

GRAND TOYS INTERNATIONAL LTD

Form 6-K

November 30, 2006

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**Form 6-K**

**REPORT OF FOREIGN PRIVATE ISSUER**

**Pursuant to Rule 13a-16 OR 15d-16**

**Of the Securities Exchange Act of 1934**

For the month of November, 2006

Commission File Number: 333-114220

**Grand Toys International Limited**

(Translation of registrant's name into English)

Room UG202, Floor UG2, Chinachem Golden Plaza, 77 Mody Road, Tsimshatsui East, Kowloon, Hong  
Kong

(Address of principal executive office)

Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form  
40-F.

Form 20-F [ X ]

Form 40-F [ ]

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(1): \_\_\_\_\_

Note: Regulation S-T Rule 101 (b)(1) only permits the submission in paper of a Form 6-K if submitted solely to provide an attached annual report to security holders.

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(7): \_\_\_\_\_

Note: Regulation S-T Rule 101(b)(7) only permits the submission in paper of a Form 6-K if submitted to furnish a report or other document that the registrant foreign private issuer must furnish and make public under the laws of the jurisdiction in which the registrant is incorporated, domiciled or legally organized (the registrant's home country), or under the rules of the home country exchange on which the registrant's securities are traded, as long as the report or other document is not a press release, is not required to be and has not been distributed to the registrant's security holders, and, if discussing a material event, has already been the subject of a Form 6-K submission or other Commission filing on EDGAR.

Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.  
Yes [ ] No [ X ]

If Yes is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b):

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**Explanatory Note:**

This Form 6-K consists of:

Exhibit 1

Notice of Annual General Meeting;

Exhibit 2

Proxy Statement;

Annex A

Director Report and Audited Consolidated Financial Statements of Grand Toys International Limited for the years ended December 31, 2005, 2004 and 2003; and

Exhibit 3

Director's Report incorporated by reference in Exhibit 2 on Annex A

SIGNATURES

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

Grand Toys International Limited

(Registrant)

Date: November 29, 2006

By: /s/ Elliot L. Bier, Chairman

(Signature)

**Exhibit 1**

**GRAND TOYS INTERNATIONAL LIMITED**

**( the Company )**

**NOTICE OF ANNUAL GENERAL MEETING**

**NOTICE IS HEREBY GIVEN** that the 2006 Annual General Meeting of the Members of the Company will be held at Room UG202, Floor UG2, Chinachem Golden Plaza, 77 Mody Road, Tsimshatsui East, Kowloon, Hong Kong on Friday, 22<sup>nd</sup> December, 2006 at 10:00 a.m. for the following purposes:

(1)

To receive and consider the consolidated audited statement of accounts of the Company for the year ended 31<sup>st</sup> December, 2005, the restated consolidated audited statement of accounts of the Company for the year ended 31<sup>st</sup> December, 2004 and the reports of the directors of the Company and the auditors thereon;

(2)

To elect or re-elect as directors of the Company in place of all directors retiring from office in accordance with Article 94 of the Articles of Association of the Company ( the Articles );

Cheng HSIEH

Douglas VAN

and a maximum of eight additional persons subject to them being duly proposed by a member for election in accordance with Article 97 of the Articles;

(3)

To approve the payment of fees to directors of the Company for the year ended 31st December, 2005 and the grant of share options to such persons;

(4)

To appoint auditors to serve until the conclusion of the next annual general meeting of the Company and to authorise the directors of the Company to fix their remuneration .

AND to consider, and if thought fit, pass with or without amendment the following resolution (5), which will be proposed as an Ordinary Resolution of the Company :

(5) **THAT**, pursuant to Section 57B of the Companies Ordinance (Cap. 32 of the Laws of Hong Kong) ( the Ordinance ), the directors of the Company be and they are hereby authorised to exercise any power of the Company to allot and issue all or any of the authorised but unissued ordinary shares in the capital of the Company to such persons and on such terms and conditions as they think fit, including (without limitation) pursuant to the Grand Toys International, Inc. Amended and Restated Stock Option Plan, responsibility for which was assumed by the Company from Grand Toys International, Inc. on 16 August 2004 and the Grand Toys International Limited 2004 Stock Option Plan, such authority to continue until the earlier of:

(i)

the conclusion of the next annual general meeting of the Company;

(ii)

the expiration of the period within which the next annual general meeting of the Company is required by the Articles of Association of the Company or the Ordinance to be held; or

(iii)

the revocation or variation of the authority given by this Resolution by an Ordinary Resolution of the members of the Company.

By Order of the Board

Director

Hong Kong, 29th November, 2006

Registered office:

Room UG202, Floor UG2, Chinachem Golden Plaza, 77 Mody Road, Tsimshatsui East, Kowloon, Hong Kong

Notes:

(a)

A member entitled to attend and vote at the meeting may appoint a proxy to attend and, on a poll, vote instead of him or her. A proxy need not be a member of the Company.

(b)

The instrument appointing a proxy or the power of attorney or other authority (if any) under which it is signed, or a notarially certified copy of such power of attorney, must be deposited at the registered office of the Company not less than 48 hours before the time of the meeting and, in default, the proxy shall not be treated as valid. Completion and return of a form of proxy shall not preclude a member from attending in person and voting at the meeting or any adjournment thereof should he or she so wish.

**Exhibit 2**

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**PROXY STATEMENT FOR  
ANNUAL GENERAL MEETING  
TO BE HELD ON DECEMBER 22, 2006**

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**GENERAL INFORMATION**

This proxy statement is furnished in connection with the solicitation of voting instructions by the Board of Directors (the Board) of Grand Toys International Limited (the Company) to be used at the Annual General Meeting of the Company to be held at the offices of the Company, Room UG202, Floor UG2, Chinachem Golden Plaza, 77 Mody Road, Tsimshatsui East, Kowloon, Hong Kong on Friday, 22nd December, 2006 at 10:00 a.m., local time, and at any adjournment thereof.

**PROPOSALS**

At the meeting, we are presenting to the members for approval the following proposals:

(1)

To receive and consider the consolidated audited statement of accounts of the Company for the year ended 31 December 2005, the restated consolidated audited statement of accounts of the Company for the year ended 31 December 2004 and the reports of the directors of the Company and the auditors thereon;



(2)

To elect or re-elect the following directors retiring from office in accordance with article 94 of the articles of association of the Company ( the Articles ):

Jeff Hsieh Cheng

Douglas Van

and a maximum of eight additional persons subject to them being duly proposed by a member for election in accordance with Article 97 of the Articles;

(3)

To approve the payment of fees to directors of the Company for the year ended 31 December 2005 and the grant of share options to such persons;

(4)

To appoint auditors to serve until the conclusion of the next annual general meeting of the Company and to authorise the directors of the Company to fix their remuneration;

(5)

To consider and if thought fit, pass with or without amendment the following resolution:

**That**, pursuant to Section 57B of the Companies Ordinance (Cap. 32 of the Laws of Hong Kong) ( the Ordinance ), the directors of the Company be and they are hereby authorised to exercise any power of the Company to allot and issue all or any of the authorised but unissued ordinary shares in the capital of the Company to such persons and on such terms and conditions as they think fit, including (without limitation) pursuant to the Grand Toys International, Inc. Amended and Restated Stock Option Plan, responsibility for which was assumed by the Company from Grand Toys International, Inc. on 16 August 2004 and the Grand Toys International Limited 2004 Stock Option Plan, such authority to continue until the earlier of:

(i)

the conclusion of the next annual general meeting of the Company;

(ii)

the expiration of the period within which the next annual general meeting of the Company is required by the Articles or the Ordinance to be held; or

(iii)

the revocation or variation of the authority given by this Resolution by an Ordinary Resolution of the members of the Company.

### QUORUM AND VOTING

Only members of the Company ( Members ) that are registered holders of ordinary shares ( Ordinary Shares ), Series A Convertible Preference Shares ( Series A Shares ) and Series B Convertible Preference Shares ( Series B Shares ) will be entitled to vote at the Meeting or any adjournment thereof. On November 21, 2006, the Company had outstanding 17,494,140 Ordinary Shares, 2,000,000 Series A Shares, 10,840,598 Series B Shares and two deferred non-voting shares. The holders of the Series A Shares and the Series B Shares are entitled to vote together with the holders of the Ordinary Shares as a single class on an as converted basis. Accordingly, the holders of the Series A Shares and the Series B Shares are entitled to cast 2,804,600 votes and 29,147,006 votes, respectively, at the meeting on a poll. The Chairman of the Meeting will demand a poll in respect of each resolution set out in the notice of the Meeting. On each such poll, a Member shall have one vote for each Ordinary Share, 1.4023 votes for each Series A Share and 2.6887 votes for each Series B Share registered in its, his or her name.

Pursuant to the Company's Articles, two Members present in person or by proxy and holding at least fifty-one percent of the paid up capital of the Company shall be a quorum. All of the proposals to be presented at the meeting require an ordinary resolution, which shall be passed if a majority of votes cast at the Meeting in respect of the resolution are cast in favour thereof.

As a holder of the Company's ADSs, you do not have the right to attend or vote at the meeting. However, you will have the right to give voting instructions on all proposals. Under the terms of the Depositary Agreement among the Company and The Bank of New York, which acts as depositary (which is referred to as the depositary), and the holders from time to time of the Company's ADSs, the depositary, as a member holding Ordinary Shares, shall endeavor (insofar as is practicable and in accordance with the Company's Articles) to vote or cause to be voted the number of Ordinary Shares represented by the Company's ADSs in accordance with the instructions of each holder of the Company's ADSs. As a holder of the Company's ADSs, if your instructions are not received by the depositary, the depositary shall appoint a person designated by us to vote the number of Ordinary Shares represented by the Company's ADSs in such manner as such person may, in his or her discretion, think fit. ***You should be aware that any person so designated by the Company intends to vote in favor of all Proposals. Accordingly, if you desire to vote against any of the Proposals, you must so instruct the depositary.***

### WHERE YOU CAN FIND MORE INFORMATION ON GRAND

The Company files annual and current reports with the SEC. You may read and copy all or any portion of our SEC reports at the SEC's public reference room at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference room. You may also obtain copies of this

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information by mail from the Public Reference Section of the SEC, 100 F Street, N.E., Room 1580, Washington, D.C. 20549, at prescribed rates, or from commercial document retrieval services. The SEC maintains a website that contains reports, proxy statements and other information, including those filed by us, at [www.sec.gov](http://www.sec.gov). You may also access our SEC filings and obtain other information about us through this website. We also maintain a website at [www.grand.com](http://www.grand.com) where our SEC filings and additional information can be found. The information contained in our website is not incorporated by reference into this proxy statement.

**PRESENTATION OF FINANCIAL STATEMENTS AND REPORTS**

**(PROPOSAL 1)**

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The Board has approved and is presenting to Members for receipt and discussion at the Meeting the Company's Consolidated Balance Sheet as of December 31, 2005 and the Consolidated Statements of Income for the year then ended and the Company's restated Consolidated Balance Sheet as of December 31, 2004 and the restated Consolidated Statements of Income for the year then ended (the Financial Statements). The Financial Statements, which are included in the Audited Consolidated Financial Statements of Grand Toys International Limited for the years ended December 31, 2005, 2004 and 2003, together with the Report of the Directors and the Report of Deloitte Touche Tohmatsu thereon are presented on Annex A attached to this proxy statement.

## ELECTION OF DIRECTORS

### (PROPOSAL 2)

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Pursuant to the Articles, all directors retire from office at the Annual General Meeting. Once elected, directors will serve until their retirement, or they otherwise vacate office, in accordance with the Articles.

The Board recommends that the Members approve the re-election of Jeff Hsieh Cheng and Douglas Van to serve as directors.

Each of such persons person recommended for election as a director has indicated that he is willing to serve as a director of the Company until the next Annual General Meeting. , and the Board of the Company has no reason to believe that any such person may become unable or unwilling to serve.

Mr. Van meets the director independence criteria set forth in Rule 10A-3(b) (1) promulgated under the US Securities Exchange Act of 1934 and Nasdaq Marketplace Rule 4200(a)(15).

Centralink Investments Limited ( Centralink ) and Cornerstone Beststep International Limited ( CBIL ), companies which are beneficially wholly-owned by Mr. Hsieh and the beneficial owners of a majority of the Company s outstanding share capital, has advised the Board that it contemplates nominating, or procuring the nomination of, at least two additional persons in addition to Mr. Hsieh and Mr. Van to serve as directors in accordance with Article 97 98 of the Articles. Each of Centralink s and CBIL s nominees will meet the director independence criteria set forth in Rule 10A-3(b)(1) promulgated under the US Securities Exchange Act of 1934 and Nasdaq Marketplace Rule 4200(a)(15).

The following sets forth the principal occupation, ages, and other information concerning Mr. Hsieh and Mr. Van. each nominee for election as a director of the Company. The information present with respect to each director has been furnished by that person.

**Jeff Hsieh Cheng, age 56**, has served as Chief Executive Officer of the Company since December 2005. Mr. Hsieh is the beneficial owner of a majority of the Company s ADSs. Mr. Hsieh has over twenty-five years of experience in the toy and toy-related business. Mr. Hsieh is the owner of various China-based manufacturing operations, including Zhejiang Playwell Toy Co. Ltd., and is also the owner of various retail operations in China and various toy and outdoor activity product distribution companies throughout the world. Mr. Hsieh holds a bachelor s degree from Soochow University.

**Douglas Van, age 49**, has, since 1988, operated a venture company and acted in a capacity of advisor, fund raiser, project financing, asset management and investor for projects and ventures ranging from real estate in the United States and China to manufacturing projects in China across different industries. Until 1988, Mr. Van worked for Exxon Chemicals in Hong Kong and the United States in various disciplines ranging from sales and marketing, plant operations and research and development. Mr. Van attended Wah Yan College in Hong Kong before attending

McGill University in Montreal, Canada, where he received a bachelor of science in chemical engineering. Mr. Van also has a Masters of business administration degree from University of Michigan, Ann Arbor.

There are no family relationships between any of the directors or executive officers of the Company.

### **Meetings, Compensation and Committees of the Board of Directors**

The Board held 7 meetings during the fiscal year ended 31st December, 2005 and acted by unanimous written consent on 5 occasions.

The Board has determined, based on written inquiries, that its incumbent directors, Messrs. Allen Perl, Douglas Van and Jack W. Flader, Jr. have no relationship with the Company whatsoever other than in their respective capacities as directors and *de minimis* holdings of Grand ADSs and, accordingly, have no material relationship with the Company that would interfere with the exercise of independent judgment and are otherwise independent under Rule 10A-3 of the Securities Exchange Act and Nasdaq Marketplace Rule 4200(a)(15).

#### Audit Committee

The Board has a standing Audit Committee that is currently chaired by Mr. Perl and also includes Messrs. Van and Flader. The Board determined that Mr. Perl qualifies as an audit committee financial expert as defined in Item 401(h) of Regulation S-K of the Exchange Act. The current Audit Committee Charter adopted by the Board is filed as an exhibit to the Company's annual report on Form 20-F for the year ended December 31, 2005. The Audit Committee met three times in the fiscal year ended 31st December, 2005.

The Audit Committee's primary purpose is to assist the Board in fulfilling its oversight responsibilities with respect to (i) the annual financial statements of the Company; (ii) the system of internal accounting and financial controls; (iii) the compliance by the Company with legal and regulatory requirements; and (iv) the internal and external audit process. The Audit Committee oversees the performance of independent accountants and internal auditors, monitors the financial reporting process and makes reports and recommendations to the Board. In connection with the exercise of its duties, the Audit Committee has the authority to engage independent accountants for special audits, review and other procedures and to retain special counsel and other experts or consultants. The Audit Committee also conducts an annual review of its charter and responsibilities.

#### Compensation Committee

The Company does not currently maintain a compensation committee.

#### Corporate Governance and Nominating Committee

The Company does not currently maintain a corporate governance and nominating committee. The Board terminated the charter of the Corporate Governance and Nominating Committee at a meeting held on 23rd March, 2005, after determining that, as a Controlled Company within the meaning of Nasdaq Marketplace Rule 4350(c)(5), it was exempt from the requirement of maintaining the committee. Instead, the Company will rely on applicable Hong Kong law regarding the nomination of directors.

#### Member Nominees

Any Member duly qualified to attend and vote at the Meeting may give notice in writing to the Company of his intention to propose a person for election as a director of the Company. Such notice must be signed by such Member

and given not less than 3 nor more than 21 days before such meeting, together with a notice in writing signed by any such person of his willingness to be elected. Such notice should also provide the name, shareholdings in the Company and contact information of the Member making the nomination, the candidate's name, address and other contact information, any direct or indirect shareholdings in the Company of the candidate, any information required to be disclosed about directors under applicable securities laws and/or Nasdaq Marketplace Rules, information regarding related party transactions with the Company and/or the Member submitting the nomination, any actual or potential conflicts of interest, the candidate's biographical data, current public and private company affiliations, employment history and qualifications and status as independent under applicable securities laws and/or the Nasdaq Marketplace Rules.

### **Shareholder Communications Policy**

Any Member who desires to communicate directly with the Board may do so by mail addressed to any individual director, a group of directors, the Board or any Committee by either name or title at c/o Grand Toys International Limited, Room UG202, Floor UG2, Chinachem Golden Plaza, 77 Mody Road, Tsimshatsui East, Kowloon, Hong Kong.

***THE BOARD OF DIRECTORS RECOMMENDS A VOTE FOR THE PROPOSAL TO RE-ELECT MESSRS  
HSIEH AND VAN AS DIRECTORS***

**APPROVAL OF PAYMENT OF DIRECTORS FEES**

**(PROPOSAL 3)**

At a meeting of the directors held on 13th August, 2004, the Board authorised the payment to each director of an annual director's fee of US\$25,000, payable quarterly in advance on the first day of each of January, April, July and October.

In addition, each director of the Company automatically receives quarterly grants of options to purchase 1,250 Grand ADSs at an exercise price equal to the average trading price of Grand ADSs on the date of grant; and each director who is not an employee of the Company receives additional quarterly grants of options to purchase 6,250 Grand ADSs at an exercise price equal to the average trading price of Grand ADSs on the date of grant.

Such payments and grants are typically made by companies such as the Company and the Board believes that such payments and grants were reasonable. A vote in favor of Proposal 3 will ratify the payments made to the directors during the year ended 31<sup>st</sup> December, 2005 and the grant of options to the directors.

***THE BOARD OF DIRECTORS RECOMMENDS A VOTE FOR THE PROPOSAL TO APPROVE THE FEES PAID AND SHARE OPTIONS GRANTED TO THE DIRECTORS IN 2005***



## APPOINTMENT OF AUDITORS

### (PROPOSAL 4)

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The Audit Committee and the Company's management are currently reviewing the Company's relationship with Deloitte Touche Tohmatsu, its independent public accountants. Deloitte Touche Tohmatsu has acted as independent public accountant for the Company since 16th August, 2004. This review may result in a determination by the Company to appoint a new firm to audit and report on the consolidated financial statements of the Company for the fiscal year ending 31st December, 2006. There is no certainty that a determination will be made before the meeting. However, if a determination is made the Board will submit the firm to the Members for approval at the meeting.

#### **Principal Accountant Fees and Services**

*Audit Fees.* The aggregate fees billed by Deloitte Touche Tohmatsu for the audit of the Company's annual financial statements and services provided in connection with statutory or regulatory filings or engagements were \$676,400 and \$523,300 in the fiscal years ended December 31, 2005 and 2004, respectively.

*Audit-Related Fees.* There were no fees billed by Deloitte Touche Tohmatsu for assurance and related services that were reasonably related to the performance of the audit or review of the Company's financial statements for the fiscal years ended December 31, 2005 and 2004, respectively.

*Tax Fees.* The aggregate fees billed by Deloitte Touche Tohmatsu for professional services rendered for tax compliance, tax advice and tax planning were \$nil and \$26,000 for the fiscal years ended December, 31, 2005 and 2004, respectively. The nature of the services performed for these fees was tax planning and advice.

*All Other Fees.* The aggregate fees billed by Deloitte Touche Tohmatsu for other fees were \$48,616 and \$26,518 for the fiscal years ended December 31, 2005 and 2004, respectively. The nature of the services performed for those fees was related to acquisitions and Sarbanes Oxley consulting. There were no other fees billed by Deloitte Touche Tohmatsu for the fiscal year ended December 31, 2005.

#### **Audit Committee Pre-Approval Policy**

The Audit Committee has established policies and procedures regarding pre-approval of all services provided by independent auditors. It is the policy of the Company that all services provided by the independent auditors shall be pre-approved by the Audit Committee and that the Company only engage the independent auditors to perform permissible non-audit services proscribed by law or regulation. Pre-approval must be detailed as to the particular services to be provided. The Audit Committee may give pre-approval of audit and permitted non-audit services at any time up to one year before the commencement of such services. The Chairman of the Audit Committee shall have, and the Audit Committee may delegate to any other member of the Audit Committee, the authority to grant pre-approval of permitted non-audit services between Audit Committee meetings, in which case, such decisions shall be presented to the full Audit Committee at its next scheduled meeting.



## ISSUANCE OF ORDINARY SHARES

### (PROPOSAL 5)

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Pursuant to the Company's Articles, the share capital of the Company is divided into 100,000,000 shares and the Company has power to issue any part of its capital with or without preference, priority or special privileges. As of November 21, 2006, of the 100,000,000 shares presently authorised, 17,494,140 Ordinary Shares, 2,000,000 Series A Shares, 10,840,598 Series B Shares and two non-voting deferred shares were issued and outstanding.

Under Hong Kong law, the Board is not permitted to issue shares without the approval of the Members. This is unlike the procedure in the United States where the board of directors of a corporation has the authority to issue shares without shareholder approval. However, it is customary for the members of a Hong Kong company to grant to the board of directors at each annual general meeting the authority to issue shares so that a company will be free to conduct business in the ordinary course.

The Board believes that the passing of an ordinary resolution to renew a general mandate authorizing the Board to exercise during the Relevant Period all the power of the Company to allot and issue all or any of the authorised but unissued Ordinary Shares to such persons and on such terms and conditions as they think fit is in the best interests of the Company. Relevant Period shall mean the period from the passing of the relevant resolution until the earlier of:

(i)

the conclusion of the next annual general meeting of the Company;

(ii)

the expiration of the period within which the next annual general meeting of the Company is required by the Articles or the Companies Ordinance (Cap. 32 of the Laws of Hong Kong) to be held; and

(iii)

the date on which the authority set out in the relevant resolution is revoked or varied by an ordinary resolution of the Members.

The authorization will allow the Company to carry out the Company's obligations under the Grand Toys International, Inc. Amended and Restated Stock Option Plan, the Grand Toys International Limited 2004 Stock Option Plan, the outstanding options and warrants which have been granted outside of the two option plans and the Company's obligations to pay dividends on its Series A Shares and Series B Shares. It will also allow the Company to issue Ordinary Shares for other legitimate business functions, including for the purpose of raising capital or for completing acquisitions.

In deciding whether to approve Proposal 5, Members should consider that authorizing the Board to issue Ordinary Shares during the Relevant Period may be disadvantageous to the Members. The issuance of Ordinary Shares will dilute the relative interests of the Members. The Board may also authorize the issuance of Ordinary Shares at an offering price which may be below the then current market price of the Grand ADSs. In addition, although the Board's mandate is to make acquisitions which are accretive to the Company, there can be no assurances that an acquisition will perform as management may expect. By giving the Board discretion to issue Ordinary Shares during the Relevant Period, the Members are, therefore, also relinquishing their right to approve the specific transactions in respect of which Ordinary Shares are issued, except as may otherwise be required by the Nasdaq Marketplace Rules.

***THE BOARD OF DIRECTORS RECOMMENDS A VOTE FOR THE PROPOSAL TO RENEW A GENERAL MANDATE AUTHORIZING THE BOARD TO ISSUE ORDINARY SHARES OF THE COMPANY DURING THE RELEVANT PERIOD.***

**ANNEX A**

**DIRECTORS REPORT AND AUDITED CONSOLIDATED FINANCIAL STATEMENTS OF GRAND TOYS INTERNATIONAL LIMITED FOR THE YEARS ENDED DECEMBER 31, 2005, 2004 AND 2003**

## Director s Report

### REPORT OF THE DIRECTORS

Grand Toys International Limited (the Company), previously known as Genius Glory Limited, was incorporated in Hong Kong as a private company limited by shares on 15<sup>th</sup> October, 2003. On 16<sup>th</sup> August, 2004, by means of a merger, the Company became the holding company of Grand Toys International Inc., a Nevada corporation (Grand US), and its subsidiaries and, immediately thereafter, acquired the entire issued share capital of Playwell International Limited, a Hong Kong private company limited by shares (Playwell). On March, 2005, Grand US acquired International Playthings, Inc. (IPI), a U.S. based distributor of toys to the specialty retail market. On December, 2005, the Company acquired the entire issued share capitals of Hua Yang Holdings Company Limited (Hua Yang) and Kord Holdings, Inc. (Kord) from a related party.

### PRINCIPAL ACTIVITIES

The principal activity of the Company is to act as the holding company of Playwell, Grand US, Hua Yang and Kord.

Playwell s four subsidiaries are:

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Hong Kong Toy Centre Limited, a Hong Kong private company limited by shares:

- o designs, develops and sells Playwell branded products, mostly plastic and wood toys for infants and young children
- o designs, develops and sells certain toy products for the Marvel license to a related party
- o acts as agent for sourcing and logistics operations for related parties

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Gatelink Mould Engineering Limited, a Hong Kong private company limited by shares:

- o manufactures moulds for related companies

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Asian World Enterprises Co., Limited, a Belize company:

- o oversees all licensing for Playwell

.

Great Wall Alliance Limited, a British Virgin Islands company :

- o holds the Playwell trademarks

Grand US has the following five principal subsidiaries:

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Grand Toys Ltd., a Canadian corporation:

- o distributes in Canada both proprietary and third party products, mostly toy-related and leisure products

.

International Playthings, Inc., a Delaware Corporation

- o distributes toy products to specialty retail stores in North America

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Grand Toys (HK) Limited, a Hong Kong private company limited by shares:

- o oversees international sales for the proprietary lines

o

handles design, development, and distribution of Crayola Dough product, mostly to the mass market in the United States

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Grand Toys (US) Limited, a Delaware USA corporation:

o

is currently non-operational

.

Ark Creations, Inc., a Delaware, USA corporation:

o

is also currently non-operational.

Hua Yang has five principal subsidiaries:

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Hua Yang Printing Holdings Company Limited

o

oversees all printing and packaging operations

.

Dongguan Hua Yang Printing Products Co. Ltd.

o

former operations of Eastern Raiser Limited, of which the assets were acquired in February 2005 packaging manufacturer

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Shenzhen Hua Yang Printing Company Limited

o

contract manufacturer of a variety of paper and board products, including books, specialty packaging and other paper products.



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Hua Yang (UK) Limited

o

handles UK and European sales for the Hua Yang group

.

Hua Yang USA, Inc.

o

handles US and North American sales for the Hua Yang group

Kord has four principal subsidiaries and five variable interest entities:

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Kord Printing Company Limited

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Kord Gifts Manufactory Limited

.

Kord Plastic Products Manufactory Company Limited

.

Kord Party Favour Manufactory Company Limited

.

Variable Interest Entities these are companies that are not owned by Kord or Grand, but of which Kord indirectly or directly controls the decision making process and has a significant economic interest in the outcome of the companies:

o

Kord (Qing Xin) Packaging Products Limited

o

Dongguan Kord Packing Products Limited

o

Qing Xin Kord Gifts Manufactory Company Limited

o

Sun Tat Toys Factory

o

Sun Tat Plastic Factory

Together, these subsidiaries and variable interest entities design and produce a broad range of party and paper goods either under the proprietary Kord brand or on an OEM basis in the case of well known brands owned by third parties. The key product groups are generic party products, decorative party products, disposable tableware products and latex masks.

### RESULTS AND APPROPRIATIONS

The results of the Company for the year ended 31<sup>st</sup> December, 2005 are set out in the Consolidated Statements of Operations.

The directors do not recommend the payment of a dividend.

### CHARITABLE DONATIONS

During the year, the Company and its subsidiaries made charitable donations in the amount of US\$5,330.

### FIXED ASSETS

The Fixed Assets are divided into five categories:

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Moulds and loose tools

.

Furniture, fixtures and equipment

.

Plant and machinery

.

Leasehold improvements

.

Motor vehicles

During the year, the Company and its subsidiaries added US\$5,484,000 worth of net fixed assets as a result of the Company's acquisitions of assets from Eastern Raiser Printing Company Limited in February 2005 and the entire issued share capital of IPI in March 2005. Other changes to fixed assets during the year resulted primarily from the purchase of plant and machinery, furniture and fixtures and moulds in the ordinary course of business.

The Company's policy regarding carrying values of Fixed Assets and their useful lives is set out in Note 2j to the Company's Consolidated Financial Statements. Specific carrying values as of 31 December, 2005 are set out in Note 6 to the Company's Consolidated Financial Statements.

## SHARE CAPITAL

During 2005, the following new shares were issued by the Company:

	Ordinary Shares	Convertible Preference Shares
Shares issued in connection with the acquisition of IPI for a deemed consideration of US\$1,600,000	582,730	-
Shares issued in lieu of cash interest of US\$145,089 on Exchangeable Note (see Issue of Debentures below)	52,175	-
Shares issued in lieu of cash dividend of US\$168,259 payable on Series A Convertible Preference Shares for the period ended 30 <sup>th</sup> June, 2005	73,030	-

Shares issued for cash at the relevant exercise prices in connection with the Company's share option schemes	15,250	-
Series A Convertible Preference Shares issued in exchange for Exchangeable Note for a deemed consideration of US\$7,675,000 (see below)	-	2,000,000
Series B Convertible Preference Shares issued in connection with the acquisition of Hua Yang and Kord for a deemed consideration of US\$41,600,793	-	10,840,598

All of the Company's issued Ordinary Shares, including the Ordinary Shares issued during the year ended 31 December, 2005 are registered in the name of The Bank of New York as depositary and issuer of American Depositary Shares ( ADSs ) which are evidenced by American Depositary Receipts. Each such ADS represents beneficial ownership of one issued share of HK\$1.00 in the capital of the Company.

All Series A Convertible Preference Shares are registered in the name of Centralink Investments Limited ( Centralink ), a company wholly beneficially owned by Jeff Hsieh Cheng ( Mr. Hsieh ), a director of the Company. All Series B Convertible Preference Shares are registered in the name of Cornerstone Beststep International Limited ( CBIL ), also a company wholly beneficially owned by Mr. Hsieh..

Further details of the movements in the Company's share capital during the year are set out in Note 10 to the Company's Consolidated Financial Statements.

#### ISSUE OF DEBENTURES

On 1st March, 2005, the Company sold to Centralink an Exchangeable Note in the principal amount of US\$7,675,000 to fund the acquisition of IPI for proceeds of US\$7,400,000. The Exchangeable Note was sold at a US\$275,000 discount in order to compensate the Mr. Hsieh, who is also the controlling shareholder of the Company, for providing the sellers of IPI with the option to require Centralink to purchase that portion of the purchase price for IPI which was paid in ADSs after the first anniversary of the closing of the IPI acquisition. The Exchangeable Note bore interest at 15% per annum and was exchanged for 2,000,000 Series A Convertible Preference Shares in the capital of the Company when the issuance such Series A Convertible Preference Shares was approved by the Company's shareholders at the Company's 2005 Annual General Meeting held on 15 April, 2005.

The Company did not issue any other debentures during 2005.

DIRECTORS

The directors of the Company during the year were:

<b>Name</b>	<b>Title</b>	<b>Appointment Date</b>
Henry Hai Lin Hu	Chairman	August 2004 ***
Elliot L. Bier	Chairman	January 2004 ****
Michael Kron		August 2004 **
Thomas J. Mitchell		August 2004 *
Robert Laverdure		August 2004 **
David J. Fremed		15 <sup>th</sup> April 2005
Allen S. Perl		15 <sup>th</sup> April 2005
Doug Van		15 <sup>th</sup> April 2005
Jeff Hsieh Cheng		20 <sup>th</sup> December 2005
Jack Flader, Jr.		20 <sup>th</sup> December 2005

Notes:

\*Mr. Mitchell resigned on 14<sup>th</sup> March, 2005

\*\* Mr. Kron and Mr. Laverdure s terms expired on 15<sup>th</sup> April, 2005 and neither of such persons sought re-election

\*\*\* Mr. Hu resigned on 31<sup>st</sup> December, 2005

\*\*\*\* Mr. Bier was elected Chairman of the Board of Directors in place of Mr. Hu on 20<sup>th</sup> December, 2005

In accordance with the Company s Articles of Association, all directors retire from office at each Annual General Meeting.

Options to acquire an equivalent number of ADSs (representing Ordinary Shares) were either granted by the Company to directors, or responsibility for the same was assumed by the Company from Grand US, during the year. Unless otherwise indicated below, the following options remained outstanding as at 31<sup>st</sup> December, 2005:

Name	Date of Grant	Date of Expiry	Number	Exercise Price (in US\$)
<b>Henry Hai Lin Hu:</b>	9/30/2004	9/30/2014	625	\$ 2.35
	12/30/2004	12/30/2004	1,250	\$ 2.65
	03/31/2005	03/31/2015	1,250	\$ 2.50
	06/30/2005	06/30/2015	1,250	\$ 2.00
	09/30/2005	09/30/2015	1,250	\$ 1.90
<b>Sub-total</b>			<b>5,625 (1)</b>	

(1) All options were rescinded with effect from 31<sup>st</sup> December, 2005 in conjunction with Mr. Hu's resignation as a director and Chief Executive Officer of the Company

<b>Elliot Bier :</b>	10/1/1999	10/1/2009	125	\$ 41.00
	1/1/2000	1/1/2010	125	\$ 27.00
	4/3/2000	4/3/2010	125	\$ 11.00
	7/3/2000	7/3/2010	125	\$ 5.62
	10/2/2000	10/2/2010	125	\$ 7.25
	10/5/2001	10/5/2011	36,000	\$ 0.95
	1/2/2002	1/2/2012	125	\$ 2.99
	4/1/2002	4/1/2012	125	\$ 2.66
	7/1/2002	7/1/2012	125	\$ 1.40
	10/1/2002	10/1/2012	125	\$ 1.19
	1/2/2003	1/2/2013	125	\$ 1.00
	4/1/2003	4/1/2013	125	\$ 1.98
	7/1/2003	7/1/2013	125	\$ 2.72
	10/1/2003	10/1/2013	125	\$ 2.60
	1/2/2004	1/2/2014	125	\$ 3.07
	4/1/2004	4/1/2014	125	\$ 3.02
	7/1/2004	7/1/2014	125	\$ 2.75
	8/13/2004	8/13/2014	300,000	\$ 2.95
	9/1/2004	9/1/2014	100,000	\$ 2.20
	9/30/2004	9/30/2014	3,750	\$ 2.35
	12/30/2004	12/30/2014	7,500	\$ 2.65
	3/31/2005	3/31/2015	7,500	\$ 2.50
	6/30/2005	6/30/2015	7,500	\$ 2.00
9/30/2005	9/30/2015	7,500	\$ 1.90	
12/20/2005	12/20/2015	100,000	\$ 1.65	
12/31/2005	12/31/2015	7,500	\$ 1.50	
<b>Sub-total</b>			<b>579,250</b>	

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<b>Michael Kron:</b>	7/1/2002	7/1/2012	125	\$ 1.40
	10/1/2002	10/1/2012	125	\$ 1.19
	1/2/2003	1/2/2013	125	\$ 1.00
	4/1/2003	4/1/2013	125	\$ 1.98
	7/1/2003	7/1/2013	125	\$ 2.72
	10/1/2003	10/1/2013	125	\$ 2.60
	1/2/2004	1/2/2014	125	\$ 3.07
	4/1/2004	4/1/2014	125	\$ 3.02
	7/1/2004	7/1/2014	125	\$ 2.75
	9/30/2004	9/30/2014	3,750	\$ 2.35
	12/30/2004	12/30/2014	7,500	\$ 2.65
	3/31/2005	3/31/2015	7,500	\$ 2.50
		<b>Sub-total</b>	<b>19,875</b>	
<b>Thomas J. Mitchell:</b>	9/30/2004	9/30/2014	3,750	\$ 2.35
	12/30/2004	12/30/2014	7,500	\$ 2.65
		<b>Sub-total</b>	<b>11,250</b>	
<b>Robert Laverdure:</b>	9/30/2004	9/30/2014	3,750	\$ 2.35
	12/30/2004	12/30/2014	7,500	\$ 2.65
	3/31/2005	3/31/2015	7,500	\$ 2.50
		<b>Sub-total</b>	<b>18,750</b>	
<b>David J. Fremed:</b>	8/16/2004	8/16/2014	300,000	\$ 2.50
	6/30/2005	6/30/2015	1,043	\$ 2.00
	9/30/2005	9/30/2015	1,250	\$ 1.90
	12/20/2005	12/20/2015	100,000	\$ 1.65
	12/31/2005	12/31/2015	1,250	\$ 1.50
		<b>Sub-total</b>	<b>403,543</b>	
<b>Allen S. Perl:</b>	6/30/2005	6/30/2015	6,182	\$ 2.00
	9/30/2005	9/30/2015	7,500	\$ 1.90
	12/31/2005	12/31/2015	7,500	\$ 1.50
		<b>Sub-total</b>	<b>21,182</b>	
<b>Doug Van:</b>	6/30/2005	6/30/2015	6,182	\$ 2.00
	9/30/2005	9/30/2015	7,500	\$ 1.90
	12/31/2005	12/31/2015	7,500	\$ 1.50
		<b>Sub-total</b>	<b>21,182</b>	

**DIRECTORS INTERESTS IN CONTRACTS**

Mr. Hsieh, who became a director on 20<sup>th</sup> December, 2005, has significant ownership interests in various companies with which the Company or its subsidiaries transacted business during 2005.

During 2005, Playwell and its subsidiaries were engaged in transactions in the ordinary course of business with the following companies owned or controlled by Mr. Hsieh:

.

Sales of products to Toy Biz Worldwide Limited with an aggregate value of US\$197,331.

.

Sales of products to Playwell Industry Ltd. with an aggregate value of US\$146,574.

.

Purchase of products from Playwell Industry Ltd. with an aggregate value of US\$4,008,122.

.

Purchase of products from Zhejiang Playwell Toy Co., Ltd. with an aggregate value of US\$4,851,388.

.

Aggregate income from sales of moulds to Toy Biz Worldwide Limited of US\$3,136,890.

.

Aggregate net expenses from mould manufacturing to Playwell Industry Ltd. of US\$ 34,211.

.

Aggregate royalty income from Guangzhou Playwell Trading Co. Ltd. of US\$234,283. Other income from Toy Biz Worldwide Limited of US\$74,228.

.

Other income from New Adventures Corporation of US\$ 25,273.

.



Other income from Playwell Industry Ltd. of US\$ 20,500.

.

Other expenses payable to Playwell Industry Ltd. of US \$6,051.

.

Purchase of Fixed asset from Playwell Industry Ltd. of US\$ 7,377.

During 2005, Grand US and its subsidiaries were engaged in transactions in the ordinary course of business with the following companies owned or controlled by Mr. Hsieh:

.

Purchase of products from Toy Biz Worldwide Limited with an aggregate value of US\$1,612,472.

.

Purchases of products from Zizzle (Hong Kong) Limited with an aggregate value of US\$ 480,000.

.

Aggregate commissions paid to Toy Biz Worldwide Limited of US\$19,429.

.

Aggregate commissions paid to Zizzle (Hong Kong) Limited of US\$797.

During 2005, Hua Yang and its subsidiaries were engaged in transactions in the ordinary course of business with the following companies owned or controlled by Mr. Hsieh:

.

Aggregate sales to Toy Biz Worldwide Limited of US\$5,744,435.

.

Aggregate sales to Playwell Industry Ltd. of US\$405,465.

.

Aggregate sales to Zizzle (Hong Kong) Limited of US\$464,732.

.

Aggregate rental income from Playwell Industry Ltd. of US\$ 55,561

During 2005, Kord and its subsidiaries were engaged in transactions in the ordinary course of business with the following companies owned or controlled by Mr. Hsieh:

Aggregate sales to Playwell Toy S.A. of US\$444,674

Aggregate sales to Playwell International Company L.L.C. of US\$16,592

Aggregate sales to China Retail Management of US\$14,424.

As noted under "Issue of Debentures" above, Centralink, a company wholly beneficially owned by Mr. Hsieh, assisted in the financing of the Company's acquisition of IPI in March 2005 by means of the Exchangeable Note.

In addition, CBIL, a company wholly beneficially owned by Mr. Hsieh, sold the entire issued share capitals of Hua Yang and Kord to the Company in December 2005 for a net purchase price of US\$41,601,000. Such net purchase price was satisfied by issuing to CBIL 10,840,598 Series B Convertible Preference Shares. Since the Company, Hua Yang and Kord were under common-control by Mr. Hsieh prior to the Company's acquisition of Hua Yang and Kord, a deemed dividend of US\$12,751,758 resulted for the year ended 31<sup>st</sup> December, 2005. Such deemed dividend was determined as being the market value of the Series B Convertible Preference Shares on the date of the public announcement of the transaction (November 30, 2005), net of US\$2,399,000, representing intercompany indebtedness between the Company and its subsidiaries on the one hand and Hua Yang and Kord and their respective subsidiaries on the other hand, and CBIL's original aggregate acquisition cost for Hua Yang and Kord of US\$31,247,000.

In conjunction with Cornerstone's acquisition of Kord Holdings, Inc. from Li San Tung in June 2004, Cornerstone issued a promissory note to Mr. Li in the principal amount of HK\$23.3 million (US\$3.0 million) which is convertible into 746,795 Grand ADSs that are owned by a Cornerstone subsidiary. Subsequent to the acquisition of Kord, on March 14, 2005, audited accounts revealed a purchase price adjustment which resulted in Cornerstone issuing an additional promissory note to Mr. Li in the principal amount of HK\$2,243,941 (US\$288,000) which is convertible into 71,921 Grand ADSs owned by a Cornerstone subsidiary. These promissory notes have a maturity date of July 30, 2006. As of November 15, 2006, Mr. Li has not exercised the notes and converted them into Grand ADSs.

Other than the transactions noted above, no contract of significance to which the Company or any of its subsidiaries was a party and in which a director of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

Date: November 29, 2006

On behalf of the Board

/s/ Elliot L. Bier

Elliot L. Bier

CHAIRMAN

**GRAND TOYS INTERNATIONAL LIMITED AUDITED CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE YEARS ENDED DECEMBER 31, 2005, 2004 AND 2003**

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Shareholders of Grand Toys International Limited

We have audited the accompanying consolidated balance sheets of Grand Toys International Limited and subsidiaries (the Company) as of December 31, 2005 and 2004 and the related consolidated statements of operations, shareholders equity and comprehensive income and cash flows for each of the three years in the 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 the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits include consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Grand Toys International Limited and subsidiaries as of December 31, 2005 and 2004 and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2005, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 24 to the financial statements, the Company is in the process of discontinuing the operations of a subsidiary manufacturing moulds in the People's Republic of China and certain toy and toy related products distribution in the United States of America and Canada. In addition, the Company undergoes loans refinancing with financial institutions and its major shareholder.

/s/DELOITTE TOUCHE TOHMATSU

Hong Kong

November 15, 2006

**Financial Statements**

Consolidated Balance Sheets

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Consolidated Statements of Cash Flows

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Notes to Consolidated Financial Statements

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**GRAND TOYS INTERNATIONAL LIMITED****Part I. Financial Information***Item 1. Consolidated Financial Statements*

## Consolidated Balance Sheets

	<b>December 31, 2005</b>	<b>December 31, 2004</b> <b>(as restated)</b>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 4,688,246	\$ 8,523,656
Pledged bank deposit	27,048	597,464
Investment securities (note 2(l))	6,387	31,859
Accounts receivable (net of allowance for doubtful accounts of \$4,643,598; 2004 - \$4,394,673)	27,457,316	17,844,344
Inventory (note 2(h))	20,335,067	11,008,050
Due from related companies (note 20)	3,516,518	5,625,200
Note receivable (note 4)	266,312	138,440
Deferred tax asset (note 12 (c))	-	-
Income tax recoverable	88,715	
Prepaid royalties (note 2(i))	2,024,993	2,251,695
Other prepaid expenses and current assets (note 5)	3,728,655	2,405,439
Total current assets	62,139,257	48,426,147
Fixed assets, net (note 6)	21,096,642	18,050,231
Goodwill (note 2(m))	26,017,533	29,197,018

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Prepaid land lease (note 2(i))	89,787	60,814
Intangibles, net (note 7)	9,040,576	10,013,483
Note receivable (note 4)	244,464	400,396
Total assets	\$ 118,628,259	\$ 106,148,089

**GRAND TOYS INTERNATIONAL LIMITED**

## Consolidated Balance Sheets

	<b>December 31, 2005</b>	<b>December 31, 2004</b> <b>(as restated)</b>
<b>Liabilities and Shareholders' Equity</b>		
Current liabilities:		
Bank indebtedness (note 8)	\$ 22,342,696	\$ 12,629,046
Trade accounts payable	16,938,467	10,339,909
Accrued payroll and related costs	2,105,788	1,065,469
Other accounts payable and accrued liabilities	10,133,977	9,188,553
Obligations under capital leases (note 9)	2,404,573	2,413,167
Due to related parties (note 20)	2,828,705	3,264,041
Income taxes payable	633,941	515,180
Total current liabilities	57,388,147	39,415,365
Long term debt (note 8)	5,110,663	788,992
Note payable (note 22)	703,964	-
Deferred tax (note 12 (c))	3,311,252	3,079,309
Obligations under capital leases (note 9)	3,452,152	4,434,073
Commitments and contingencies (notes 17 and 18)		
Shareholders' equity:		
Capital stock (note 10):	2,120,360	2,026,346
Voting ordinary shares, \$0.13 par value		
100,000,000 ordinary shares authorized		
16,310,467 ordinary shares issued and outstanding		
(2004 15,587,282)		
Preference stock (note 10)		



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2,000,000 Series A preference shares , \$0.13 par value (2004 Nil)	260,000	-
10,840,598 Series B preference shares , \$0.13 par value (2004 Nil)	1,409,278	-
Deferred non-voting stock (note 10)		
2 deferred non-voting share, \$0.13 par value	-	-
Additional paid-in capital	69,826,118	50,331,294
(Accumulated loss) retained earnings	(25,549,243)	5,777,153
Accumulated other comprehensive income- cumulative currency translation adjustment	595,568	295,557
Total shareholders equity	48,662,081	58,430,350
Total liabilities and shareholders' equity	\$ 118,628,259	\$ 106,148,089

*See accompanying notes to audited consolidated financial statements.*

**GRAND TOYS INTERNATIONAL LIMITED**

## Consolidated Statement of operations

	<b>Years ended December 31</b>		
	<b>2005</b>	<b>2004</b>	<b>2003</b>
		<b>(as restated)</b>	
Net sales			
- External	\$ 120,792,623	\$ 59,722,236	14,806,468
- Affiliated companies	10,536,906	15,810,635	24,568,970
Total net sales	131,329,529	75,532,871	39,375,438
Cost of goods sold	99,506,552	60,458,768	33,538,951
Gross profit	31,822,977	15,074,103	5,836,487
Other operating income	(1,918,250)	(482,312)	(896,023)
Operating costs and expenses:			
General and administrative	23,492,605	9,490,171	2,141,280
Selling and distribution expenses	9,886,407	3,317,275	638,498
Depreciation and amortization	2,697,431	1,564,595	398,478
Impairment on intangible assets and goodwill	12,487,867	-	-
Total operating costs and expenses	48,564,310	14,372,041	3,178,256
Operating (loss) income	(14,823,083)	1,184,374	3,554,254
Non-operating expense (income):			
Interest expense	1,937,524	464,048	23,835
Interest income	(53,310)	(45,065)	(5,051)
Impairment loss on investment securities	25,477	31,785	-
	1,909,691	450,768	18,784

Total non-operating expense  
(income)

(Loss) earnings before income taxes	(16,732,774)	733,606	3,535,470
Income taxes:			
Current	549,521	727,385	536,045
Deferred	(313,591)	65,106	(22,705)
Total income taxes	235,930	792,491	513,340
Net (loss) earnings from continuing operations	(16,968,704)	(58,885)	3,022,130
Discontinued operations:			
Earnings from operations of distributed subsidiaries	-	-	1,239,236
(Loss) earnings from operations	\$ (16,968,704) \$	(58,885) \$	4,261,366
Dividends (note 10(h))	(14,357,692)	-	-
Net (loss) earnings available to ADS shareholders	\$ (31,326,396) \$	(58,885) \$	4,261,366

*See accompanying notes to audited consolidated financial statements.*

**GRAND TOYS INTERNATIONAL LIMITED**

## Consolidated Statement of Operations, continued

	<b>Years ended December 31</b>		
	<b>2005</b>	<b>2004</b>	<b>2003</b>
		<b>(as restated)</b>	
(Loss) earnings per American			

Depository

Shares ( ADS ):

Weighted average ADS outstanding:

Basic	16,137,667	12,092,592	10,000,000
Diluted	18,191,015	12,807,160	10,000,000
Net (loss) earnings - Continuing operations:			
Basic	\$ (1.94)	\$ (0.00)	\$ 0.30
Diluted	(1.94)	(0.00)	N/A
Net earnings - Discontinued operations:			
Basic	-	-	0.13
Diluted	-	-	N/A
Net (loss) earnings available to ADS shareholders			
Basic	(1.94)	(0.00)	0.43
Diluted	(1.94)	(0.00)	N/A

N/A refers to not applicable

*See accompanying notes to audited consolidated financial statements.*

**GRAND TOYS INTERNATIONAL LIMITED**

## Consolidated Statements of Shareholders' Equity and Comprehensive Income

	Preference Stock	Capital Stock	Additional Paid in Capital	Retained Earnings	Accumulated other comprehensive income	Total
January 01, 2003	\$ -	\$ 13	\$ -	\$ 24,382,458	\$ 286	\$ 24,382,757
Net earnings for the period				4,261,366		4,261,366
Foreign currency adjustment					21,514	21,514
Total comprehensive income				4,261,366	21,514	4,282,880
Distribution of subsidiaries to holding companies				(22,807,786)		(22,807,786)
December 31, 2003	-	13	-	5,836,038	21,800	5,857,851
Share purchase on merger		2,025,418	26,628,377			28,653,795
Hua Yang and Kord acquisition			23,699,206			23,699,206
Net earnings for the period				(58,885)		(58,885)

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Foreign currency adjustment					273,757	273,757
Total Comprehensive income				(58,885)	273,757	214,872
ADs issued on option exercises		915	5,633			6,548
Compensation expense			(1,922)			(1,922)
December 31, 2004, as restated	-	2,026,346	50,331,294	5,777,153	295,557	58,430,350
Net loss for the period				(16,968,704)		(16,968,704)
Foreign currency adjustment					300,011	300,011
Total comprehensive income				(16,968,704)	300,011	(16,668,693)
Issue of (note 10):						
Series A Preference Shares	260,000	92,031	10,540,757			10,892,788
Series B Preference Shares	1,409,278		8,943,273			10,352,551
Dividends on (note 10):						
Series A Preference Shares				(571,198)		(571,198)
Deemed dividend				(991,426)		(991,426)
Series B Preference Shares				(43,310)		(43,310)
Deemed dividend				(12,751,758)		(12,751,758)
ADs issued on option exercises		1,983	15,130			17,113

Compensation							
expense			(4,336)				(4,336)
December 31,							
2005	\$ 1,669,278	\$ 2,120,360	\$ 69,826,118	\$ (25,549,243)	\$ 595,568	\$ 48,662,081	

*See accompanying notes to audited consolidated financial statements.*

**GRAND TOYS INTERNATIONAL LIMITED**

## Consolidated Statements of Cash Flows

	<b>2005</b>	<b>For the years ended December 31</b>	
		<b>2004</b>	<b>2003</b>
		<b>(as restated)</b>	
Cash flows from operating activities:			
Net (loss) earnings from continuing operations	\$ (16,968,704)	\$ (58,885)	\$ 3,022,130
Adjustments for:			
Depreciation and amortization General and administrative	2,697,431	1,564,595	398,478
Depreciation and amortization Cost of goods sold	3,172,113	1,445,179	39,206
Impairment loss and write off of fixed assets	765,712	-	-
Impairment on intangible and goodwill	12,487,867	-	-
Income taxes	549,521	727,385	536,045
Deferred income taxes	(313,591)	65,106	(22,705)
Product development write-off	-	7,790	-
Assets write-off	203,834	2,217	-
(Gain) loss on disposal of fixed assets	(131,224)	129,586	20,452
Compensation expense	(4,336)	(1,922)	-
Impairment loss on investment securities	25,477	31,785	-
Net change in operating working capital items (note 14)			
	(6,985,030)	(9,959,611)	(2,977,037)
Net cash (used for) provided by operating activities from continuing operations			
	(4,500,930)	(6,046,775)	1,016,569
Net cash provided by operating activities from discontinued operations			
	-	-	2,747,246
Net cash (used for) provided by operating activities			
	(4,500,930)	(6,046,775)	3,763,815



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Cash flows from investing activities:			
Proceeds from disposal of equipment	180,149	579	21,160
Decrease (increase) in pledged time deposit	570,484	(597,464)	-
Acquisition of business, net of cash acquired	(7,546,084)	1,268,786	-
Settlement of note receivable	827,017	-	-
Increase in other assets	-	(356,524)	-
Settlement of note receivable	-	63,301	-
Increase in intangibles	(3,244)	(20,428)	-
Additions to equipment and leasehold improvements	(2,583,542)	(2,971,297)	(449,291)
Net cash used for investing activities from continuing operations	(8,555,220)	(2,613,047)	(428,131)
Net cash used for investing activities from discontinued operations	-	-	(33,887)
Net cash used for investing activities	(8,555,220)	(2,613,047)	(462,018)
Cash flows from financing activities:			
Increase (decrease) in bank indebtedness	12,814,943	7,191,161	(2,615,643)
Repayment of bank indebtedness	(2,100,000)	-	-
Decrease in amount due to ultimate holding company		1,050,535	
Issuance of share capital on merger	-	8,700,000	-
Repayment of obligation under a capital lease	(2,829,052)	(1,400,221)	(54,218)
Proceeds from ADSs exercise	17,113	1,914	-
Increase (decrease) in trust receipt loans	1,199,401	(235,985)	-
Other	118,335	(45,636)	33,570
Net cash provided by (used for) financing activities from continuing operations	9,220,740	15,261,768	(2,636,291)
Net cash provided by (used for) financing activities from discontinued operations	-	-	(8,594,624)
Net cash provided by (used for) financing activities	9,220,740	15,261,768	(11,230,915)
Net (decrease) increase in cash and cash equivalents	(3,835,410)	6,601,946	(7,929,118)
	8,523,656	1,921,710	9,850,828

Cash and cash equivalents, beginning  
of period

Cash and cash equivalents, end of period	\$	4,688,246	\$	8,523,656	\$	1,921,710
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*See accompanying notes to audited consolidated financial statements.*

Supplemental disclosure of cash flow information (note 15) and major non-cash transactions (note 16)

## **GRAND TOYS INTERNATIONAL LIMITED**

### Notes to audited Consolidated Financial Statements

Grand Toys International Limited (the Company), a Nasdaq SmallCap listed company, is organized under the laws of the Hong Kong Special Administrative Region of the People's Republic of China (Hong Kong). The Company's main operating subsidiaries are Hua Yang Holdings Co., Ltd. (Hua Yang), Kord Holdings, Inc. (Kord), and Playwell International Limited (Playwell), which are organized under the laws of Hong Kong, and Grand Toys International, Inc. (Grand US), which is organized under the laws of Nevada, United States of America (US). The Company, through its Hong Kong, US and Canadian operating subsidiaries, develops, manufactures and distributes toy and toy related products, prints and assembles books and specialty packaging and manufactures, distributes paper party goods and other licensed products throughout the world.

The Company was formerly a subsidiary of Grand US. It became the parent of Grand US on August 16, 2004, pursuant to a reorganization merger. Immediately after the reorganization merger, the Company acquired Playwell. For accounting purposes, the acquisition has been accounted for as a reverse acquisition, in which Playwell was the acquirer.

On March 1, 2005, Grand US acquired International Playthings Inc. (IPI), a New Jersey, US toy distributor (see note 22(b)). The operating results for IPI have been included in the consolidated results of the Company since March 1, 2005.

On December 23, 2005, the Company purchased the shares of Hua Yang and Kord, which were owned by Cornerstone Beststep International Limited (Cornerstone Beststep), a subsidiary of Cornerstone Overseas Investments Limited (Cornerstone). Hua Yang and Kord were acquired by Cornerstone on May 24, 2004 and June 18, 2004, respectively, and were subsequently transferred to Cornerstone Beststep. The Company, Hua Yang and Kord were under the common control of the Company's main shareholder, Jeff Hsieh, who owned beneficially 62% of the Company's outstanding shares and was the sole beneficial owner of Hua Yang and Kord. The purchase method of accounting for the business combination was used; however, due to the common control of the entities, the Company has restated its financial statements back to the date of common control as if Hua Yang and Kord were part of the Company on the dates that they were acquired by Cornerstone (see note 22(c)). Under this method of accounting, the excess of the value paid to Cornerstone Beststep over the original cost of Hua Yang and Kord is reflected as a non-recurring deemed dividend in the 2005 financial statements. Further, the Company's acquisition costs are treated as restructuring costs and recorded as an expense in the 2005 financial statements.

Through Hua Yang, on February 1, 2005 the Company acquired Eastern Raiser, a PRC company which engages in the printing and assembling of books and specialty packaging (see note 22(a)).

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Except as otherwise indicated, references to the Company include Grand Toys International Limited and its subsidiaries and the variable interest entities in which the Company is deemed to be the primary beneficiary.

Consolidated principal subsidiaries and variable interest entities at December 31, 2005 are as follows:

Name of subsidiary	Place of incorporation registration and Operations	Proportion ownership Interest held by the Company		Principal activities
		Directly %	Indirectly %	
Playwell International Limited:		100	-	Investment holding
Great Wall Alliance limited	British Virgin Islands	-	100	Playwell registration
Asian World Enterprises Co. Limited	Belize	-	100	Licenses holding
Hong Kong Toy Center Limited	Hong Kong	-	100	Distribution
Gatelink Mould Engineering Limited	Hong Kong	-	100	Manufacturing of moulds
Grand Toys International Inc:	United States	100	-	Distribution
Grand Toys (US) Ltd	United States	-	100	Investment holding
Grand Toys Ltd	Canada	-	100	Distribution
Ark Creations, Inc	United States	-	100	Dormant
Grand Toys (HK) Limited	Hong Kong	-	100	Distribution
International Playthings Inc.	United States	-	100	Distribution
Hua Yang Holdings Co., Limited:	Cayman Islands	100	-	Investment holding
Hua Yang Printing Holdings Company Limited	Hong Kong	-	100	Printing operations
Dong Guan Hua Yang Printing Products Company Ltd	People's Republic of China	-	100	Factory
Shenzhen Hua Yang Printing Products Company Ltd	People's Republic of China	-	100	Factory
Hua Yang (UK) Limited	United Kingdom	-	100	Sales liaison
Hua Yang USA, Inc	United States	-	100	Sales liaison
Kord Holdings, Inc.:	British Virgin Islands	100	-	Investment holding
Kord Printing Company Limited	Hong Kong	-	100	Printing operations
Kord Gifts Manufactory Limited	Hong Kong	-	100	Printing operations
Kord Plastic Manufactory Company Limited	Hong Kong	-	100	Printing operations

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Kord Party Favour Manufactory Limited	Hong Kong	-	100	Printing operations
Variable Interest entities				
Kord (Qing Xin) Packing products Limited	People's Republic of China	-	100	Subcontracting work for printing operations
Dongguan Kord Packing products Limited	People's Republic of China	-	100	Sales and manufacturing
QingXin Kord Gifts Manufactory Company Limited	People's Republic of China	-	97	Subcontracting work
Sun Tat Toys Manufactory	Hong Kong	-	100	Subcontracting work
Sun Tat Toys Factory	People's Republic of China	-	100	Subcontracting work
Sun Tat Plastic Manufactory	Hong Kong	-	100	Subcontracting work
Sun Tat Plastic Factory	People's Republic of China	-	100	Subcontracting work

**1.**

**Restatement of prior year consolidated financial statements:**

The Company acquired the shares of Hua Yang and Kord on December 23, 2005 from a related company, which was under the common control of the Company's majority shareholder, Jeff Hsieh Cheng. As a result of the transaction, the Company's consolidated financial statements for the year 2004 presented have been restated by including the results of the two subsidiaries as if they had been part of the consolidated group since the date that they were acquired by Cornerstone.

Following is a summary of significant balance sheet and income statement captions, earnings per share and also statements of shareholders' equity and comprehensive income before and after the restatement:

**(a)**

**Consolidated Balance Sheet:**

December 31, 2004

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	As restated	As originally reported
Current assets	\$ 48,426,147	\$ 20,456,349
Fixed assets, net	18,050,231	2,251,824
Prepaid land lease	60,814	-
Goodwill	29,197,018	14,736,315
Intangibles, net	10,013,483	6,627,184
Note receivable	400,396	-
<b>Total assets</b>	<b>\$ 106,148,089</b>	<b>\$ 44,071,672</b>
Current liabilities	39,415,365	7,420,313
Deferred tax	3,079,309	1,381,167
Long term Debt	788,992	-
Obligations under capital leases	4,434,073	-
<b>Total liabilities</b>	<b>\$ 47,717,739</b>	<b>\$ 8,801,480</b>
Shareholders equity		
Capital stock	2,026,346	2,026,346
Additional paid-in capital	50,331,294	26,632,088
Retained earnings	5,777,153	6,344,586
Accumulated other comprehensive income-cumulative		
currency translation adjustment	295,557	267,172
Total shareholders equity	58,430,350	35,270,192
<b>Total liabilities and shareholders equity</b>	<b>\$ 106,148,089</b>	<b>\$ 44,071,672</b>

(b)

**Consolidated Statement of Operations and earnings per share**

	For the year ended December 31, 2004	
	As restated	As originally reported
Net sales	\$ 75,532,871	\$ 29,464,959
Cost of goods sold	60,458,768	21,627,695
<b>Gross profit</b>	<b>15,074,103</b>	<b>7,837,264</b>
Other operating income	(482,312)	(304,842)
Total operating costs and expenses	14,372,041	7,099,774
Operating income	1,184,374	1,042,332
Non-operating expenses (income)	450,768	(14,307)
<b>Earnings before income taxes</b>	<b>733,606</b>	<b>1,056,639</b>

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Income taxes	792,491	548,091
Net (loss) earnings from continuing operations	(58,885)	508,548
<b>Earnings per ADS:</b>		
Net (loss) earnings available to ADS shareholders		
- basic	\$ 0.00	\$ 0.04
- diluted	0.00	