 10-K/A

In March 2005, the Company issued 20,000 unregistered shares to its public relations company, First Global Media, Inc. for services rendered. At the same time, the Company issued 5,000 unregistered shares to Barrow Street Research for services, and 5,000 unregistered shares to a business consultant as payment for services.

In September 2005, the Company issued 1,286,669 shares of restricted common stock to pay off a business loan of \$913,750 plus accrued interest of \$51,251 to LGT Computer Inc.

In October 2005, the Company issued 1,219,512 shares of restricted common stock for the liquidation of the 1,000,000 shares of Series A Preferred Stock that were issued by the Company as part of the original purchase of the Company from SOYO Taiwan in October 2002.

Throughout the year, 5,645,330 unregistered shares were issued to various corporations and individuals to buy back the Company's trade debt.

### (f) Equity Compensation Plan Information

Through December 31, 2004, the Company did not have any Equity Compensation Plans. 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

19

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. However, since Mr. Chok and Ms. Chu, husband and wife, are directors who own more than 50% of the company, shareholder approval is essentially a formality, hence the grant date of the stock options is July 22, 2005.

On July 22, 2005, the Company issued 2,889,000 option grants to employees at a strike price of \$.75. One third of those options will vest and be available for purchase on July 22, 2006, one third on July 22, 2007, and one third on July 22, 2008. The grants will expire if unused on July 22, 2010. The options do not have requisite service period nor market, performance, and service conditions.

### ITEM 6. SELECTED FINANCIAL DATA

The following selected consolidated financial data of the Company is presented as of and for each of the three years ended December 31, 2005, 2004, and 2003. 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".

Edgar Filing: SOYO GROUP INC - Form 10-K/A

Selected Consolidated Statements of Operations Data:

	Year Ended December 31,				
	2005	2004	2003	2002	2001
Net revenue	\$38,263,032	\$32,426,414	\$31,034,239	\$49,644,417	\$63,091,1
Income (loss) from operations	52,686	(3,913,683)	(980,347)	(10,892,574)	(342,0
Net Income (Loss) attributable to common shareholders	\$ (633,443)	(4,143,978)	(984,588)	(10,733,458)	(390,4
Net income (loss) per common share	(.01)	(0.10)	(0.02)	(0.35)	(0.

20

Selected Consolidated Balance Sheet Data:

	2005	2004	2003	2002	2001
Total Assets	\$16,907,390	\$ 7,500,437	\$ 12,729,453	\$ 20,914,784	\$ 26,309,
Long Term Payable to Soyo Taiwan	0	0	12,000,000	12,000,000	
Shareholders' Equity	1,477,703	(4,057,028)	(12,136,783)	(11,152,195)	(418,

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

(Deficit)

---

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, 2005.

This Annual Report on Form 10-K for the fiscal year ended December 31, 2005 contains "forward-looking" statements within the meaning of Section 27A of the Securities Act of 1933, as amended, including statements that include the words "believes", "expects", "anticipates", or similar expressions. These forward-looking statements 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

21

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, 2005 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, 2005, 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, 2005 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

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

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, mail-order catalogs and e-tailers to the consumers throughout North America and Latin America.

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. 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

22

shares represented 51% of the outstanding shares of VWHC 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 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 48,681,511 shares outstanding as of December 31, 2005.

Subsequent to this transaction, SOYO Taiwan maintained an equity interest in SOYO, and continued to be the primary supplier of inventory to SOYO, and was the Company's major creditor. In addition, there was no change in the management of SOYO and no new capital was invested. As a result, for financial reporting purposes, this transaction was accounted for as a recapitalization of SOYO Nevada, pursuant to which the accounting basis of SOYO Nevada continued unchanged subsequent to the transaction date. Accordingly, the pre-transaction financial statements of SOYO Nevada are now the historical financial statements of the Company, and pro forma information has not been presented, as this transaction is not a business combination.

In conjunction with this transaction, SOYO Nevada transferred \$12,000,000 of accounts payable to SOYO Taiwan to long-term payable, without interest, due December 31, 2005. (see "Liquidity and Capital Resources - December 31, 2005).

SOYO Taiwan also agreed to continue to provide computer parts and components to SOYO on an open account basis at the quantities required and on a timely basis to enable SOYO to continue to conduct its business operations at budgeted levels, which were not less than a level consistent with the operations of SOYO Nevada's business in 2001 and 2000. This supply commitment was effective through December 31, 2005, although SOYO Nevada did not purchase any goods from SOYO Taiwan in 2005 .

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

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

Nevada's year end.

Ming Tung Chok, the Company's President, Chief Executive Officer and Director and Nancy Chu, the Company's Chief Financial Officer, Secretary and Director, are husband and wife, and are the primary members of SOYO Nevada management referred to above. Andy Chu, the President and major shareholder of SOYO Taiwan, is the brother of Nancy Chu.

23

The Company sells to both distributors and retailers. Revenues through such distribution channels for each of the three years ended December 31, 2005, 2004 and 2003 are summarized as follows:

	Year Ended December 31,					
	2005	%	2004	%	2003	%
-----						
Revenues						
-----						
Distributors	\$22,312,488	58.3	\$14,704,452	45.3	\$13,055,046	42.1
-----						
Retailers	\$15,950,544	41.7	\$17,721,962	54.7	\$17,979,193	57.9
-----						
Total	\$38,263,032	100.0	\$32,426,414	100.0	\$31,034,239	100.0
-----						

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. During the year ended December 31, 2004, the Company had one customer (SYX Distribution, Inc., otherwise known as Tiger Direct) that accounted for revenues of \$8,591,711, equivalent to 26% of net revenues. During the year ended December 31, 2003, the same customer accounted for revenues of \$9,943,855, equivalent to 32% of net revenues.

Revenues by geographic segment are summarized as follows:

	Year Ended December 31,					
	2005	%	2004	%	2003	%
-----						
Revenues						
-----						
United States	\$20,055,470	56.7	\$25,936,978	80.0	\$23,043,136	74.3
-----						
Other N. America	1,615,080		N/A		N/A	
-----						

Edgar Filing: SOYO GROUP INC - Form 10-K/A

Central and South America	\$2,993,532	7.8	\$ 6,317,907	19.5	\$ 7,391,804	23.8
Hong Kong and other locations	\$13,598,950	35.4	\$ 171,529	0.5	\$ 599,299	1.9
Total	\$38,263,032	100.0	\$32,426,414	100.0	\$31,034,239	100.0

During the years 2003 and 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

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

24

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.

Financial Outlook:

During early 2003, as a result of the Company changing its product mix to focus on the sales of higher margin products and the decrease in market pressures on the Company's gross margin resulting from the West Coast dock strike in September and early October 2002, the Company's gross margin improved compared to 2002. The Company incurred a net loss attributable to common stock in 2003 of \$984,588.

In 2004, the Company increased sales by 4.5 % over 2003 despite a significant change in the core offerings for sale. The emphasis switched from motherboards and hardware to peripherals, leading to a more diverse product offering. Also in 2004, the Company introduced its VoIP products. The Company incurred a net loss in 2004 of \$3,920,245.

In 2005, the Company completed its transition 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. Late in the year, the Company publicized plans to introduce several new models in 2006, including LCD panels as large as 47". The Company is now working with multiple manufacturers of these products.

The VoIP division completed the development and testing cycle on products, and entered into its first large contract with Arizona State University. The

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

division also made inroads into the market in mainland China, and purchased fixed assets and equipment to support the product line in coming years. The VoIP Division should add significantly to the Company's profitability in 2006.

On March 28, 2005 the Company announced that an accredited investor, 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.

As a general rule, the Company has been totally reliant upon the cash flows from its operations to fund future growth. As noted above, the Company completed a small private placement in 2005, 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. However, throughout the year and as of the date of this filing, the Company did not have any established credit facilities in place, and had no reliable external sources of liquidity in place, other than advances from officers, directors and shareholders.

25

The Company has begun and continues to implement the following steps to increase its financial position, liquidity, and long term financial health:

- The Company has completely revised its product mix toward higher margin products
- The Company has improved the number and credit quality of its customer accounts.
- The Company has arranged additional supply sources and no longer purchases inventory from SOYO Taiwan.
- The Company moved its office and warehouse operations into a larger, more efficient facility in September 2003.

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

### 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.

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

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.

26

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. However, 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 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:

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



## Edgar Filing: SOYO GROUP INC - Form 10-K/A

activities of the entity" in accordance with APB 9, as amended by APB 30,

27

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 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.

28

### ALLOWANCE FOR DOUBTFUL ACCOUNTS

The Company regularly analyzes customer balances, and, when it becomes evident a

## Edgar Filing: SOYO GROUP INC - Form 10-K/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.

### 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

29

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.

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

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 \$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

30

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 Doubtful Accounts.** The provision for doubtful accounts 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.

**Adjustment of Allowance-** The Company did a thorough analysis of it's provision for bad debts in 2005, and concluded that the allowance was too high. As a result, the Company adjusted the allowance by \$462,234, resulting in income of

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

the same amount.

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 \$514,920 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, streamlined expenses and the reversal of a portion of the allowance for bad debts. 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 \$26,190 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 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 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

31

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.

Results of Operations:

Years Ended December 31, 2004 and 2003-

Net Revenues. Net revenues increased by \$1,392,175 or 4.5% to \$32,426,414 in

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

2004 as compared to \$31,034,239 in 2003. The increase in net revenues was primarily attributable to increased penetration in the Latin American market while undergoing a radical change in our core offerings for sale.

During the years ended December 31, 2004 and 2003, the Company offered price protection to certain customers under specific programs aggregating \$295,999 and \$766,904 respectively, which reduced net revenues and accounts receivable accordingly. Although price protection offered to customers was significantly decreased in 2004, it was partially offset by an increase in marketing fees, which increased G&A expenses.

Gross Margin (Deficit). Gross margin was \$2,216,372 or 6.8 % in 2004, as compared to \$3,073,862 or 9.9 % in 2003. Gross margin decreased in 2004 as compared to 2003, 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. Consequently, sales at lower margins were made to reduce inventory levels, especially of older inventory.

Sales and Marketing Expenses. Selling and marketing expenses increased by \$762,762 or 94 %, to \$1,577,609 in 2004, as compared to \$814,847 in 2003. The increase was primarily due to marketing expenses on new product lines and higher marketing expenses in new markets, as described in the Sales and Marketing section of item 1 of this report..

General and Administrative Expenses. General and administrative expenses increased by \$727,592 or 25.7 %, to \$3,560,710 in 2004, as compared to \$2,833,118 in 2003. There were several reasons for the increase. First, the Company had accounting and legal fees increase by over \$400,000 as a result of the problems with the 2003 audit. The Company also paid over \$300,000 to contractors who were hired to assist with the 2003 audit and resolve the internal control problems highlighted in the audit. The Company does not expect those costs to recur in 2005.

32

Provision for Doubtful Accounts. The provision for doubtful accounts increased to \$956,738 in 2004, as compared to \$390,555 in 2003, primarily as a result of several large charge offs, including Dinastia for approximately \$250,000 when they declared bankruptcy.

Depreciation and Amortization. Depreciation and amortization of property and equipment was \$34,998 in 2004 as compared to \$15,689 in 2003. The large increase resulted from the large increase in depreciable assets following the move to Ontario, California.

Loss from Operations. The loss from operations was \$3,913,683 for the year ended December 31, 2004, as compared to a loss from operations of \$980,347 for the year ended December 31, 2003.

Interest Expense. Interest expense decreased to \$23,371 in 2004, as compared to \$26,248 in 2003.

Interest Income. Interest income was \$0 in 2004, as compared to \$26,252 in 2003. Through the year, the Company had no balances in interest bearing accounts.

Other Income. Other income/expense was \$17,609 in 2004, as compared to \$(3,445) in 2003.

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

Provision for Income Taxes. Provision for income taxes of \$800 was booked for both 2004 and 2003.

Net Loss. The net loss was \$3,920,245 for the year ended December 31, 2004, as compared to a net loss of \$984,588 for the year ended December 31, 2003.

Preferred Stock Dividends. Preferred stock dividends were \$1,173,753 in 2005, \$223,733 in 2004, and \$0 in 2003.

Net Operating Loss Carryforwards:

As of December 31, 2005, the Company had federal and state net operating loss carryforwards of approximately \$4,500,000 and \$70,000 respectively,, expiring in various years through 2024, which can be used to offset future taxable income, if any. The Company's net operating losses were reduced by \$10,500,000 for the forgiveness of debt for tax purposes. 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.

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%

33

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, 2005:

Transactions involving SOYO Taiwan. Beginning with the formation of SOYO Nevada in October 1998, the Company relied on the financial support from SOYO Taiwan for inventory and capital to provide the resources necessary to conduct operations. Through October 24, 2002, SOYO Nevada was a wholly-owned subsidiary of SOYO Taiwan. Subsequent to that date, SOYO Taiwan continued to provide inventory to SOYO, and agreed to continue to provide inventory to SOYO on an open account basis through December 31, 2005. However, with the change in the Company's direction in 2004, that agreement became moot. SOYO did not order nor receive any inventory from SOYO Taiwan in 2005.

In conjunction with the October 2002 transaction, SOYO Nevada transferred \$12,000,000 of accounts payable to SOYO Taiwan to long-term payable, without interest, due December 31, 2005. SOYO Taiwan also agreed to continue to provide computer parts and components to SOYO on an open account basis at the quantities required and on a timely basis to enable SOYO to continue to conduct its business operations at budgeted 2003 levels, which was not less than a level consistent with the operations of SOYO Nevada's business in 2001 and 2000. This supply commitment was effective through December 31, 2005.

During the years ended December 31, 2004, 2003 and 2002, the Company purchased inventory from SOYO Taiwan aggregating \$14,004,259, \$20,188,354, and \$42,219,164 respectively. At December 31, 2004 and 2003, the Company had short-term accounts payable to SOYO Taiwan of \$1,314,910 and \$6,557,253 respectively, and a long-term payable to SOYO Taiwan of \$0 and \$12,000,000 respectively. As stated

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

earlier, the Company purchased no inventory from SOYO Taiwan in 2005, and had no payables to SOYO Taiwan at December 31, 2005.

During the years ended December 31, 2004 and 2003, the Company received price protection from SOYO Taiwan aggregating \$0 and \$651,215 respectively, which reduced inventories and accounts payable to SOYO Taiwan accordingly. The Company received no price protection from SOYO Taiwan in 2005.

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

34

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 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.

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

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.

35

For the year ended December 31, 2004, the Company recorded aggregate dividends of \$223,733, consisting of dividends based on the stated value of the Class B convertible preferred stock of \$114,195, which were declared and expensed through the issuance of an additional 114,195 shares of Class B Convertible Preferred Stock, and dividends based on the accretion of the discount on the Class B Convertible Preferred Stock of \$109,538.

Through March 31, 2006, 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 \$178,088 from operating activities during the year ended December 31, 2005, as opposed to utilizing cash of \$183,925 from operating activities during the year ended December 31, 2004, and compared to providing cash of \$58,489 in operating activities during the year ended December 31, 2003.

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. The usage of cash in 2003 was primarily a result of increased payments to SOYO Taiwan for inventory purchases.

At December 31, 2005 the Company's cash and cash equivalents had decreased by \$460,057 to \$828,294, as compared to \$1,288,351 at December 31, 2004.

The Company had working capital of \$689,141 at December 31, 2005, as compared to a working capital deficit of \$4,256,905 at December 31, 2004, resulting in current ratios of 1.04 to 1 and .63:1 at December 31, 2005 and 2004, respectively.

Accounts receivable increased to \$7,278,520 at December 31, 2005, as compared to \$2,076,882 at December 31, 2004, an increase of \$5,201,638. The large increase was due to several factors. Most importantly, sales increased 18% during the year, and a large part of the increase was in December. The demand for the Company's LCD televisions and monitors was sufficient that the Company was able to sell all of its inventory to retailers for the Christmas season, resulting in large receivables over the year end period. We did not give discounts or other considerations to retailers to sell any products prior to year end.

Inventories increased to \$7,991,030 at December 31, 2005, as compared to \$3,862,911 at December 31, 2004, an increase of \$4,128,119 or 107%. These numbers are very deceptive, as inventory in transit at December 31, 2005 was



## Edgar Filing: SOYO GROUP INC - Form 10-K/A

\$2,686,298, and inventory shipped FOB destination but not yet received by customers on December 31, 2005 was approximately \$3.0 million. That means that inventory in the warehouse was only \$2,241,000. The inventory was very low due

36

to high sales volume, and correspondingly, the inventory in transit was very high as the Company fills orders for products and attempts to stock consumer products for future sales.

Accounts payable increased by \$4,402,907 to \$13,977,579 at December 31, 2005 as compared to \$9,574,672 at December 31, 2004. The reason for the increase is the increased business volume. The increase partially offsets a large increase in receivables for the same time period.

Accrued liabilities increased to \$1,287,108 at December 31, 2005, as compared to \$829,043 at December Less than 1 2-3 4-5 years Over 5 31, 2004, an increase year years years of \$458,065 or 55%. The increase is due to the Company accruing additional expenses over the year end period for expenses incurred in 2005 but paid in 2006.

Investing Activities. The Company expended \$621,970, \$158,670, and \$4,589 in 2005, 2004 and 2003 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.

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.

In October 2005, the Company borrowed \$165,000 from an individual for working capital purposes.

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 the Company announced that an accredited investor, 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

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

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.

37

### Principal Commitments:

A summary of the Company's contractual cash obligations as of December 31, 2005, is as follows:

Contractual Cash Obligations	Less than 1 year	2-3 years	4-5 years	Over 5 years
Operating Leases	\$210,983	\$407,659	N/A	N/A
Advances from Directors	N/A	N/A	N/A	N/A
Notes Payable/ Short Term Loan	\$165,000	N/A	N/A	N/A
Purchase Commitments	\$119,013			
<b>Total</b>	<b>\$494,996</b>	<b>\$407,659</b>		

At December 31, 2005, 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 \$119,013.

At December 31, 2005, 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. could be considered off-balance sheet arrangements.

### 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, 2005 and 2004 are primarily short-term in nature and non-interest bearing, the Company does not have any risk from an increase in interest rates. However, to the extent that the Company arranges new interest-bearing borrowings in the future, an increase in current interest rates would cause a commensurate increase in the interest expense related to such borrowings.

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

ITEM 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
2. Consolidated Balance Sheets as of December 31, 2005 and 2004
3. Consolidated Statements of Operations for the years ended December 31, 2005, 2004 and 2003
4. Consolidated Statements of Shareholders' Equity (Deficit) for the years ended December 31, 2005, 2004 and 2003
5. Consolidated Statements of Cash Flows for the years ended December 31, 2005, 2004 and 2003
6. Notes to Consolidated Financial Statements.

39

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

	Page ----
Report of Independent Registered Public Accounting Firm	
- Vasquez & Company LLP	41
- Grobstein, Horwath & Company LLP	42
Consolidated Balance Sheets - December 31, 2005 and 2004	43-44
Consolidated Statements of Operations - Years Ended December 31, 2005, 2004 and 2003	45
Consolidated Statements of Shareholders' Equity (Deficit) - Years Ended December 31, 2005, 2004 and 2003	46

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

Consolidated Statements of Cash Flows - Years Ended December 31, 2005, 2004 and 2003	47-48
Notes to Consolidated Financial Statements - Years Ended December 31, 2005, 2004 and 2003	49-

40

### REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

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

We have audited the accompanying consolidated balance sheets of Soyo Group, Inc. and Subsidiary (the "Company") as of December 31, 2005 and 2004, and the related consolidated statements of operations, shareholders' equity (deficit) and cash flows for each of the years in the two-year period ended December 31, 2005. 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 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 financial reporting. Our audit 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 includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes 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.

In our opinion, the consolidated 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, 2005 and 2004, and the consolidated results of their operations and their cash flows for each of the

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

years in the two-year period ended December 31, 2005, in conformity with accounting principles generally accepted in the United States of America.

Vasquez & Company LLP

/s/ Vasquez & Company LLP

Los Angeles, California  
March 13, 2006

41

### REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

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

We have audited the accompanying consolidated balance sheets of Soyo Group, Inc. and Subsidiary (the "Company") as of December 31, 2003 and 2002, and the related consolidated statements of operations, shareholders' deficiency and cash flows for the years then ended. 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 consolidated 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 financial reporting. Our audit 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 consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated 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, 2003 and 2002, and the consolidated results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1 to the consolidated financial statements, the Company has suffered recurring operating losses, has limited operating cash flows and working capital resources, and has a shareholders' deficiency, which raise substantial doubt about its ability to continue as a going concern. Management's plans in regard to these matters are also described in Note 1. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

As discussed in Note 5 to the consolidated financial statements, effective January 1, 2002, the Company adopted the provisions of Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets".

/s/ Grobstein, Horwath & Company LLP

Sherman Oaks, California  
May 12, 2004

42

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

	December 31,	
	2005	2004
ASSETS		
CURRENT		
Cash and cash equivalents	\$ 828,294	\$ 1,288,351
Accounts receivable, net of allowance for doubtful accounts of \$589,224 and \$1,074,550 at December 31, 2005 and 2004 respectively	7,278,520	2,076,882
Inventories, including \$0 and \$1,893,442 purchased from SOYO Computer, Inc. in 2005 and 2004 respectively	7,991,030	3,862,911
Prepaid Expenses	20,984	25,416
Income tax refund receivable	0	47,000
Total Current Assets	16,118,828	7,300,560
Property and Equipment	867,122	245,153
Less: accumulated depreciation and amortization	(115,480)	(80,087)
	751,642	165,066
Deposits	36,920	34,811

Edgar Filing: SOYO GROUP INC - Form 10-K/A

Total Assets \$ 16,907,390 \$ 7,500,437

43

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

	December 31,	
	2005	2004
-----	-----	-----
LIABILITIES		
-----	-----	-----
CURRENT		
-----	-----	-----
Accounts payable - SOYO Computer, Inc	\$ 0	\$ 1,314,910
-----	-----	-----
Accounts payable - Other	13,977,579	8,259,762
-----	-----	-----
Total Accounts Payable	13,977,579	9,574,672
-----	-----	-----
Accrued liabilities	1,287,108	829,043
-----	-----	-----
Advances from officers, directors and major shareholder	0	240,000
-----	-----	-----
Business Loan	0	913,750
-----	-----	-----
Short Term Loan	165,000	0
-----	-----	-----
Current Liabilities	15,429,687	11,557,465
-----	-----	-----
Total Liabilities	15,429,687	11,557,465
-----	-----	-----
EQUITY		
-----	-----	-----
Class A Preferred stock, \$0.001 par value, Issued and outstanding - 0 shares (1,000,000 shares - 2004)	0	1,000
-----	-----	-----
Class B Preferred stock, \$0.001 par value, Issued and outstanding - 2,797,738 shares in 2005, 2,614,195 shares in 2004	1,702,486	1,527,733

Edgar Filing: SOYO GROUP INC - Form 10-K/A

Preferred Stock Backup Withholding	(84,999)	0
Common stock, \$0.001 par value Authorized - 75,000,000 shares, Issued and outstanding - 48,681,511 shares (40,530,000 shares - 2004)	48,682	40,000
Additional paid-in capital	17,225,738	11,155,000
Accumulated deficit	(17,414,204)	(16,780,761)
Total Shareholders' Equity (Deficit)	1,477,703	(4,057,028)
Total Liabilities plus Shareholders' Equity (Deficit)	\$ 16,907,390	\$ 7,500,437

44

SOYO Group, Inc. and Subsidiary  
Consolidated Statements of Operations

	Year Ended December 31,		
	2005	2004	2003
Net revenues	\$ 38,263,032	\$ 32,426,414	\$ 31,034,239
Cost of revenues, including inventory purchased from SOYO Computer, Inc. of \$0, \$14,004,259 and \$20,188,354 in 2005, 2004 and 2003 respectively	34,905,874	30,210,042	27,960,377
Prior years' purchase discounts and allowances settled in 2005	(1,335,812)	0	0
Gross margin	4,692,970	2,216,372	3,073,862
Costs and expenses:			
Sales and marketing	911,039	1,577,609	814,847
General and administrative	3,659,338	3,560,710	2,833,118
Provision for doubtful accounts	34,513	956,738	390,555
Adjustment of Allowance	(462,234)	0	0



Edgar Filing: SOYO GROUP INC - Form 10-K/A

-----	-----	-----	-----
Depreciation and amortization:			
-----	-----	-----	-----
Property and equipment	35,394	34,998	15,689
-----	-----	-----	-----
Total costs and expenses	4,178,050	6,130,055	4,054,209
-----	-----	-----	-----
Income (Loss) from operations	514,920	(3,913,683)	(980,347)
-----	-----	-----	-----
Other income (expense):			
-----	-----	-----	-----
Interest income	5,301	0	26,252
-----	-----	-----	-----
Interest expense	(129,567)	(23,371)	(26,248)
-----	-----	-----	-----
Other income (expense)	150,456	17,609	(3,445)
-----	-----	-----	-----
Other income (expense), net	26,190	(5,762)	(3,441)
-----	-----	-----	-----
Income (Loss) before provision (benefit) for income taxes	541,110	(3,919,445)	(983,788)
-----	-----	-----	-----
Provision for income taxes	800	800	800
-----	-----	-----	-----
Net Income (loss)	540,310	(3,920,245)	(984,588)
-----	-----	-----	-----
Less: Dividends on Convertible Preferred Stock	(1,173,753)	(223,733)	--
-----	-----	-----	-----
Net loss attributable to common shareholders	(633,443)	(4,143,978)	\$ (984,588)
-----	-----	-----	-----
Net loss per common share - Basic and diluted	(.01)	(0.10)	(0.02)
-----	-----	-----	-----
Weighted average number of shares of common stock outstanding - Basic and diluted	48,511,681	40,000,000	40,000,000
-----	-----	-----	-----

45

SOYO Group, Inc. and Subsidiary  
Consolidated Statements of Shareholders' Equity (Deficit)  
Years Ended December 31, 2005, 2004 and 2003

Additional

Edgar Filing: SOYO GROUP INC - Form 10-K/A

	Common Stock		Preferred Stock	Paid In
	Shares	Par Value	Shares	Capital
Balance, December 31, 2001	28,182,750	28,183	1,000,000	470,8
Shares of common stock retained by shareholders in October 2002 transaction	11,817,250	11,817	--	(11,8
Net loss for the year ended December 31, 2002	--	--	--	--
Balance, December 31, 2002	40,000,000	40,000	1,000,000	459,0
Net loss for the year ended December 31, 2003	--	--	--	--
Balance, December 31, 2003	40,000,000	40,000	1,000,000	459,0
Issuance of Preferred Stock for Long Term Debt	--	--	2,500,000	10,696,0
Dividends	--	--	114,195	--
Accretion of Discount	--	--	--	109,538
Net loss for the year ended December 31, 2004	--	--	--	--
Balance, December 31, 2004	40,000,000	40,000	3,614,195	11,155,0
Issuance of Common Stock for Private Placement	500,000	500	--	499,5
Issuance of Common Stock for Services	30,000	30	--	--
Issuance of Common Stock for Payment of Accounts Payable	5,645,330	5,645	--	3,608,7
Issuance of Common Stock for Payment of Loan	1,286,669	1,287	--	963,7
Issuance of Common Stock for Conversion of Preferred Stock	1,219,512	1,220	(1,000,000)	998,7
Accretion of Discount	--	--	--	174,753
Preferred Stock Backup Withholding	--	--	--	(84,999)
Net Income	--	--	--	--
Preferred Stock Dividends	--	--	--	--
	48,681,511	48,682	2,614,195	17,225,7

Edgar Filing: SOYO GROUP INC - Form 10-K/A

	Years Ended December 31,		
	2005	2004	2003
-----			
OPERATING ACTIVITIES			
-----			
Net Income (loss)	\$ 540,310	\$ (3,920,245)	\$ (984,588)
-----			
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
-----			
Depreciation	35,394	34,998	15,689
-----			
Provision for doubtful accounts	34,513	956,738	390,555
-----			
Loss on disposition of fixed assets	--	--	7,600
-----			
Changes in operating assets and liabilities:			
-----			
(Increase) decrease in:			
-----			
Accounts receivable	(5,236,151)	3,785,110	(483,860)
-----			
Inventories	(4,128,119)	1,173,214	7,322,130
-----			
Prepaid expenses	51,432	18,557	6,741
-----			
Deposits	(2,109)	(9,776)	24,965
-----			
Increase (decrease) in:			
-----			
Accounts payable - SOYO Computer, Inc	(1,314,910)	(5,242,343)	(6,246,682)
-----			
Accounts payable - other	9,332,236	2,783,763	921,179
-----			
Accrued liabilities	509,316	236,059	(915,240)
-----			
Net cash provided by (used in) operating activities	(178,088)	(183,925)	58,489
-----			
INVESTING ACTIVITIES			
-----			
Purchase of property and equipment	(621,970)	(158,670)	(4,589)
-----			
Net cash used in investing activities	(621,970)	(158,670)	(4,589)
-----			

Edgar Filing: SOYO GROUP INC - Form 10-K/A

47

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

FINANCING ACTIVITIES			
Net decrease in revolving note payable	--	--	(1,200,000)
Decrease in restricted cash	--	--	1,000,000
Advances from officer, director and major shareholder	165,000	--	360,000
Business Loan	--	913,750	--
Repayment of advances to officer, director and major shareholder	(240,000)	--	(120,000)
Proceeds from issuance of common stock	500,000	--	--
Payment of backup withholding taxes on accreted dividends on preferred stock	(84,999)	--	--
Net cash provided by financing activities	340,001	913,750	40,000
CASH AND CASH EQUIVALENTS:			
Net increase (decrease)	(460,057)	571,155	93,900
At beginning of year	1,288,351	717,196	623,296
At end of year	\$ 828,294	\$ 1,288,351	\$ 717,196
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:			
Cash paid for interest	97,783	23,371	26,248
Cash paid for income taxes	800	800	1,000
NON-CASH INVESTING AND FINANCING ACTIVITIES			

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

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	174,753	109,538	--
-----	-----	-----	-----
Deemed dividend on Class A preferred stock	999,000	--	--
-----	-----	-----	-----
Noncash dividend on Class B preferred stock	--	114,195	--
-----	-----	-----	-----

48

SOYO Group, Inc. and Subsidiary  
Notes to Consolidated Financial Statements  
Years Ended December 31, 2005, 2004 and 2003

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.

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 the difference between \$12,000,000 and the value of the preferred stock. This forgiveness was treated as a capital transaction. Payment was

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

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 were to 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 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.

49

Based on the terms of the agreement between SOYO Taiwan and the third party, and specifically the limitation on the purchaser collecting no 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.

At the time of the transaction, SOYO Taiwan also agreed to continue to provide computer parts and components to SOYO on an open account basis at the quantities required and on a timely basis to enable SOYO to continue to conduct its business operations at budgeted 2003 levels, which is not less than a level consistent with the operations of SOYO Nevada's business in 2001 and 2000. This supply commitment was effective through December 31, 2005.

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

On October 24, 2002, the primary members of SOYO Nevada management were Ming Tung Chok, the Company's President, Chief Executive Officer and Director, and Nancy Chu, the Company's Chief Financial Officer, 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.

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

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, communications services and computer 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).

50

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.

In 2003, the Company was selling only computer equipment, although the plans to expand the product lines were being developed.

In 2004, the emphasis switched from motherboards and hardware to peripherals. Also in 2004, the Company introduced its VoIP products, which was part of the reason for the improved performance in 2005.

The Company sold over LCD monitors and televisions in 2005.

Through December 31, 2004, the Company has been totally reliant upon the cash flows from its operations. Through 2004, the Company did not have any external sources of liquidity, other than advances from an officer, director, major shareholder, and LGT Computers, Inc.

On March 28, 2005 the Company announced that an accredited investor, 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.

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

The Company has been totally reliant upon the cash flows from its operations to fund future growth. As noted above, the Company completed a small private placement in 2005, 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. However, throughout the year and as of the date of this filing, the Company did not have any established credit facilities in place, and had no reliable external sources of liquidity in place, other than advances from officers, directors and shareholders.

The Company has begun and continues to implement the following steps to increase its financial position, liquidity, and long term financial health:

- The Company has completely revised its product mix toward higher margin products
- The Company has improved the number and credit quality of its customer accounts.
- The Company has arranged additional supply sources and no longer purchases inventory from SOYO Taiwan.
- The Company moved its office and warehouse operations into a larger, more efficient facility in September 2003.

51

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

## 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 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.

Estimates recorded for warranties are based on historical data. The number and percentage of customers applying for warranties differs based on the price and sophistication of the product sold. For example, the number of customers applying for a warranty on a \$1,000 television will always exceed the number of customers applying for warranty coverage on a \$40 memory storage device. As



## Edgar Filing: SOYO GROUP INC - Form 10-K/A

such, that historical data is analyzed by management, and accruals to account for warranty costs are booked based on the relevant data, and adjusted if necessary to account for any special situations that may arise, such as aggressive sales incentive programs, or any special warranty programs that might have been offered.

Company policy is not to enter into guaranteed sales contracts, and the Company does not offer a refund policy for returned merchandise. For a period of one year, SOYO will replace any defective parts or workmanship, or at the Company's option, replace any defective product with a new product. After one year, SOYO will assist the customer by repairing or replacing any necessary parts, at the customer's expense.

If a special situation exists, and the Company agrees to accept merchandise back from a customer for credit, that credit is booked as a reduction to net revenues.

52

Amounts for sales incentives are booked based upon the type of sales incentive being offered. The Company offers three types of sales incentives to customers: Co-op advertising credits, price protection, and sales discounts. In each case, the exact amount of the incentive is known up front, and the amount of the incentive is booked as a reduction to net revenues.

SOYO's return policy is similar for all consumer electronics and computer parts. For a period of one year, SOYO will replace any defective parts or workmanship, or at the Company's option, replace any defective product with a new product. After one year, SOYO will assist the customer by repairing or replacing any necessary parts, at the customer's expense.

### 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 market value.

During the years ended December 31, 2005, 2004 and 2003, the Company wrote-down the value of its inventory by \$0, \$47,084 and \$429,230 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.

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

### 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

53

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, 2005 and 2004.

### 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.

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.

Our revenue recognition policy for our consumer electronics, computer peripherals, and communications hardware businesses is designed to recognize revenue when it is earned. To that end, the Company recognizes revenue when there is evidence of an arrangement, title and risk of loss have passed, delivery has occurred, the sales price is fixed and collection of the related receivable is reasonably assured. Based on the contracts with each customer, the point where title is transferred is either at shipment or when the goods are received by the customer.

The Company offers price protection to its customers where SOYO Group, Inc. has published a Price List which reflects a reduced cost. Price Protection will be available for current inventory only which is on hand on the effective date of the price reduction, and for those products which maybe in-transit and for those products which have been invoiced directly from SOYO Group, Inc. within the Prior thirty (30) calendar days period. In these cases, the amount of price protection is calculated and recognized as a reduction of revenue.

Our revenue recognition policy differs for our communications equipment. The Company acts as an agent when it sells phone minutes and phone cards. The Company recognizes net revenue as an agent under EITF 99-19, Reporting Revenue Gross as a Principal versus Net as an Agent. Revenue from phone minutes and phone cards amounted to \$616,946 in 2005 and is not considered material. The Company will make revenue policy disclosure specific to this business when it becomes material.

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.

Price protection is a concession given by a vendor to the Company to compensate for the difference between the price of the product paid by the Company and a subsequent price reduction of the product. Price protection is an adjustment to product cost and accounts payable. Price protection is accrued when the price reduction of the product is determinable.

Rebate is a concession given by a vendor to the Company based on sales volume. Rebate is an adjustment to product cost and accounts payable. Rebate is accrued when the sales volume is attained.

Product returns pertain to the return of defective merchandise, customer dissatisfaction returns, and product returns per the return of product provision under the vendor agreement. Product returns is an adjustment to product cost and accounts payable. Product return is matched with the period when the product was purchased, including estimates to be incurred in the subsequent period.

Cooperative advertising and marketing are concessions given by a vendor to the Company in accordance with an agreement. Cooperative advertising and marketing are adjustments to marketing expenses and accounts payable.

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.

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

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, 2005, 2004, and 2003 were \$849,897, \$1,481,441, and \$728,488 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. These potentially dilutive securities were not

56

included in the calculation of loss per share for the years ended December 31, 2005, 2004 and 2003 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, 2005, 2004 and 2003.

### 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

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

items of comprehensive income or loss for the years ended December 31, 2005, 2004 and 2003.

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, 2005 approximate their respective fair values due to the short-term nature of those instruments.

p. Stock-Based Compensation

In December 2004, SFAS No. 123R, "Share-based Payment" was issued and replaces SFAS No. 123, "Accounting for Stock-Based Compensation" and supersedes Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees." SFAS 123R requires the measurement of all employee share-based payments, including grants of employee stock options, using a fair-value based model. Deferred compensation calculated under the fair value method would then be amortized into income over the respective vesting period of the stock option. The accounting provisions of SFAS 123R are effective for reporting periods beginning after June 15, 2005.

The Company currently accounts 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"). 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..

If the fair value based method under FAS 123 had been applied in measuring stock-based compensation expense for the years ended December 31, 2005 and 2004, the pro forma on net loss and net loss per share would have been as follows:

57

	December 31, 2005 -----
Net loss attributable to common shareholders, as reported	\$ (633,443)
Add: Stock based employee compensation expense included in reported net loss, net of related tax effects	--
Deduct: Total Stock-based employee compensation expense determined under fair-value based method for all awards not included in net loss	(238,103) -----

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

Pro-forma net loss attributable to common shareholders	\$ (871,546)
	=====
Loss per share:	
Basic and diluted - as reported	\$ (0.01)
Basic and diluted - pro-forma	\$ (0.02)

Through December 31, 2004, the Company did not have any Equity Compensation Plans. 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. However, since Mr. Chok and Ms. Chu, husband and wife, are directors who own more than 50% of the company, shareholder approval is essentially a formality, hence the grant date of the stock options is July 22, 2005.

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

The options do not have requisite service period nor market, performance, and service conditions.

### 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.

58

### r. Recent Accounting Pronouncements

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

SFAS 154 requires voluntary changes in accounting principle be retrospectively applied to financial statements from previous periods unless such application is impracticable. Changes in depreciation, amortization, or

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

depletion for long-lived, non-financial assets are accounted for as a change in accounting estimate that is affected by a change in accounting principle, under the newly issued standard.

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

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

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

59

SFAS 153 is effective on January 1, 2006. The adoption of SFAS 153 is not expected to have an impact on the Company's consolidated financial statements or disclosures.

On December 16, 2004, the FASB issued SFAS No. 123R, "Share-Based Payment," ("SFAS 123R") which is a revision of SFAS No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123"). Statement 123R supersedes APB Opinion No. 25, "Accounting for Stock Issued to Employees," and amends SFAS No. 95, "Statement of Cash Flows." Generally, the approach in SFAS 123R is similar to the approach described in SFAS 123. SFAS 123R requires all share-based payments to employees to be recognized in the income statement based on their grant date fair values over the corresponding service period and also requires an estimation of forfeitures when calculating compensation expense. The Company must adopt SFAS 123R no later than January 1, 2006. SFAS 123R permits public companies to adopt its requirements using one of three methods: the "modified prospective" method, the "modified retrospective" method to January 1, 2005, or the "modified retrospective" method to all prior years for which SFAS 123 was effective. The Company has not yet determined which adoption method it will utilize.

In November 2004, the FASB issued SFAS No. 151, "Inventory Costs, an amendment of ARB No. 43, Chapter 4." SFAS 151 amends the guidance in ARB No. 43, Chapter 4, "Inventory Pricing," to clarify the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material (spoilage). Paragraph 5 of ARB 43, Chapter 4, previously stated that ". . . under some circumstances, items such as idle facility expense, excessive

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

spoilage, double freight, and rehandling costs may be so abnormal as to require treatment as current period charges. . . ." SFAS 151 requires that those items be recognized as current-period charges regardless of whether they meet the criterion of "so abnormal." In addition, SFAS 151 requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities.

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

60

### 3. Accounts Receivable

The Company's accounts receivable at December 31, 2005 and 2004 are summarized as follows:

	December 31,	
	2005	2004
Accounts receivable	\$ 7,867,744	\$ 3,151,432
Less: allowance for doubtful accounts	(589,224)	(1,074,550)
	\$ 7,278,520	\$ 2,076,882

Changes in the allowance for doubtful accounts for the years ended December 31, 2005 and 2004 are summarized as follows:

	2005	2004
Balance, beginning of year	\$ 1,074,550	\$ 856,386
Add: Amounts provided during the year	34,513	956,738
Less: Amounts written off during the year	(57,605)	(738,574)
Less: Adjustment based on current estimate	(462,234)	--
Balance, end of year	\$ 589,224	\$ 1,074,550

The Company's management believes that the balance of the allowance for doubtful accounts at December 31, 2005 was sufficient to cover any past due accounts



## Edgar Filing: SOYO GROUP INC - Form 10-K/A

whose collection was considered doubtful.

During 2005, the Company began factoring its invoices to improve cash flow. As a result of this activity, the Company obtained the services of credit experts to evaluate its new and existing customer base. Based on the expert evaluations, and several deals struck with creditors to pay off debt in manageable installments, the Company believes that its 2005 provision for doubtful accounts is adequate, as was the provision for 2004.

As mentioned above, the Company began factoring its invoices in 2005 to improve cash flow. At December 31, 2005, \$580,363 of the Company's receivables had been factored and were owned by Wells Fargo.

Prior to 2005, management would book a certain percentage of sales each quarter to the allowance for doubtful accounts. During 2005, the Company hired a consultant to analyze the allowance. The result of this analysis was that the allowance was more than triple the amount the Company considered uncollectible. As a result, a reversal was made to bring the allowance in line with the estimate of uncollectible accounts, plus an additional reserve to account for unexpected losses. Since that time, management continues to review the account quarterly, and the allowance is maintained to represent the estimate of uncollectible accounts, plus an additional reserve to account for unexpected losses.

61

There were significant changes to the aging of accounts receivable between 2004 and 2005. The amount of past due receivables has dropped substantially, and two customers whose accounts had been considered uncollectible in 2004 began making payments in 2005, thereby changing the status of those accounts back to collectable. Additionally, the Company changed its product mix in 2005, resulting in a large number of new customers. As a result, the Company is now selling to many more customers, thereby reducing its credit risk.

The biggest change to the entire process from 2004 to 2005 is the way customer credit was evaluated. In 2004, the Company did all of the evaluation of customer credit internally. In 2005, the Company began factoring its invoices to improve cash flow. As a result, the factor buying the invoices began analyzing the Company's customers. The Company received a substantial benefit from this arrangement, as all customers credit was analyzed by external experts. As a result of getting this information from the experts, and the widely enhanced customer base, the Company believes that it improved the management of its receivables in 2005.

All of our receivables are 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 they switched over to Accord, those transactions were "with recourse".

#### 4. Property and Equipment

At December 31, 2005 and 2004, property and equipment consisted of the following:

Edgar Filing: SOYO GROUP INC - Form 10-K/A

	December 31,	
	2005	2004
Computer and Equipment	\$ 744,176	\$ 62,255
Furniture and Fixtures	27,943	24,333
Leasehold Improvements	83,928	149,890
Automobiles	11,075	8,675
Less: Accumulated Depreciation	(115,480)	(80,087)
Total	\$ 751,642	\$ 165,066

For the years ended December 31, 2005, 2004 and 2003, depreciation and amortization expense related to property and equipment was \$35,394, \$34,998 and \$15,689 respectively.

62

5. Goodwill

Goodwill represents the excess of the purchase price over the fair value of the identifiable net assets acquired in an acquisition in 1999, accounted for using the purchase method. Goodwill was being amortized on the straight-line basis over a three year period.

Effective January 1, 2002, the Company adopted the provisions of Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets", which eliminated the amortization of goodwill. No impairment was recorded upon the adoption of this accounting standard. At January 1, 2002, goodwill was \$1,251,325, less accumulated amortization of \$862,018. At December 31, 2002, goodwill was reviewed for impairment and the remaining balance of \$389,307 was charged to operations.

6. 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 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.

7. 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

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

market price of the stock was \$0.75.

### 8. 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:

Years Ending December 31,  
-----

2006	210,983
2007	212,692
2008	194,967

Rent expense for the years ended December 31, 2005, 2004 and 2003 was \$238,836, \$229,718 and \$276,044 respectively.

#### b. Legal Proceedings

On August 2, 2004, a lawsuit was filed in California Superior Court entitled Gerry Normandan. et al, v. Soyo Inc. Case No. RCV 082128. The case seeks class action status and alleges defects in motherboards which Soyo distributes, and that the Company misrepresented and omitted material facts concerning the motherboards. The plaintiff seeks restitution and disgorgement of all amounts obtained by defendant as a result of alleged misconduct, plus interest, actual damages, punitive damages and attorneys' fees. The Company is vigorously defending the lawsuit and believes that it will be resolved with no material adverse effect on the Company.

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

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.

63

## 9. Income Taxes

For the year ended December 31, 2005, the Company believes that all income taxes due are offset by federal and state net operating loss carryforwards. For the years ended December 31, 2004 and 2003, the Company incurred net losses and accordingly, had no tax liability, other than minimum state franchise taxes.

As of December 31, 2005, the Company had federal and state net operating loss carryforwards of \$4,500,000 and \$70,000 respectively, expiring in various years through 2024, which can be used to offset future taxable income, if any. The Company's net operating losses were reduced by \$10,500,000 for the forgiveness of debt for tax purposes. 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.

The reconciliation of the effective income tax rate to the Federal statutory rate is as follows:

	Year ended December 31,	
	2004	2005
Federal income tax	34%	34%
State income tax	9%	9%
Effect of net operating loss and net operating loss carry forward	(43%)	(43%)
Effective income tax rate	0%	0%

## 10. Significant Concentrations

## a. Customers

The Company sells to both distributors and retailers. Revenues through such distribution channels for the years ended December 31, 2005, 2004 and 2003 are summarized as follows:

	Year Ended December 31,					
	2005		2004		2003	
	\$	%	\$	%	\$	%
Revenues						
Distributors	\$22,312,488	58.3	\$14,704,452	45.3	\$13,055,046	42.1
Retailers	\$15,950,544	41.7	\$17,721,962	54.7	\$17,979,193	57.9

Edgar Filing: SOYO GROUP INC - Form 10-K/A

Total	\$38,263,032	100.0	\$32,426,414	100.0	\$31,034,239	100.0
-------	--------------	-------	--------------	-------	--------------	-------

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.

65

During the year ended December 31, 2004, the Company had one customer (SYX Distribution, Inc., otherwise known as Tiger Direct) that accounted for revenues of \$8,591,711, equivalent to 26% of net revenues. During the year ended December 31, 2003, the same customer accounted for revenues of \$9,943,855, equivalent to 32% of net revenues.

b. Geographic Segments

Revenues by geographic segment are summarized as follows:

	Year Ended December 31,					
	2005	%	2004	%	2003	%
Revenues						
United States	\$20,055,470	56.7	\$25,936,978	80.0	\$23,043,136	74.3
Other N. America	1,615,080		N/A		N/A	
Central and South America	\$2,993,532	7.8	\$6,317,907	19.5	\$7,391,804	23.8
Hong Kong and other locations	\$13,598,950	35.4	\$171,529	0.5	\$599,299	1.9
Total	\$38,263,032	100.0	\$32,426,414	100.0	\$31,034,239	100.0

During the years 2003 and 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.

Revenues by product line are summarized as follows:

Edgar Filing: SOYO GROUP INC - Form 10-K/A

Year Ended December 31,						
	2005	%	2004	%	2003	%
Revenues						
Consumer Electronics	\$18,739,719	49.0	N/A		N/A	
Computer parts and peripherals	18,906,367	49.4	N/A		N/A	
Voice and Communication	616,946	1.6	N/A		N/A	
Total	\$38,263,032	100.0	\$32,426,414		\$31,034,239	

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

66

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.

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. The sales had relatively low margin, and not a business that the Company planned to be in long term.

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 year ended December 31, 2005, the Company did not purchase any products from SOYO Taiwan. As of December 31, 2005, no more than 39% of the products distributed by the SOYO Group are 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

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

SOYO Taiwan as of and for the years ended December 31, 2005, 2004 and 2003:

	December 31,		
	2005	2004	2003
Accounts payable to SOYO Taiwan	\$0	\$1,314,910	\$ 6,557,253
Long-term payable to SOYO Taiwan	\$0	\$0	\$12,000,000

	Years Ended December 31,		
	2005	2004	2003
Purchases from SOYO Taiwan	\$0	\$14,004,259	\$20,188,354
Payments to SOYO Taiwan	\$873,050	\$19,154,603	\$18,842,244

67

During the years ended December 31, 2005, 2004 and 2003, the Company received price protection from SOYO Taiwan of \$0, \$0, and \$651,215, respectively, which reduced inventory and accounts payable accordingly.

### 11. 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 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 48,681,511 shares outstanding as of December 31, 2005.

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

### 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

68

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 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.



## Edgar Filing: SOYO GROUP INC - Form 10-K/A

Based on the terms of the agreement between SOYO Taiwan and the third party, and specifically the limitation on the purchaser collecting no more than \$1,630,000 of the \$12,000,000 from the Company without the prior consent of SOYO

69

Taiwan, the Company has determined that this transaction is in substance a capital transaction. Accordingly, the Company recorded the issuance of the Class B preferred stock at its fair market value in 2004, with the difference between the \$12,000,000 long-term payable and the fair market value of the Class B preferred stock credited to additional paid-in capital. The difference between the fair market value and the liquidation value of the Class B preferred stock will be recognized as an additional dividend to the Class B preferred stockholder, and will be accreted through December 31, 2008.

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, 2005, the only warrants outstanding were those issued to Evergreen Technology as part of the private placement completed in March 2005, and described above. The Company has created a stock option plan, but as of December 31, 2005, the plan had not yet been approved by the shareholders, and no options granted under the plan had vested.

## 12. Quarterly Results (Unaudited)

Presented below is a summary of the quarterly results of operations for the years ended December 31, 2005 and 2004.

	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	\$38,263,032
Gross margin	\$1,522,035	\$1,054,872	\$206,771	\$1,909,292	\$4,692,970
Income (loss) from Operations	\$308,724	\$36,760	(\$944,641)	\$651,843	\$52,686
Other Income (Expense), Net	\$77,951	\$65,359	\$582,449	(\$237,335)	\$488,424
Income (loss)	\$386,675	\$102,119	(\$362,192)	\$414,508	\$541,110

Edgar Filing: SOYO GROUP INC - Form 10-K/A

before taxes					
Income taxes				800	800
Net Income (loss)	\$386,675	\$102,119	(\$362,192)	\$413,708	\$540,310
				70	
Dividends	\$39,213	\$42,458	\$42,935	\$1,049,147	\$1,173,753
Net Income (Loss) Attributable to Common Shareholders	\$347,462	\$59,661	(\$405,127)	(\$635,439)	(\$633,443)
Net income (loss) per common share - Basic					
Diluted	.01	--	(.01)	(.01)	(.01)
	.01	--	(.01)	(.01)	(.01)
Weighted average number of common shares outstanding -					
Basic	48,681,511	48,681,511	48,681,511	48,681,511	48,681,511
Diluted	52,736,204	52,736,204	48,681,511	48,681,511	48,681,511
	March 31, 2004	June 30, 2004	Sept 30, 2004	Dec 31, 2004	Total
Net revenues	\$8,594,302	\$10,194,388	\$9,347,427	\$4,290,297	\$32,426,414
Gross margin	1,113,168	398,972	307,513	396,719	2,216,372
Income (loss) from Operations	94,705	(924,036)	(809,416)	(2,274,936)	(3,913,683)
Other Income (Expense), Net	--	(4,745)	(4,745)	3,728	(5,762)

Edgar Filing: SOYO GROUP INC - Form 10-K/A

Income (loss) before taxes	94,705	(928,781)	(814,161)	(2,271,208)	(3,919,445)
Income taxes					
Net Income (loss)	94,705	(928,781)	(814,161)	(2,271,208)	(3,919,445)
Net income (loss) per common share -					
Basic	\$ --	(\$ .02)	(\$ .02)	(\$ .06)	(\$ .10)
Diluted	\$ --	(\$ .02)	(\$ .02)	(\$ .06)	(\$ .10)
Weighted average number of common shares outstanding -					
Basic	40,000,000	40,000,000	40,000,000	40,000,000	
Diluted	40,000,000	40,000,000	40,000,000	40,000,000	

71

During the year, 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.

Effective July 23, 2004, the Company dismissed Grobstein, Horwath & Company LLP ("Grobstein"), as the Company's independent registered public accounting firm. Effective July 26, 2004, the Company engaged Vasquez & Company LLP ("Vasquez") as the Company's new independent registered public accounting firm. The dismissal of Grobstein and the engagement of Vasquez were approved by the Company's Board of Directors.

During the year ended December 31, 2003, and the subsequent interim period from January 1, 2004 through July 26, 2004, neither the Company, nor anyone on its behalf, consulted with Vasquez regarding; (i) either the application of accounting principles to a specified transaction, either completed or proposed; or the type of audit opinion that might be rendered on the Company's financial statements and no written report or oral advice was provided that Vasquez concluded was an important factor considered by the Company in reaching a decision as to the accounting, auditing or financial reporting issue; or (ii) any matter that was either the subject of a disagreement as defined at Item 304(a)(1)(iv) or a reportable event as defined at Item 304 (a)(1)(iv) of Regulation S-K.

Grobstein audited the Company's financial statements for the fiscal years

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

ended December 31, 2002 and 2003. Grobstein's reports for these periods did not contain an adverse opinion or a disclaimer of opinion, nor were they qualified or modified as to audit scope or accounting principles, except that such reports contained a modification paragraph that indicated that as a result of the Company's losses from operations there was substantial doubt about the Company's ability to continue as a going concern.

During the fiscal years ended December 31, 2002 and 2003, and the interim period from January 1, 2004 through July 23, 2004, there were no disagreements with Grobstein on any matter of accounting principles or practices, financial

72

statement disclosure, or auditing scope or procedure, which disagreements, if not resolved to the satisfaction of Grobstein, would have caused such firm to make reference to the subject matter of the disagreements in connection with its reports on the Company's financial statements. In addition, there were no such events as described under Item 304(a)(1)(v) of Regulation S-K during the fiscal years ended December 31, 2002 and 2003 and the interim period from January 1, 2004 through July 23, 2004, except that (a) as described in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2003 (Item 9A) and Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2004 (Item 4), the Company's disclosure controls and procedures were not adequate, (b) by letter dated July 15, 2004, Grobstein stated that it noted certain deficiencies involving internal controls that Grobstein considered to be significant deficiencies that, in the aggregate, constitute material weaknesses under standards established by the American Institute of Certified Public Accountants. Grobstein discussed the significant deficiencies and material weaknesses set forth in the above mentioned letter with the Company's Board of Directors.

Effective February 10, 2003, the Company, dismissed Gerald R. Perlstein, CPA ("Perlstein"), as the Company's independent accountant. Effective February 10, 2003, the Company engaged Grobstein, Horwath & Company LLP, ("Grobstein") as the Company's new independent accountants. Perlstein had been retained by the Company as its independent accountant on January 31, 2000. The dismissal of Perlstein and the engagement of Grobstein were approved by the Company's Board of Directors.

Prior to Grobstein becoming the independent accountants for the Company, neither the Company, nor anyone on its behalf, consulted with Grobstein regarding either the application of accounting principles to a specific completed or proposed transaction, or the type of audit opinion that might be rendered on the Company's financial statements; or any matter that was the subject of a disagreement or event as defined at Item 304 (a) (1)(iv) of Regulation S-K.

Perlstein audited the Company's financial statements for the fiscal years ended July 31, 2001 and 2002. During his engagement, Perlstein's reports for these periods did not contain an adverse opinion or a disclaimer of opinion, nor were they qualified as to audit scope or accounting principles, however, Perlstein's report for these fiscal years was modified to reflect uncertainty with respect to the Company's ability to continue as a going concern.

During the fiscal years ended July 31, 2001 and 2002 and the interim period from August 1, 2002 through February 10, 2003, there were no disagreements with Perlstein on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure, which disagreements, if not resolved to the satisfaction of Perlstein, would have caused such firm to make reference to the subject matter of the disagreements in connection with its

report on the Company's financial statements. In addition, there were no such events as described under Item 304(a)(1)(iv)(B) of Regulation S-K during the fiscal years ended July 31, 2001 and 2002 and the interim period from August 1, 2002 through February 10, 2003.

Effective February 13, 2003, the Company, dismissed Malone & Bailey PLLC ("M & B"), as the independent accountants of its wholly-owned subsidiary, SOYO Nevada, Inc. The dismissal of M & B and the engagement of Grobstein were approved by the Company's Board of Directors.

Prior to Grobstein becoming the independent accountants for the Company, neither the Company, nor anyone on its behalf, consulted with Grobstein regarding either the application of accounting principles to a specific or contemplated transaction, or the type of audit opinion that might be rendered on the Company's financial statements; or any matter that was the subject of a disagreement or event as defined at Item 304 (a) (1) (iv) of Regulation S-K.

M & B audited the Company's financial statements for the fiscal years ended December 31, 2000 and 2001. M & B's reports for these periods did not contain an adverse opinion or a disclaimer of opinion, nor were they qualified as to audit scope or accounting principles.

During the fiscal years ended December 31, 2000 and 2001 and the interim period from January 1, 2001 through February 13, 2003, there were no disagreements with M & B on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure, which disagreements, if not resolved to the satisfaction of M & B, would have caused such firm to make reference to the subject matter of the disagreements in connection with its report on the Company's financial statements. In addition, there were no such events as described under Item 304(a)(1)(IV)(B) of regulation S-K during the fiscal years ended December 31, 2000 and 2001 and the interim period from January 1, 2001 through February 13, 2003.

#### ITEM 9A. CONTROLS AND PROCEDURES

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

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) as of the end of the period covered by this Form 10-K and have concluded, based on that evaluation, that as of such dates, 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 the fact that the Company's system of internal control requires considerable manual intervention to do the following: (1) properly record accounts payable to vendors for purchases of inventory, (2) to properly record adjustments to

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

inventory per the general ledger to physical inventory balances, (3) to properly record inventory adjustments to the lower of cost or market using the average inventory method, (4) to have adequate controls over interim physical inventory procedures, and (5) to generate timely and accurate financial information to allow for the preparation of timely and complete financial statements. The Company did not have an adequate financial reporting process because of the aforementioned material weaknesses, including the difficulty in identifying and assembling all relevant contemporaneous documentation for ongoing business transactions, and significant turnover in the Company's financial staff. 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 period ended December 31, 2005.

A significant deficiency should be classified as a material weakness if, by itself or in combination with other control deficiencies, it results in more than a remote likelihood that a material misstatement in the company's annual or interim financial statements will not be prevented or detected.

To address these significant deficiencies and material weaknesses, the Company took the following corrective actions:

While the Company is searching for a new accounting manager, the Company has retained a financial consultant and former CPA to oversee the day to day management of the accounting department. The Company has recently added additional personnel to complete the day to day accounting tasks. The Company needs and is seeking to immediately hire an Accounting Manager and additional personnel to focus on financial accounting and reporting issues.

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

75

records inventory adjustments to the lower of cost or market. These tasks will be supervised by the financial consultant until the new Accounting Manager is hired.

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.

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

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

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

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

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

ITEM 9B. OTHER INFORMATION- NONE

### PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

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, 2006. The Company's Board of Directors is comprised of only one class. All 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.

76

Name	Age	Position Held
Ming Tung Chok	45	Chief Executive Officer and Director
Nancy Chu	49	Chief Financial Officer, Secretary and Director
Paul F. Risberg	44	Director
Chung Chin Keung	39	Director
Zhi Yang Wu	35	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.

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

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.

Chung Chin Keung was appointed in October 2005 as an independent non-executive director and audit 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.

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.

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 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

77

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.

Daniel Hou was appointed in October 2005 as an independent non-executive director and audit compensation member. Mr. Hou has served as the president of Reyes Electronics Inc., a computer peripheral supplier he founded in 1986. Mr. Hou received a B.A. degree in chemistry from National Chung-Hsing University, Taiwan, in 1973 and a master's degree in material science from the University of Utah in 1978. Mr. Hou resigned from the Board of Directors effective December 31, 2005 for medical reasons.

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.



## Edgar Filing: SOYO GROUP INC - Form 10-K/A

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.

78

### 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 2006 Annual meeting, the date of which has not yet been set.

### 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 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

The following table sets forth the compensation paid during fiscal year

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

ended December 31, 2005, 2004 and 2003 to the Company's Chief Executive Officer and Chief Financial Officer.

79

### SUMMARY COMPENSATION TABLE

Name	Year	Salary	Bonus	Other Compensation
Ming Tung Chok President and CEO	2005	\$144,000	N/A	N/A
	2004	\$144,000		
	2003	\$144,000		
Nancy Chu Chief Financial Officer	2005	\$120,000		
	2004	\$120,000		
	2003	\$120,000		

Through December 31, 2004, the Company did not maintain any employee benefit plans. 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.

On February 17, 2006, the Company held a special meeting to vote on the 2005 Employee Stock Option Compensation Plan. The record date for the determination of shareholders entitled to vote was January 27, 2006. The plan was approved by shareholder vote.

#### 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, 2006 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, 2005; 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 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	24.50%
Nancy Chu	14,209,548	29.00%
Paul F. Risberg	19,000	.04%
Chung Chin Keung	10,000	.02%

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

Zhi Yang Wu	10,000	.02%
-----		
All officers and directors as a group (3)	26,248,548	53.58%
-----		
Urmston Capital (4)	4,054,693	8.28%
-----		

80

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

(2) The percentage ownership is based upon 48,987,511 shares outstanding on March 30, 2006.

(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 \$0.69 per share on December 31, 2005, the holder would have 4,054,693 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.

81

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,

	2005	2004
--	------	------

Edgar Filing: SOYO GROUP INC - Form 10-K/A

Accounts payable to SOYO Taiwan	\$0	\$1,314,910
Long-term payable to SOYO Taiwan	\$0	\$0

Years Ended December 31,

	2004	2003	2002
Purchases from SOYO Taiwan	\$0	\$14,004,259	\$20,188,354
Payments to SOYO Taiwan	\$873,050	\$19,154,603	\$18,842,244

During the years ended December 31, 2005, 2004 and 2003, the Company received price protection from SOYO Taiwan of \$0, \$0 and \$651,215 respectively, which reduced inventory and accounts payable accordingly.

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 2005 and 2004.

	2005	2004
Audit Fees (1)	\$ 107,000	\$ 143,510
Tax Fees	13,000	15,640
All Other Fees		
Total Fees	\$ 120,000	\$ 159,150

82

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

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

## Edgar Filing: SOYO GROUP INC - Form 10-K/A

### ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

#### (a) Exhibits.

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.
4.1	Agreement and Plan of Reorganization, Incorporated herein by reference to the Form 8-K, File No. 333-42036, filed on October 30, 2002.
10.1	Commitment Supply Agreement dated October 15, 2002, , Incorporated herein by reference to the Form 10-K, File No. 333-42036, filed on April 15, 2003
10.2	Accounts Payable Deferral Agreement dated October 24,2002, Incorporated herein by reference to the Form 10-K, File No. 333-42036, filed on April 15, 2003
10.3	Exclusive Distribution Agreement dated October 24, 2002, Incorporated herein by reference to the Form 10-K, File No. 333-42036, filed on April 15, 2003
10.4	SOYO Group Agreement with China Unicom dated February 1, 2004
10.5	Office Lease at 140 S. Vintage Ave., Ontario, CA dated August 21, 2003
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
23.2	Consent of Independent Registered Public Accounting Firm, Grobstein, Horwath & 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
99.1	Sarbanes-Oxley Act Section 906 Certification

Edgar Filing: SOYO GROUP INC - Form 10-K/A

\*Filed herein

83

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: February 26, 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: February 26, 2007 By /s/ Ming Tung Chok  
-----  
Name: Ming Tung Chok  
Title: President, Chief Executive Officer and Director

Dated: February 26, 2007 By /s/ Nancy Chu  
-----  
Name: Nancy Chu  
Title: Chief Financial Officer, Secretary and

Dated: February 26, 2007 By /s/ Paul F. Risberg  
-----  
Name: Paul F. Risberg  
Title: Director

Dated: February 26, 2007 By /s/ Chung Chin Keung  
-----  
Name: Chung Chin Keung  
Title: Director

Dated: February 26, 2007 By /s/ Zhi Yang Wu  
-----  
Name: Zhi Yang Wu  
Title: Director

84