BKN International AG
2006 ANNUAL REPORT

New York London Cologne Barcelona


BKN

Financial Calendar

Publication of Annual Report 2006	**28 November 2006**
Annual General Meeting 2006	**22 February 2007**
Publication of Results - 1st half 2007	**17 May 2007**

Contents

Consolidated Management Report & Chairman and Chief Executive Statement

We are pleased to present the financial results of BKN International AG, a global animation production and distribution company ("BKN" or the "Company") that is listed on the Frankfurt and London Stock Exchanges. We license our product in approximately 95 countries and dub in about 30 languages. This Consolidated Report of the Management Board will cover audited financial statements under IAS accounting rules for the period ended 30 September 2006 and compared to the similar period in fiscal 2005.

The Company had a very strong year during which we have launched new products and increased our client base, successfully expanded into the United States and Europe especially in our Home Entertainment segment, increased our profitability and significantly strengthened our balance sheet.

A. Group Structure

- The Group consists of BKN International AG, the parent company in Germany, with active operating trading subsidiaries in the United Kingdom ("BKN New Media Ltd" and "BKN Home Entertainment Ltd"), the United States ("BKN New Media Inc." and "BKN Home Entertainment Inc.") and Spain ("BKN New Media SL").

- The Group creates, produces, distributes and markets animated properties for television and DVD distribution, as well as licenses its characters for licensing and merchandising and the internet.

- The Company reports in Euro and trades in Euro, UK Sterling, Singapore Dollars and US Dollars.

- The Company is listed on the General Standard of the Frankfurt Stock Exchange (March 2000) and on the Alternative Investment Market of the London Stock Exchange (December 2003).

B. Film Catalogue and New Properties

- We have successfully expanded the Company's film catalogue, at 30 September 2006, to 76 titles and 1,909 episodes compared to 65 titles and 1,770 episodes as published in our 2005 Annual Report. BKN now owns the 6th largest film library of global animation which was recently appraised positively reflecting in part the quality and quantity of our assets but also the enhanced state of the market for family entertainment overall.

- The Company expanded the property entitled *Legend of the Dragon* this year by delivering an additional 13 episodes and expanding total sales by €2.5 million to €9.1 million to date have exceeded management's expectations.

- The *Kong* franchise continues to expand with our recent delivery of the Kong - Return to the Jungle film in state of the art 3D animation. In fiscal 2006, we added another €1.8 million in sales from this important franchise.

- One of our most exciting new developments and series is *Dork Hunters from Outer Space* (26 episodes), a new action based comedy. We have high expectations for this property globally and the response from the customers has been strong for autumn 2007 initial release for TV, DVD and Licensing sales.

- Another key product is Zorro - Generation Z (26 or 39 episodes). This iconic property should result in very strong TV, DVD and Licensing sales in 2007 and 2008.

- We now have a slate of 8 feature films (7 have been produced in state of the art 3D animation) for direct-to-DVD release. Legend of the Dragon launched on 23 October 2006, Kong-Return to the Jungle on 13 November 2006 and A Christmas Carol on 20 November 2006. It is our plan to release one title monthly in 2007.

- The film catalogue continues to deliver strong earnings on a steady pace as the Company finds new markets for its products.

- We now have our own DVD label in the UK and Ireland and DVD distributors in major markets worldwide. We expect to achieve high growth in our DVD segment in 2007.

C. Financial Highlights

- Turnover increased 16% to €13.9 million (Prior year: €12 million). In addition, a sum of €0.3 million was phased into fiscal 2007 due to delivery of the films in October 2006 versus the planned September 2006.

- Total expenses increased 4% to €9.2 million in part based on lower amortization due to strong current and forecast library sales as per company policy (Prior year: €8.8 million)

- Earnings or Profit before tax increased 39% to €4.1 million (Prior year: €3.0 million)

- Underlying Net Income (before deferred tax gains) increased 37% to €4.1 million (Prior Year: €3.0 million)

- Net Income increased 5% to €4.5 million (Prior year: €4.3 million)

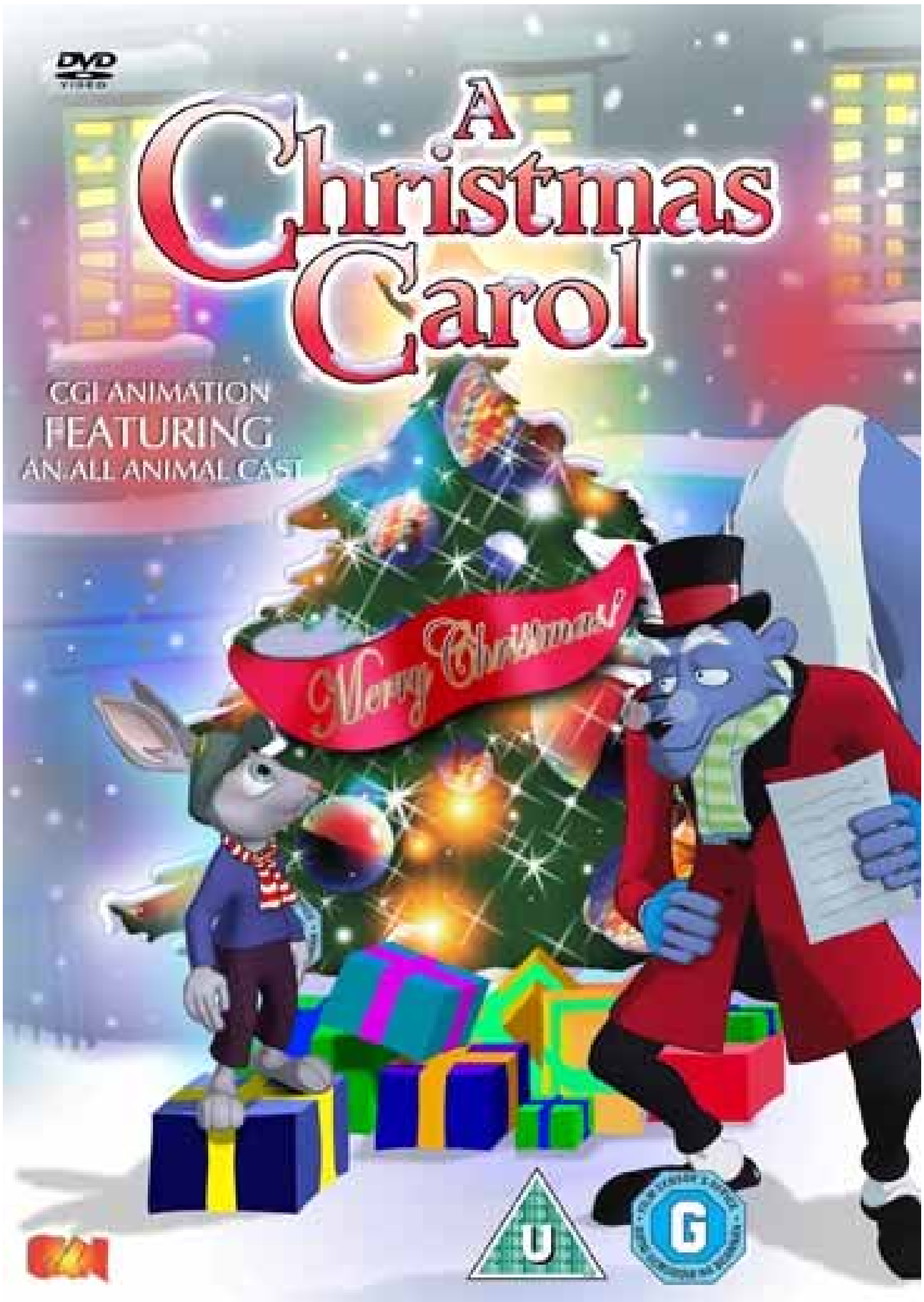
- Underlying EPS (before deferred tax gains) increased 37% to €0.26 (Prior Year: €0.19)

- EPS increased 4% to €0.29 (Prior Year: €0.28)

- Cash on hand totals €1.6 million versus €384,000 last year.

- Programming rights asset value increased to €36.6 million from €23.6 million in 2005.

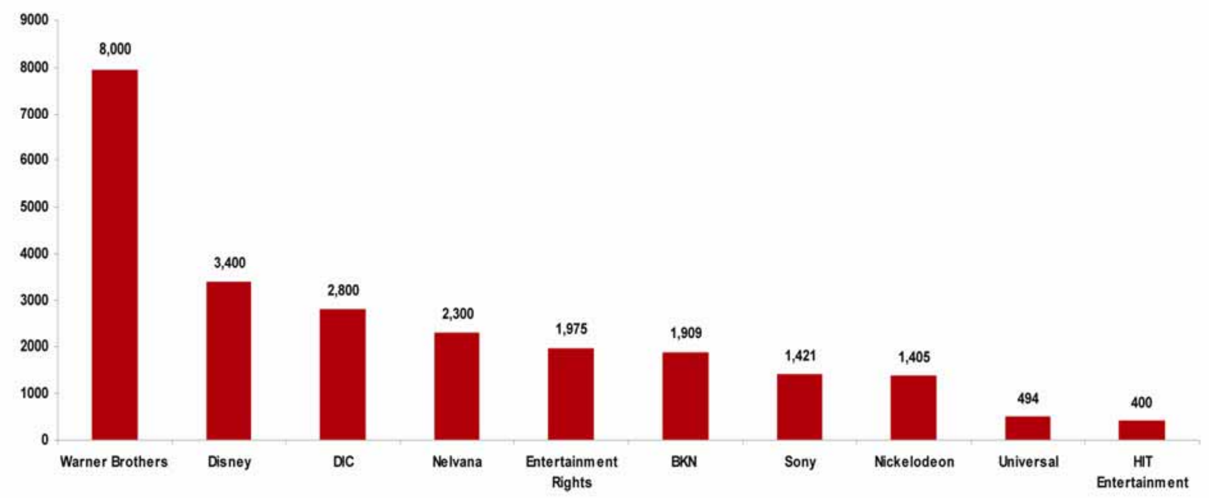
- The Company employs at the year end 36 full-time employees and consultants versus 25 at the end of 2005. The Company estimates that approximately 400 people work on the production of its shows at various locations and for various vendors.



D. Business & Operating Environment

The children's market sector has experienced a number of changes in the last five years. In 2002 and 2003, most content suppliers struggled as broadcasters experienced reduced advertising income and therefore cut their acquisition budgets. A modest rebound was experienced in 2004 and 2005 and it seems like the current environment is more buoyant. While prices for animation have not increased, and in most cases remain flat, there are a number of dedicated 24-hour animation channels in the world (by some estimates, as many as 700) that require children's content, both from catalogues as well as new productions. Good examples include recent and upcoming launches in Germany of both the Nickelodeon and Cartoon Network channels and the new children's digital channel in the UK in February 2006 by ITV. The larger suppliers of global content are experiencing success as the key to children's entertainment is global content, not locally produced animation.

TOP 10 WORLDWIDE CATALOGUES
Library size – Number of half-hour episodes



(Source: Company Estimates/DIC Entertainment Holdings Inc.'s Offering Memorandum)

E. Internet and New Media

In this past fiscal year, the value of the internet for video streaming has truly expanded. BKN has a philosophy of not entering into licenses for such valuable rights until the market matures as this value is likely to increase substantially. Unlike many of our local competitors who own selected rights and therefore do not often control the internet streaming rights, BKN does hold these rights in perpetuity to all of its key titles like Zorro - Generation Z, Dork Hunters from Outer Space, Legend of the Dragon, Kong - The Animated Series, UBOS, Roswell Conspiracies, Extreme Dinosaurs, Pocket Dragon Adventures, SkySurfer Strike Force, Starla and the Jewel Riders, our entire film titles, etc.

Successful US-based kids websites are delivering strong audiences traditionally reserved for TV viewing as follows (the Rating is a percentage of total kids 6-11 and the Impressions reflects the actual total audience):

Television	K6-11 Rating	K6-11 Impressions
Nickelodeon	4.9	1,189,230
Cartoon Network	2.7	655,290
Kids WB!	2.0	485,400
ABC	1.5	364,050
Disney Channel	1.5	364,050
Fox Kids	1.3	315,510
DIC Kids	1.3	315,510
CBS	0.7	169,890
NBC	0.6	142,620
Toon Disney/Jetix	0.4	97,080

Source: NTI (Nielsen Television Index, 2005/2006 (Season)

Internet	K6-11 Rating	K6-11 Impressions
Disney Online	11.9	2,886,000
Nickelodeon Online	10.0	2,424,000
Disney Channel.com	8.9	2,171,000
Cartoon Network.com	6.5	1,589,000
Yahooligans	3.0	718,000
Nick Jr.	1.8	442,000
EA Online	1.6	393,000
PBS Kids	1.5	365,000
Playhouse Disney	1.5	356,000
Kids AOL	1.4	346,000

Source: Nielsen NetRatings Inc.

F. Financial Position

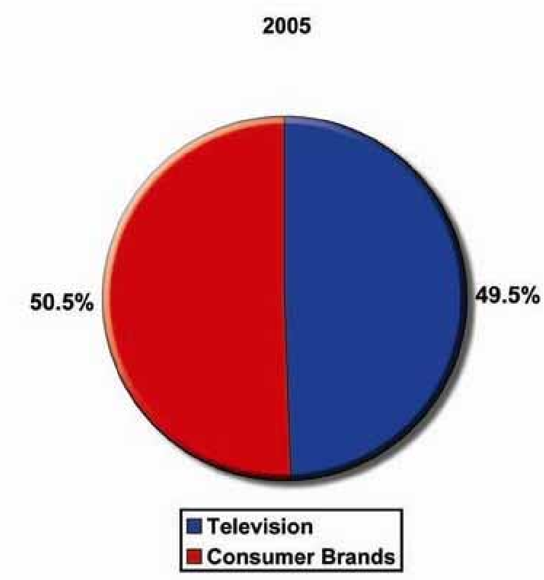
The Company is generating good cash flow from operations and investing further into its long-term assets as the market for its products is strong. The Company is in a strong tax position, with tax losses available for future use in some of its operating territories.

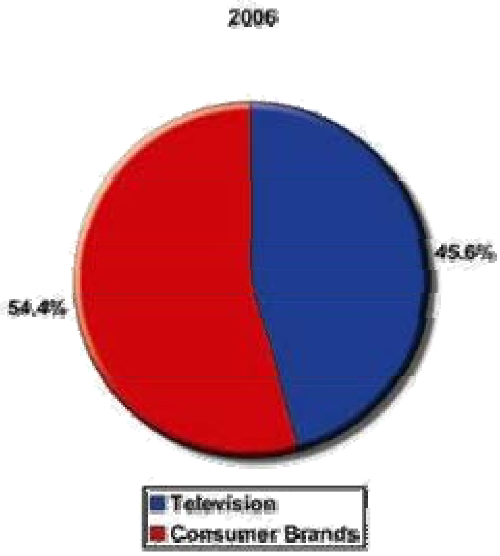
Following the completion of a standard tax audit in Germany which covered the years 1999 to 2004, the tax losses have been finally assessed. This therefore secures the use of such losses as off-settable against future taxable profits and underpins the deferred tax asset the Company carries on its balance sheet.

For further information, see Notes to Accounts section.

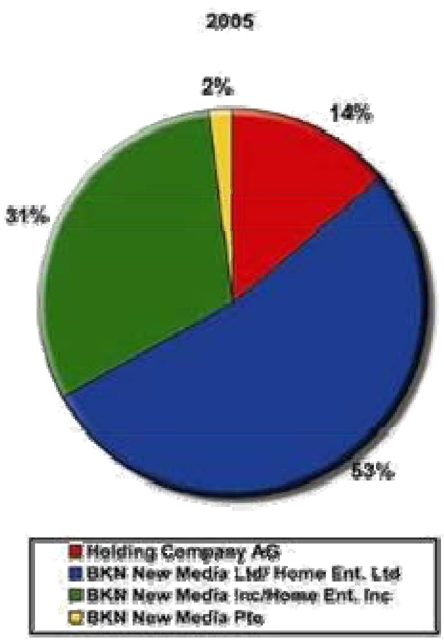
G. Segment Reporting

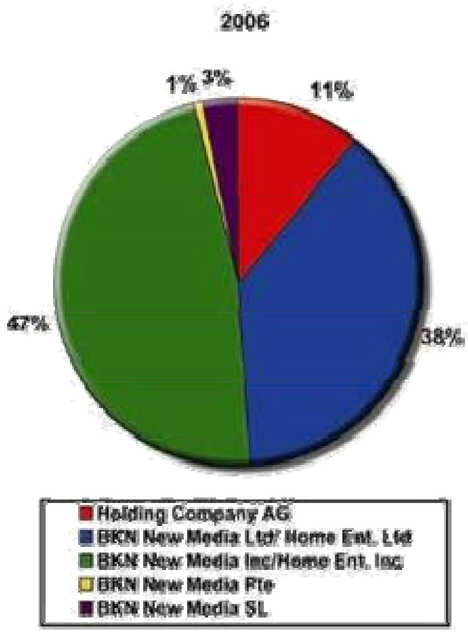
i. Turnover by Segment in %





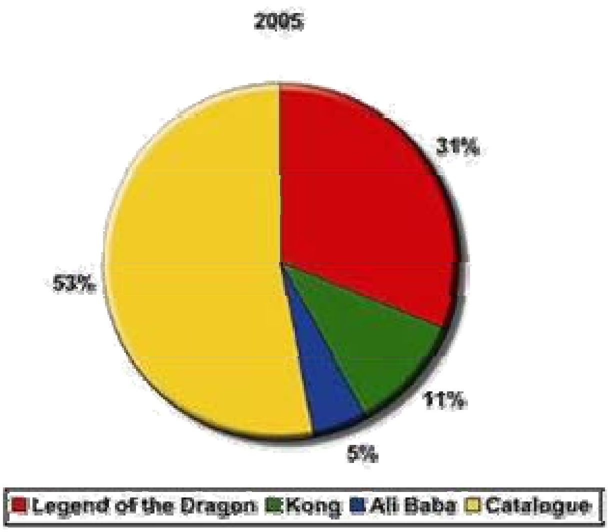
ii. Turnover by Company in %

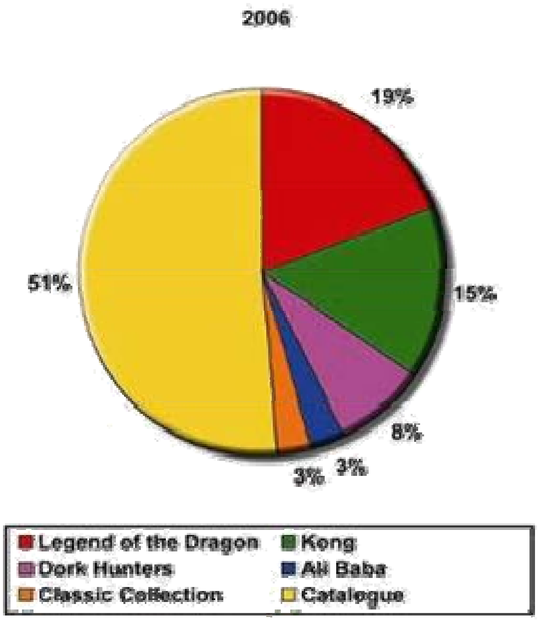




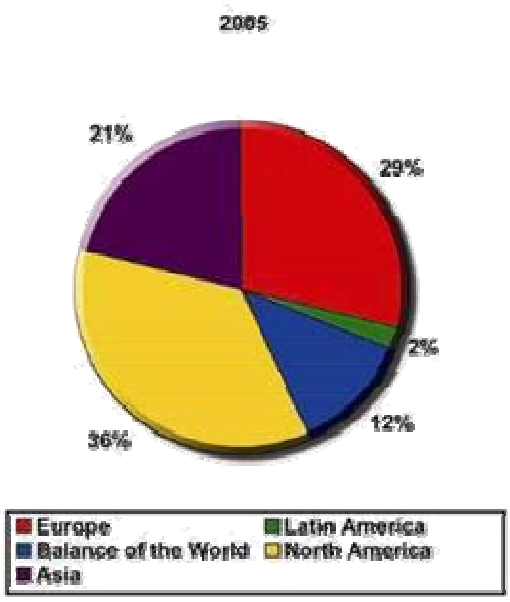
The Company is experiencing its largest growth in BKN New Media Ltd based in London and BKN New Media Inc. based in New York. These two subsidiaries are entering into the most contracts with customers worldwide, but our Barcelona office is poised to issue many new contracts in fiscal 2007.

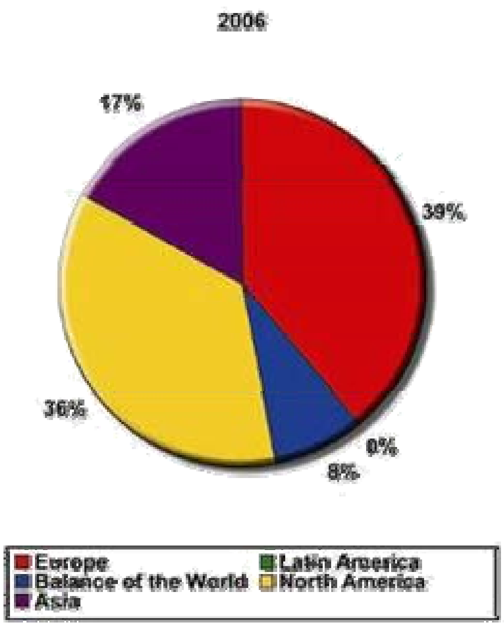
iii. Turnover by Property in %





iv. Sales by Region in %





H. Convertible Notes and Stock Options

In fiscal 2006, we issued several Notes totalling €8.7 million to US investors allowing them to convert into shares of the Company at varying prices as agreed. These Notes are due in 2010 although some monthly payments begin as early as March 2007 as planned in our cash flow forecasts. At the end of fiscal 2006, the potential shares, which can be converted including warrants, equals approximately 3.6 million at an average share price of approximately €4.20.

The Management Board holds a combined 725,000 stock options at €3.90 strike price due to convert in spring 2008 and there are 8,500 options issued several years ago to employees at a €3.86 strike price.

As we expand further in 2007, it is likely that the stock option plan will be made available to a greater amount of executives to ensure key staff retention and to incentivize delivery of stronger Company performance.

The Company did not have any capital increases in fiscal year 2006.

I. The Management and Supervisory Boards, Key Talent

- The management team is well experienced and seasoned in the industry. Allen Bohbot (CEO) and Wayne Mowat (CFO) make up the Management Board and oversee the Company on a daily basis. Ben Heng is no longer with the Company due to the closing of the Singapore office.

- Nicola Andrews is Director - Sales and Marketing for the US, UK/Ireland, Australia/New Zealand as well as French and German speaking territories and Pan-territory deals.

- Laura Tapias is Managing Director for Spanish, Portuguese and Italian-speaking markets.

- Matthew Graham-Clare is Managing Director of all Home Entertainment activities.

- Richard Ungar is Executive Producer on all titles.

- There are three seasoned non-executive Directors that comprise the Supervisory Board including Karl Benetz as Chairman with Robert Paff and Michael Jack Kugler.

J. Corporate Governance

- The Company is in good standing with the Frankfurt and London Stock Exchanges and complies with all rules and regulations.

- The Company has met all of the recommendations of the German Corporate Governance Code of Good Conduct, with regards to a company our size and complexity, with the exception of incentive based compensation for the Supervisory Board members who earn a flat annual compensation.

- The Management and Supervisory Boards met either in person or telephonically on nine separate occasions during the fiscal year and in addition, numerous telephone conversations took place between members of both boards to ensure full and accurate communication. The Management Board supplied the Supervisory Board with sufficient and comprehensive information throughout the year. In addition, there is an audit committee of directors to ensure proper transparency and control of the companies' activities. The Boards cooperated closely for the benefit of the enterprise.

- The Company has no borrowing or lending relationship with any of its Directors.

K. Business Risks

As with any business, there are variable risks such as:

- At this time, the Company does not hedge against currency fluctuation. While we report in Euro and maintain accounts in Euro, Sterling, Singapore Dollars and US Dollars, a majority of our sales are in US Dollars and this is matched by a majority of our costs. The Company engages vendors throughout the world for its productions (Los Angeles, China, India, Manila) and such contracts are typically in US Dollars. The Company believes that it is properly managing this currency fluctuation and has no need at this time to create hedging instruments whose cost would outweigh the benefit. The 2006 exchange position was a net gain of €55,000.

- Historically, we have not been dependent on DVD sales as this has been a small part of our turnover. Recently, we have dramatically expanded this activity and business segment. Although the DVD market is not growing as rapidly, it is still a huge and BKN can claim a more lucrative share.

- Our major suppliers, as noted above, are in foreign locations as typical of the animation industry. We believe that all are credible, well funded and professional. The global nature of the industry allows the Company to source the best producers in cost and quality regardless of territory. We have not experienced any significant delays in production but this is always possible.

- We are expanding at a rapid pace. We believe that our creative and production staffs are well in control of all productions and budgets with local control at all locations.

- The children's market has historically been cyclical. At various points in the past two decades, the market has been over-supplied and at other points, it has starved for intellectual content. While we believe that the market is in a good place at this time, and will be for the near term, this is likely to change but only over the longer term. Although delivery platforms are expanding from solely TV and DVD towards the internet, BKN as an IP owner is well positioned to transition accordingly.

- Prices for children's content have been mostly flat in the last few years and it is not expected that the industry has any real pricing power. This is mitigated by the expansion of new channels dedicated to the sector.

- There are a number of producers, primarily in France and Canada, that have access to government subsidies and the broadcasters in those markets favor local producers. The Company does not receive any subsidies from any source although some of our partners may. It does not appear that other jurisdictions will expand government involvement in the sector and this seems in hand at this time. BKN's lack of dependence on governmental subsidies means that we have full control of the quality of our products which assures delivery of global rather than local content in all forms and venues.

- We trade in multiple jurisdictions throughout the world and the possibility of litigation to protect our assets and rights is increased by the increased turnover. We always protect our properties with filings with the US Copyright and Trademark Office and the European Union Trademark Office, but there is always a chance that vendors and/or licensees cause us to litigate to protect our assets.

L. Annual General Meeting

The next meeting is set for Thursday, 22 February 2007 in Cologne.

M. Outlook

The markets look healthy for children's animation in the near term with hundreds of dedicated animated children's channels operating throughout the world. The Company is strategically well placed to take advantage with our London office handling Continental Europe and Asia via our Melbourne, Australia presence, our New York office handling North America and our Barcelona office handling the important markets of Spain, Portugal, Italy and Latin America.

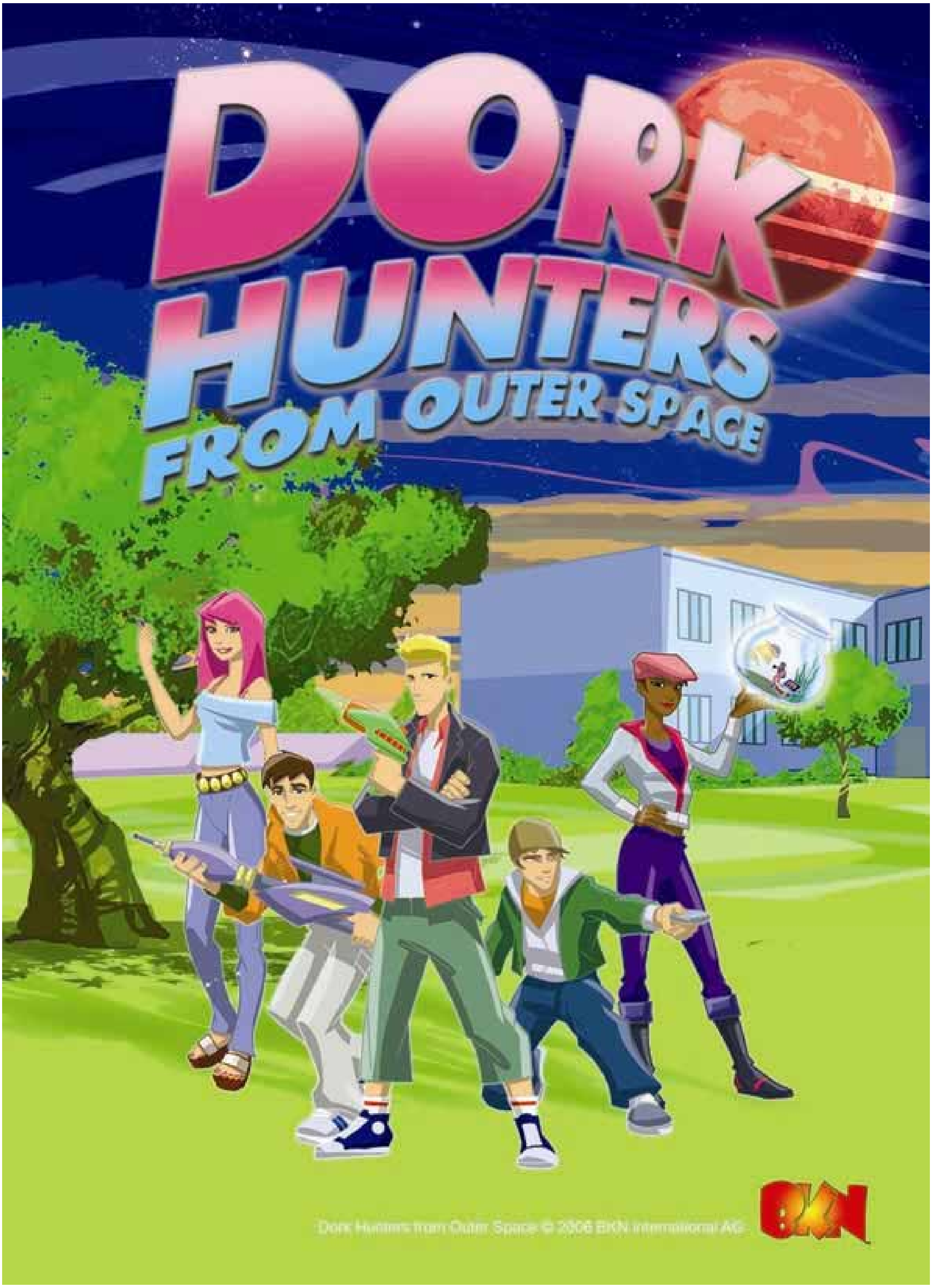
Due to an extensive effort to expand on the DVD and traditional licensing and merchandising, we believe that our income streams will be more diversified in 2007 and beyond. We expect major revenue contributors in 2007 to come from Zorro - Generation Z, Dork Hunters from Outer Space, Legend of the Dragon, the feature film titles and the film catalogue. We are expecting a well balanced revenue structure and contribution from several major projects.

We delivered record net earnings for the Company in fiscal 2006 of €4.5 million (€0.29 EPS) even without the benefit of a major deferred tax credit in 2005, and we feel that fiscal 2007 will reflect further expansion on both turnover and earnings in the range of 20-30% and that the outlook for the Company is strong.

Cologne, November 2006
The Management Board

Allen J. Bohbot
Chairman & CEO

Wayne Mowat
Chief Financial Officer


DORK
HUNTERS
FROM OUTER SPACE
Dork Hunters from Outer Space © 2006 BKN International AG
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Auditors' Opinion for the Fiscal Year Ended 30 September 2006

(Translation of the original German version)

We have audited the consolidated financial statements of BKN International AG, Cologne, including the balance sheet, income statement, statement of changes in equity, cash flow statement and notes to the consolidated financial statement, together with the group management report for the financial year from 1 October 2005 to 30 September 2006. The preparation of the consolidated financial statements and the group management report according to the IFRS as applicable in the EU and the supplementary provisions of Section 315a Par. 1 HGB (German Commercial Code) as well as the supplementary provisions of the articles of association are the responsibility of the company's legal representatives. Our responsibility is to express an opinion on the consolidated financial statements and the management report based on our audit. In addition, we were asked to assess whether, on the whole, the consolidated financial statements conform with the IFRS.

We conducted our audit of the consolidated financial statements in accordance with Section 317 HGB and the generally accepted German standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (IDW). Those standards require that we plan and perform the audit such that misstatements and violations materially affecting the presentation of the net assets, financial position, and results of operations in the consolidated financial statements in accordance with the applicable accounting principles and in the management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the group and evaluations of possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the consolidated financial statements and the management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the annual accounts of the companies included in the consolidated financial statements, the definition of the consolidated entity, accounting and consolidation principles used and significant estimates made by the legal representatives, as well as evaluating the overall presentation of the consolidated financial statements and management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

According to our assessment based on the knowledge attained from the audit, we are satisfied that the consolidated financial statements conform with the IFRS as applicable in the EU and with the supplementary provisions under Section 315a Par. 1 HGB as well as the supplementary provisions of the articles of association and, on the whole, the IFRS, and give a true and fair view of the net assets, financial position and results of operations of the company in accordance with the above provisions. The management report is consistent with the consolidated financial statements, provides a suitable understanding of the group's position and suitably presents the opportunities and risks concomitant with future development.

NEXIA DEUTSCHLAND GMBH
Wirtschaftsprüfungsgesellschaft

Signed by	Signed by
Dr. Weyer Wirtschaftsprüfer	Pütz Wirtschaftsprüfer

Düsseldorf, 10 November 2006

Consolidated Balance Sheets for Fiscal 2006

(in thousands of €)

ASSETS

		T€	30 Sep 2006 T€	Prior Year T€	Notes
A. Fixed and Intangible assets					II., VIII. A., XVII.
1.	Intangible Assets	36,591		23,602	
2.	Fixed Assets	127		69	
			36,718	23,671	
B. Other Long term assets					
1.	Other Assets	223		220	VIII. B. 1.
2.	Deferred Tax Asset	2,209		1,502	II., VI., VIII. B. 2.
3.	Deferred Financing Costs	738		188	VI., VIII. B. 3.
			3,170	1,910	
C. Current Assets					
1.	Accounts receivable, trade	1,496		2,048	II., VIII. C. 1.,
2.	Other current assets	789		1,272	VIII. C. 2.
3.	Cash and cash equivalents	1,648		384	VIII. C. 3.
			3,933	3,704	
			43,821	29,285	

LIABILITIES

		T€	30 Sep 2006 T€	Prior Year T€	Notes
A. Shareholders Equity					VIII. D.
1.	Common Stock	15,718		15,718	
2.	Additional paid in capital	8,286		8,161	
3.	Other comprehensive income	136		197	
4.	Retained earnings	4,495		0	
			28,635	24,076	
B. Long term liabilities					
1.	Bonds	12,604		3,851	VI., VIII. E. 1.
2.	Deferred tax liability	441		172	II., VI., VIII. E. 2.
3.	Deferred long term liabilities	14		22	VIII. E. 3.
			13,059	4,045	
C. Short term liabilities					
1.	Accrued expenses	961		903	II., VI., VIII. F. 1.
2.	Accounts payable, trade	1,166		261	VIII. F. 2.
			2,127	1,164	
			43,821	29,285	

Consolidated Statements of Operations for Fiscal 2006

(in thousands of € - except shared data and number of employees)

	Year to date 30 Sep 2006	Year to date 30 Sep 2005	Notes
Revenues			
Television - Catalogue	5,740	5,481	
Consumer Brands - Catalogue	6,870	5,617	
Production/Other	1,283	869	
Total Sales Revenues	13,893	11,967	VII, IX 1 (I,2)
Expenses			
Depreciation and amortisation	1,430	2,679	II, IX 6
Producer fees and other direct operating costs	985	232	IX 3
Salaries and employee benefits	2,993	2,099	IX 4
Other Expenses	3,742	3,761	IX 7
Total expenses	9,150	8,771	
Other Expenses			
Interest costs	625	225	IX 8
Income before income tax	4,118	2,971	
Provision for income tax	(377)	(1,318)	VI, IX 9
Net income current year	4,495	4,289	
earnings per share	28.6	28.1	XI
diluted eps	26.0	27.9	
basic number of shares	15,717,566	15,250,095	
diluted no of shares	19,875,809	16,183,960	
Number of employees including directors at the end of the year	36	25	

The retained earnings statement is included as a separate paragraph in the notes to the consolidated statements. VIII. D.

Consolidated Statements of Cash flows for Fiscal 2006

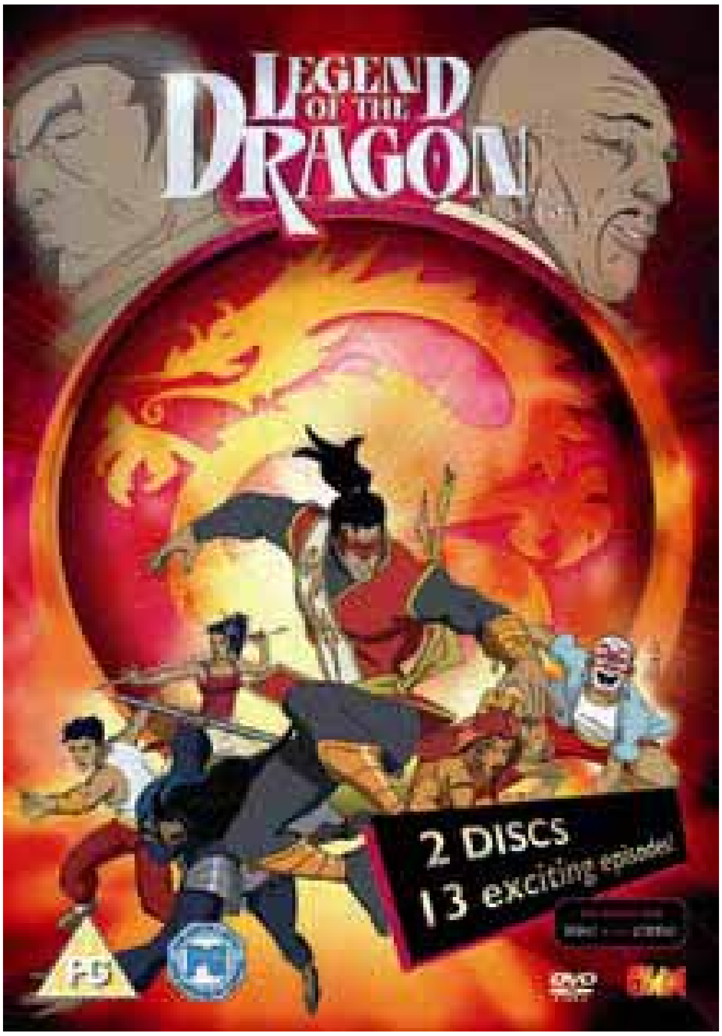
(in thousands of €)

	30.09 2006	30.09 2005
	T€	**T€**
Cash Flow from Operations		
Net Income	+4,495	+4,289
- Depreciation and Amortisation	+1,430	+2,679
- Deferred Taxes	-438	-1,130
	5,487	5,638
Changes in operating assets and liabilities		
- Accounts receivable, trade	+552	-178
- Other Current Assets	+483	+466
- Other Long Term Assets	-3	-2
- Deferred Financing costs	-550	+154
- Accounts payable, trade	+905	+60
- Accruals	+58	-108
- Others	-69	+72
Net cash generated from operating activities	6,863	6,102
Cash Flow from Investing activities		
- Intangible Assets/Programme rights	-14,370	-10,206
- Fixed Assets	-107	-19
Net cash used in investing activities	-14,477	-10,225
Cash Flow from Financing activities		
- Convertible Bond	+8,753	-1,149
- Proceeds from issuance of share capital	+125	+3,436
Net cash provided by financing activities	8,878	+2,287
Net Increase/(decrease) in cash and cash equivalents	1,264	-1,836
Cash and cash equivalents at beginning of period	384	2,220
Cash and cash equivalents at end of period	1,648	384

Consolidated Statements of Stockholder's Equity for Fiscal 2006

(in thousands of €)

	Common Stock	Additional Paid-In Capital	Retained/ Earnings/ (Accumulated Deficit)	Other Comprehensive Income/(Loss)	Total Stockholders' Equity
Balance at 30 September 2005	**15,718**	**8,161**	**0**	**197**	**24,076**
Net profit for the period from 1 October to 30 September 2006			4,495		4,495
Convertible Bond Warrant proceed		125			125
Foreign Currency Translation Adjustment				(61)	(61)
Balance at 30 September 2006	**15,718**	**8,286**	**4,495**	**136**	**28,635**



Notes to the Consolidated Financial Statements for the year ended 1 October 2005 to 30 September 2006

I. General Notes

The consolidated financial statements of BKN International AG, Cologne, Germany for the year ending 30 September 2006 have been prepared subject to all the International Financial Reporting Standards (IFRS) in force at the closing date, as published by the International Accounting Standards Board (IASB) and to all binding interpretations of the International Financial Reporting Interpretations Committee (IFRIC) relating to the last accounting year. This is the 2nd year of IFRS reporting with periods before 1 October 2004 being reported under US-Gaap.

The Income Statement has been prepared using the total cost format. With a view to improving clarity of presentation, some items from the balance sheet and income statement have been combined. These items are shown separately and explained in the appendix.

The Group's functional currency is the euro (€).

The consolidated financial statements and consolidated management board report for BKN International AG, Cologne for the year ended 30 September 2006, prepared in accordance with §292a HGB (German Commercial code), will be published in the Federal Gazette and deposited with the Companies Register for the District Court of Cologne under ref. 32514. They will also be posted on the company's website at www.bknkids.com.

II. Accounting Policies

All companies included in this consolidation apply the same accounting and valuation methods.

Cash and Cash Equivalents. These include bank cash balances and credits with a maturity date of three months or less at the date of purchase or investment.

Accounts Receivable and other assets. On initial valuation, these are shown in the balance sheet at face value. Subsequent valuations will be recognised at fair value. Where the recoverable sum of accounts receivable or other assets is lower than the amortised costs on the balance sheet date, then this sum is used as the basis. Identifiable risks are taken into account by means of suitable value adjustments.

Sales. These are realised at the point at which the service is provided.

Intangible assets acquired for consideration and with a limited operational life. These are valued at purchase cost where it is probable that the BKN Group will benefit from a future economic use of these intangible assets, and where the purchase costs can be reliably determined. The assets are subject to regular straight-line depreciation during their estimated economic life.

Programme assets (cartoons and film rights). These are capitalised at purchase cost. It is strictly not possible to determine the operational life of programme assets with sufficient accuracy. The book value is subject each year to a loss of value test. This involves using discounting methods to establish the expected cash surpluses for the next three years on the basis of anticipated potential sales revenue for the programme assets. Where the sum achievable is less than the corresponding book value, additional depreciation of the asset is carried out (impairment test). In all cases, programme titles are fully depreciated after nine years.

Property, plant and equipment. These are capitalised at either purchase or production cost and subject to regular straight-line depreciation corresponding to their expected life. Expenditure on maintenance and repairs is entered as ongoing expenditure. Borrowed capital costs are not included in the purchase or production costs.

The following periods of use apply across the Group and essentially form the basis of regular depreciation of intangible assets and property, plant and equipment:

Other intangible assets	3 years
Property, plant and equipment	
Operating and business equipment	3-7 years

Deferred tax. Under the terms of IAS 12, we are required to establish deferred tax on different valuations of assets and liabilities in IFRS and tax accounts and on consolidation procedures as well as on realisable loss carryforwards. This included the establishment of asset-side tax accruals in so far as the use of the tax loss carryforwards are currently regarded as probable and foreseeable.

Financial liabilities. These are recognised initially at purchase cost and in subsequent years at amortised cost.

Accounts payable and other liabilities. These are capitalised initially at repayment cost. In subsequent years all liabilities are valued at amortised repayment cost.

Tax provisions. Except for deferred tax, income tax provisions were made only in Germany where there was a taxable profit that could not be fully utilised against tax losses brought forward under the scheme of minimum taxation. With regard to **other provisions**, foreseeable risks and uncertain obligations are taken into account to the value of their likely occurrence. The values recognised are the best estimate of the expenditure required to fulfil the current obligation as at the balance sheet date. Long-term provisions are to be recorded in the form of deferred tax liabilities.

Preparation of the consolidated financial statements requires that the management board make certain estimates and assumptions that may affect the reported figures for revenue, expenditure, assets, liabilities and contingent liabilities when drawing up the balance sheet. The actual figures may differ from the estimates given and based on the information available.

III. Consolidated companies

The consolidated financial statements cover all subsidiaries in which BKN AG is entitled, either directly or indirectly, to a majority of the voting rights. Inclusion in the consolidated financial statements dates from the point at which this controlling share is obtained and ends when this is no longer the case.

As at 30 September 2006, the following companies were included in the consolidation:

- BKN International AG
- BKN New Media Ltd., London
- BKN Home Entertainment Ltd., London*
- BKN New Media Inc., New York
- BKN Home Entertainment Inc., New York (formerly BKN International Inc.)
- BKN Studios Inc., New York (not trading)
- BKN New Media SL, Barcelona*
- BKN Mew Media Pte. Ltd., Singapore (closed October 2006)

* New company

The list of consolidated companies is changed compared to the previous year.

IV. Consolidation policy

The capital consolidation of fully consolidated companies is carried out using the revaluation method. Goodwill or value adjustments were not applicable.

Internal Group sales, expenditure and revenue, all receivables and payables between the consolidated companies and the results of internal group transactions affecting income or expenses (where present) are eliminated.

V. Currency translation

The translation of overseas companies' year-end figures into euros was carried out as per IAS 21 in accordance with the 'functional currency' principle. Since the Group companies operate their own businesses independently, the functional currency is basically identical to the national currency of each company. Translation of asset-side and liability-side items was therefore carried out on the basis of the middle rate on the closing date. Items included in the income statement were valued at the annual average rate. Currency differences arising from the translation of net assets with rates that have changed since the previous year are recognised directly in equity. Capital is consolidated on the basis of historic translation rates.

The rates of exchange employed for translation have changed as follows over the last year with respect to the euro:

	Middle rate on closing date		Annual average rate	
	30.09.2006	30.09.2005	2005/2006	2004/2005
	€	€	€	€
1 USD	0.7883	0.8304	0.8139	0.8467
1 GBP	1.4761	1.4639	1.4603	1.4676
1 SPD	0.4970	0.4917	0.5017	0.4747

Foreign currency monetary items in the year-end accounts of the individual Group companies are translated at the rate applicable on the closing date. Any resulting currency profits or losses are recorded directly with effect on net income.

VI. Notes on §292a HGB

The conditions for exemption from the preparation of consolidated financial statements according to German accounting regulations (§292a HGB) are met. This report has therefore been supplemented with the details required for exemption from the obligation to prepare a Group financial statement and management report in accordance with German law. The assessment of these conditions is based on German Accounting Standard no. 1 (DRS 1), published by the German Standardisation Council, entitled

‘Exempt consolidated financial statements under §292a HGB of the German Accounting Standards Committee (DRSC)’.

Essentially, the accounting and consolidation methods used by the Company under IASB rules applied by the company differ from German accounting rules in the following respects:

Financial instruments

Under both German accounting and IFRS rules, financial instruments (securities, receivables, derivatives) are initially valued at purchase cost. Under HGB, subsequent valuations must strictly adhere to the lowest value principle. Under IFRS rules, however, subsequent valuations are made according to fair value or amortised cost as per IAS 39 depending on their classification. As a result, unrealised profits and losses are also shown. Changes in the fair value of financial instruments that are attributable to the ‘Available for sale’ category are recognised directly in equity up to the point of realisation. Under IFRS, derivative financial instruments must always be recognised at fair value either as an asset or liability. Changes in fair value are recorded with immediate effect on net income.

Intangible assets

Under IFRS, internally generated intangible assets must be capitalised, whereas under German accounting rules, the inclusion of internally generated intangible assets on the assets side is not permitted.

Deferred tax

The determination of deferred tax is based on the balance sheet-oriented liability method. For tax accruals on the assets side, the requirement for recognition is comprehensive. This applies equally to loss carryforwards where there is a sufficient probability that they can be used. Deferred tax accruals on the assets side must be subject to regular impairment review and be reduced by a suitable amount where required. In calculating tax, the rate used is that applicable with future effect on the basis of the legislation as it stands on the balance sheet date. Offsetting of deferred tax assets and liabilities is only permitted under the conditions imposed by IAS 12. Under German accounting rules, only deferred tax assets and liabilities need be formed on consolidating entries. The inclusion of other deferred tax assets is optional, whereas, under HGB, tax loss carryforwards are not permitted. The calculation of tax is based on current tax rates.

Other provisions

Under IFRS, some HGB provisions are shown as liabilities. Moreover, in contrast with the German accounting rules, provisions for expenditure are not permitted. Under IFRS, provisions are always included at their most likely value. Under German accounting rules, however, the principle of caution generally leads to higher provisions.

Liabilities

Under IFRS, liabilities represent financial instruments in the sense of IAS 39 and must therefore be classified and accounted for in the balance sheet as such. Under German accounting rules, liabilities are reported in the balance sheet at repayment value in accordance with the strict lowest value principle.

Foreign currency translation

Under IFRS, unrealised currency exchange profits and losses in relation to foreign currency receivables and liabilities must be included with effect on net income. The imparity principle does not apply.

Convertible bonds

Under IFRS, convertible bonds are regarded as compound financial instruments made up of liability and equity components.

Issue costs are divided between the liability and equity components of the convertible bond in the ratio of their book values on the issue date. The proportion allocated to the equity component is recognised directly in equity.

IPO costs

Under IFRS the direct costs of issuing shares are recognised directly in equity with the revenue from the flotation (share premium), whereas under German accounting rules these costs are recorded as expenditure in the income statement.

Financing Costs

Under IFRS, transactions linked to the increase in borrowed capital are capitalised costs and must be amortised over the financing term.

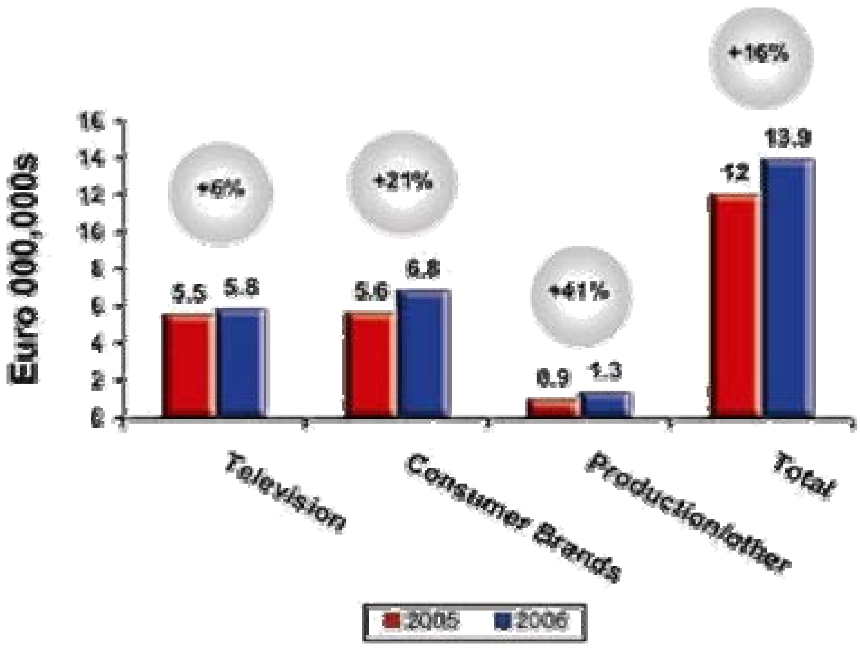
VII. Segment Report

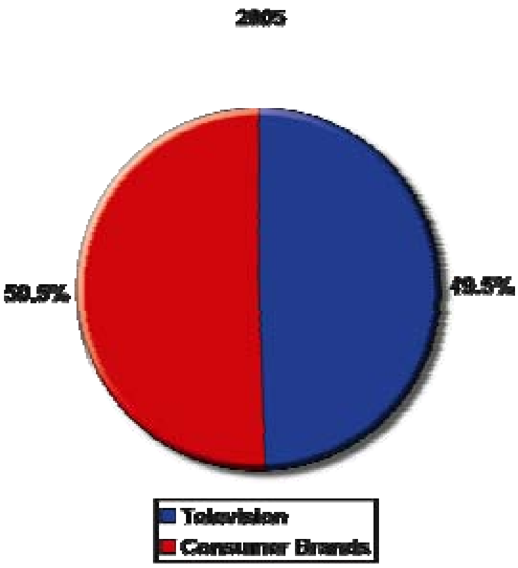
BKN International AG is a global enterprise that produces children's animated cartoon films and markets the rights to these films worldwide.

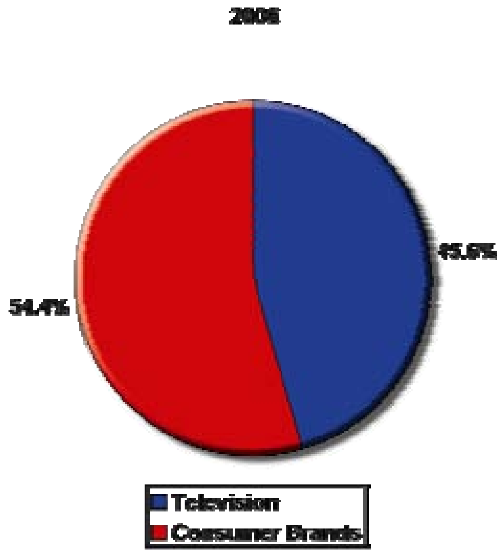
In addition to the head office in Cologne, the company is represented by subsidiaries in London, New York and Singapore.

1. Segmentation of Revenues

The primary segmentation of sales follows from the income statement and shows the following development:

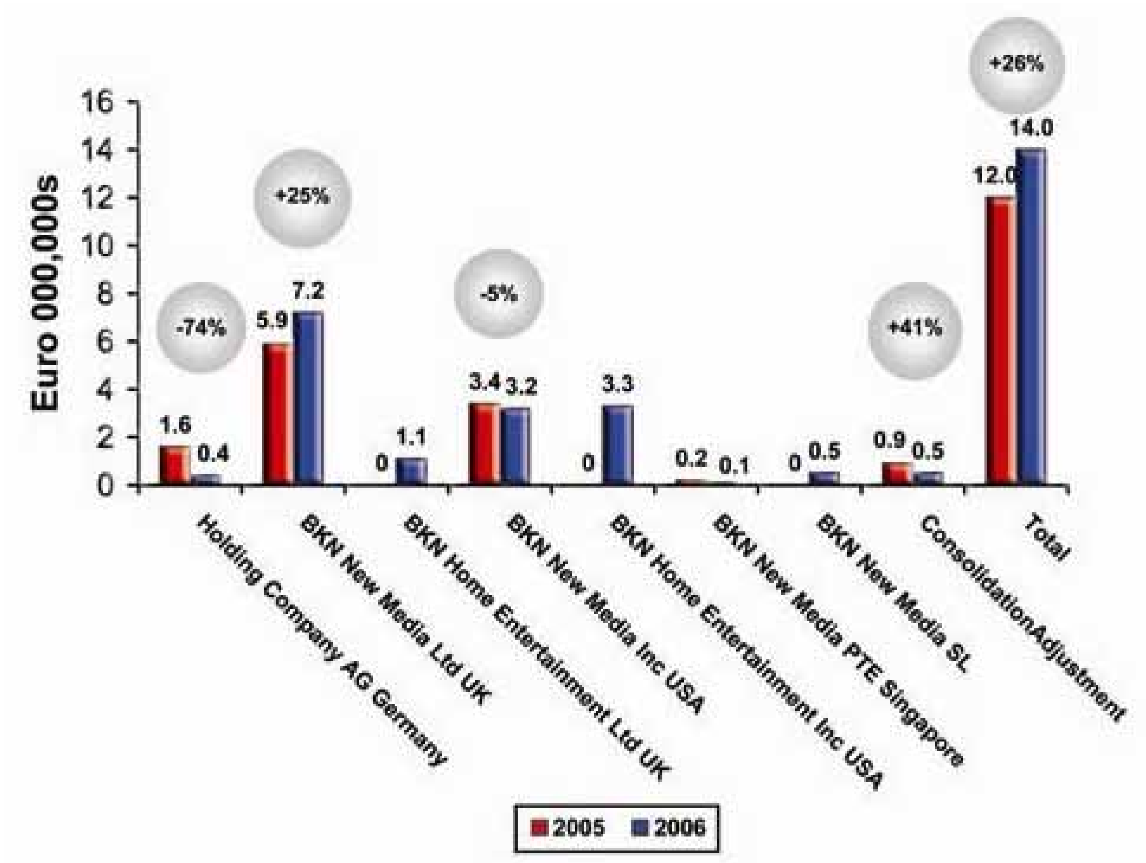


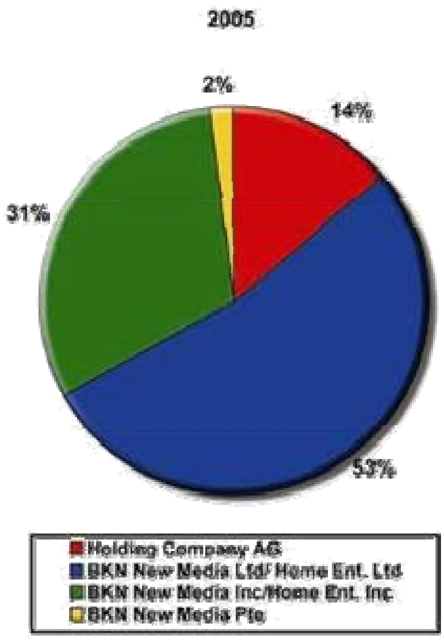


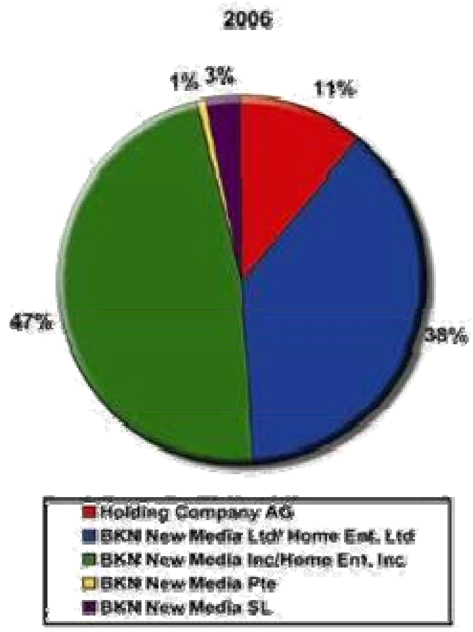


Segmentation by the costs and investments linked to the sales areas or by employees is not possible as divisional sales are based on the same economic and personnel resources. A purely percentage-based distribution has not been undertaken as it would provide little useful information.

2. Revenues by Company

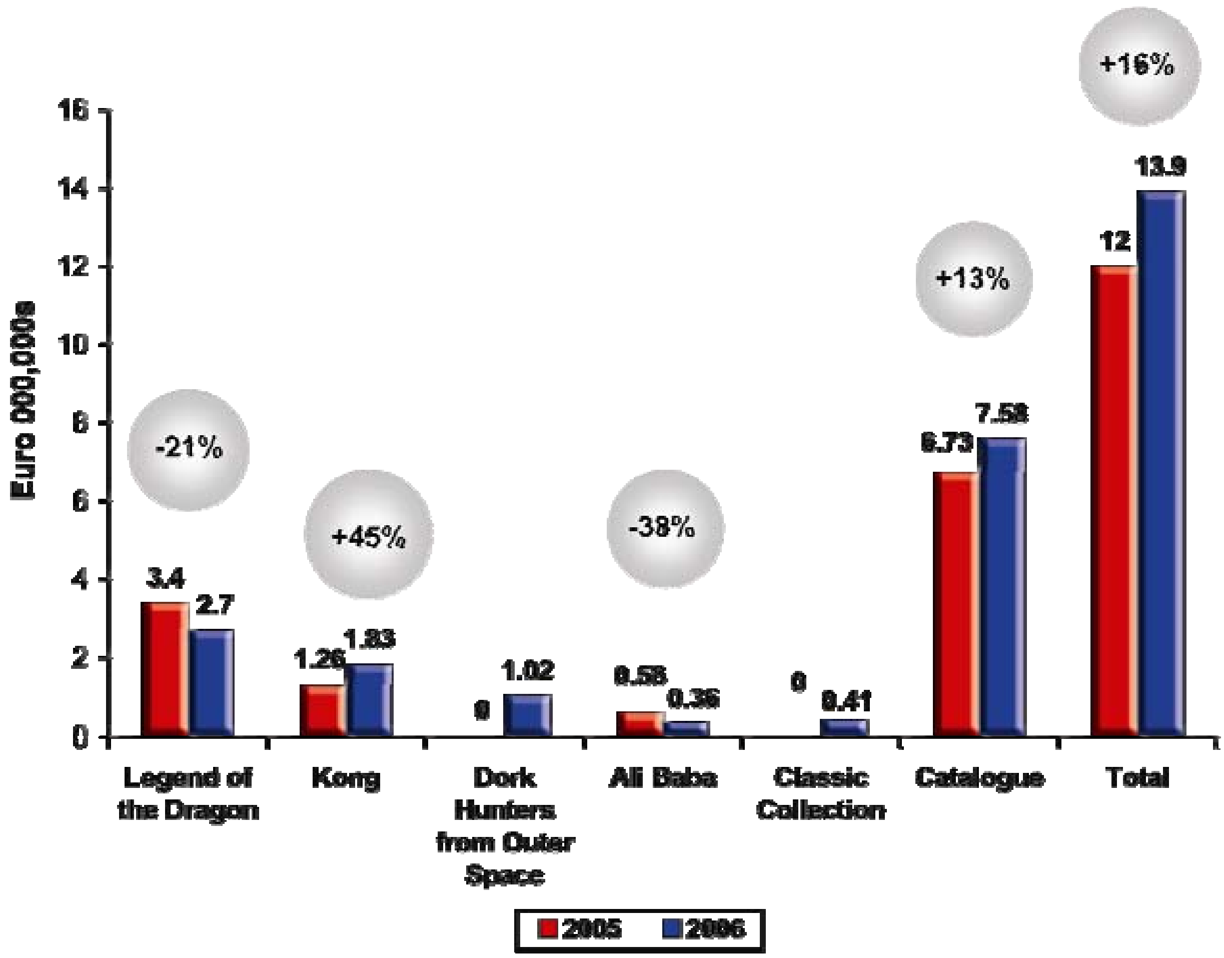


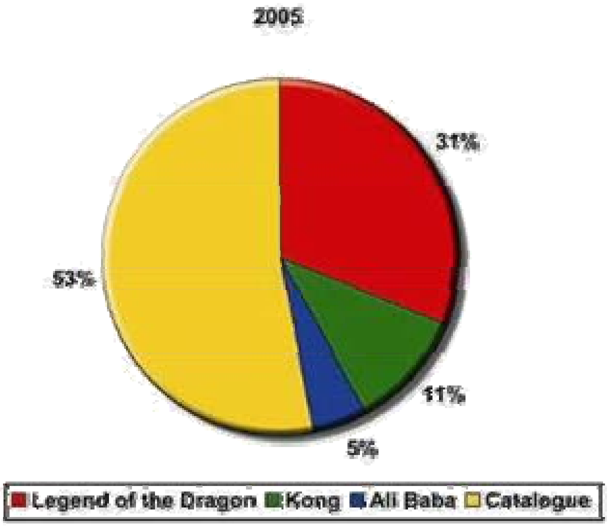


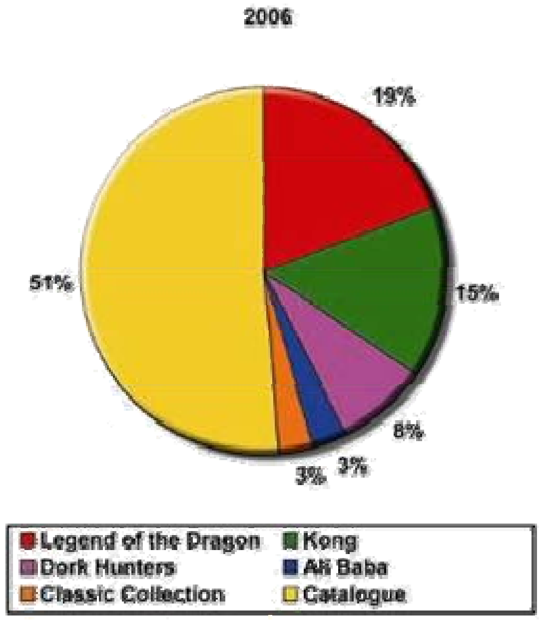


As the sales-generating assets (programme assets) are held exclusively by the parent company, and as the parent company represents the entire Group financing, the subsidiaries have no segment assets or segment liabilities relevant to the report.

3. <u>Segmentation by sources of revenue</u>







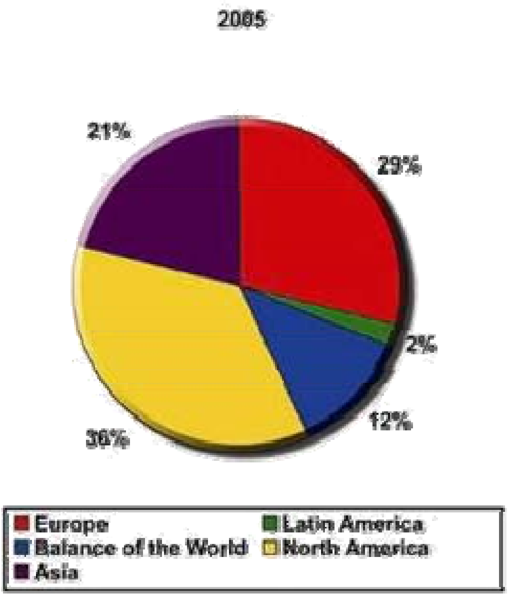
The principal segment asset is made up of the programme rights whose book values are shown below:

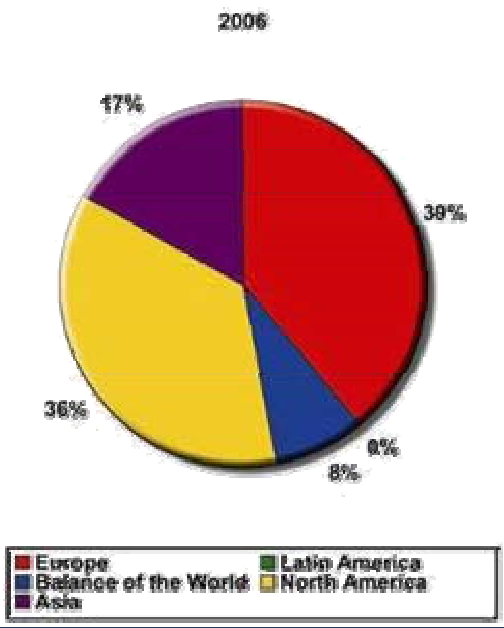
	€ (000s)
Legend of the Dragon	6,650
Kong (various titles)	4,436
Ali Baba	750
Dork Hunters from Outer Space	5,443
Classic Collection	1,823
Remaining programme catalogue	5,868
	24,970
Titles in progress with no contribution to turnover	11,593
Total programme assets	36,563

The business is primarily financed through the issue of share capital (82.2%) and the convertible loan stock (13.2%). A segment-related allocation of financing is not possible.

4. Segmentation by Geographical Area

Sales revenue was generated in the following regions:





Neither segment assets and segment liabilities nor costs and employees can be usefully allocated on the basis of geographical criteria.

VIII. Notes on the balance sheet

A. Fixed and intangible assets

The development of intangible assets and property, plant and equipment including the depreciation apportionable to the accounting year as well as the composition of the item can be seen in detail from the attached consolidated statement of changes in fixed assets.

The figure of T€36,563 shown for programme assets includes work in progress totalling T€ 11,593 which has not yet been depreciated.

The programme assets are used as security for the convertible loan stock issued in the accounting years 2003/2004, thru to 2005/2006.

B. Other long-term assets

1. Other assets

This item primarily relates to the payment of security deposits in connection with the leasing of business premises in Germany and abroad.

2. Deferred tax

This item was established as a result of the tax loss carryforwards of the companies included in the consolidation.

Calculation of this item is based on the following assumptions:

Tax loss carryforwards in the Group on balance sheet date approximately	T€	57,000
Thereof included in the deferred tax calculation	T€	6,135

This figure takes into account both the forecast results of the group Companies for 2007 – 2009 less an appropriate valuation allowance and the offsettable loss carryforwards in the individual companies.

Tax asset at a weighted tax rate in the Group of 36% (according to country including any offsettable loss carryforwards)	T€	2,209

3. Deferred financing costs

Where they are attributable to the liability component on the balance sheet date, costs in connection with the issue of the convertible loan stock are deferred and amortised over the term of the financing.

C. Current assets

1. Accounts receivable

This item includes receivables from sales made and provided that are to be recognised at fair value. Bad debt allowances of T€366 (previous year: T€48) were made to cover potentially unrecoverable amounts.

2. Other assets

This item includes advance part-payments in connection with operations of T€ 488 (previous year T€ 1,037), advance payments for running costs of T€ 170 (previous year T€ 113) and VAT receivables of T€ 131 (previous year T€ 122).

3. Cash and cash equivalents

This item primarily covers cash and bank balances of the Group companies. Foreign currency amounts were translated at the balance sheet date. The Management Board may make use of these resources without restriction.

D. Equity

The composition and development of the equity position can be seen in detail in the attached consolidated statement of changes in equity.

As at the closing date, the following shares were issued or contingently issued through option and convertible rights:

Shares issued:	15,717,566
Option rights:	733,500
Convertible rights:	3,624,743

The reconciliation of consolidated net profit for the period to the balance sheet is as follows:

	30.9.2006	Previous year
	T€	T€
Consolidated net profit	4,495	4,289
Loss carryforward	0	69,006
	4,495	64,717
Taken to share premium	0	64,717
Accumulated profit	4,495	0

E. Non-current liabilities

1. Convertible loan

On 29 September 2004, the company issued a convertible bond with a total value of €4,950,000.00 at a rate of 5%. The convertible bond expires in March 2008. The convertible bond entitles the creditor to 909,091 individual bearer shares. The company also issued an option bond with a value of €50,000 at a rate of 5%.

The option bond also expires in March 2008. The option bond contains 227,274 subscription warrants entitling the holder to 227,274 individual bearer shares. The price for the subscription warrants is €0.50 each, making a total revenue of €113,637. Revenue from the sale of the subscription warrants was taken to the share premium.

Following exchange declarations made on 13 April 2005, 2 May 2005 and 7 June 2005, the holder of the convertible bond took up a total of 211,000 new individual bearer shares equivalent to a proportionate interest in the capital stock of €1.00 per share. The transfer was effected by the exchange of fractional bonds with a total face value of €1,148,895. By way of assignment, the creditor transferred a partial amount from the fractional bond with a face value of €1,148,895 to BKN AG, which recognised this amount in its liability from the convertible bond.

In presentation of the convertible bond, the equity component (fair value of the option) was waived on account of its negligible size.

The fair value of the liability component will be recognised by the management board to the extent of its reported book value (nominal value).

On 12 October 2005, the company issued a convertible bond with a total value of €4,500,000 to Laurus funds at a coupon rate fixed at US prime rate plus 1%. The bond expires in August 2010. The bond entitles the creditor to 1,000,000 individual bearer shares.

As part of the same deal on 1 January 2006 also issued a 2nd bond to the same company with a value of €1,125,000 as well as on same day a €50,000 option bond. Both of these were at same coupon interest terms of US prime plus 1%. These 2nd bonds expire in January 2011. The option bonds contains 250,000 subscription warrants at a price of €0.50 each.

On 23 August 2006, the company issued a 3rd convertible bond with a total value of €3,200,000 to Anacapa Funding at a coupon rate fixed as US prime rate plus 2%. The bond expires in December 2010. The bond entitles the creditor to 1,000,000 individual bearer shares.

The convertible bonds are secured by the pledging of programme rights.

2. Deferred tax (liability)

This item is based on different presentations in the financial statements of the subsidiary companies and in the consolidated balance sheet with respect to the following items:

	Difference	Deferred tax	
	T€	%	T€
Intangible assets	455	37.0	168
Deferred financing costs	738	37.0	273
	1,193	37.0	441

3. Other liabilities

The term varies between two and five years. No securities have been provided.

F. Current liabilities

1. Provisions

Provisions were established on the basis of reasonable commercial principles for uncertain liabilities. For the most part, they refer to cost accruals for the last accounting year.

The most important items are:

	30.9.2006	Previous year
	T€	T€
Personnel: ancillary costs	258	294
Bonus payments	260	217
Legal, consultancy and audit costs	160	183
Supervisory Board remuneration	60	60
Accrued interest	78	48
Costs of general meeting	48	48
Other	82	53
Trade tax on income	15	0
	961	903

2. Accounts payable

This item includes outstanding obligations arising from supplies and services. These are recognised at the fulfilment amount. In all cases, payment is due in less than one year. There are no securities relating to these obligations.

IX. Notes on Income Statement

1. Sales revenue

This item covers all external sales of the group after deduction of in-Group supplies and services. The distribution of sales revenue is based on classification as per the income statement and on segment reporting.

2. Other operating revenue

This item concerns capitalised services (material and personnel costs) generated internally in the production of intangible assets on the basis of direct costs to the company. In addition, the previous year's figure primarily contained currency profits.

3. Producer charges and direct operating costs

This item covers marketing costs and other sales-related costs.

4. Salaries and social security expenses

This item covers payroll including performance-related remuneration and mandatory social security payments divided up as follows:

	2005/2006	2004/2005
	T€	T€
Payroll	2,744	1,974
Social security contributions and related salary costs	249	125
	2,993	2,099

Expenses linked to voluntary retirement benefit schemes were T€15 (previous year:T€ 7).

5. Number of employees

For the accounting year 2005/2006, the Group employed an average of 30 persons excluding directors in total (previous year: 17).

6. Depreciation of intangible fixed assets and property, plant and equipment

With respect to depreciation, T€50 corresponds to scheduled depreciation (previous year: T€20) and T€1,380 to additional unscheduled depreciation as a result of the impairment test (previous year: T€2,659). The difference from the previous year of T€1279 primarily concerns the smaller unscheduled write-downs of programme assets.

7. Other operating expenses

This item primarily includes:

8. Other operating expenses

This item primarily includes:

	2005/2006	2004/2005
	T€	T€
Rents	677	652
Advertising costs	536	329
Legal and consultancy costs	670	479
Accounting Costs	150	178
Travel, etc.	281	231
Corporate administration and insurance	673	660
Supervisory board remuneration	60	60
Office costs	329	161
Currency losses	0	206
Bad Debt	366	70
Legal settlement	0	755
Other	0	(20)
	3,742	3,761

9. Net interest income

This item is made up as follows:

	2005/2006	2004/2005
	T€	T€
Interest expenses	670	229
Interest income	45	4
	625	225

10. Income taxes

This item is made up as follows:

	2005/2006	2004/2005
	T€	T€
Misc. revenue and withholding taxes	46	12
Trade tax on income	15	0
Deferred tax expenses	269	172
Deferred tax benefit	(707)	(1,502)
	(377)	(1,318)

With regard to the deferred taxes, please refer to the corresponding remarks on the balance sheet items in question.

Actual annual tax expenditure is calculated including recognition of loss carryforwards as follows):

	2005/2006	2004/2005
	T€	T€
Pre-tax profit	2,738	2,971
National tax charge	1,030	1,070
Tax relief from use of loss carryforwards	(1,015)	-1,070
Misc. local revenue and withholding tax	46	12
Actual tax expenditure	61	12

X. Notes on Cash Flow Statement

The cash flow statement shows the origin and use of payment streams in the accounting years 2005/2006 and 2004/2005. A distinction is made between payment streams from current operations and from investment and financing activities. Cash and cash equivalents cover all bank balances and credits where these are available within three months.

The net change in cash and equivalents from current operations has been adjusted for currency translation effects.

The net change in cash and equivalents from investment and financing activities is calculated on a cash basis.

The net change in cash and equivalents from current operations, however, is calculated indirectly from the accounting profit.

XI. Earnings per share

Undiluted earnings per share for the accounting year 2005/2006 are €0.29 (previous year: €0.28).

Undiluted earnings per share are calculated by dividing the figure for consolidated profit by the weighted number of shares issued. For the accounting year 2005/2006 the weighted number of shares issued was 15,717,566 (previous year: 15,250,095).

The change in the weighted number of shares issued compared with the previous year is a result of the capital increase in the reporting year and the partial exercise of the convertible loan.

Diluted earnings per share for the accounting year 2005/2006 are €0.26 (previous year: €0.28). Diluted earnings per share are calculated under the assumption that those outstanding option rights with an exercise price below the market price are exercised and also covers the possible take-up of shares from the convertible loans as well as the interest payments saved in the event of conversion. As the quoted value of BKN AG shares as at 30 September 2006 was below the exercise price established in the share option programme and the exercise of these options is thus unlikely, no assessment was made of fair value.

XII. Other financial obligations

Except for the liabilities shown in the balance sheet, the only contingent liabilities and securities for third-party liabilities exist in the form of rental obligations as detailed below:

	30.9.2006	30.9.2005
	T€	T€
Under one year	446	465
Between two and five years	1,152	1,418
	1,598	1,883

XIII. Related parties

1. The Management Board and other members of management in key positions as well as members of the Supervisory Board are counted at BKN AG as related parties in the sense of IAS 24. Their remuneration is detailed fully in the notes on company bodies.

2. According to information available to the company as per §21 WpHG, Management Board and Supervisory Board members hold interests in the company of less than 10% each though with more than 5% of voting rights.

3. Transactions between the company and its subsidiaries, who are related parties, were eliminated in the course of consolidation and are not set out in this appendix.

4. There are no other relationships or transactions with related parties.

XIV. Stock option plan

1. The Company established a new stock option plan on 17 March 2005. This plan is subject to the following provisions:

- The company may issue 1,492,748 options in a first tranche.
- The option rights may be exercised no earlier than two years after they are granted.
- The option rights expire, if they are not exercised, after five years, reckoned from the date of allocation.
- Option holders are entitled to subscribe for one share per option right. The exercise price is €3.90 per share. This was revised down from €6.02 on 12 January 2006.
- The option may only be exercised if the quoted price on the days prior to exercise of the options has at least reached the minimum price.

As at 30 September 2005, the Company had granted a total of 733,500 option rights. 740,000 of these option rights were allocated on 17 March 2005 and cannot be exercised before 13 January 2008.

No compensation charge was recorded in the Income Statement.

As at 30 September 2006 members of the Management Board held a total of 725,000 options.

2. The 8,500 option rights still existing from a previous option plan are held by company employees.

3. No option rights are held by members of the supervisory board.

XV. Litigation

There are two claims against the Company in the US related to its 2002 re-structuring. The Management Board has received legal opinions that neither claim is of validity for a variety of facts including that neither the Company, nor any of the company in the BKN Group, ever contracted with the claimants and that German law is not applicable to the claims.

XVI. Notes on transition to IFRS

The consolidated financial statements for the accounting year to 30 September 2006 were prepared for the second time under IFRS. Before 30 September 2004 and since the foundation of the Company, all consolidated financial statements were prepared under US-GAAP.

As in this case there have been no material or accounts disclosure-related differences using IFRS accounting as opposed to the previous US-GAAP accounting standards, there is no need for a equity reconciliation statement.

The equity position as at 1 October 2003 as the date of transition to IFRS (the last consolidated financial statements under US-GAAP were presented for the accounting year to 30 September 2004) and equity as at 30 September 2004 as the closing date for the last consolidated financial statements under US-GAAP do not reveal any anomalies related to transition.

The development of equity is therefore based exclusively on the attached statement of change in consolidated equity.

XVII. Other information

1. Details of Company bodies

In accordance with the articles of association, the Supervisory Board is made up of three members. As at 30 September, these members were:

Herr Karl Benetz, Durbach/Baden, Chairman (since 17 January 2003)
Mr Jack Kugler, Greenwich, USA, Deputy Chairman (since 14 March 2002)
Mr Robert K Paff, Creedmoor, USA (since 17 January 2003)

The composition of the Management Board for the accounting year 2005/2006 was as follows:

Mr Allen Bohbot, New York, USA, Chairman (since 1 February 2001)
Mr Wayne Mowat, London, GB (since 1 November 2003)
Mr Ben Heng Chin Guan, Singapore (since 8 September 2004 until resignation 31 August 2006)

The total remunerations of the members of the Management Board for the accounting year 2005/2006 were €1,167,215. This figure includes performance-related remuneration of €210,495 (previous year: €1,049,970, of which performance-related : €217,517). Full details are not published due to the relating share holders resolution dated 16 February 2006 according to §286 para. 5 HGB.

The total remunerations of the supervisory board for the accounting year 2005/2006 were €60,000 (previous year: €60,000).

2. Auditors Fees

The auditors have charged in total €119,000 for audit services and €31,000 for tax consulting.

3. Declaration of compliance with the German Corporate Governance Codex

The updated declaration of compliance as per §161 AktG on observation of the German Corporate Governance Codex was presented to BKN AG by the Management Board and the Supervisory Board of BKN AG in October 2006. This declaration was made permanently available to shareholders on the Company's website.

4. Information as required by §314 para. 1 no. 10 and 11 HGB

The Group does not make use of any derivative financial instruments in the sense of §314 para. 1 no.10 HGB.

5. Approval of the Consolidated Financial Statements

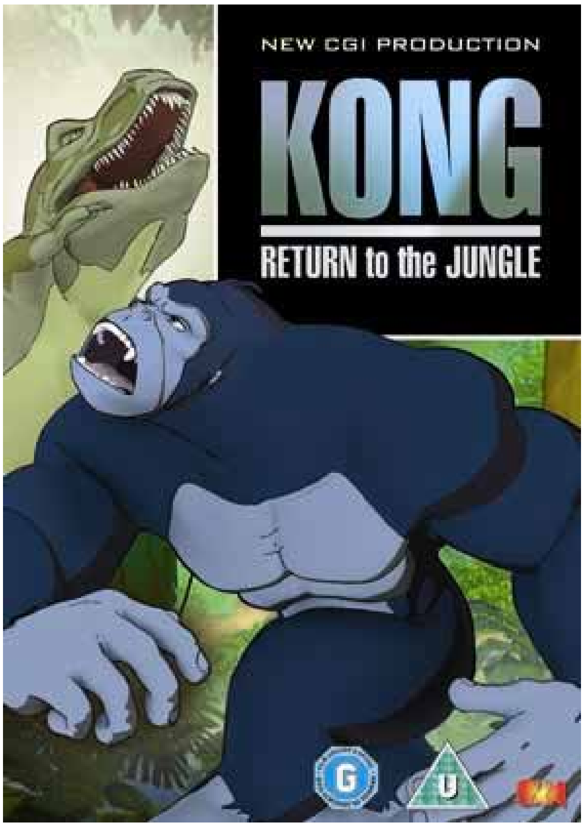
It is expected that the Consolidated Financial Statements will be approved on 27 November 2006 at a joint meeting of the Supervisory Board and Management Board in the presence of the auditor and subsequently released for publication.

Cologne, November 2006

The Management Board

Signed
Allen Bohbot

Signed
Wayne Mowat



Appendix 1

Consolidated statement of changes in fixed assets as at 30 September 2006

	Cost					Depreciation				Net Book Value	
	01/10/2005	Additions	Disposals	Reclassification	30/09/2006	01/10/2005	Additions	Disposals	30/09/2006	30/09/2006	Previous year
	T€	T€	T€	T€	T€	T€	T€	s	T€	T€	T€
I. Intangible assets											
1. Software	518	29	0	0	547	518	1	0	519	28	0
2. Programme assets	77,270	14,341	0	700	92,311	54,368	1,380	0	55,748	36,563	22,902
3. Advance payments	700	0	0	-700	0	0	0	0	0	0	700
	78,488	14,370	0	0	92,858	54,886	1,381	0	56,267	36,591	23,602
II. Property, plant and equipment											
1. Operating and business equipment	102	107	0	0	209	33	49	0	82	127	69
Total fixed assets	78,590	14,477	0	0	93,067	54,919	1,430	0	56,349	36,718	23,671

Report of the Supervisory Board for Fiscal 2006

During the year under review, the Supervisory Board oversaw the Management Board regarding the tasks imposed upon it by law and the Articles of Association, and monitored the management activity during the period. Further, the Management Board reported regularly on progress in achieving goals set for the current period and on the prospects for future periods.

The Supervisory Board met six times throughout the period and was kept informed by the Management Board through regular oral and written reports on the Company's progress, financial situation and all major investments and strategies.

The financial accounts and management board report together with the consolidated financial accounts and the consolidated management board report were audited and each given an unqualified auditor's report by Nexia Deutschland GmbH Wirtschaftsprüfungsgesellschaft, who were appointed auditors for the year by resolution of the Annual Shareholders Meeting on 16 February 2006 and further received appropriate instructions from the Supervisory Board. We agree with the auditing results. The Supervisory Board has checked the financial statements and management report as well as the consolidated financial statements and the consolidated management board report. No objections have been raised thereby. These financial statements provided by the Management Board were approved today by the Supervisory Board and are thereby finalised.

The Supervisory Board agrees with the Management Board's suggestion as regards the application of the net profit for the year.

The Supervisory Board thanks management and the Company's employees at the various locations for the performance that contributed to the outcome of the year under review.

Cologne, November 2006

Karl Benetz

Chairman of the Supervisory Board

The Supervisory Board

Mr. Karl Benetz
Chairman of the Supervisory Board
Businessman, appointed
17 January 2003

Mr. Robert Paff
Businessman, appointed
17 January 2003

Mr. Jack Kugler
Businessman, appointed 14 March 2002

The Management Board

Mr. Allen Bohbot
Chairman/CEO
Appointed 1 February 2001

Mr. Wayne Mowat
Appointed 1 November 2003

Mr. Ben Heng
Appointed 8 September 2004
Resigned 31 August 2006

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