

# CGS

**CHINA GROUND SOURCE ENERGY LIMITED**

*(Incorporated in the Cayman Islands with limited liability)*

Stock Code: 8128



THIRD QUARTERLY REPORT  
**2010**

**CHARACTERISTICS OF THE GROWTH ENTERPRISE MARKET (THE “GEM”) OF THE STOCK EXCHANGE OF HONG KONG LIMITED (THE “STOCK EXCHANGE”)**

**GEM has been positioned as a market designed to accommodate companies to which a higher investment risk may be attached than other companies listed on the Stock Exchange. Prospective investors should be aware of the potential risks of investing in such companies and should make the decision to invest only after due and careful consideration. The greater risk profile and other characteristics of GEM mean that it is a market more suited to professional and other sophisticated investors.**

**Given the emerging nature of companies listed on GEM, there is a risk that securities traded on GEM may be more susceptible to high market volatility than securities traded on the Main Board of the Stock Exchange and no assurance is given that there will be a liquid market in the securities traded on GEM.**

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*This report, for which the directors (the “Directors”) of China Ground Source Energy Limited (the “Company”) collectively and individually accept full responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited for the purpose of giving information with regard to the Company. The Directors, having made all reasonable enquiries, confirm that to the best of their knowledge and belief the information contained in this report is accurate and complete in all material respects and not misleading or deceptive, and there are no other matters the omission of which would make any statement herein or this report misleading.*

**HIGHLIGHTS**

Revenue was approximately HK\$277 million for the Review Period.

Profit attributable to owners of the Company for the Review Period amounted to approximately HK\$53 million.

No dividend was declared for the Review Period.

**FINANCIAL REVIEW**

The following table provide brief summary of our Company's financial results. For more detailed information, please refer to the unaudited consolidated financial statements for the periods ended 31 December 2010 (the "Review Period") and 2009.

	Three months ended 31 December		Nine months ended 31 December	
	2010 HK\$'000 (Unaudited)	2009 HK\$'000 (Unaudited) (Restated)	2010 HK\$'000 (Unaudited)	2009 HK\$'000 (Unaudited) (Restated)
<b>Continuing operations:</b>				
<i>Revenue</i>				
– Shallow ground energy utilization system	98,509	120,687	277,211	299,587
– Dividend income	–	–	–	1,256
<b>Total revenue from continuing operations</b>	<b>98,509</b>	<b>120,687</b>	<b>277,211</b>	<b>300,843</b>
<b>Discontinued operations:</b>				
<i>Revenue</i>				
– Sewage and gas treatment income	–	10,353	14,016	22,294
– Sales of communication cables and optical cables	–	–	–	45,578
<b>Total revenue from discontinued operations</b>	<b>–</b>	<b>10,353</b>	<b>14,016</b>	<b>67,872</b>
<b>Profit/(loss) for the period from continuing operations</b>	<b>13,605</b>	<b>25,069</b>	<b>42,893</b>	<b>36,021</b>
<b>Profit/(loss) for the period</b>	<b>13,605</b>	<b>24,163</b>	<b>55,375</b>	<b>(133,033)</b>
<b>Profit/(loss) attributable to owners of the Company</b>	<b>12,736</b>	<b>22,770</b>	<b>53,482</b>	<b>(135,517)</b>

During the Review Period, the Group's revenue from continuing operations (excluding dividend income) amounted to approximately HK\$277 million which was contributed by shallow ground energy utilization segment as compared with approximately HK\$300 million in the last corresponding period.

On 27 August 2010, the Board announced the disposal of the entire interest in sewage and gas treatment business segment and, therefore, this segment has been classified as discontinued operations during this Review Period.

The Group's gross profit margin (excluding dividend income) for the Review Period mainly contributed by shallow ground energy utilization segment, were 41.82% and 41.76% for the nine months ended 31 December 2010 and 2009 respectively.

Administrative expenses amounted to HK\$67 million and HK\$87 million for the nine months ended 31 December 2010 and 2009 respectively. The decrease is mainly due to a lower stock compensation expense of share option with vesting period of 1-3 years.

Selling and distribution costs increased by approximately HK\$3 million, or 36% as compared with that of nine months ended 31 December 2009. The increase is primarily due to the increase of after sales service cost of company projects.

Finance costs decreased by 66% to HK\$7.5 million for the nine months ended 31 December 2010 as compared with that of the last corresponding period. The decrease in interest expense reflects lower debt levels due to conversion of convertible notes to ordinary share capital on 14 September 2010.

Profit attributable to owners of the Company for the Review Period amounted to approximately HK\$53 million as compared to a loss of HK\$136 million in the last corresponding period. The results of last corresponding period included a HK\$161 million charge for impairment of goodwill related to our Shenzhen Lisai business as a result of impairment test.

## **BUSINESS REVIEW AND PROSPECTS**

During the period under review, the Group continued to focus on business of developing ground source energy as an alternative source of energy for heating. The business is mainly operated through Beijing Enterprises Ever Source Ltd. and its subsidiaries ("HYY"). The results in the first three quarters of this fiscal year meet the expectation as benefitted from the government's new energy policy. On the other hand, projects with larger contract sums were completed gradually within this period.

Shallow ground source energy is a clean, highly-efficient and environmentally-friendly renewable energy, which continuously gained international attention and promotion. In cooperation with Trane, HYY ground source energy heat pump environmental systems, which are based on HYY's international invention – the single well circulation ground heat exchange technology, have been successfully applied in schools in Nebraska, United States. As the two-year heating operation achieved significant energy saving, the systems were awarded “Energy Star” by the government on 10 January 2011.

HYY has accumulated ten years of valuable experience of development and research of ground source energy as an alternative source of energy for heating. In October 2010, Beijing Energy Saving and Environmental Protection Association hosted the “Experts Review Meeting for HYY ground source energy heat pump systems operating for over 7 years in Beijing”. The group of experts has given HYY ground source energy heat pump systems and single-well recycling ground source energy collection technology with positive affirmation and comment, and expressed precious advices in the meeting.

The PRC Government has expressly stated in its “12th Five-Year Plan” that “with a construction resource-saving and environmentally-friendly society as the basis and means of accelerating the transformation of economic development will be firmly adhered to. It will thoroughly implement the State’s fundamental policies in resource conservation and environmental protection, which shall include energy saving, reduction of greenhouse gas emissions density, development of circular economy, and promoting low carbon technologies, thereby to take the path of sustainable development.” The concept of utilisation of ground source energy as an alternative energy for heating has been brought into regional development planning by governments at various levels.

Shallow ground source energy, as an alternative energy for heating, is both environmentally-friendly and energy-saving. HYY ground source energy heat pump environmental systems with proprietary ground source energy collection technology has been fully recognised by experts, which meets the national and international strong demands for environment protection and new energy. The Group will further speed up its development on the basis of this keen demand and capture the existing opportunities, we are of confident that, with the focus and dedication on the business of developing ground source energy as an alternative energy for heating, the potential is enormous and the direction is correct.

In December 2010, Mr. Xu Shengheng, the substantial shareholder and executive director of the Company, entered into the Subscription Agreement for subscription of 234,704,000 Shares at the Subscription Price of HK\$0.3184 per Share. The proceeds will be used principally for investment in Wanghaixincheng Project, a model project of HYY ground source energy heat pump environmental systems’ energy station, for the purpose of developing infrastructure for utilising ground source energy as a source of energy for heating in Wafangdian, Dalian. The Subscription was completed on 18 January 2011.

**CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME**

For the nine months ended 31 December 2010

	Notes	Three months ended 31 December		Nine months ended 31 December	
		2010 HK\$'000 (Unaudited)	2009 HK\$'000 (Unaudited) (Restated)	2010 HK\$'000 (Unaudited)	2009 HK\$'000 (Unaudited) (Restated)
<b>Continuing Operations</b>					
Revenue	2	98,509	120,687	277,211	300,843
Cost of sales		(56,232)	(68,843)	(161,268)	(174,493)
Gross profit		42,277	51,844	115,943	126,350
Other operating income		1,448	4,379	15,457	38,375
Selling and distribution costs		(4,297)	(3,708)	(11,344)	(8,334)
Administrative expenses		(24,154)	(17,366)	(66,519)	(87,025)
Other operating expenses		-	-	-	(11,772)
Profit/(loss) from operations		15,274	35,149	53,537	57,594
Share of results of associates & jointly controlled entity		111	1,065	774	1,426
Finance costs		-	(9,647)	(7,488)	(22,001)
Profit/(loss) before tax	3	15,385	26,567	46,823	37,019
Income tax expense	4	(1,780)	(1,498)	(3,930)	(998)
Profit/(loss) for the period from continuing operation		13,605	25,069	42,893	36,021
<b>Discontinued Operation</b>					
Profit/(loss) for the period from discontinued operations	5	-	(906)	12,482	(169,054)
Profit/(loss) for the period		13,605	24,163	55,375	(133,033)

**CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (Cont'd)**

For the nine months ended 31 December 2010

	Notes	Three months ended 31 December		Nine months ended 31 December	
		2010 HK\$'000 (Unaudited)	2009 HK\$'000 (Unaudited) (Restated)	2010 HK\$'000 (Unaudited)	2009 HK\$'000 (Unaudited) (Restated)
Other comprehensive income/(expenses):					
Exchange differences arising from translation of foreign operation		2,353	231	4,188	2,738
Release of exchange translation reserve upon disposal of subsidiary		-	-	(6,218)	(515)
Release of asset revaluation reserve in relation to leasehold buildings upon disposal of subsidiaries		-	-	-	1,321
<hr/>					
Other comprehensive income/(expense) for the period		2,353	231	(2,030)	3,544
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Total comprehensive income/(expense) for the period		15,958	24,394	53,345	(129,489)
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Profit/(loss) attributable to:					
Owners of the Company		12,736	22,770	53,482	(135,517)
Non-controlling interests		869	1,393	1,893	2,484
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		13,605	24,163	55,375	(133,033)
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Total comprehensive income/(expense) attributable to:					
Owners of the Company		14,656	23,002	50,260	(135,885)
Non-controlling interests		1,302	1,392	3,085	6,396
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		15,958	24,394	53,345	(129,489)
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Earnings/(loss) per share					
From continuing and discontinued operations:					
Basic-(HK Cents)	7	0.70	1.35	3.02	(8.46)
Diluted-(HK Cents)		0.69	1.35	2.96	(8.46)
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From continuing operations:					
Basic-(HK Cents)		0.70	1.40	2.32	2.09
Diluted-(HK Cents)		0.69	1.40	2.27	2.09
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Notes to account:

## 1. BASIS OF PREPARATION

The condensed consolidated financial statements have been prepared in accordance with the applicable disclosure requirements of Chapter 18 of the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (the GEM Listing Rules) and with accounting principles generally accepted in Hong Kong Financial Reporting Standards (“HKFRS”), Hong Kong Accounting Standards and Interpretations (collectively, “new HKFRSs”) issued by the Hong Kong Institute of Certified Public Accountants (the “HKICPA”).

The accounting policies adopted in the preparation of this financial statements are consistent with those adopted in preparing the annual audited financial statements for the year ended 31 March 2010.

The condensed consolidated accounts have not been audited by the Company’s auditors, but have been reviewed by the Company’s audit committee.

## 2. REVENUE

Revenue represents the net invoiced value of goods sold, after allowances for returns, trade discounts and business tax where applicable, and services rendered.

An analysis of the Group’s revenue is as follows:

	Three months ended		Nine months ended	
	31 December		31 December	
	2010	2009	2010	2009
	HK\$’000	HK\$’000	HK\$’000	HK\$’000
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
		(Restated)		(Restated)
<b>Continuing operations:</b>				
Shallow ground energy utilization	<b>98,509</b>	120,687	<b>277,211</b>	300,843
<b>Discontinued operations:</b>				
Environmental protection	–	10,353	<b>14,016</b>	22,294
Transmission	–	–	–	45,578
	–	10,353	<b>14,016</b>	67,872



**3. PROFIT/(LOSS) BEFORE TAX**

	Three months ended		Nine months ended	
	31 December		31 December	
	2010	2009	2010	2009
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
		(Restated)		(Restated)
<b>Continuing operations:</b>				
Cost of sales	56,232	68,843	161,268	174,493
Staff costs (including directors' emoluments)	7,548	8,491	22,521	22,451
Depreciation	797	563	3,543	5,131
Minimum lease payments under operating leases in respect of land and buildings	1,461	1,692	4,873	5,434
Share based payment	3,200	–	18,922	26,357

**4. INCOME TAX EXPENSE**

	Three months ended		Nine months ended	
	31 December		31 December	
	2010	2009	2010	2009
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
		(Restated)		(Restated)
<b>Continuing operations:</b>				
PRC corporate income tax	1,507	678	2,992	2,048
Deferred tax	273	820	938	(1,050)
	1,780	1,498	3,930	998

## 5. DISPOSAL OF SUBSIDIARIES

- (a) On 13 September 2010, the Group disposed of a wholly owned subsidiary, IIN Network Technology Limited and its subsidiaries to an independent third party at a consideration of HK\$30,000,000.

The profit/(loss) from the discontinued operation for the period is analysed as follows:

	From 1 October 2010 to 31 December 2010 HK\$'000 (Unaudited)	Three months ended 31 December 2009 HK\$'000 (Unaudited) (Restated)	From 1 April 2010 to 31 December 2010 HK\$'000 (Unaudited)	Nine months ended 31 December 2009 HK\$'000 (Unaudited) (Restated)
Loss of environmental protection operation for the period	-	(906)	<b>(3,567)</b>	(7,626)
Impairment loss recognised in respect of goodwill	-	-	-	(161,428)
Gain on disposal of environmental protection operation	-	-	<b>16,049</b>	-
	-	(906)	<b>12,482</b>	(169,054)

**5. DISPOSAL OF SUBSIDIARIES (Cont'd)**

(a) (Cont'd)

The results of the discontinued operation for the period were as follows:

	From 1 October 2010 to 31 December 2010 HK\$'000 (Unaudited)	Three months ended 31 December 2009 HK\$'000 (Unaudited) (Restated)	From 1 April 2010 to 31 December 2010 HK\$'000 (Unaudited)	Nine months ended 31 December 2009 HK\$'000 (Unaudited) (Restated)
Revenue	-	10,353	14,016	67,872
Cost of sales	-	(8,744)	(13,424)	(62,256)
Selling expenses	-	-	-	(4,470)
Administrative expenses	-	(1,884)	(4,644)	(8,574)
Finance costs	-	-	-	(1,599)
Impairment loss recognised in respect of goodwill	-	-	-	(161,428)
Other operating expenses	-	(2,268)	-	(4,604)
Other revenue	-	1,637	485	5,854
Gain on disposal of subsidiary	-	-	16,049	-
Profit/(loss) before tax	-	(906)	12,482	(169,205)
Income tax expense	-	-	-	151
Profit/(loss) for the period	-	(906)	12,482	(169,054)

(b) On 4 August 2010, the Group disposed of 100% owned subsidiary, Hunan IIN International Co. Limited ("Hunan IIN") to an independent third party at a minimal consideration.

Hunan IIN had no significant contribution to the turnover and results of the Group for the nine months ended 31 December 2010.

**6. DIVIDEND**

The Board does not recommend payment of a dividend for the Review Period (2009: NIL).

## 7. EARNINGS/(LOSS) PER SHARE

The calculation of the basic and diluted earnings (loss) per share attributable to the owners of the Company is based on the following information:

	Three months ended		Nine months ended	
	31 December		31 December	
	2010	2009	2010	2009
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
		(Restated)		(Restated)
<b>Earnings</b>				
Earnings for the purpose of				
basic earnings and diluted earnings				
(loss) per share	<b>12,736</b>	22,770	<b>53,482</b>	(135,517)
<b>Number of shares</b>	<b>'000</b>	<b>'000</b>	<b>'000</b>	<b>'000</b>
Weighted average number of				
ordinary shares for the basic				
earnings per share	<b>1,830,103</b>	1,688,278	<b>1,769,006</b>	1,601,964
Effect of dilutive potential ordinary shares:				
Share options	<b>18,923</b>	–	<b>35,390</b>	–
Weighted average number of ordinary				
shares for the purpose of diluted				
earnings per share	<b>1,849,026</b>	1,688,278	<b>1,804,396</b>	1,601,964

The denominator for the purposes of calculating basic loss per share for the 3 months ended 31 December 2009 and nine months ended 31 December 2009 have been adjusted to reflect the consolidation of shares in February 2010 on the basis of four shares consolidated into one share.

**7. EARNINGS/(LOSS) PER SHARE (Cont'd)****From continuing operations:**

	Three months ended		Nine months ended	
	31 December		31 December	
	2010	2009	2010	2009
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
		(Restated)		(Restated)
Profit/(loss) for the period attributable to owners of the Company	<b>12,736</b>	22,770	<b>53,482</b>	(135,517)
Less: (Profit) loss for the period from discontinued operation	-	906	<b>(12,482)</b>	169,054
Earnings for purposes of basic and diluted earnings per share from continuing operations	<b>12,736</b>	23,676	<b>41,000</b>	33,537

The denominators used are the same as those detailed above for both basic and diluted earnings per share

**From discontinued operations:**

Basic earnings (loss) per share from discontinued operations is HK\$0.70 cents per share (nine months ended 31 December 2009: HK\$(10.55) cents per share) based on profit (loss) for the period from discontinued operations of HK\$12,482,000 (nine months ended 31 December 2009: loss for the period of HK\$169,054,000) and the denominators detailed above for basic earnings (loss) per share.

The computation of diluted loss per share of the Group from continuing and discontinued operations for each of the three months and nine months ended 31 December 2009 does not assume the conversion of the Group's outstanding convertible notes and share options since their exercise would result in a decrease in loss per share from continuing and discontinued operations.

**8. CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (UNAUDITED)**

For the nine months ended 31 December 2009

	Attributable to owners of the Company											
	Share capital	Share premium	Statutory reserve	Convertible notes reserve	Capital reserve	Assets revaluation reserve	Share-based payment reserve	Exchange translation reserve	Accumulated Profit/(Losses)	Non-controlling Total interests	Total	
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
<b>At 1 April 2009 (Unaudited)</b>												
(as originally stated)	440,935	516,630	289	123,680	-	1,321	779	7,957	(207,622)	883,969	54,654	938,623
Restatement of prior periods and opening balances	-	-	-	24,440	-	-	-	(69)	(6,426)	17,945	1,377	19,322
<b>At 1 April 2009 (as restated)</b>	440,935	516,630	289	148,120	-	1,321	779	7,888	(214,048)	901,914	56,031	957,945
Loss for the period	-	-	-	-	-	-	-	-	(135,517)	(135,517)	2,484	(133,033)
Other comprehensive income (expense) for the period	-	-	-	-	-	(1,321)	-	(366)	1,319	(368)	3,912	3,544
<b>Total comprehensive income (expense)</b>	-	-	-	-	-	(1,321)	-	(366)	(134,198)	(135,885)	6,396	(129,489)
Disposal of subsidiary	-	-	-	-	-	-	-	-	-	-	(11,384)	(11,384)
Placing of new shares	85,800	-	-	-	-	-	-	-	-	85,800	-	85,800
Transaction costs attributable to placing of new shares	-	(507)	-	-	-	-	-	-	-	(507)	-	(507)
Recognition of share-based payment expenses	-	-	-	-	-	-	26,357	-	-	26,357	-	26,357
Acquisition of additional interest in a subsidiary	-	-	-	-	-	-	-	-	(6,318)	(6,318)	-	(6,318)
Appropriations	-	-	849	-	-	-	-	-	(849)	-	-	-
<b>At 31 December 2009 (as restated)</b>	526,735	516,123	1,138	148,120	-	-	27,136	7,522	(355,413)	871,361	51,043	922,404

**8. CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (UNAUDITED) (Cont'd)**

For the nine months ended 31 December 2010

	Attributable to owners of the Company											
	Share capital	Share premium	Statutory reserve	Convertible notes reserve	Capital reserve	Assets revaluation reserve	Share-based payment reserve	Exchange translation reserve	Accumulated Profit/(Losses)	Total	Non-controlling interests	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
<b>At 1 April 2010 (audited)</b>	529,387	517,867	1,139	87,910	-	-	26,240	6,713	(412,766)	756,490	45,237	801,727
Profit for the period	-	-	-	-	-	-	-	-	53,482	53,482	1,893	55,375
Other comprehensive income (expense) for the period	-	-	-	-	-	-	-	(3,222)	-	(3,222)	1,192	(2,030)
Total comprehensive income (expense)	-	-	-	-	-	-	-	(3,222)	53,482	50,260	3,085	53,345
Disposal of subsidiary	-	-	(5)	-	-	-	-	-	-	(5)	-	(5)
Exercise of share options	14,883	9,788	-	-	-	-	(8,911)	-	-	15,760	-	15,760
Conversion of convertible notes	26,871	95,384	-	(44,537)	-	-	-	-	-	77,718	-	77,718
Waiver of convertible notes	-	-	-	(18,473)	32,235	-	-	-	18,473	32,235	-	32,235
Cancellation of convertible notes	-	-	-	(24,900)	-	-	-	-	5,521	(19,379)	(19,379)	-
Grant of share options	-	-	-	-	-	-	18,922	-	-	18,922	-	18,922
Appropriations	-	-	1,517	-	-	-	-	-	(1,517)	-	-	-
<b>At 31 December 2010 (Unaudited)</b>	<b>571,141</b>	<b>623,039</b>	<b>2,651</b>	<b>-</b>	<b>32,235</b>	<b>-</b>	<b>36,251</b>	<b>3,491</b>	<b>(336,807)</b>	<b>932,001</b>	<b>48,322</b>	<b>980,323</b>

## DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS OR SHORT POSITIONS IN THE SHARE CAPITAL OF THE COMPANY AND ITS ASSOCIATED CORPORATIONS

As at 31 December 2010, the interests or short positions of the directors and the chief executive of the Company in the shares, underlying shares and debentures of the Company or its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) which will be required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short position which they are taken or deemed to have taken under such provisions of the SFO), or which will be required to be entered into the register kept under Section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to Rules 5.46 to 5.67 of the GEM Listing Rules, were as follows:

### (A) LONG POSITION IN SHARES AND EQUITY DERIVATIVES

Name of director	Capacity	Number of issued ordinary shares of US\$0.04 each in the Company held and the capacity			Aggregate interests	Approximate percentage of the aggregate interests
		Interests in shares	Approximate percentage of interests in shares	Interests under equity derivatives		
Ms. Chan Wai Kay, Katherine (Note 1)	Beneficial owner	-	-	30,750,000	40,824,000	2.23%
	Interest of spouse	10,074,000	0.55%	-		
Mr. Wu Shu Min (Note 2)	Beneficial owner	36,505,750	1.99%	28,600,000	65,105,750	3.56%
Mr. Xu Shengheng (Note 3)	Beneficial owner	608,319,000	33.23%	25,350,000	634,371,000	34.65%
	Interest of spouse	702,000	0.04%	-		
Ms. Chan Man Kuen Laura (Note 4)	Beneficial owner	1,250,000	0.07%	1,500,000	2,750,000	0.15%



Notes:

1. Ms. Chan Wai Kay Katherine ("Ms. Chan") is interested in 30,750,000 Shares issuable pursuant to exercise of share options of the Company, details of such share options can be referred to part (b) of this section and Mr. Chow Ming Joe Raymond ("Mr. Chow"), spouse of Ms. Chan, holds 10,074,000 Shares of the Company ("Shares"). Under the SFO, Ms. Chan is deemed to be interested in 10,074,000 Shares in which Mr. Chow is interested.
2. Mr. Wu Shu Min is interested in 36,505,750 Shares and 28,600,000 Shares issuable pursuant to exercise of share options of the Company, details of such share options can be referred to part (b) of this section.
3. Mr. Xu Shengheng ("Mr. Xu") is interested in 373,615,000 Shares, 25,350,000 Shares issuable pursuant to exercise of share options of the Company, details of such share options can be referred to part (b) of this section. In addition, Mr. Xu is also interested in 234,704,000 Shares pursuant to the Subscription as required to be notified to the Company and the Stock Exchange pursuant to the SFO, details of the Subscription can be referred to the Company's circular dated 21 December 2010. Subsequently, 234,704,000 Shares were allotted and issued to Mr. Xu on 18 January 2011 upon the completion of the Subscription. Ms. Luk Hoi Man ("Ms. Luk"), the spouse of Mr. Xu, holds 702,000 Shares. Therefore, under SFO, Mr. Xu is deemed to be interested in the 702,000 Shares in which Ms. Luk is interested.
4. Ms. Chan Man Kuen Laura holds 1,250,000 Shares and 1,500,000 Shares issuable pursuant to exercise of share options of the Company, details of such share options can be referred to part (b) of this section.

## (B) LONG POSITION UNDER EQUITY DERIVATIVES

(i) *The Previous Scheme*

On 22 November 2001, the Company conditionally adopted a share option scheme (the "Previous Scheme") for a period of ten years from the date on which the Previous Scheme was adopted. The Previous Scheme became unconditional on 30 November 2001. The Previous Scheme was terminated on 7 August 2010 but the provisions of the Previous Scheme shall remain in force to the extent necessary to give effect to the exercise of any options granted prior thereto or as may be required in accordance with the provisions of the Previous Scheme. As at 31 December 2010, the following directors of the Company were interested in the following options under the Previous Scheme:

Name of director	Date of grant	Exercise period	Exercise price per share HK\$	Number of share options outstanding as at 31 December 2010
Ms. Chan Wai Kay Katherine	23 June 2009	23 June 2009 to 21 December 2011	0.3304	13,750,000
Mr. Xu Shengheng	23 June 2009	23 June 2009 to 21 December 2011	0.3304	13,750,000
Mr. Wu Shu Min	7 March 2002	7 March 2002 to 21 December 2011	1.8600	2,500,000
	5 June 2003	5 June 2003 to 21 December 2011	0.3120	750,000
	23 June 2009	23 June 2009 to 21 December 2011	0.3304	13,750,000
Mr. Soo Kim Fui Jeffrey	23 June 2009	23 June 2009 to 21 December 2011	0.3304	8,750,000

Name of director	Date of grant	Exercise period	Exercise price per share HK\$	Number of
				share options outstanding as at 31 December 2010
Mr. Fu Hui Zhong	23 June 2009	23 June 2009 to 21 December 2011	0.3304	3,750,000
Mr. Jia Wenzeng	23 June 2009	23 June 2009 to 21 December 2011	0.3304	1,250,000
Mr. Chow Wan Hoi Paul	23 June 2009	23 June 2009 to 21 December 2011	0.3304	1,250,000

(ii) *The New Plan*

On 28 July 2010, the Company, by a shareholders' resolution, conditionally adopted a new share option scheme (the "New Plan") for a period of ten years from the date on which the New Plan became unconditional. On 7 August 2010, the New Plan became unconditional and effective. Pursuant to the New Plan, the board of directors was authorised, at its absolute discretion, to grant options to eligible participants, including directors of the Company or any of its subsidiaries, as defined in accordance with the terms of the New Plan, to subscribe for shares in the Company under the terms of the New Plan. As at 31 December 2010, the following directors of the Company were interested in the following options under the New Plan:

Name of director	Date of grant	Exercise period	Exercise price per share HK\$	Number of share options outstanding
				as at 31 December 2010
Ms. Chan Wai Kay Katherine	9 September 2010	9 September 2010 to 8 September 2020	0.426	17,000,000
Mr. Xu Shengheng	9 September 2010	9 September 2010 to 8 September 2020	0.426	11,600,000
Mr. Wu Shu Min	9 September 2010	9 September 2010 to 8 September 2020	0.426	11,600,000
Mr. Soo Kim Fui Jeffrey	9 September 2010	9 September 2010 to 8 September 2020	0.426	6,000,000
Mr. Fu Hui Zhong	9 September 2010	9 September 2010 to 8 September 2020	0.426	4,000,000
Ms. Chan Man Kuen Laura	9 September 2010	9 September 2010 to 8 September 2020	0.426	1,500,000
Mr. Jia Wenzeng	9 September 2010	9 September 2010 to 8 September 2020	0.426	1,500,000
Mr. Chow Wan Hoi Paul	9 September 2010	9 September 2010 to 8 September 2020	0.426	1,500,000

Save as disclosed above, as at 31 December 2010, none of the directors, chief executive of the Company or their respective associates had any interests or short positions in the shares, underlying shares and debentures of the Company or its associated corporations (within the meaning of Part XV of the SFO) which will be required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short position which they are taken or deemed to have taken under such provisions of the SFO), or which will be required to be entered into the register kept under Section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the minimum standards of dealing by directors of the Company as referred to in Rules 5.46 to 5.67 of the GEM Listing Rules.

### INTERESTS DISCLOSEABLE UNDER SFO AND SUBSTANTIAL SHAREHOLDERS

So far as is known to the directors of the Company, as at 31 December 2010, persons (other than directors or chief executive of the Company) who had interests or short positions in the shares or underlying shares of the Company which would fall to be disclosed to the Company and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO or which were required pursuant to Section 336 of the SFO, to be entered into the register referred to therein, were as follows:

#### LONG POSITIONS

Name	Capacity	Interest in shares	Percentage of interests in shares	Interests under equity derivatives	Aggregate interests	Percentage of aggregate interests
China Standard Limited (Note 1)	Beneficial owner	125,000,000	6.83%	–	125,000,000	6.83%
Financial International Holdings Ltd. (Note 2)	Beneficial owner	131,429,000	7.18%	–	131,429,000	7.18%
Grand Concord Group Ltd. (Note 2)	Beneficial owner/ Interest of controlled corporation	131,429,000	7.18%	–	131,429,000	7.18%
Luk Hoi Man (Note 3)	Beneficial owner Interest of spouse	702,000 608,319,000	0.04% 33.23%	– 25,350,000	634,371,000	34.65%

*Notes:*

1. These are the consideration shares issued to China Standard Limited pursuant to the acquisition, details of which can be referred to the Company's circular dated 3 October 2007.
2. Financial International Holdings Limited is wholly-owned by Grand Concord Group Ltd. Therefore, under SFO, Grand Concord Group Ltd. is deemed to be interested in 131,429,000 Shares.
3. Ms. Luk Hoi Man ("Ms. Luk"), the spouse of Mr. Xu Shengheng ("Mr. Xu"), holds 702,000 Shares. Mr. Xu is interested in 608,319,000 Shares and 25,350,000 Shares issuable pursuant to exercise of share options of the Company. Therefore, under SFO, Ms. Luk is deemed to be interested in 608,319,000 Shares and 25,350,000 underlying shares issuable upon the exercise of the share options of the Company in which Mr. Xu is interested.

Save as disclosed above, as at 31 December 2010, the directors of the Company were not aware of any other person (other than directors or chief executive of the Company) who had an interest or short position in the shares or underlying shares of the Company which would fall to be disclosed to the Company and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO or which were required, pursuant to Section 336 of the SFO, to be entered into the register referred to therein.

**OUTSTANDING SHARE OPTIONS**

As at 31 December 2010, options to subscribe for an aggregate of 262,817,000 shares were outstanding (including the directors of the Company as disclosed above). Details of which as at 31 December 2010 were as follows:

Date of grant of share options	As at 1 April 2010	Granted during the period	Exercised during the period	Lapsed during the period	As at 31 December 2010	Vesting period of share options	Exercise period of share options	Exercise price per share HK\$
1 March 2002	75,000	-	-	-	75,000	-	1 March 2002 to 21 December 2011	1.9000
7 March 2002	2,500,000	-	-	-	2,500,000	-	7 March 2002 to 21 December 2011	1.8600
5 June 2003	750,000	-	-	-	750,000	-	5 June 2003 to 21 December 2011	0.3120
29 May 2007	2,750,000	-	-	-	2,750,000	-	29 May 2007 to 21 December 2011	0.8560
23 June 2009	131,450,000	-	47,700,000	-	83,750,000	-	23 June 2009 to 21 December 2011	0.3304
9 September 2010	-	77,992,000	-	-	77,992,000	-	9 September 2010 to 8 September 2020	0.4260
9 September 2010	-	31,666,667	-	-	31,666,667	9 September 2010 to 8 September 2011	9 September 2010 to 8 September 2020	0.4260
9 September 2010	-	31,666,667	-	-	31,666,667	9 September 2010 to 8 September 2012	9 September 2010 to 8 September 2020	0.4260
9 September 2010	-	31,666,666	-	-	31,666,666	9 September 2010 to 8 September 2013	9 September 2010 to 8 September 2020	0.4260
	<u>137,525,000</u>	<u>172,992,000</u>	<u>47,700,000</u>		<u>- 262,817,000</u>			

## **COMPETITION AND CONFLICT OF INTERESTS**

None of the directors, the management shareholders or substantial shareholders of the Company or any of their respective associates has engaged in any business that competes or may compete with the business of the Group or has any other conflict of interests with the Group.

## **CODE ON CORPORATE GOVERNANCE PRACTICE**

The Company has complied with the code provisions of the Code on Corporate Governance Practice set out in Appendix 15 of the GEM Listing Rules throughout the Review Period.

## **AUDIT COMMITTEE**

The Company has established an audit committee with written terms of reference which deal clearly with its authority and duties. The audit committee's primary duties are to review and to supervise the financial reporting process and internal control system of the Group and to provide advice and comments to the directors of the Company.

The audit committee currently comprises three independent non-executive Directors, namely, Mr. Jia Wenzeng, Ms. Laura Chan Man Kuen and Mr. Paul Chow Wan Hoi. Mr. Jia Wenzeng is the chairman of the audit committee. The audit committee has reviewed the Group's unaudited results for the Review Period and has provided advice and comment thereon.

## **SECURITIES TRANSACTIONS BY DIRECTORS**

The Company has not adopted its own code of conduct regarding securities transactions by directors, but having made specific enquiry of all directors and the Company was not aware of any non-compliance with the required standard of dealings as set out in Rules 5.48 to 5.67 of the GEM Listing Rules and its code of conduct regarding securities transactions by directors during the Review Period.



**PURCHASE, REDEMPTION OR SALE OF LISTED SECURITIES OF THE COMPANY**

During the Review Period, neither the Company nor any of its subsidiaries purchased, redeemed or sold any of the Company's listed securities.

As at the date of this report, the Board comprises Ms. Chan Wai Kay, Katherine, Mr. Xu Shengheng, Mr. Wu Shu Min and Mr. Jeffrey Soo Kim Fui as executive Directors, Mr. Fu Hui Zhong as non-executive Director, Ms. Laura Chan Man Kuen, Mr. Jia Wenzeng and Mr. Paul Chow Wan Hoi as independent non-executive Directors.

By Order of the Board of  
**China Ground Source Energy Limited**  
**Chan Wai Kay, Katherine**  
*Chairman*

Hong Kong, 11 February 2011