

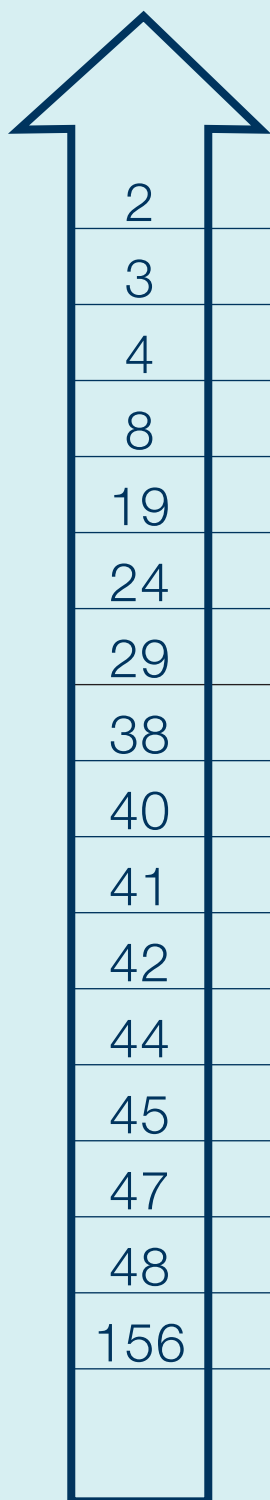


北控水務集團有限公司  
BEIJING ENTERPRISES WATER GROUP LIMITED

# *Annual Report*

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BEIJING ENTERPRISES WATER GROUP LIMITED

# ***ANNUAL REPORT 2009***

# CORPORATE INFORMATION

## BOARD OF DIRECTORS

### Executive Directors

Mr. Zhang Honghai (*Chairman*)  
Mr. Liu Kai  
Mr. E Meng  
Mr. Jiang Xinhao  
Mr. Hu Xiaoyong (*Chief Executive Officer*)  
Mr. Zhou Min  
Mr. Li Haifeng  
Ms. Qi Xiaohong  
Mr. Ju Yadong  
Mr. Zhang Tiefu

### Independent Non-executive Directors

Mr. Shea Chun Lok, Quadrant  
Mr. Zhang Gaobo  
Mr. Guo Rui  
Ms. Hang Shijun  
Mr. Wang Kaijun

## AUDIT COMMITTEE

Mr. Shea Chun Lok, Quadrant (*Chairman*)  
Mr. Guo Rui  
Mr. Zhang Gaobo

## REMUNERATION COMMITTEE

Mr. Zhang Gaobo (*Chairman*)  
Mr. Guo Rui  
Ms. Qi Xiaohong

## COMPANY SECRETARY

Mr. Tung Woon Cheung, Eric

## STOCK CODE

371

## WEBSITE

[www.bewg.com.hk](http://www.bewg.com.hk)

## REGISTERED OFFICE

Canon's Court  
22 Victoria Street  
Hamilton HM 12  
Bermuda

## HEAD OFFICE AND PRINCIPAL PLACE OF BUSINESS

Room 4301, 43/F.  
Central Plaza  
18 Harbour Road  
Wanchai  
Hong Kong  
Tel: (852) 2796 9963  
Fax: (852) 2796 9972

## PRINCIPAL SHARE REGISTRAR AND TRANSFER AGENT

Butterfield Fulcrum Group (Bermuda) Limited  
Rosebank Centre  
11 Bermudiana Road  
Pembroke HM08  
Bermuda

## HONG KONG SHARE REGISTRAR AND TRANSFER OFFICE

Tricor Tengis Limited  
26/F., Tesbury Centre  
28 Queen's Road East  
Wanchai  
Hong Kong

## AUDITORS

Ernst & Young

## PRINCIPAL BANKERS

In Hong Kong:  
China Construction Bank, Hong Kong Branch  
DBS Bank Ltd., Hong Kong Branch

In Mainland China:  
Bank of Beijing  
Bank of China  
The Industrial and Commercial Bank of China

# GROUP STRUCTURE

As at 31 December 2009



# Listed on the Main Board of The Stock Exchange of Hong Kong Limited

## CHAIRMAN'S STATEMENT



Dear Shareholders,

2009 was a marvellous year in the development of Beijing Enterprises Water Group Limited (the "Company"; together with its subsidiaries, the "Group"). The Group persists in adhering to position itself as a leading integrated water system solution provider, and continues to upkeep our "market-oriented approach, solid capital foundation, advanced technology and sound management" vision. Apart from focusing on its core business on water supply and sewage treatment business, the Group had significantly expanded in China market by means of equity interest's joint venture, equity interest acquisition, entrusted management, TOT and BOT, and further successfully promoted itself into international markets.

The Group gained recognition from the industry for being ranked the first by Chinawater.com (中國水網) among the "2009 Top Ten PRC Water Service Outstanding New Enterprises" (2009年中國水務行業十大新銳企業), second among the "2009 Top Ten Influential Enterprises in the PRC's Water Industry" (2009年中國水務行業十大影響力企業), and was short-listed as "Global Water Companies in 2009" (全球2009年度水務公司) and "2009 Top 50 Water Companies in the World" (2009年世界水務公司50強) by GWI, an international renowned water consulting institute.

### BUSINESS REVIEW

The revenue of the Group for the period from 1 January 2009 to 31 December 2009 was HK\$1,730 million. Basic earnings per share for the year was HK6.11 cents.

During the year, the Group pursued its innovative development towards market expansion, industry integration, investment and finance as well as management enhancement, thereby achieving outstanding results in all respects.

Taking advantage of our own strengths in market competition, the Group has annual newly-added water volume exceeding 2,000,000 tonnes per day, setting a new record as being the "Newly added water treatment capacity by a single enterprise in a single year" in the PRC water industry. Among which the 180,000 tonnes per day normal water recycling project in Jinzhou was the largest single normal water recycling project ever bidded in China, and the 400,000 tonnes per day Hengling sewage treatment project in Shenzhen was the largest single sewage treatment project ever bidded in China in recent years. The Group acquired the 60% operating rights of sewage treatment plants in Hainan Province, the most influential entrustment project in the PRC. This move created a new module of integrating market-oriented, intensification and specialisation of entrustment management in sewage treatment industry.

## CHAIRMAN'S STATEMENT

During the year, the Group with Yunnan Water Industry Investment Co., Ltd. (雲南省水務產業投資有限公司) had established a joint venture company named as Yunnan Beijing Enterprises City Investment Water Co., Ltd. (雲南中科城投水務有限公司) in Kunming. Aiming at expanding the water market in Yunnan Province, the Company had successfully tendered a bid on the BOT project of Kunming Konggang Sewage Treatment Plant (昆明空港污水處理廠) with a design capacity of 200,000 tonnes per day. In addition, The Group entered into a memorandum with the Malaysian government in respect of constructing sewage treatment plants. If the project could be materialised, the Group will be responsible for the design, construction and operation, thus representing the typical expansion of a PRC water enterprise into international markets by unique advantages of a "Technology with Capital".

## MANAGEMENT TEAM

The Group re-arranged the structure of Group's operating mechanism and divided its operating and management units in China into five business regions, namely Eastern China, Southern China, Western China, North-eastern China and Shandong region. Setting up the target responsibility system for each person-in-charge of business region and optimising the incentive system, the Group would monitor at its preliminary stage to be promoted as the mode of "core business moving down" as well as enhance the staff to be pro-active and efficient workers, as a result, the Group would ensure that responsibility, authority and interests were integrated in this respect.

The Group strengthened the procedures in budget planning at its preliminary stage, target performance review at its interim stage, supervising in work-in-progress, monitoring the bidding and tendering processes of construction projects, economic certification, taking stringent control of changes in design and progress on investment projects. The Group reinforced the information flow, interaction and feedback among each business region of the Group as well as second-line companies so as to timely monitor the market, construction and operation trend. With the scientific management, the Group will continuously improve its internal control and management standard.

## DEVELOPMENT STRATEGY

In 2010, the Group will continue to focus on its core businesses, including water supply, sewage treatment, normal water recycling, seawater desalination and sludge treatment, and to strengthen its management and consolidates its resources so that we will upkeep our market competitiveness and resist on any potential risk ahead.

By adopting a market-oriented approach, the Group will speed up the cultural assimilation with merger and acquisition targets and joint venture partners. We shall rationalise our business training and talent selection mechanism to provide an opportunity for every dedicated and hardworking staff to demonstrate his/her ability to be promoted at higher level position, with an aim to improve the Group's management standard as well as to optimise our management control system.

## CHAIRMAN'S STATEMENT

Besides proceeding with the Malaysian projects, we also intend to strengthen our efforts in developing projects in other overseas markets so as to support the simultaneous development of both domestic and overseas markets. At the same time, the Group will increase its recruitment on the international talents so as to protect our development in overseas markets smoothly.

The sludge treatment market is just taking off, the competitive pioneer with commanding edge in the future market will be a leader. The Group will plan proactively in 2010 to establish a team of experts in research of the sludge treatment industry, and making this field as one of key contributors in our future developments. At the same time, seawater desalination industry has already shown signs of commercialisation and marketable. The Group will import the related core technology by ways of an introduction and develop our own research as well as having the human talents and market resources in reserve for business development from time to time when opportunities arise.

The Group continues to further developing our technology innovation team by introducing and assimilating advance overseas technology as well as improving our competent research and development platform with innovative capability. We will leverage the powerful technology ability of National and Municipal Sewage Treatment and Resources Engineering Centre. On the other hand, we will co-operate with Tsinghua University to establish an international platform in research and development. The Group will maintain our leading position in research and development, new technology utilisation and equipment commercialisation within the industry through research participation in key national projects and technological integration on sewage treatment system in small-medium cities.

## FUTURE OUTLOOK

Facing the approaching low carbon economy, the PRC government continues to intensify the reform of the pricing of resources-type products and environmental protection charges, implement the price discrimination mechanism for electric and water supply for local livings, optimise the agricultural water utilisation pricing policy and reform the water sewage charging system. The above measures pave tremendous opportunities in the water industry.

Under the requirements of COD emission reduction binding indices, the PRC urban sewage treatment ratios had increased stably. By the end of 2009, the number of sewage treatment plants operating in the PRC had reached approximately 2,000 units with a design capacity of over 100 million tonnes per day. In the past 10 years, the average growth rate in capacity of sewage treatment plants was approximately 20%. With ammonia and nitrogen being included as emission assessment in the reduction indicators under the "Twelve Five-year Plan", the water market will enter into an unprecedented new era in the years to come.



## CHAIRMAN'S STATEMENT

The Group will strictly adhere to our position as the “leading integrated water system solution provider”. Through pooling together the talents and efforts of all our staff and working conscientiously, we will excel our innovative mechanism to the fullest extent and further strengthen our core competitiveness. By leveraging on our multifold strengths in investment, financing, design, research and development and management, we will be able to complete integrating the water industry business chain, realise our targets that we are pursuing in “leader in cost control, leader in technology, leader in management mechanism, leader in market development, leader in capital operation”. With this new edge, we are confident to reach new breakthrough and sustain a healthy and ever growing business.

Lastly, I would like to extend my sincere gratitude to all shareholders, customers, staff and joint venture partners for their relentless support to the Group.

**Zhang Honghai**

*Chairman*

31 March 2010

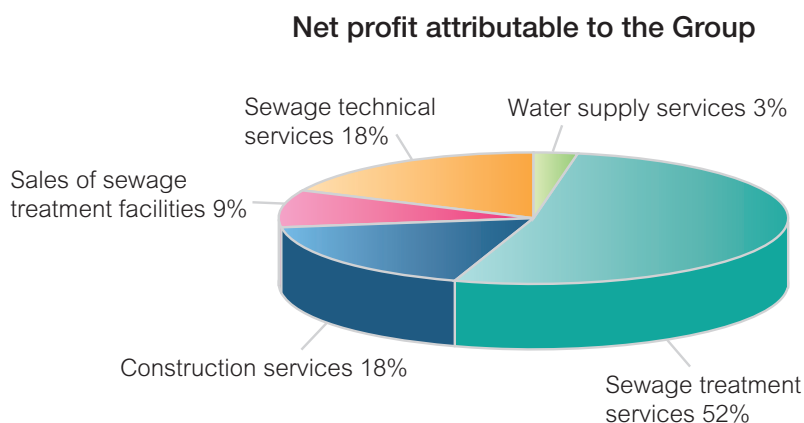
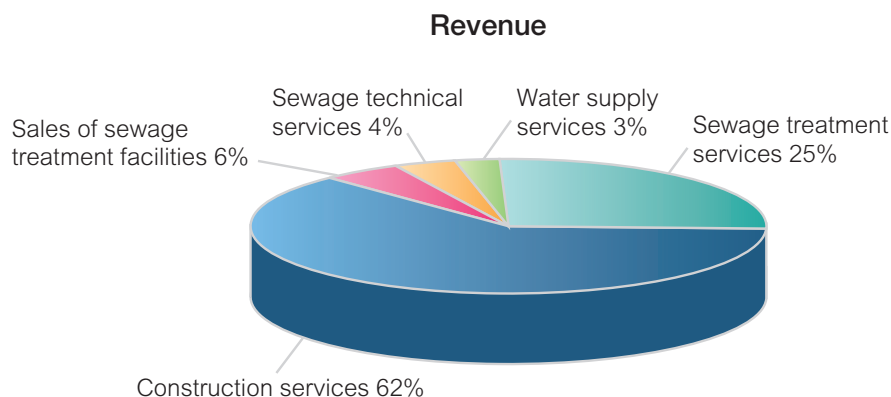
# MANAGEMENT DISCUSSION AND ANALYSIS

In order to align the financial year end date of the Company with that of its holding company, Beijing Enterprises Holdings Limited (“BEHL”), the board of directors (the “Board”) resolved to change the financial year end date of the Company from 30 June to 31 December commencing from the financial year 2008. As a result, the previous financial period covers an eighteen-month period from 1 July 2007 to 31 December 2008 (“the last period”). Accordingly, the comparative amounts presented for the consolidated income statement and the related notes, which were prepared for the period ended 31 December 2008, are not comparable.

The Year 2009 has been a fruitful year for the Group. The Group delivered strong results with total revenue of HK\$1,730.0 million, representing an increase of 5.1 times of that in last period of HK\$337.7 million. Profit attributable to shareholders of the Company recorded an impressive growth of 6.2 times from HK\$31.0 million in the last period to HK\$192.7 million. The remarkable performance of revenue and profit attributable to shareholders of the Company was mainly due to the successful strategic move to water industry. As the Group consolidated the water business since August 2008, only five months result regarding the water business was reflected last period. Whereas, full year contribution from water business was recorded this year. Apart from this, the Group’s rapid business expansion also contributed to the encouraging result this year.

## 1. FINANCIAL HIGHLIGHTS

The analysis of the Group’s financial results during the year is set out in details below:



## MANAGEMENT DISCUSSION AND ANALYSIS

|                                      | Revenue        |             | GP ratio | Net profit attributable to the Group |             |
|--------------------------------------|----------------|-------------|----------|--------------------------------------|-------------|
|                                      | HK\$'M         | %           |          | HK\$'M                               | %           |
| Sewage treatment services            | 439.7          | 25%         | 63%      | 148.0                                | 52%         |
| Water supply services                | 60.5           | 3%          | 38%      | 6.7                                  | 3%          |
| Construction services                | 1,065.8        | 62%         | 12%      | 53.0                                 | 18%         |
| Sewage technical services            | 69.2           | 4%          | 92%      | 51.7                                 | 18%         |
| Sales of sewage treatment facilities | <u>94.8</u>    | <u>6%</u>   | 25%      | <u>24.1</u>                          | <u>9%</u>   |
| Business results                     | <u>1,730.0</u> | <u>100%</u> |          | <u>283.5</u>                         | <u>100%</u> |
| Others <sup>#</sup>                  |                |             |          | <u>(90.8)</u>                        |             |
| Total                                |                |             |          | <u>192.7</u>                         |             |

# Others included the share of profit of an associate (after deduction of minority interests) of HK\$4.0 million, head office overheads of HK\$51.0 million and convertible bonds interest of HK\$43.8 million.

## 2. BUSINESS REVIEW

The principal business of the Group includes operations in sewage treatment services and water supply services, construction services, sewage technical services and sales of sewage treatment facilities. The coverage of the Group's water plants has extended to 13 provinces. As at 31 December 2009, the Group has 47 sewage treatment plants, 4 water supply plants and 3 reclaimed plants. The design capacity was increased by 2,067,100 tonnes per day to 3,597,100 tonnes per day, representing an increase of 2.4 times as compared with the capacity of 1,530,000 tonnes per day as at 31 December 2008. The increment of 2,067,100 tonnes per day includes Build-Operate-Transfer ("BOT") projects of 868,500 tonnes, Transfer-Operate-Transfer ("TOT") projects of 765,000 tonnes, Build-Transfer ("BT") and EPC projects of 92,600 tonnes, a self-owned project of 200,000 tonnes per day and an entrustment project of 141,000 tonnes per day.

# MANAGEMENT DISCUSSION AND ANALYSIS

## 2.1 Water operation services

|                               | Number<br>of plants | Design<br>capacity<br>(Tonnes/Day) | Actual<br>processing<br>capacity<br>during<br>the year<br>(Tonnes (Mil)) | Revenue<br>HK\$'(M) | Profit<br>attributable<br>to<br>shareholder<br>HK\$'(M) |
|-------------------------------|---------------------|------------------------------------|--|---------------------|---|
| Sewage treatment<br>services: |                     |                                    |  |                     |   |
| – Western                     | 8                   | 560,000                            | 115.9  | 115.0               | 40.4  |
| – Southern                    | 4                   | 530,000                            | 154.6  | 160.8               | 52.2  |
| – Shandong                    | 6                   | 255,000                            | 82.8   | 100.2               | 30.6  |
| – Eastern                     | 2                   | 170,000                            | 22.4   | 48.0                | 19.6  |
| – Northern                    | 1                   | 100,000                            | 8.7  | 15.7                | 5.2   |
|                               | 21                  | 1,615,000                          | 384.4  | 439.7               | 148.0   |
| Water supply<br>services      | 3                   | 150,000                            | 34.6   | 60.5                | 6.7   |
| Total                         | 24                  | 1,765,000                          | 419.0  | 500.2               | 154.7   |

### 2.1.1 Sewage treatment services

Sewage treatment is the Group's major source of profit. As at 31 December 2009, sewage treatment capacity of 1,615,000 tonnes per day is in operation. The average price of water treatment is approximately HK\$1.07 per tonne. The actual aggregate processing volume for the year was 384.4 million tonnes (average daily processing volume of 1,162,000 tonnes and average daily treatment rate of 72%) contributing revenue of HK\$439.7 million during the year (25% of the Group's total revenue). Net profit attributable to the Group was HK\$148.0 million. The information of sewage treatment service in China is as follows:

#### Western China

Western China is the region with the largest operating capacity in the Group. There were eight sewage treatment plants with total daily design capacity of 560,000 tonnes, representing an increase of 245,000 tonnes per day or 43.8% as compared with 315,000 tonnes per day last year. They are mainly located in Guangxi, Sichuan and Guizhou. The actual processing volume for the year was 115.9 million tonnes and operating revenue of HK\$115.0 million was recorded during the year. Net profit attributable to the Group amounted to HK\$40.4 million.

# MANAGEMENT DISCUSSION AND ANALYSIS

## Southern China

The operating volume of Southern China is 530,000 tonnes per day which is same as last year. Since projects secured during this year are mainly BOT projects, there is no increment in operating volume this year. As of 31 December 2009, the Group has four plants in this region and are mainly located in Guangdong and Hunan

provinces. The actual aggregate processing volume for the year amounted to 154.6 million tonnes and an operating revenue of HK\$160.8 million and net profit attributable to the Group of HK\$52.2 million were recorded during the year.



## Shandong

The total daily processing capacity of Shandong region is 255,000 tonnes which is same as last year. There are six plants in Shandong region. The actual processing volume for the year was 82.8 million tonnes contributing operating revenue of HK\$100.2 million during the year. Net profit attributable to the Group was HK\$30.6 million.



## Eastern China

The growth in Eastern China is encouraging this year. The total daily processing capacity increased by 130,000 tonnes to 170,000 tonnes this year, representing an increase of 4.3 times from 40,000 tonnes last year. There are 2 water plants in Eastern China. They are mainly located in Zhejiang Provinces. The actual processing

volume for the year amounted to 22.4 million tonnes and operating revenue was HK\$48.0 million during the year. Net profit attributable to the Group was HK\$19.6 million.

## Northern China

During the year, the Group started to tap into Northern China's market. Currently, the Group has secured a project in Jinzhou, Liaoning Province. The daily processing volume is 100,000 tonnes. The project has achieved actual processing volume of 8.7 million tonnes since it entered into the Group in August 2009. The operating revenue was HK\$15.7 million during this year. Net profit attributable to the Group was HK\$5.2 million.



# MANAGEMENT DISCUSSION AND ANALYSIS

## 2.1.2 Water supply services



As at 31 December 2009, the Group has three water supply plants in operation. Total water supply capacity of these projects is 150,000 tonnes per day. The acquisition of Binzhou project in last year has marked the beginning of the Group's investment in water supply market. The project is located in Shandong province with water supply capacity of 50,000 tonnes per day. During this year, the Group also acquired Guigang

project in Guangxi with water supply capacity of 100,000 tonnes per day. The aggregate actual processing volume is 34.6 million tonnes. These projects recorded revenue of HK\$60.5 million (3% of the Group's total revenue) and net profit attributable to the Group of HK\$6.7 million. The Group sees great growth potential from this sector in near future.

## 2.2 Water plants construction services

The Group has entered into a number of service concession contracts on a BOT basis in respect of its sewage treatment business. Under HK(IFRIC)-Int 12 *Service Concession Arrangements*, the Group recognises the construction revenue with reference to the fair value of the construction service delivered in the building phase. The fair value of such service is estimated on a cost-plus basis with reference to a prevailing market rate of gross margin at the inception date of service concession agreement. Construction revenue is recognised by using the percentage-of-completion method.



The Group is continuously extending its footprint throughout China. Riding on our competitive bidding strategy, we have successfully won a number of BOT bids during this year. Together with the organic growth of existing plants, the Group has kicked off the construction of various projects. During the year, twenty water plants were under construction. These water plants are mainly located in Guangdong, Sichuan, Shandong, Zhejiang, Heilongjiang and Hunan provinces. The total daily design capacity of these water plants is 1,046,500 tonnes. Changping and Qi Qi Har are our first attempt to build reclaimed water plant which requires higher treatment technologies input. Total construction revenue for BOT projects was HK\$983.5 million and net profit attributable to the Group was HK\$52.6 million. Most of these projects shall commence its operation in next year.

Apart from BOT projects, the Group also secured 2 BT ("Build-Transfer") projects in Tongling Anhui during this year. The aggregate design capacity is 85,000 tonnes. Total construction revenue from BT projects HK\$82.3 million and net profit attributable to the Group was HK\$0.4 million.

# MANAGEMENT DISCUSSION AND ANALYSIS

## 2.3 Sewage technical services

The Group, being an integrated water system solution provider in water market, has not only acquired extensive experience in bidding, building and operating waste water treatment projects, but also successfully marketed its patented treatment technology, “LIER-POOLK” to other operators. The patented treatment technology is characterised as cost-saving and has achieved the highest national emission standard – Grade 1A. Revenue from the provision of technical services was HK\$69.2 million which represents 4% of the Group’s total revenue. The net profit attributable to the Group was HK\$51.7 million.

## 2.4 Sales of sewage treatment facilities

During the year, the Group entered into a services and facilities agreement with Beijing Enterprises Holdings Environment Technology Co. Ltd (北京北控環保工程技術有限公司, “BE-Environment”) for the sales of sewage treatment related machineries and facilities to BE-Environment. BE-Environment is an indirect wholly-owned subsidiary of BEHL. Such machineries and facilities are purchased by BE-Environment for its sewage treatment project in Hai Kou City, the PRC. During the year, sewage treatment facilities of HK\$94.8 million were sold to BE-Environment. The net profit attributable to the Group was HK\$24.1 million.

## 3. FINANCIAL ANALYSIS

### 3.1 Revenue

Driven by the strong performance of water treatment business, the Group recorded a more than five times increase in revenue to HK\$1,730.0 million (Last period: HK\$337.7 million). The Group successfully transformed itself to a water service provider started from August 2008. As such, revenue for last period only represents five months result for water business. Additionally, various BOT and BT projects have been kicked off its construction work during this year and contributed an increase in construction revenue by HK\$934.5 million from HK\$131.3 million in last period to HK\$1,065.8 million for this year.

### 3.2 Cost of sales

Cost of sales for the year amounted to HK\$1,214.1 million which mainly included construction cost of HK\$939.9 million and operating cost of water plants of HK\$197.9 million. The construction cost was mainly represented by the subcontracting charges. For the operating cost of water plants, majority were electricity charges of HK\$60.4 million, staff cost of HK\$19.6 million and major overhaul charge of HK\$20.8 million. Major overhaul charge was the estimated expenditure to be incurred for the restoration of water plants before they are handed over to the grantor at the end of service arrangement. The amount was estimated based on discounted future cash outlays on major overhauls during the service concession periods. The amount was charged to income statement based on amortisation method during the service concession periods.

# MANAGEMENT DISCUSSION AND ANALYSIS

## 3.3 Gross profit margin

During the year, gross profit margin declined from 45.8% to 29.8%. The decline was mainly due to change in revenue source combination during this year. The revenue contribution from construction service increased significantly from 39% last period to 62% this year. The gross margin of construction revenue is 12% for this year, which is comparatively lower than other business sectors and therefore the gross margin of the Group decreased.

## 3.4 Other income and gains, net

The Group recorded other income of HK\$26.2 million during this year (last period: HK\$11.4 million). The increase was mainly due to sludge treatment fee income of HK\$12.8 million.

## 3.5 Administrative expenses

Administrative expenses for the year was HK\$127.0 million (last period: HK\$42.3 million). The increment was mainly contributed by the increase in staff cost by HK\$31.7 million as a result of the Group's business expansion during this year.

## 3.6 Finance costs

Finance costs was mainly represented by interest on bank and other borrowings of HK\$85.5 million (last period: HK\$28.9 million) and imputed interest on convertible bonds of HK\$43.9 million (last period: HK\$35.4 million). The imputed interest expense was resulted from accounting treatment and it did not affect the actual cashflow of the Group. Increase in interest on bank and other borrowings was due to the increase in bank borrowings for the finance of business development.

## 3.7 Income tax

Income tax expense for the year included current PRC income tax of HK\$12.0 million. The effective tax rate for PRC operation was around 4.3% which was lower than the PRC income tax rate of 25% as some of the subsidiaries enjoyed tax concession benefit. Deferred tax for the year was HK\$36.6 million.



# MANAGEMENT DISCUSSION AND ANALYSIS

## 3.8 Liquidity and financial resources

As at 31 December 2009, the Group's cash and cash equivalents amounted to HK\$876.9 million (2008: HK\$834.9 million). The Group's total borrowings amounted to HK\$3,204.3 million as at 31 December 2009 (2008: HK\$1,884.3 million), comprising convertible bonds of HK\$582.7 million (2008: HK\$669.3 million), finance lease payable of HK\$10.4 million (2008: HK\$15.9 million), and bank and other borrowings of HK\$2,611.2 million (2008: HK\$1,199.1 million). The increase in bank and other borrowings was mainly due to the increase in capital expenditure on business development during this year. Included in the balance is the bank borrowings carried in HK head office of HK\$501.4 million. The remaining balance of HK\$2,109.8 million is carried in PRC subsidiaries for the financing of construction of water plants and thus was mainly repayable in long term. Only 37% of the PRC bank and other borrowings are repayable within one year. The gearing ratio (defined as sum of bank and other borrowings and finance lease payable, net of cash and cash equivalents, divided by the total equity) was 0.58 as at 31 December 2009 (2008: 0.19). The increase in gearing ratio was mainly attributable to increase in bank and borrowings. As at 31 December 2009, the Group had banking facilities amounting to HK\$1.38 billion, of which HK\$0.88 billion were unutilised. The banking facilities are of 1-3 years term.

## 3.9 Capital expenditures

During the year, the Group's total capital expenditures were HK\$1,680.1 million (last period: HK\$271.9 million), of which HK\$71.7 million was paid for the acquisition of property, plant and equipment and intangible assets while HK\$1,477.8 million was spent on construction and acquisition of water plants and HK\$130.6 million was the consideration for acquisition of equity interest in subsidiaries. The significant increase in capital expenditures was in line with the expansion plans of the Group.

## 4. FUTURE PROSPECT

As of to date, the Group has 56 water treatment projects located in Sichuan, Shandong, Guangdong, Hunan, Zhejiang and Guangxi with a daily water treatment capacity of 4.5 million tonnes. With our rapid increase in market share, the Group was enlisted and ranked second in the "2009 Top Ten Influential Enterprises survey conducted by h2o-China.com".

In 2010, facing with opportunities and challenges, the Group could strongly feel the importance of our responsibilities and the difficult tasks ahead. However, we believe, under the strong leadership of the Board and also the support of the significant resources from BEHL, we can adhere to our market-oriented, capital-oriented, technology-oriented and management-oriented approach to consolidate our basic management, cultivate harmonious corporate culture. We will adhere to our water operation business, specify our development strategy, clarify our group structure, make progress aggressively under same mentality and ethics and to endeavour the Group to become an international "leading integrated water system solution provider".

# MANAGEMENT DISCUSSION AND ANALYSIS

## 4.1 Development Strategy in 2010:

### 4.1.1 *Adjusting our strategies and concentrating superior resources to promote principal business expansion*

In 2010, the Group has determined its marketing guideline of “concentrating superior resources to fight a war of annihilation”, to continuously promote high quality and rapid principal businesses development. The Group targets its capacity growth in 2010 at 2.48 million tonnes per day. Additionally, the Group must breakthrough in sludge treatment and seawater desalination business.

### 4.1.2 *Continuous improvement in management and optimising control system*

In 2010, the Group will take market-oriented initiatives to re-allocate corporate resources and delegation to frontline staff; implement an open capital policy to safeguard our steady business development; establish a modern corporate governance system to secure further development; create a harmonious and containment corporate culture to encourage cultural integration of acquirees and strategic partners; form comprehensive training program and promotion mechanism to provide opportunities for entrusted staff to offer their best.

Following our management guidelines and objectives in aspects of quality, environment and career health and security of “technological innovation, people-oriented, water source preservation and benefiting mankind” in 2010, we will implement management system on those areas to achieve scientification, process-based and standardisation, and together with our human-oriented principal, we could improve our organisational effectiveness.

### 4.1.3 *Adopting flexible strategies and breakthrough by merger & acquisition*

Facing the current intensifying competition in the PRC water business market and the decreasing trend in project scale, numbers of quality projects will continue to drop. As such, our development target could not be achieved through competing for projects from the market solely, and merger & acquisition will gradually become the effective means for corporate expansion in scale. With our determination on the “flexible, multi-pronged and innovative” market strategy in 2010, we will increase our resources input and strive for making breakthrough by merger & acquisition within the industry.

# MANAGEMENT DISCUSSION AND ANALYSIS

## *4.1.4 Looking into overseas market and developing international business*

On 11 November 2009, the Group entered into a memorandum with the Malaysian government in respect of around 20 sewage treatment service projects involving investment, construction and operation of sewage treatment plants and ancillary pipeline network. If such investment becomes materialised, it will pave a new start for the Group in entering into the overseas markets.

Besides implementing the Malaysian projects, we also intend to strengthen our efforts in developing projects in other overseas markets in 2010 in order to support simultaneous development of both domestic and overseas markets. At the same time, the Group will strengthen the international exposures of our human resources for protecting our smooth development in overseas markets.

## *4.1.5 Aim at emerging field and make efforts in capturing opportunities*

The sludge treatment market is just taking off, pioneers will have a leading and commanding edge in the future market. In 2010, the Group will plan proactively to establish a team of experts in sludge treatment industry, and making this field as one of key contributors in future developments. At the same time, seawater desalination industry has already shown signs of commercialisation and the market is taking shape. The Group will acquire core technology through introduction and research. We will also capture human and marketing resources in a timely manner for business development when opportunities arise.

## *4.1.6 Increasing input in research and development and reinforcing innovation*

In 2010, the Group will continue to further the development of our technology innovation team by introducing and assimilating advance overseas technology as well as improving our competent research and development platform with innovation capability. We will also leverage the powerful technology ability of National and Municipal Sewage Treatment and Resources Engineering Centre. In addition, we will cooperate with Tsinghua University to establish an international platform in research and development. The Group will maintain our leading position in research and development, new technology utilisation and equipment commercialisation within the industry through research participation in key national projects and technological integration on sewage treatment system in small-medium cities.

# MANAGEMENT DISCUSSION AND ANALYSIS

## EMPLOYEES AND REMUNERATION POLICIES

As at 31 December 2009, the Group employed 1,514 employees. The Group's remuneration packages are generally structured by reference to market terms and individual merit. Salaries are normally reviewed on an annual basis based on performance appraisals and other relevant factors.

## SIGNIFICANT INVESTMENTS AND ACQUISITIONS

During the year, the Group acquired 66.67% equity interests in Guigang Water for HK\$59.6 million. Meanwhile, the Group acquired additional 10.78% equity interest in Beijing Enterprises Z.K.C. Environmental Co., Ltd. ("BE-ZKC") for HK\$167.1 million. Apart from this, the Group had no material significant investments and acquisitions of subsidiaries and affiliated companies during the year ended 31 December 2009.

## CHARGES ON THE GROUP'S ASSETS

The secured bank loans and the finance lease payable of the Group as at 31 December 2009 are secured by the Group's equity interest in a subsidiary, certain of the Group's bank balances and mortgages over certain of the sewage treatment concession rights, land use rights and certain operating facilities of the sewage treatment plants which are under the management of the Group pursuant to the relevant service concession agreements signed with the grantors. The aforesaid land use rights and operating facilities are normally registered under the names of the relevant entities in the Group and are required to be returned to the grantors at the end of the respective service concession periods. Saved as disclosed above, the Group did not have any charges on the Group's assets.

## FOREIGN EXCHANGE EXPOSURE

The Group's exposure to currency exchange rate is minimal as majority of the subsidiaries of the Company operates in the PRC with most of the transaction denominated and settled in RMB. Accordingly, the Group has not used derivative financial instruments to hedge its foreign currency risk.

## CONTINGENT LIABILITIES

At 31 December 2009, the Group did not have any significant contingent liabilities (2008: Nil).

At 31 December 2009, corporate guarantees of RMB714,000,000 (equivalent to HK\$810,995,000) (2008: a corporate guarantee of RMB324,000,000 (equivalent to HK\$367,999,000)) were given by the Company to the banks in connection with bank loans of an equivalent amount granted to the subsidiaries of the Company.

# CORPORATE GOVERNANCE REPORT

The Company is committed to maintaining the quality of corporate governance so to ensure better transparency of the Company, protection of shareholders' and stakeholders' rights and enhance shareholder value.

In the opinion of the Board, the Company had complied with all code provisions set out in the Code on Corporate Governance Practices ("CG Code") contained in Appendix 14 of Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") during the year and up to the date of publication of this report, except for the certain deviations disclosed hereinbelow.

## BOARD OF DIRECTORS

### Composition and role

The Board currently consists of fifteen directors: comprising ten executive directors, namely, Mr. Zhang Honghai, Mr. Liu Kai, Mr. E Meng, Mr. Jiang Xinhao, Mr. Hu Xiaoyong, Mr. Zhou Min, Mr. Li Haifeng, Ms. Qi Xiaohong, Mr. Ju Yadong, Mr. Zhang Tiefu; and five independent non-executive directors ("INED(s)"), namely, Mr. Shea Chun Lok, Mr. Zhang Gaobo, Mr. Guo Rui, Ms. Hang Shijun and Mr. Wang Kaijun. One of the INEDs namely, Mr. Shea Chun Lok, has the professional and accounting qualifications required by the Listing Rules. The function of the Board is to formulate corporate strategy and business development. The Board has met regularly during the year to approve acquisition and disposal, connected transactions, placing of shares and monitoring the financial performance of the Group in pursuit of its strategic goals. Control and day to day operation of the Company is delegated to the chief executive officer and the management of the Company. There is no relationship among members of the Board in respect of financial, business, family or other material/relevant relationship.

# CORPORATE GOVERNANCE REPORT

## Board Meeting

Attendance records of the Board meetings for the year ended 31 December 2009 set out below:

| Name of Director                                | Number of meetings attended/held |
|---|----------------------------------|
| Mr. Zhang Honghai                               | 2/2                              |
| Mr. Liu Kai                                     | 1/2                              |
| Mr. E Meng                                      | 2/2                              |
| Mr. Jiang Xinhao                                | 1/2                              |
| Mr. Hu Xiaoyong                                 | 2/2                              |
| Mr. Wang Taoguang (resigned on 29 January 2010) | 2/2                              |
| Mr. Wu Xiaoming (resigned on 20 April 2009)     | 1/1                              |
| Mr. Zhou Min                                    | 2/2                              |
| Mr. Li Haifeng                                  | 2/2                              |
| Ms. Qi Xiaohong                                 | 1/2                              |
| Mr. Ju Yadong                                   | 2/2                              |
| Mr. Zhang Tiefu (appointed 20 April 2009)       | 1/1                              |
| Mr. Shea Chun Lok, Quadrant                     | 2/2                              |
| Mr. Zhang Gaobo                                 | 1/2                              |
| Mr. Guo Rui                                     | 2/2                              |
| Ms. Hang Shijun                                 | 1/2                              |
| Mr. Wang Kaijun                                 | 1/2                              |

## CHAIRMAN AND CHIEF EXECUTIVE OFFICER

The chairman of the Company is Mr. Zhang Honghai and the chief executive officer of the Company is Mr. Hu Xiaoyong. The Company has complied with code provision A.2.1 which stipulates that the roles of chairman and chief executive officer should be separate and should not be performed by the same individual.

## INDEPENDENT NON-EXECUTIVE DIRECTORS

Code provision A.4.1 of CG Code stipulates that non-executive directors should be appointed for a specific term, subject to re-election. The non-executive directors of the Company have not been appointed for a specific term as they are subject to retirement by rotation and re-election at annual general meeting in accordance with the Byelaws of the Company.

The Company has received, a written an annual confirmation from each of the INEDs confirming his independence pursuant to Rule 3.13 of the Listing Rules. The Company considers all of the INEDs are independent.

# CORPORATE GOVERNANCE REPORT

## DIRECTORS' SECURITIES TRANSACTIONS

The Company has adopted the Model Code as set out in Appendix 10 of the Listing Rules as the code of conduct in respect of securities transactions of the directors (the "Model Code"). Having made specific enquiry of all directors, the Company has confirmed that all directors have complied with the required standards set out in the Model Code and its code of conduct regarding directors' securities transactions during the year.

## CODE ON CORPORATE GOVERNANCE PRACTICES

During the year, in the opinion of the Board, the Company had complied with all code provisions set out in the CG Code, except for two code provisions under the CG Code. The Company held two full board meetings instead of at least four full board meetings during the year under review as required under code provision A.1.1. The non-executive directors of the Company were not appointed for a specific term that was deviated from the requirement under code provision A.4.1. The deviations are appropriate as the board of directors of the Company considers that it is more efficient to hold board meetings to address emerging issue as appropriate and non-executive directors are subject to retirement by rotation and re-election at an annual general meeting in accordance with the Bye-laws of the Company. As such, the Board considers that sufficient measures are in place to ensure the company's corporate governance practices are no less exacting than those set out in the CG Code.

## BOARD COMMITTEES

The Board has established two board committees to strengthen its functions and corporate governance practices, namely, Audit Committee and Remuneration Committee. The Audit Committee and the Remuneration Committee perform their specific roles in accordance with their respective written terms of reference.

The Board does not establish a nomination committee but will consider setting up one at an appropriate time. Currently all new appointments and re-appointments to the Board are subject to the approval of board members.

### Audit Committee

The Company's Audit Committee is composed of three independent non-executive directors, currently, Mr. Shea Chun Lok, Chairman (Chairman of the Audit Committee), Mr. Zhang Gaobo, and Mr. Guo Rui. The Audit Committee members performed their duties within written terms of reference formulated by the Company in accordance with the requirements of the Listing Rules.

The Audit Committee is responsible for considering all relationships between the Company and the auditing firm (including the provision of non-audit services), monitoring the integrity of the Company's financial statements, any issues arising from the audit and any other auditors may wish to raise and review of the Company's internal control and risk management.

# CORPORATE GOVERNANCE REPORT

Summary of work done during the year: Reviewed the financial statements for the period from 1 January 2009 to 30 June 2009 and for the year ended 31 December 2009, considered and approved the audit work of the auditors, and reviewed the business and financial performance of the Company and the internal control system and risk management.

The Audit Committee held two meetings during the year with an attendance rate of 100%.

## Remuneration Committee

The Company's Remuneration Committee was established in 2008. The Remuneration Committee comprises one executive director namely, Ms. Qi Xiaohong and two INEDs namely, Mr. Zhang Gaobo (Chairman of the Remuneration Committee) and Mr. Guo Rui. The Remuneration Committee members performed their duties within written terms of reference formulated by the Company in accordance with the requirements of the Listing Rules.

The Remuneration Committee is responsible of developing remuneration policies and in overseeing remuneration packages of the directors whether the emoluments offered are appropriate to the duties and performance of the respective individuals concerned. It is the Company's policy to offer remuneration packages which are competitive and sufficient to retain such individuals and no director is involved in decision of his own remuneration. The Remuneration Committee did not hold any meeting during the year under review.

## AUDITORS' REMUNERATION

The audit committee of the Company is responsible for considering the appointment of the external auditors and reviewing any non-audit functions performed by the external auditors, including whether such non-audit functions could lead to any potential material adverse effect on the Company. During the year under review, auditors' remuneration for audit services was approximately HK\$4 million and for non-audit service assignments was approximately HK\$2 million, which represented an agreed-upon procedures engagement in connection with the Group's interim financial report, tax compliance service and financial and tax due diligence services.

## INTERNAL CONTROLS

The Board has overall responsibility for the system of internal controls of the Company and for reviewing its effectiveness. The Board is committed to implementing an effective and sound internal control system to safeguard the interest of shareholders and the Group's assets. The Board has delegated to the management the implementation of the system of internal controls and reviewing of all relevant financial, operational, compliance controls and risk management functions within an established framework.



## CORPORATE GOVERNANCE REPORT

The Board has conducted a review of the effectiveness of the system of internal control of the Company. In view of strengthening the internal control system to meet with the continuous corporate and business development of the Company, the Board will conduct an internal company-wide study to review and enhance the internal control system.

### **DIRECTORS' RESPONSIBILITY STATEMENT**

The directors are responsible of the preparation of accounts for each financial period which give a true and fair view of the state of affairs of the Group and of the results and cash flows for that period. In preparing the accounts for the year ended 31 December 2009, the directors have selected suitable accounting policies and applied them consistently; adopted appropriate Hong Kong Financial Reporting Standards and Hong Kong Accounting Standards; made adjustments and estimates that are prudent and reasonable; and have prepared the accounts on a going concern basis. The directors are also responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company.

# DIRECTORS AND SENIOR MANAGEMENT

Our Board currently consists of fifteen directors, comprising ten executive directors and five independent non-executive directors.

## DIRECTORS

### Executive Directors

**Mr. Zhang Honghai** (“Mr. Zhang”), aged 57, was appointed as the Chairman and an Executive Director of the Company in May 2008. Mr. Zhang is a Vice Chairman and the Chief Executive Officer of Beijing Enterprises Holdings Limited (stock code: 392). He also serves as a director of Beijing Enterprises Group Company Limited, an executive director of Beijing Development (Hong Kong) Limited (stock code: 154) and the Chairman and a non-executive director of China Information Technology Development Limited (stock code: 8178). Mr. Zhang graduated from Peking University in 1982 and subsequently obtained a master’s degree in business studies at the International Business School of Hunan University and was awarded the title of Senior Economist. In 2008, Mr. Zhang graduated from the EMBA program of Peking University. Mr. Zhang has worked for the Beijing Municipal Government for many years. Prior to joining the Company, Mr. Zhang was the director of the Foreign Affairs Office of the People’s Government of Beijing Municipality and Hong Kong and Macao Affairs Office of the People’s Government of Beijing Municipality. Mr. Zhang is currently the Vice President of the Beijing Chinese Overseas Friendship Association. Mr. Zhang initially worked as Deputy General Manager and was then promoted to Vice Chairman and General Manager of Beijing International Trust Investment Limited during the period from 1990 to 1998, and has accumulated extensive experience in corporate management.

**Mr. Liu Kai** (“Mr. Liu”) aged 56, was appointed as an Executive Director of the Company in February 2008. He is also an Executive Director and a Vice President of Beijing Enterprises Holdings Limited (stock code: 392). He graduated from Tsinghua University with a bachelor’s degree in mechanical engineering in 1979, and later obtained a postgraduate degree in domestic economics and management and legal professional studies from the State Administration Institute. In 2007, Mr. Liu graduated from the EMBA program of Tsinghua University. Prior to joining the Company, Mr. Liu served as a Senior Executive of the Beijing Transportation Bureau and the Beijing Transportation Corporation. Mr. Liu has many years of experience in economics and management.

**Mr. E Meng** aged 51, was appointed as an Executive Director of the Company in February 2008. He is also an Executive Director and an Executive Vice President of Beijing Enterprises Holdings Limited (stock code: 392), the Chairman and an Executive Director of Beijing Development (Hong Kong) Limited (stock code: 154), and an Independent Non-executive Director of JLF Investment Company Limited (stock code: 472). Mr. E Meng graduated from China Science and Technology University with a master’s degree in engineering. He is a PRC senior accountant with the qualifications of PRC certified accountant, asset appraiser, certified real estate appraiser and tax appraiser. From 1988 to 1997, he was the Deputy Director of Beijing New Technology Development Zone and concurrently acting as the Director of the Department of Financial Auditing, the General Manager of Investment Operation Company, the chief accountant of Beijing Tianping Accounting Firm and the Deputy Director of the State-owned Assets Management Office of Beijing Haidian District. Mr. E Meng has extensive experience in economics, finance and enterprise management.

## DIRECTORS AND SENIOR MANAGEMENT

**Mr. Jiang Xinhao** (“Mr. Jiang”), aged 45, was appointed an Executive Director of the Company in June 2008. Mr. Jiang also serves as Executive Director and Vice President of Beijing Enterprises Holdings Limited (stock code: 392) and the Chief Operational Officer of Beijing Enterprises Group Company Limited. Mr. Jiang graduated from Fudan University in 1987 with a bachelor’s degree in law, and then in 1992 with a master’s degree in law. Mr. Jiang was a lecturer at Peking University between 1992 and 1994. From 1995 to 1997, Mr. Jiang was a Deputy General Manager of Jingtai Finance Company in Hong Kong, and subsequently a Director and Vice President of BHL Industrial Investment Company. From 1997 to February 2005, Mr. Jiang was a Director and the Chief Executive Officer of Tramford International Limited, a public company listed on Nasdaq. Mr. Jiang was a Manager of the investment development department of Beijing Holdings Limited and a General Manager of Beijing BHL Investment Center between May 2000 and February 2005. He served as a Policy Analyst of the Chinese State Commission of Restructuring Economic System from 1987 to 1989. Mr. Jiang has many years of experience in economics, finance and corporate management.

**Mr. Hu Xiaoyong** (“Mr. Hu”), aged 45, was appointed as a chief executive officer and an Executive Director of the Company in August 2008. Mr. Hu holds an EMBA of the Tsinghua University. He was the Vice Chairman of the China Environmental Service Industry Association (全國工商聯環境服務業商會). Mr. Hu is now the Chairman of Beijing Enterprises Z.K.C. Environmental Co., Ltd. (北控中科成環保集團有限公司).

**Mr. Zhou Min** (“Mr. Zhou”), aged 46, was appointed as an Executive Director and a Vice President of the Company in August 2008. Mr. Zhou graduated with an EMBA from the Tsinghua University and is the Vice Chairman of Mianyang Zhejiang Chamber of Commerce (綿陽市浙江商會). Mr. Zhou previously worked in the People’s Bank of China, Yongkang Branch of Zhejiang Province (浙江省人民銀行永康支行), the Industrial and Commercial Bank of China, Yongkang Branch of Zhejiang Province (浙江省工商銀行永康支行), and was the Chairman of Beijing Jingsheng Investment Company Limited (北京景盛投資有限公司). Mr. Zhou is now a Director and the Chief Financial Officer of Beijing Enterprises Z.K.C. Environmental Co., Ltd. (北控中科成環保集團有限公司).

**Mr. Li Haifeng** (“Mr. Li”), aged 39, was appointed as an Executive Director and a Vice President of the Company in August 2008. Mr. Li holds a Bachelor degree in Law from the Peking University. He was an Assistant to President of Founder Group (方正集團) and the Executive Vice President of Founder Xintiandi Software Technology Co. Ltd. (方正新天地軟件科技有限公司). Mr. Li is now the Chairman of the Supervisory Committee of Beijing Enterprises Z.K.C. Environmental Co., Ltd. (北控中科成環保集團有限公司) and a Director of China Field Development Limited, responsible for exploring business opportunities in water market in the P.R.C.

## DIRECTORS AND SENIOR MANAGEMENT

**Ms. Qi Xiaohong** (“Ms. Qi”), aged 42, was appointed as an Executive Director of the Company in May 2008 and a member of Remuneration Committee. Ms. Qi graduated from Capital Normal University and subsequently obtained a master degree in economic management at Capital University of Economics and Business. She has worked for the Beijing Municipal Government for many years. She joined Beijing Enterprises Holdings Limited in 1997 and is now an assistant to CEO and a general manager of Administration Department of Beijing Enterprises Holdings Limited, responsible for corporation administration and human resources management.

**Mr. Ju Yadong** (“Mr. Ju”), aged 57, was appointed an Executive Director of the Company in May 2008. Mr. Ju graduated from Nanjing University in 1983 and subsequently obtained a master degree when teaching, and was promoted to an associate professor. Mr. Ju has worked in fields of banking, trust funds and securities since 1992, mainly responsible for analysis of macro-economy, corporations and industries, acquisitions and mergers, market and securities as well as corporate management of owned and entrusted assets. Mr. Ju joined Beijing Enterprises Holdings Limited in 2005 as a manager of Investment Department and is responsible for research on investment projects, establishment of database, and project examination and reporting for approval. Mr. Ju has accumulated rich academic knowledge and years of practical experience in operation of capital market as well as development and management of investment projects.

**Mr. Zhang Tiefu** (“Mr. Zhang”), aged 47, was appointed as an Executive Director and a Vice President of the Company in April 2009. Mr. Zhang graduated from Jilin Industrial Institute with a bachelor’s degree of engineering in 1983. He further studied business administration in the University of International Business and Economics in 1998. He has been awarded the titles of senior engineer and senior international finance manager. Mr. Zhang served as the senior manager in China Nation Printing Materials Corporation (中國印刷物資總公司) since 1986. He joined Beijing Enterprises Holdings Limited as manager in 2001, and is concurrently acting the director and a general manager of Beijing Bei Kong Water Production Co., Ltd. (北京北控制水有限公司) and a director of Beijing Yanjing Beer Co., Ltd. (北京燕京啤酒有限公司). He has extensive experiences in economics, market development and corporate management. He joined the group in April 2009.

# DIRECTORS AND SENIOR MANAGEMENT

## Independent non-executive Directors

**Mr. Shea Chun Lok, Quadrant** (“Mr. Shea”), aged 43, was appointed as an Independent Non-Executive Director and the Chairman of audit committee of the Company in May 2002. Mr. Shea graduated from Monash University of Australia with a Bachelor Degree in Business. He is also a fellow member of CPA Australia, a member of Chartered Institute of Management Accountants, Institute of Certified Public Accountants of Singapore and Hong Kong Institute of Certified Public Accountants. Mr. Shea currently serves as Financial Controller of a main board listed company in Hong Kong. Mr. Shea has been working as a company secretary and qualified accountant in various Hong Kong main board listed companies for many years. He has substantial experience as a financial controller of listed companies.

**Mr. Zhang Gaobo** (“Mr. Zhang”), aged 45, was appointed as an Independent Non-Executive Director of the Company in May 2008. Mr. Zhang is also a member of the Audit Committee and the Chairman of the Remuneration Committee of the Company. He obtained a Bachelor’s degree in science from Henan University in 1985 and later graduated from Peking University with a master’s degree in Economics in 1988. From February 1988 to February 1991, Mr. Zhang was a deputy chief of the Policy Division of the Hainan Provincial Government. During his tenure with the Hainan Provincial Government, he was responsible for drafting of economic policies for the Hainan Provincial Government. From March 1991 to 1993, Mr. Zhang was the deputy chief of Financial Markets Administration Committee of PBOC Hainan Branch and was responsible for the regulation of financial markets in Hainan Province. From January 1992 to 1994, Mr. Zhang was the chairman of Hainan Stock Exchange Centre and had the overall responsibility for the operation of Hainan Stock Exchange Centre. Mr. Zhang is a Founding Partner and Chief Executive Officer of Oriental Patron Financial Group and is responsible for formulating the investment strategies, monitoring the investment performance and approving investment decisions for the group. Mr. Zhang is also an executive director and the Chief Executive Officer of OP Financial Investments Limited (stock code: 1140), a company listed on the Stock Exchange of Hong Kong Limited and a non-executive director of Vimetco N.V., a company listed on the London Stock Exchange.

**Mr. Guo Rui** (“Mr. Guo”), aged 42, was appointed as an Independent non-executive Director in May 2008. He is also a member of the Audit Committee and a member of the Remuneration Committee of the Company. Mr. Guo is President of Paragon Investment Co. Ltd, an investment management organisation that invests in real estate, clean energy, healthcare and pharmaceuticals, biotechnology, financial institutes, mining and manufacturing sectors. Mr. Guo also serves as director of Shanghai Xingye Investment Limited and is a former Senior Consultant of Arthur Andersen LLC from 1999 to 2001. Mr. Guo holds a bachelor degree of computer science from Peking University and a master degree of computer engineering from Northwestern University, U.S.A.

## DIRECTORS AND SENIOR MANAGEMENT

**Ms. Hang Shijun** (“Ms. Hang”), aged 68, was appointed as an Independent Non-Executive Director of the Company in August 2008. She is graduated from the Beijing Industrial University majored in Water Supply and Drainage in 1963. Ms. Hang has been working in the Beijing Municipal Engineering Design Research Institute (北京市政工程設計研究總院) since 1966 and is now the Chief Technology Officer of its Project Center. Ms. Hang is an expert in sewage treatment, solid wastes treatment and disposal as well as recycled water (reused water) technology and project.

**Mr. Wang Kaijun** (“Mr. Wang”), aged 49, was appointed as an Independent non-executive Director of the Company in August 2008. Mr. Wang holds a Doctor degree from the Environmental Technology Department of the Wageningen Agricultural University in the Netherlands. Mr. Wang previously worked as an Assistant Technology Manager of DHV Engineering Consultancy in the Netherlands and the Chief Engineer of Beijing Municipal Environmental Protection Technology Research Centre (北京市環境保護科學研究院). He is now the Assistant Officer of Beijing Water Environment Research and Facility Center (北京市水環境研究和設備中心) and the Assistant Chief Engineer of State Urban Environmental Pollution Control and Engineering Research Centre (國家城市環境污染控制工程研究中心). Mr. Wang has been working in the research, exploration and promotion of sewage control technology and policy over the years. Academically, Mr. Wang has much unique opinion and contributions on the research of hydrolysis-aerobic process theory, aerobic and anaerobic reactor theory and design, expansion control of active sludge, etc. Mr. Wang also expanded the new research fields on municipal sewage hydrolysis-aerobic treatment process, anaerobic efficient reactor, sludge treatment and disposal, livestock dejection treatment and rural environmental protection, all of which exemplified his scientific research spirit of continuous advancement and innovation.

# REPORT OF THE DIRECTORS

The directors present their report and the audited financial statements of the Group for the year ended 31 December 2009.

## PRINCIPAL ACTIVITIES

The Company is engaged in investment holding and the sale of sewage treatment facilities, and the principal subsidiaries are engaged in, where applicable, the construction of sewage and water treatment plants, sewage treatment, water treatment and distribution, the provision of technical services and licensing of technical know-how that are related to sewage treatment in China. Details of the principal activities of the principal subsidiaries are set out in note 19 to the financial statements.

## RESULTS AND DIVIDEND

The Group's profit for the year ended 31 December 2009 and the state of affairs of the Company and the Group at that date are set out in the financial statements on pages 40 to 155.

The directors do not recommend the payment of a dividend for the year ended 31 December 2009.

## SUMMARY FINANCIAL INFORMATION

A summary of the published results, assets and liabilities and equity of the Group for the last five financial years, as extracted from the audited financial statements and the annual report of the Company for the period ended 31 December 2008, is set out on page 156. This summary does not form part of the audited financial statements.

## CHARITABLE CONTRIBUTIONS

During the year, the Group made charitable contributions totalling HK\$76,000.

## MAJOR CUSTOMERS AND SUPPLIERS

During the year, the five largest customers of the Group together accounted for 40% of the Group's revenue and aggregate purchases attributable to the Group's five largest suppliers accounted for 41% of the Group's total purchases for the year. Sales to the largest customer accounted for 10% of the Group's revenue and purchases from the largest supplier accounted for 14% of the Group's purchases.

At no time during the year did a director, an associate of a director or a shareholder of the Company (which to the best knowledge of the directors owns more than 5% of the Company's share capital) have a beneficial interest in any of the Group's five largest customers or suppliers.

## PROPERTY, PLANT AND EQUIPMENT

Details of movements in the property, plant and equipment of the Company and the Group during the year are set out in note 14 to the financial statements.

# REPORT OF THE DIRECTORS

## SHARE CAPITAL AND CONVERTIBLE BONDS

Details of movements in the share capital and convertible bonds of the Company during the year, together with the reasons therefor, are set out in notes 28 and 31 to the financial statements, respectively.

## RESERVES

Details of movements in the reserves of the Company and the Group during the year are set out in note 29(b) to the financial statements and in the consolidated statement of changes in equity, respectively.

## DISTRIBUTABLE RESERVES OF THE COMPANY

At 31 December 2009, the Company's reserves available for distribution to shareholders amounted to HK\$1,947,861,000.

Under the Companies Act 1981 of Bermuda (as amended), the Company's contributed surplus account is available for distribution to the shareholders of the Company. However, the Company cannot declare or pay a dividend, or make a distribution out of these reserves if:

- (a) it is, or would after the payment be, unable to pay its liabilities as they become due; or
- (b) the realisable value of its assets would thereby be less than the aggregate of its liabilities and its issued share capital and share premium accounts.

## DIRECTORS

The directors of the Company during the year and up to the date of this report were:

### Executive Directors

Mr. Zhang Honghai (*Chairman*)

Mr. Liu Kai

Mr. E Meng

Mr. Jiang Xinhao

Mr. Hu Xiaoyong (*Chief Executive Officer*)

Mr. Wang Taoguang

(resigned on 29 January 2010)

Mr. Wu Xiaoming

(resigned on 20 April 2009)

Mr. Zhou Min

Mr. Li Haifeng

Ms. Qi Xiaohong

Mr. Ju Yadong

Mr. Zhang Tiefu

(appointed on 20 April 2009)

### Independent Non-executive Directors

Mr. Shea Chun Lok, Quadrant

Mr. Zhang Gaobo

Mr. Guo Rui

Ms. Hang Shijun

Mr. Wang Kaijun

In accordance with Bye-law 99(B) of the Company, Messrs. Jiang Xinhao, Hu Xiaoyong, Zhou Min, Li Haifeng and Zhang Gaobo shall retire by rotation from office as directors at the forthcoming annual general meeting and being eligible, offer themselves for re-election.



# REPORT OF THE DIRECTORS

## BIOGRAPHIES OF DIRECTORS AND SENIOR MANAGEMENT

The biographical details of the directors and the senior management of the Company are set out on pages 24 to 28 of this annual report.

## DIRECTORS' SERVICE CONTRACTS

None of the directors who are proposed for re-election at the forthcoming annual general meeting has a service contract with the Company or any of its subsidiaries which is not determinable by the Company within one year without payment of compensation, other than statutory compensation.

## DIRECTORS' INTERESTS AND SHORT POSITIONS IN SHARES AND UNDERLYING SHARES

At 31 December 2009, the interests and short positions of the directors and their associates in the share capital and underlying shares of the Company and its associated corporations within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO"), as recorded in the register maintained by the Company pursuant to Section 352 of the SFO, or as otherwise notified to the Company and The Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code"), were as follows:

### (i) Long positions in the shares and underlying shares of the Company

| Name of Director  | Nature of Interest                                 | Number of shares/<br>underlying shares<br>of the Company | Approximate<br>percentage<br>of the issued<br>share capital |
|-------------------|--|--|---|
| Mr. Hu Xiaoyong   | Interest of controlled corporation <i>(Note 1)</i> | 585,547,693  | 16.82%  |
| Mr. Wang Taoguang | Interest of controlled corporation <i>(Note 2)</i> | 324,152,081  | 9.31%   |
| Mr. Zhou Min      | Interest of controlled corporation <i>(Note 1)</i> | 585,547,693  | 16.82%  |

#### Notes:

- Messrs. Hu Xiaoyong and Zhou Min are interested in Tenson Investment Limited as to 52.62% and 44.93%, respectively. Tenson Investment Limited holds 129,021,081 shares and 456,526,612 underlying shares and therefore is interested in 585,547,693 shares in total.
- The share capital of Newton Finance Holdings Limited is beneficially owned as to 50% by Mr. Wang Taoguang and his spouse, Ms. Zhang Lan, respectively. Newton Finance Holdings Limited holds 125,383,413 shares and 198,768,668 underlying shares, both of whom are regarded as interested in the 324,152,081 shares in which Newton Finance Holdings Limited is interested.

## REPORT OF THE DIRECTORS

### DIRECTORS' INTERESTS AND SHORT POSITIONS IN SHARES AND UNDERLYING SHARES *(Continued)*

#### (ii) Long positions in the shares of associated corporations

| Name of Director | Number of shares of BEHL | Approximate percentage of the issued share capital<br><i>(Note)</i> |
|------------------|--------------------------|---|
| Mr. E Meng       | 30,000                   | 0.003%  |
| Mr. Jiang Xinhao | 13,000                   | 0.001%  |

*Note:* Based on the total number of issued shares of BEHL of 1,137,371,000 shares as at 31 December 2009.

Save as disclosed above, as at 31 December 2009, none of the directors or the chief executive had registered an interest or a short position in the shares, underlying shares or debentures of the Company or any of its associated corporations that was required to be recorded pursuant to Section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code.

### DIRECTORS' RIGHTS TO ACQUIRE SHARES

Saved as disclosed under the heading "Directors' interests and short positions in shares and underlying shares" above, at no time during the year were rights to acquire benefits by means of the acquisition of shares in or debentures of the Company granted to any director or their respective spouses or minor children, or were any such rights exercised by them; or was the Company, or any of its holding companies, subsidiaries and fellow subsidiaries a party to any arrangement to enable the directors to acquire such rights in any other body corporate.

### DIRECTORS' INTERESTS IN CONTRACTS OF SIGNIFICANCE

No contracts of significance to which the Company or any of its holding companies, subsidiaries and fellow subsidiaries was a party and in which a director of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year.

### SUBSTANTIAL SHAREHOLDERS

At 31 December 2009, the register of substantial shareholders maintained by the Company pursuant to Section 336 of Part XV of the SFO shows that the following shareholders had notified the Company of relevant interests in the issued share capital of the Company.

# REPORT OF THE DIRECTORS

## SUBSTANTIAL SHAREHOLDERS *(Continued)*

### Interests in the shares and underlying shares

| Name  | Number of ordinary shares and underlying shares held,<br>capacity and nature of interest |                                      |               | Percentage of<br>the Company's<br>issued share capital |
|---|--|--------------------------------------|---------------|--|
|   | Directly<br>beneficially<br>owned  | Through<br>controlled<br>corporation | Total         |  |
| Beijing Enterprises Environmental Construction Limited ("BE Environmental") | 1,997,000,000 <sup>(a)</sup>   | –                                    | 1,997,000,000 | 57.35%   |
| BEHL  | –  | 1,997,000,000 <sup>(b)</sup>         | 1,997,000,000 | 57.35%   |
| Beijing Enterprises Group (BVI) Company Limited ("BE Group BVI")            | –  | 1,997,000,000 <sup>(c)</sup>         | 1,997,000,000 | 57.35%   |
| 北京控股集團有限公司<br>("Beijing Enterprises Group")                                 | –  | 1,997,000,000 <sup>(d)</sup>         | 1,997,000,000 | 57.35%   |
| Tenson Investment Limited <sup>(e)</sup>                                    | 585,547,693  | –                                    | 585,547,693   | 16.82%   |
| Newton Finance Holdings Limited <sup>(f)</sup>                              | 324,152,081  | –                                    | 324,152,081   | 9.31%  |
| Faith Access Holdings Limited <sup>(g)</sup>                                | 203,528,540  | –                                    | 203,528,540   | 5.84%  |

# REPORT OF THE DIRECTORS

## Notes:

- (a) BE Environmental holds 1,997,000,000 shares.
- (b) BEHL is deemed to be interested in the 1,997,000,000 shares by virtue of its controlling interests in its wholly owned subsidiary, BE Environmental.
- (c) The interest disclosed includes the shares owned by BEHL as detailed in note (b). BEHL is held directly as to 36.16% by BE Group BVI. Accordingly, BE Group BVI is deemed to be interested in the shares owned by BEHL.
- (d) The interest disclosed includes the shares owned by BE Group BVI as detailed in note (c). BE Group BVI is held directly as to 100% by Beijing Enterprises Group. Accordingly, Beijing Enterprises Group is deemed to be interested in the shares held by BE Group BVI.
- (e) The share capital of Tenson Investment Limited is beneficially owned as to 52.62% by Mr. Hu Xiaoyong and as to 44.93% by Mr. Zhou Min. Tenson Investment Limited holds 129,021,081 shares and 456,526,612 underlying shares, both of whom are regarded as interested in the 585,547,693 shares in which Tenson Investment Limited is interested.
- (f) The share capital of Newton Finance Holdings Limited is beneficially owned as to 50% by Mr. Wang Taoguang and Ms. Zhang Lan, respectively. Newton Finance Holdings Limited holds 125,383,413 shares and 198,768,668 underlying shares, both of whom are regarded as interested in the 324,152,081 shares in which Newton Finance Holdings Limited is interested.
- (g) The entire share capital of Faith Access Holdings Limited is beneficially owned by Mr. Luo Dongfeng. Faith Access Holdings Limited holds 71,623,815 shares and 131,904,725 underlying shares.

## PURCHASE, SALE AND REDEMPTION OF THE COMPANY'S LISTED SECURITIES

During the year ended 31 December 2009, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities.

## EMOLUMENT POLICY

The emolument policy of the employee of the Group is set up by the Remuneration Committee on the basis of their merit, qualifications and competence.

The emoluments of the directors of the Company are decided by the Remuneration Committee, having regard to the Company's operating results, individual performance and comparable market statistics.

# REPORT OF THE DIRECTORS

## PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive rights under the Company's Bye-laws, or the laws of Bermuda, which would oblige the Company to offer new shares on a pro-rata basis to existing shareholders.

## SUFFICIENCY OF PUBLIC FLOAT

Based on the information that is publicly available to the Company and within the knowledge of the directors, at least 25% of the Company's total issued capital was held by the public as at the date of this report.

## CONNECTED TRANSACTIONS

On 30 June 2009, BE-ZKC, a non wholly-owned subsidiary indirectly held by the Company, and Hong Qiao Investment Company Limited ("Hong Qiao"), the two existing shareholders of Shenzhen Bei Kong Chuang Xin Investment Company Limited ("Bei Kong Chuang Xin"), entered into the equity interests change agreement with Bei Kong Chuang Xin, pursuant to which Hong Qiao would decrease its capital contribution to RMB33,091,950.41 whereas BE-ZKC would increase its capital contribution by RMB86,908,049.59 to RMB266,908,049.59 to maintain the registered capital of Bei Kong Chuang Xin at RMB300,000,000. In this circumstance, Hong Qiao is a connected person of the Company and the entering into of the equity interests change agreement constitutes a connected transaction for the purposes of Chapter 14A of the Listing Rules. As the applicable percentage ratios in respect of the equity interests change agreement exceed 5% but are below 25%, this transaction also constitutes a discloseable transaction under Chapter 14 of the Listing Rules. After completion of the equity interests change agreement, the shareholding of BE-ZKC and Hong Qiao in Bei Kong Chuang Xin was in proportion of 88.97% and 11.03% respectively. In consideration of Hong Qiao's further persistent contribution to Bei Kong Chuang Xin, the rights for (i) profit sharing, (ii) the priority right to subscribe for additional capital of Bei Kong Chuang Xin; (iii) the voting power at the shareholders' meeting of Bei Kong Chuang Xin and (iv) nomination of candidates for directors of Bei Kong Chuang Xin will be distributed between BE-ZKC and Hong Qiao on a 60% and 40% basis. This transaction had been approved by independent shareholders of the Company at the special general meeting held on 24 September 2009. Details of this transaction can be found on the websites of the Company and the Stock Exchange.

On 30 June 2009, the Company as the seller entered into the conditional services and facilities agreement with Beijing Enterprises Holdings Environment Technology Co., Ltd. as the purchaser, pursuant to which the purchaser had conditionally agreed to purchase the water treatment related machineries and facilities, and services for installation, setting and testing of those water treatment related machineries and facilities at the consideration of RMB83,557,400 (equivalent to approximately HK\$94,904,000) from the seller. In this circumstance, the purchaser is regarded as a connected person of the Company under the Listing Rules and the entering into of the conditional services and facilities agreement constitutes a connected transaction for the purposes of Chapter 14A of the Listing Rules. As one of the applicable percentage ratios of the services and facilities agreement exceed 25% but is below 100%, the provision of the services and facilities also constitutes a major transaction under Chapter 14 of the Listing Rules. This transaction had been approved by independent shareholders of the Company at the special general meeting held on 24 September 2009. Details of this transaction can be found on the websites of the Company and the Stock Exchange.

## REPORT OF THE DIRECTORS

On 23 December 2009, the Company as the seller entered into the services and facilities agreement with Beijing Enterprises Water Group (Hainan) Co., Ltd. as the purchaser, pursuant to which the purchaser had agreed to purchase the water treatment related machineries and facilities, and services for installation, setting and testing of those water treatment related machineries and facilities at the consideration of RMB21,300,000 (equivalent to approximately HK\$24,184,000) from the seller. In this circumstance, the purchaser is regarded as a connected person of the Company under the Listing Rules and the entering into of the services and facilities agreement constitutes a connected transaction for the purposes of Chapter 14A of the Listing Rules. As the relevant applicable percentage ratios in respect of the services and facilities agreement exceed 5% but less than 25%, the provision of the services and facilities also constitutes a discloseable transaction under Chapter 14 of the Listing Rules. This transaction had been approved by independent shareholders of the Company at the special general meeting held on 19 February 2010. Details of this transaction can be found on the websites of the Company and the Stock Exchange.

## CORPORATE GOVERNANCE

The Company is committed to maintaining high standards of corporate governance and continued to uphold a good, solid and sensible framework of corporate governance and has complied with the Code on Corporate Governance Practices as set out in Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange during the year ended 31 December 2009, except for the certain deviations. Further information on the Company's corporate governance practices is set out in the Corporate Governance Report.

## COMPLIANCE WITH THE MODEL CODE

The Company has adopted the Model Code as set out in Appendix 10 of the Listing Rules as its code of conduct regarding Directors' securities transactions. Having made specific enquiry of the directors, all of the directors have complied with, for any part of the accounting period covered by this annual report, the required standard set out in the Model Code.

## AUDITORS

Ernst & Young retire and a resolution for their re-appointment as auditors of the Company will be proposed at the forthcoming annual general meeting.

## REPORT OF THE DIRECTORS

### EVENT AFTER THE REPORTING PERIOD

Details of the significant event after the reporting period of the Group are set out in note 48 to the financial statements.

### APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements of the Group for the year ended 31 December 2009 were approved by the board of directors on 31 March 2010.

On behalf of the Board

**Zhang Honghai**

*CHAIRMAN*

Hong Kong, 31 March 2010

# INDEPENDENT AUDITORS' REPORT



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## To the shareholders of Beijing Enterprises Water Group Limited

*(Incorporated in Bermuda with limited liability)*

We have audited the financial statements of Beijing Enterprises Water Group Limited set out on pages 40 to 155, which comprise the consolidated and company statements of financial position as at 31 December 2009, and the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

## DIRECTORS' RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

The directors of the Company are responsible for the preparation and the true and fair presentation of these financial statements in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants and the disclosure requirements of the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

## AUDITORS' RESPONSIBILITY

Our responsibility is to express an opinion on these financial statements based on our audit. Our report is made solely to you, as a body, in accordance with Section 90 of the Bermuda Companies Act 1981, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free from material misstatement.



# INDEPENDENT AUDITORS' REPORT *(Continued)*

**To the shareholders of Beijing Enterprises Water Group Limited** *(Continued)*

*(Incorporated in Bermuda with limited liability)*

## **AUDITORS' RESPONSIBILITY** *(Continued)*

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and true and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

## **OPINION**

In our opinion, the financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2009 and of the Group's profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

**Ernst & Young**

*Certified Public Accountants*

Hong Kong

31 March 2010

# CONSOLIDATED INCOME STATEMENT

Year ended 31 December 2009

|   |              | Year ended<br>31 December<br>2009<br>HK\$'000 | Period from<br>1 July 2007 to<br>31 December<br>2008<br>HK\$'000 |
|---|--------------|---|--|
|   | <i>Notes</i> |   |  |
| REVENUE   | 6            | 1,730,013                                     | 337,681  |
| Cost of sales   |              | <u>(1,214,083)</u>                            | <u>(182,878)</u>   |
| Gross profit  |              | 515,930                                       | 154,803  |
| Other income and gains, net                                       | 6            | 26,178  | 11,388   |
| Selling and distribution costs                                    |              | (2,492)                                       | –  |
| Administrative expenses   |              | (127,008)                                     | (42,294)   |
| Other operating expenses, net                                     |              | <u>(14,658)</u>                               | <u>(7,677)</u>   |
| PROFIT FROM OPERATING ACTIVITIES                                  | 7            | 397,950                                       | 116,220  |
| Finance costs   | 8            | (125,132)                                     | (60,273)   |
| Share of profit/(loss) of an associate                            | 20           | <u>4,565</u>                                  | <u>(811)</u>   |
| PROFIT BEFORE TAX   |              | 277,383                                       | 55,136   |
| Income tax  | 11           | <u>(48,637)</u>                               | <u>(12,234)</u>  |
| PROFIT FOR THE YEAR/PERIOD  |              | <u>228,746</u>                                | <u>42,902</u>  |
| ATTRIBUTABLE TO:  |              |   |  |
| Shareholders of the Company                                       | 12           | 192,711                                       | 30,984   |
| Minority interests  |              | <u>36,035</u>                                 | <u>11,918</u>  |
|   |              | <u>228,746</u>                                | <u>42,902</u>  |
| EARNINGS PER SHARE ATTRIBUTABLE TO<br>SHAREHOLDERS OF THE COMPANY | 13           |   |  |
| – Basic   |              | <u>HK6.11 cents</u>                           | <u>HK3.82 cents</u>  |
| – Diluted   |              | <u>HK5.35 cents</u>                           | <u>HK3.72 cents</u>  |

# CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

Year ended 31 December 2009

|  | Year ended<br>31 December<br>2009<br><i>HK\$'000</i> | Period from<br>1 July 2007 to<br>31 December<br>2008<br><i>HK\$'000</i> |
|--|--|---|
| PROFIT FOR THE YEAR/PERIOD   | <u>228,746</u>                                       | <u>42,902</u>   |
| OTHER COMPREHENSIVE LOSS   |  |   |
| Share issue expenses   | –  | (2,968)   |
| Exchange differences on translation of foreign operations          | <u>(1,025)</u>                                       | <u>(3,997)</u>  |
| TOTAL COMPREHENSIVE LOSS FOR THE YEAR/PERIOD,<br>NET OF TAX OF NIL | <u>(1,025)</u>                                       | <u>(6,965)</u>  |
| TOTAL COMPREHENSIVE INCOME FOR THE YEAR/PERIOD                     | <u>227,721</u>                                       | <u>35,937</u>   |
| ATTRIBUTABLE TO:   |  |   |
| Shareholders of the Company  | 191,752  | 24,381  |
| Minority interests   | <u>35,969</u>  | <u>11,556</u>   |
|  | <u>227,721</u>                                       | <u>35,937</u>   |

# CONSOLIDATED STATEMENT OF FINANCIAL POSITION

31 December 2009

|   | <i>Notes</i> | 2009<br><i>HK\$'000</i> | 2008<br><i>HK\$'000</i> |
|---|--------------|-------------------------|-------------------------|
| <b>ASSETS</b>                                     |              |                         |                         |
| Non-current assets:                               |              |                         |                         |
| Property, plant and equipment                     | 14           | 232,027                 | 13,414                  |
| Prepaid land premiums                             | 15           | 27,060                  | –                       |
| Goodwill  | 16           | 1,575,451               | 1,466,915               |
| Operating concessions                             | 17           | 399,132                 | 429,589                 |
| Other intangible assets                           | 18           | 3,293                   | 1,656                   |
| Interest in an associate                          | 20           | –                       | 25,313                  |
| Available-for-sale investment                     | 21           | 454                     | 454                     |
| Amounts due from contract customers               | 23           | 1,085,700               | –                       |
| Receivables under service concession arrangements | 17           | 1,916,822               | 1,238,309               |
| Trade receivables                                 | 24           | 51,710                  | –                       |
| Prepayments, deposits and other receivables       | 25           | 205,190                 | 119,324                 |
| Deferred tax assets                               | 35           | 31,071                  | 27,112                  |
| Total non-current assets                          |              | <u>5,527,910</u>        | <u>3,322,086</u>        |
| Current assets:                                   |              |                         |                         |
| Prepaid land premiums                             | 15           | 644                     | –                       |
| Inventories                                       | 22           | 7,139                   | 4,133                   |
| Amounts due from contract customers               | 23           | 49,930                  | 200,462                 |
| Receivables under service concession arrangements | 17           | 137,443                 | 135,347                 |
| Trade receivables                                 | 24           | 99,192                  | 9,029                   |
| Prepayments, deposits and other receivables       | 25           | 710,579                 | 302,099                 |
| Restricted cash and pledged deposits              | 27           | 14,019                  | 8,066                   |
| Cash and cash equivalents                         | 27           | 876,861                 | 834,936                 |
| Total current assets                              |              | <u>1,895,807</u>        | <u>1,494,072</u>        |
| <b>TOTAL ASSETS</b>                               |              | <u><b>7,423,717</b></u> | <u><b>4,816,158</b></u> |

# CONSOLIDATED STATEMENT OF FINANCIAL POSITION *(Continued)*

31 December 2009

|   | <i>Notes</i>    | 2009<br><i>HK\$'000</i> | 2008<br><i>HK\$'000</i> |
|---|-----------------|-------------------------|-------------------------|
| EQUITY AND LIABILITIES                                    |                 |                         |                         |
| <b>Equity attributable to shareholders of the Company</b> |                 |                         |                         |
| Issued capital  | <i>28</i>       | 348,219                 | 240,507                 |
| Reserves  | <i>29(a)(i)</i> | 2,274,686               | 1,517,794               |
|   |                 | <b>2,622,905</b>        | 1,758,301               |
| <b>Minority interests</b>                                 |                 | <b>388,911</b>          | 239,656                 |
| <b>TOTAL EQUITY</b>                                       |                 | <b>3,011,816</b>        | 1,997,957               |
| Non-current liabilities:                                  |                 |                         |                         |
| Other payables and accruals                               | <i>37</i>       | 37,554                  | 69,328                  |
| Bank and other borrowings                                 | <i>30</i>       | 1,320,222               | 986,868                 |
| Convertible bonds   | <i>31</i>       | 582,737                 | 669,275                 |
| Finance lease payable                                     | <i>32</i>       | 4,743                   | 10,559                  |
| Provision for major overhauls                             | <i>33</i>       | 91,792                  | 69,006                  |
| Deferred income   | <i>34</i>       | 23,378                  | 1,178                   |
| Deferred tax liabilities                                  | <i>35</i>       | 100,305                 | 59,707                  |
| Total non-current liabilities                             |                 | <b>2,160,731</b>        | 1,865,921               |
| Current liabilities:                                      |                 |                         |                         |
| Trade payables  | <i>36</i>       | 445,227                 | 85,195                  |
| Other payables and accruals                               | <i>37</i>       | 482,551                 | 632,205                 |
| Income tax payable  |                 | 26,770                  | 17,328                  |
| Bank and other borrowings                                 | <i>30</i>       | 1,290,946               | 212,241                 |
| Finance lease payable                                     | <i>32</i>       | 5,676                   | 5,311                   |
| Total current liabilities                                 |                 | <b>2,251,170</b>        | 952,280                 |
| <b>TOTAL LIABILITIES</b>                                  |                 | <b>4,411,901</b>        | 2,818,201               |
| <b>TOTAL EQUITY AND LIABILITIES</b>                       |                 | <b>7,423,717</b>        | 4,816,158               |

Zhang Honghai  
*Director*

Zhou Min  
*Director*

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

Year ended 31 December 2009

| Attributable to shareholders of the Company      |                            |                                   |   |  |  |  |                              |                   |                                |                          |
|--|----------------------------|-----------------------------------|---|--|--|--|------------------------------|-------------------|--------------------------------|--------------------------|
| Notes  | Issued capital<br>HK\$'000 | Share premium account<br>HK\$'000 | Contributed surplus<br>HK\$'000<br>(note 29(a)(ii)) | Convertible bond equity reserve<br>HK\$'000<br>(note 31) | Exchange fluctuation reserve<br>HK\$'000 | PRC reserve funds<br>HK\$'000<br>(note 29(a)(iii)) | Retained profits<br>HK\$'000 | Total<br>HK\$'000 | Minority interests<br>HK\$'000 | Total equity<br>HK\$'000 |
|  |                            |                                   |   |  |  |  |                              |                   |                                |                          |
| At 1 July 2007                                   | 8,328                      | -                                 | (400)   | -  | 974                                      | -  | 22,534                       | 31,436            | -                              | 31,436                   |
| Total comprehensive income/(loss) for the period | -                          | (2,968)                           | -   | -  | (3,635)                                  | -  | 30,984                       | 24,381            | 11,556                         | 35,937                   |
| Issue of new shares                              | 28(a) and (b)              | 80,679                            | 768,237   | -  | -  | -  | -                            | 848,916           | -                              | 848,916                  |
| Issue of convertible bonds                       |                            | -                                 | -   | -  | 364,524                                  | -  | -                            | 364,524           | -                              | 364,524                  |
| Conversion of convertible bonds                  | 28(c)                      | 151,500                           | 460,211   | -  | (120,780)                                | -  | -                            | 490,931           | -                              | 490,931                  |
| Acquisition of subsidiaries                      | 39                         | -                                 | -   | -  | -  | -  | -                            | -                 | 228,327                        | 228,327                  |
| Disposal of subsidiaries                         | 40                         | -                                 | -   | -  | (1,887)                                  | -  | -                            | (1,887)           | -                              | (1,887)                  |
| Dividend paid to a minority shareholder          |                            | -                                 | -   | -  | -  | -  | -                            | -                 | (227)                          | (227)                    |
| Transfer to reserves                             |                            | -                                 | -   | -  | -  | 17,902   | (17,902)                     | -                 | -                              | -                        |
| At 31 December 2008 and 1 January 2009           | 240,507                    | 1,225,480*                        | (400)*  | 243,744*   | (4,548)*                                 | 17,902*  | 35,616*                      | 1,758,301         | 239,656                        | 1,997,957                |
| Total comprehensive income/(loss) for the year   | -                          | -                                 | -   | -  | (959)                                    | -  | 192,711                      | 191,752           | 35,969                         | 227,721                  |
| Issue of new shares                              | 28(b)                      | 22,668                            | 281,087   | -  | -  | -  | -                            | 303,755           | -                              | 303,755                  |
| Issue of convertible bonds                       |                            | -                                 | -   | -  | 52,439                                   | -  | -                            | 52,439            | -                              | 52,439                   |
| Conversion of convertible bonds                  | 28(c)                      | 85,044                            | 310,811   | -  | (79,197)                                 | -  | -                            | 316,658           | -                              | 316,658                  |
| Capital contributions from minority shareholders |                            | -                                 | -   | -  | -  | -  | -                            | -                 | 245,062                        | 245,062                  |
| Acquisition of subsidiaries                      | 39                         | -                                 | -   | -  | -  | -  | -                            | -                 | 50,069                         | 50,069                   |
| Acquisition of minority interests                |                            | -                                 | -   | -  | -  | -  | -                            | -                 | (177,999)                      | (177,999)                |
| Disposal of a subsidiary                         | 40                         | -                                 | -   | -  | -  | -  | -                            | -                 | (3,846)                        | (3,846)                  |
| Transfer to reserves                             |                            | -                                 | -   | -  | -  | 29,448   | (29,448)                     | -                 | -                              | -                        |
| At 31 December 2009                              | 348,219                    | 1,817,378*                        | (400)*  | 216,986*   | (5,507)*                                 | 47,350*  | 198,879*                     | 2,622,905         | 388,911                        | 3,011,816                |

\* These reserve accounts comprise the consolidated reserves of HK\$2,274,686,000 (2008: HK\$1,517,794,000) in the consolidated statement of financial position.

# CONSOLIDATED STATEMENT OF CASH FLOWS

Year ended 31 December 2009

|   | Notes | Year ended<br>31 December<br>2009<br>HK\$'000 | Period from<br>1 July 2007 to<br>31 December<br>2008<br>HK\$'000 |
|---|-------|---|--|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>   |       |   |  |
| Profit before tax   |       | 277,383                                       | 55,136   |
| Adjustments for:  |       |   |  |
| Bank interest income  | 6     | (5,789)                                       | (9,193)  |
| Dividend income from financial assets at fair value through profit or loss                    | 6     | –   | (137)  |
| Gain on disposal of financial assets at fair value through profit or loss, net                | 6     | –   | (718)  |
| Loss on disposal of items of property, plant and equipment, net                               | 7     | 53  | 17   |
| Loss on disposal of other intangible assets   | 7     | 75  | –  |
| (Gain)/loss on disposal of subsidiaries   | 7     | 2,922   | (760)  |
| Loss on disposal of an associate  | 7     | 326   | –  |
| Depreciation  | 7     | 14,370  | 1,230  |
| Amortisation of operating concessions   | 7     | 19,426  | 5,799  |
| Amortisation of other intangible assets   | 7     | 256   | 78   |
| Impairment/(reversal of impairment) of receivables under service concession arrangements, net | 7     | (408)   | 1,748  |
| Impairment/(reversal of impairment) of trade receivables, net                                 | 7     | 612   | (69)   |
| Impairment of other receivables, net  | 7     | 592   | 205  |
| Impairment of amounts due from contract customers   | 7     | 6,273   | –  |
| Provision for major overhauls   | 33    | 20,775  | 7,285  |
| Finance costs   | 8     | 132,434                                       | 65,524   |
| Share of (profit)/loss of an associate  |       | (4,565)                                       | 811  |
|   |       | <b>464,735</b>                                | <b>126,956</b>   |
| Decrease in prepaid land premiums   |       | 301   | –  |
| Decrease/(increase) in inventories  |       | 1,207   | (1,247)  |
| Increase in receivables under service concession arrangements                                 |       | (490,241)                                     | (24,376)   |
| Increase in amounts due from contract customers   |       | (829,240)                                     | (90,893)   |
| Decrease/(increase) in trade receivables  |       | (138,709)                                     | 601  |
| Increase in prepayments, deposits and other receivables                                       |       | (644,315)                                     | (341,204)  |
| Increase/(decrease) in trade payables   |       | 319,389                                       | (20,197)   |
| Increase/(decrease) in other payables and accruals  |       | 183,193                                       | (63,768)   |
| Increase in deferred income   |       | 5,946   | –  |
| Exchange adjustments  |       | (1,274)                                       | (1,204)  |
| Cash used in operations   |       | <b>(1,129,008)</b>                            | <b>(415,332)</b>   |
| Mainland China income tax paid  |       | <b>(2,662)</b>                                | <b>(2,351)</b>   |
| Net cash flows used in operating activities   |       | <b>(1,131,670)</b>                            | <b>(417,683)</b>   |

# CONSOLIDATED STATEMENT OF CASH FLOWS *(Continued)*

Year ended 31 December 2009

|   | <i>Notes</i> | <b>Year ended<br/>31 December<br/>2009<br/>HK\$'000</b> | Period from<br>1 July 2007 to<br>31 December<br>2008<br>HK\$'000 |
|---|--------------|---|--|
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>                                     |              |   |  |
| Purchases of items of property, plant and equipment                             | 14           | (61,274)  | (4,591)  |
| Purchases of operating concessions  | 17           | (44,043)  | –  |
| Purchases of other intangible assets  | 18           | (1,887)   | (522)  |
| Acquisition of subsidiaries   | 39           | 4,140   | 18,274   |
| Acquisition of minority interests   |              | (55,453)  | –  |
| Disposal of subsidiaries  | 40           | 20,708  | 9,748  |
| Proceeds from disposal of a partial interest in an associate                    |              | 2,271   | –  |
| Purchase of financial assets at fair value through profit or loss               |              | –   | (48,642)   |
| Proceeds from disposal of financial assets at fair value through profit or loss |              | –   | 49,791   |
| Increase in restricted cash and pledged deposits                                |              | (5,953)   | (7,991)  |
| Interest received   | 6            | 5,789   | 9,193  |
| Dividend received from financial assets at fair value through profit or loss    | 6            | –   | 137  |
| <b>Net cash flows from/(used in) investing activities</b>                       |              | <b>(135,702)</b>  | <b>25,397</b>  |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>                                     |              |   |  |
| Proceeds from issue of new ordinary shares                                      | 28(a)        | –   | 98,800   |
| Share issue expenses  | 28           | –   | (2,968)  |
| Issue of convertible bonds  | 31           | –   | 900,000  |
| Capital contributions by minority shareholders                                  |              | 245,062   | –  |
| New loans   |              | 1,433,380   | 504,384  |
| Repayment of loans  |              | (277,176)   | (272,251)  |
| Capital element of finance lease rental payments                                |              | (5,451)   | (714)  |
| Interest paid   |              | (85,545)  | (28,860)   |
| Interest element of finance lease rental payments                               |              | (1,015)   | (643)  |
| Dividend paid to a minority shareholder   |              | –   | (227)  |
| <b>Net cash flows from financing activities</b>                                 |              | <b>1,309,255</b>  | <b>1,197,521</b>   |
| <b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>                                |              | <b>41,883</b>   | <b>805,235</b>   |
| Cash and cash equivalents at beginning of year/period                           |              | 834,936   | 29,287   |
| Effect of foreign exchange rate changes, net                                    |              | 42  | 414  |
| <b>CASH AND CASH EQUIVALENTS<br/>AT END OF YEAR/PERIOD</b>                      | 27           | <b>876,861</b>  | <b>834,936</b>   |



# STATEMENT OF FINANCIAL POSITION

31 December 2009

|   | Notes | 2009<br>HK\$'000        | 2008<br>HK\$'000        |
|---|-------|-------------------------|-------------------------|
| <b>ASSETS</b>                               |       |                         |                         |
| Non-current assets:                         |       |                         |                         |
| Property, plant and equipment               | 14    | 321                     | 466                     |
| Interests in subsidiaries                   | 19    | <u>2,738,231</u>        | <u>2,885,694</u>        |
| Total non-current assets                    |       | <u>2,738,552</u>        | <u>2,886,160</u>        |
| Current assets:                             |       |                         |                         |
| Trade receivables                           | 24    | 85,693                  | –                       |
| Prepayments, deposits and other receivables | 25    | 586,713                 | 200                     |
| Cash and cash equivalents                   | 27    | <u>8,697</u>            | <u>15,376</u>           |
| Total current assets                        |       | <u>681,103</u>          | <u>15,576</u>           |
| <b>TOTAL ASSETS</b>                         |       | <b><u>3,419,655</u></b> | <b><u>2,901,736</u></b> |
| <b>EQUITY AND LIABILITIES</b>               |       |                         |                         |
| Equity:                                     |       |                         |                         |
| Issued capital                              | 28    | 348,219                 | 240,507                 |
| Reserves                                    | 29(b) | <u>1,947,861</u>        | <u>1,445,226</u>        |
| <b>TOTAL EQUITY</b>                         |       | <b><u>2,296,080</u></b> | <b><u>1,685,733</u></b> |
| Non-current liabilities:                    |       |                         |                         |
| Convertible bonds                           | 31    | <u>582,737</u>          | <u>669,275</u>          |
| Current liabilities:                        |       |                         |                         |
| Trade payables                              | 36    | 34,285                  | –                       |
| Other payables and accruals                 | 37    | 5,107                   | 546,728                 |
| Bank and other borrowings                   | 30    | <u>501,446</u>          | <u>–</u>                |
| Total current liabilities                   |       | <u>540,838</u>          | <u>546,728</u>          |
| <b>TOTAL LIABILITIES</b>                    |       | <b><u>1,123,575</u></b> | <b><u>1,216,003</u></b> |
| <b>TOTAL EQUITY AND LIABILITIES</b>         |       | <b><u>3,419,655</u></b> | <b><u>2,901,736</u></b> |

Zhang Honghai  
Director

Zhou Min  
Director

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 1. CORPORATE INFORMATION

Beijing Enterprises Water Group Limited (the “Company”) is a limited liability company incorporated in Bermuda and shares of which are listed on the Main Board of The Stock Exchange of Hong Kong Limited (the “Stock Exchange”).

During the year, the Company and its subsidiaries (collectively the “Group”) were involved in the following principal activities in Mainland China, the People’s Republic of China (the “PRC”):

- construction of sewage and water treatment plants and pipelines
- provision of sewage treatment services
- provision of water treatment services and distribution and sale of piped water
- sale of sewage treatment facilities
- provision of technical services and licensing of technical know-how that are related to sewage treatment

The immediate holding company of the Company is Beijing Enterprises Environmental Construction Limited (“BE Environmental”), which is incorporated in the British Virgin Islands and a wholly-owned subsidiary of Beijing Enterprises Holdings Limited (“BEHL”, a company whose shares are listed on the Main Board of the Stock Exchange). In the opinion of the directors, the ultimate holding company is 北京控股集團有限公司 (“Beijing Enterprises Group”), which is a state-owned enterprise established in the PRC and is wholly-owned by The State-owned Assets Supervision and Administration Commission of the People’s Government of Beijing Municipality.

## 2. BASIS OF PRESENTATION

The Group’s current liabilities exceeded its current assets by approximately HK\$355 million as at 31 December 2009. The directors consider that, based on the Group’s profit forecast and cash flow projection and unutilised banking facilities and on the assumption that such facilities will continue to be available from the Group’s principal bankers, the Group will have sufficient funds available to enable it to operate as a going concern. Accordingly, the financial statements have been prepared on a going concern basis which assumes, among other things, the realisation of assets and satisfaction of liabilities in the normal course of business.

Should the Group be unable to achieve the above and continue in business as a going concern, adjustments would have to be made to restate the values of assets to their recoverable amounts, to provide for further liabilities which might arise and to reclassify non-current assets and liabilities as current assets and liabilities, respectively.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.1 BASIS OF PREPARATION

These financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards (“HKFRSs”) (which include all Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards (“HKASs”) and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants (the “HKICPA”), accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention, except for financial assets at fair value through profit and loss, which have been measured at fair value. These financial statements are presented in Hong Kong dollars (“HK\$”) and all values are rounded to the nearest thousand except when otherwise indicated.

Owing to the change of the financial year end date of the Company from 30 June to 31 December with effect from 4 March 2008, the financial statements of the Company for the period ended 31 December 2008 cover a period of eighteen months from 1 July 2007 to 31 December 2008. Accordingly, the comparative amounts presented for the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows and related notes, which were prepared for the period from 1 July 2007 to 31 December 2008, are not comparable.

### Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries for the year ended 31 December 2009. Adjustments are made to bring into line any dissimilar accounting policies that may exist. The results of subsidiaries are consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases. All income, expenses and unrealised gains and losses resulting from intercompany transactions and intercompany balances within the Group are eliminated on consolidation in full.

The acquisition of subsidiaries during the year has been accounted for using the purchase method of accounting. This method involves allocating the cost of the business combinations to the fair value of the identifiable assets acquired, and liabilities and contingent liabilities assumed at the date of acquisition. The cost of the acquisition is measured at the aggregate of the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Contingent consideration is recognised if the adjustment is probable and can be measured reliably. Subsequent measurement to the contingent consideration affects goodwill.

Minority interests represent the interests of outside shareholders not held by the Group in the results and net assets of the Company’s subsidiaries. An acquisition of minority interests is accounted for using the parent entity extension method whereby the difference between the consideration and the book value of the share of the net assets acquired is recognised in the consolidated statement of financial position as goodwill or in the consolidated income statement as an excess over cost of acquisition, where appropriate.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.2 CHANGES IN ACCOUNTING POLICY AND DISCLOSURES

The Group has adopted the following new and revised HKFRSs for the first time for the current year's financial statements:

|   |  |
|---|--|
| HKFRS 1 and HKAS 27 Amendments          | Amendments to HKFRS 1 <i>First-time Adoption of HKFRSs</i> and HKAS 27 <i>Consolidated and Separate Financial Statements – Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate</i> |
| HKFRS 2 Amendments                      | Amendments to HKFRS 2 <i>Share-based Payment – Vesting Conditions and Cancellations</i>  |
| HKFRS 7 Amendments                      | Amendments to HKFRS 7 <i>Financial Instruments: Disclosures – Improving Disclosures about Financial Instruments</i>  |
| HKFRS 8                                 | <i>Operating Segments</i>  |
| HKFRS 8 Amendment*                      | Amendment to HKFRS 8 <i>Operating Segments – Disclosure of Information about Segment Assets</i> (early adopted)  |
| HKAS 1 (Revised)                        | <i>Presentation of Financial Statements</i>  |
| HKAS 18 Amendment*                      | Amendment to Appendix to HKAS 18 <i>Revenue – Determining Whether an Entity is Acting as a Principal or as an Agent</i>  |
| HKAS 23 (Revised)                       | <i>Borrowing Costs</i>   |
| HKAS 32 and HKAS 1 Amendments           | Amendments to HKAS 32 <i>Financial Instruments: Presentation</i> and HKAS 1 <i>Presentation of Financial Statements – Puttable Financial Instruments and Obligations Arising on Liquidation</i>              |
| HK(IFRIC)-Int 9 and HKAS 39 Amendments  | Amendments to HK(IFRIC)-Int 9 <i>Reassessment of Embedded Derivatives</i> and HKAS 39 <i>Financial Instruments: Recognition and Measurement – Embedded Derivatives</i>                                       |
| HK(IFRIC)-Int 13                        | <i>Customer Loyalty Programmes</i>   |
| HK(IFRIC)-Int 15                        | <i>Agreements for the Construction of Real Estate</i>  |
| HK(IFRIC)-Int 16                        | <i>Hedges of a Net Investment in a Foreign Operation</i>   |
| HK(IFRIC)-Int 18                        | <i>Transfers of Assets from Customers</i> (adopted from 1 July 2009)   |
| Improvements to HKFRSs (October 2008)** | Amendments to a number of HKFRSs   |

\* Included in *Improvements to HKFRSs 2009* (as issued in May 2009).

\*\* The Group adopted all the improvements to HKFRSs issued in October 2008 except for the amendments to HKFRS 5 *Non-current Assets Held for Sale and Discontinued Operations – Plan to Sell the Controlling Interest in a Subsidiary*, which is effective for annual periods beginning on or after 1 July 2009.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.2 CHANGES IN ACCOUNTING POLICY AND DISCLOSURES *(Continued)*

Other than as further explained below regarding the impact of Amendments to HKFRS 1 and HKAS 27, HKFRS 8 and HKAS 1 (Revised), the adoption of these new and revised HKFRSs has had no significant financial effect on these financial statements and there have been no significant changes to the accounting policies applied in these financial statements.

**(a) Amendments to HKFRS 1 *First-time Adoption of HKFRSs* and HKAS 27 *Consolidated and Separate Financial Statements – Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate***

The HKAS 27 Amendment requires all dividends from subsidiaries, jointly-controlled entities and associates to be recognised in the income statement in the parent's separate financial statements. The distinction between pre and post acquisition profits is no longer required. However, the payment of such dividends requires the Group to consider whether there is an indicator of impairment. The amendment is applied prospectively. HKAS 27 has also been amended to deal with the measurement of the cost of investments where a parent reorganises the structure of its group by establishing a new entity as its parent. As the Group is not a first-time adopter of HKFRSs, the HKFRS 1 Amendment is not applicable to the Group.

**(b) HKFRS 8 *Operating Segments***

HKFRS 8, which replaces HKAS 14 *Segment Reporting*, specifies how an entity should report information about its operating segments, based on information about the components of the entity that is available to the chief operating decision maker for the purposes of allocating resources to the segments and assessing their performance. The standard also requires the disclosure of information about the products and services provided by the segments, the geographical areas in which the Group operates, and revenue from the Group's major customers. The Group concluded that the operating segments determined in accordance with HKFRS 8 are the same as the business segments previously identified under HKAS 14. These revised disclosures, including the related revised comparative information, are shown in note 5 to the financial statements.

The Group has early adopted in these financial statements the Amendment to HKFRS 8 issued in *Improvements to HKFRSs 2009* which clarifies that segment assets need only to be reported when those assets are included in measures that are used by the chief operating decision maker.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.2 CHANGES IN ACCOUNTING POLICY AND DISCLOSURES *(Continued)*

### (c) HKAS 1 (Revised) *Presentation of Financial Statements*

HKAS 1 (Revised) introduces changes in the presentation and disclosures of financial statements. The revised standard separates owner and non-owner changes in equity. The statement of changes in equity includes only details of transactions with owners, with all non-owner changes in equity presented as a single line. In addition, this revised standard introduces the statement of comprehensive income, with all items of income and expense recognised in the income statement, together with all other items of recognised income and expense recognised directly in equity, either in one single statement, or in two linked statements. The Group has elected to present two statements.

## 3.3 ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS

The Group has not applied the following new and revised HKFRSs, that have been issued but are not yet effective, in these financial statements:

|  |  |
|--|--|
| HKFRS 1 (Revised)  | <i>First-time Adoption of Hong Kong Financial Reporting Standards</i> <sup>1</sup>   |
| HKFRS 1 Amendments   | <i>Amendments to HKFRS 1 First-time Adoption of Hong Kong Financial Reporting Standards – Additional Exemptions for First-time Adopters</i> <sup>2</sup>                         |
| HKFRS 1 Amendment  | <i>Amendments to HKFRS 1 First-time of Hong Kong Financial Reporting Standards – Limited Exemption from Comparative HKFRS 7 Disclosures for First-time Adoption</i> <sup>4</sup> |
| HKFRS 2 Amendments   | <i>Amendments to HKFRS 2 Share-based Payment – Group Cash-settled Share-based Payment Transactions</i> <sup>2</sup>  |
| HKFRS 3 (Revised)  | <i>Business Combinations</i> <sup>1</sup>  |
| HKFRS 9  | <i>Financial Instruments</i> <sup>6</sup>  |
| HKAS 24 (Revised)  | <i>Related Party Disclosures</i> <sup>5</sup>  |
| HKAS 27 (Revised)  | <i>Consolidated and Separate Financial Statements</i> <sup>1</sup>   |
| HKAS 32 Amendment  | <i>Amendment to HKAS 32 Financial Instruments: Presentation – Classification of Rights Issues</i> <sup>3</sup>   |
| HKAS 39 Amendment  | <i>Amendment to HKAS 39 Financial Instruments: Recognition and Measurement – Eligible Hedged Items</i> <sup>1</sup>  |
| HK(IFRIC)-Int 14 Amendments  | <i>Amendments to HK(IFRIC)-Int 14 Prepayments of a Minimum Funding Requirement</i> <sup>5</sup>  |
| HK(IFRIC)-Int 17   | <i>Distributions of Non-cash Assets to Owners</i> <sup>1</sup>   |
| HK(IFRIC)-Int 19   | <i>Extinguishing Financial Liabilities with Equity Instruments</i> <sup>4</sup>  |
| Amendments to HKFRS 5 included in <i>Improvements to HKFRSs</i> issued in October 2008 | <i>Amendments to HKFRS 5 Non-current Assets Held for Sale and Discontinued Operations – Plan to Sell the Controlling Interest in a Subsidiary</i> <sup>1</sup>                   |
| HK Interpretation 4 (Revised in December 2009)   | <i>Leases – Determination of the Length of Lease Term in respect of Hong Kong Land Leases</i> <sup>2</sup>   |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.3 ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS

*(Continued)*

- <sup>1</sup> *Effective for annual periods beginning on or after 1 July 2009*
- <sup>2</sup> *Effective for annual periods beginning on or after 1 January 2010*
- <sup>3</sup> *Effective for annual periods beginning on or after 1 February 2010*
- <sup>4</sup> *Effective for annual periods beginning on or after 1 July 2010*
- <sup>5</sup> *Effective for annual periods beginning on or after 1 January 2011*
- <sup>6</sup> *Effective for annual periods beginning on or after 1 January 2013*

Further information about those changes that are expected to be relevant to the Group is as follows:

- (a) HKFRS 3 (Revised) introduces a number of changes in the accounting for business combinations that will impact the amount of goodwill recognised, the reported results in the period that an acquisition occurs, and future reported results. HKAS 27 (Revised) requires that a change in the ownership interest of a subsidiary without loss of control is accounted for as an equity transaction. Therefore, such a change will have no impact on goodwill, nor will it give rise to a gain or loss. Furthermore, the revised HKAS 27 changes the accounting for losses incurred by the subsidiary as well as the loss of control of a subsidiary. Other consequential amendments were made to HKAS 7 *Statement of Cash Flows*, HKAS 12 *Income Taxes*, HKAS 21 *The Effects of Changes in Foreign Exchange Rates*, HKAS 28 *Investments in Associates* and HKAS 31 *Interests in Joint Ventures*. The Group expects to adopt HKFRS 3 (Revised) and HKAS 27 (Revised) from 1 January 2010. The changes introduced by these revised standards must be applied prospectively and will affect the accounting of future acquisitions, loss of control and transactions with minority interests.
- (b) HKFRS 9 issued in November 2009 is the first part of phase 1 of a comprehensive project to entirely replace HKAS 39 *Financial Instruments: Recognition and Measurement*. This phase focuses on the classification and measurement of financial assets. Instead of classifying financial assets into four categories, an entity shall classify financial assets as subsequently measured at either amortised cost or fair value, on the basis of both the entity's business model for managing the financial assets and the contractual cash flow characteristics of the financial assets. This aims to improve and simplify the approach for the classification and measurement of financial assets compared with the requirements of HKAS 39. HKAS 39 is aimed to be replaced by HKFRS 9 in its entirety by the end of 2010. The Group expects to adopt HKFRS 9 from 1 January 2013.
- (c) HKAS 24 (Revised) clarifies and simplifies the definition of related parties. It also provides for a partial exemption of related party disclosure to government-related entities for transactions with the same government or entities that are controlled, jointly controlled or significantly influenced by the same government. The Group expects to adopt HKAS 24 (Revised) from 1 January 2011 and is in the process of making an assessment of the impact upon the adoption of the revised standard on the Group's related party disclosures.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.3 ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS

(Continued)

- (d) HK(IFRIC)-Int 17 standardises practice in the accounting for non-reciprocal distributions of non-cash assets to owners. The Group expects to apply the interpretation from 1 January 2010 prospectively. The interpretation clarifies that (i) a dividend payable should be recognised when the dividend is appropriately authorised and is no longer at the discretion of the entity; (ii) an entity should measure the dividend payable at the fair value of the net assets to be distributed; and (iii) an entity should recognise the difference between the dividend paid and the carrying amount of the net assets distributed in the income statement. Other consequential amendments were made to HKAS 10 *Events after the Reporting Period* and HKFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*. While the adoption of the interpretation may result in changes in certain accounting policies, the interpretation is unlikely to have any significant financial impact on the Group.
- (e) The amendments to HKFRS 5 clarify that all assets and liabilities of a subsidiary shall be classified as held for sale if an entity has a sale plan involving loss of control of the subsidiary, regardless of whether the entity will retain a non-controlling interest. The Group expects to adopt the amendments from 1 January 2010. The changes must be applied prospectively and will affect future sale transactions or plans involving loss of control of a subsidiary.

Apart from the above, the HKICPA has issued *Improvements to HKFRSs 2009* in May 2009 which sets out amendments to a number of HKFRSs primarily with a view to removing inconsistencies and clarifying wording. Except for the amendment to HKAS 18 and the amendment to HKFRS 8 which were early adopted, the Group expects to adopt the amendments from 1 January 2010. There are separate transitional provisions for each standard. While the adoption of some of the amendments may result in changes in accounting policies, none of these amendments are expected to have a significant financial impact on the Group. Those amendments that are expected to be relevant to the Group are as follows:

- (a) HKFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*: Clarifies that (i) the disclosures required in respect of non-current assets (or a disposal group) classified as held for sale or a discontinued operation are those set out in HKFRS 5; (ii) the general requirements of HKAS 1 still apply (e.g., source of estimation uncertainty); and (iii) the disclosures in other HKFRSs are not required unless:
- (i) those HKFRSs specifically require disclosures in respect of non-current assets (or disposal groups) classified as held for sale or discontinued operations; or
  - (ii) the disclosures relate to the measurement of assets or liabilities within a disposal group that are outside the scope of measurement requirements of HKFRS 5 and disclosures are not disclosed elsewhere in the financial statements.



# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.3 ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS

(Continued)

- (b) HKAS 1 *Presentation of Financial Statements*: States that the terms of a liability that could result, at anytime, in its settlement by the issuance of equity instruments at the option of the counterparty do not affect its classification.
- (c) HKAS 7 *Statement of Cash Flows*: Requires that only expenditures that result in a recognised asset in the statement of financial position can be classified as a cash flow from investing activities.
- (d) HKAS 17 *Leases*: Removes the specific guidance on classifying land as a lease. As a result, leases of land should be classified as either operating or finance leases in accordance with the general guidance in HKAS 17.
- (e) HKAS 36 *Impairment of Assets*: Clarifies that the largest unit permitted for allocating goodwill acquired in a business combination is the operating segment as defined in HKFRS 8 *Operating Segments* before aggregation for financial reporting purposes.
- (f) HKAS 38 *Intangible Assets*: Clarifies that (i) if an intangible asset acquired in a business combination is identifiable only with another intangible asset, the acquirer may recognise the group of assets as a single asset provided that the individual assets have similar useful lives; and (ii) the valuation techniques presented for determining the fair value of intangible assets acquired in a business combination that are not traded in active markets are only examples and are not restrictive on the methods that can be used.

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Subsidiaries

A subsidiary is an entity whose financial and operating policies the Company controls, directly or indirectly, so as to obtain benefits from its activities.

The results of subsidiaries are included in the Company's income statement to the extent of dividends received and receivable. The Company's interests in subsidiaries are stated at cost less any accumulated impairment losses.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### Joint ventures

A joint venture is an entity set up by contractual arrangement, whereby the Group and other parties undertake an economic activity. The joint venture operates as a separate entity in which the Group and the other parties have an interest.

The joint venture agreement between the venturers stipulates the capital contributions of the joint venture parties, the duration of the joint venture and the basis on which the assets are to be realised upon its dissolution. The profits and losses from the joint venture's operations and any distributions of surplus assets are shared by the venturers, either in proportion to their respective capital contributions, or in accordance with the terms of the joint venture agreement.

A joint venture is treated as:

- (a) a subsidiary, if the Group/Company has unilateral control, directly or indirectly, over the joint venture;
- (b) a jointly-controlled entity, if the Group/Company does not have unilateral control, but has joint control, directly or indirectly, over the joint venture;
- (c) an associate, if the Group/Company does not have unilateral or joint control, but holds, directly or indirectly, generally not less than 20% of the joint venture's registered capital and is in a position to exercise significant influence over the joint venture; or
- (d) an equity investment accounted for in accordance with HKAS 39, if the Group/Company holds, directly or indirectly, less than 20% of the joint venture's registered capital and has neither joint control of, nor is in a position to exercise significant influence over the joint venture.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### Associate

An associate is an entity, not being a subsidiary or a jointly-controlled entity, in which the Group has a long term interest of generally not less than 20% of the equity voting rights and over which it is in a position to exercise significant influence.

The Group's interest in an associate is stated in the consolidated statement of financial position at the Group's share of net assets under the equity method of accounting, less any accumulated impairment losses. The Group's share of the post-acquisition results and reserves of the associate is included in the consolidated income statement and consolidated reserves, respectively. Unrealised gains and losses resulting from transactions between the Group and its associate are eliminated to the extent of the Group's interest in the associate, except where unrealised losses provide evidence of an impairment of the asset transferred. Adjustments are made to bring into line any dissimilar accounting policies that may exist.

### Related parties

A party is considered to be related to the Group if:

- (a) the party, directly or indirectly through one or more intermediaries, (i) controls, is controlled by, or is under common control with, the Group; (ii) has an interest in the Group that gives it significant influence over the Group; or (iii) has joint control over the Group;
- (b) the party is an associate;
- (c) the party is a member of the key management personnel of the Group or its holding companies;
- (d) the party is a close member of the family of any individual referred to in (a) or (c); or
- (e) the party is an entity that is controlled, jointly controlled or significantly influenced by or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (c) or (d).

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### **Goodwill**

Goodwill arising on the acquisition of subsidiaries represents the excess of the cost of the business combination over the Group's interest in the net fair value of the acquirees' identifiable assets acquired, and liabilities and contingent liabilities assumed as at the date of acquisition.

Goodwill arising on acquisition is recognised in the consolidated statement of financial position as an asset, initially measured at cost and subsequently at cost less any accumulated impairment losses.

The carrying amount of goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. The Group performs its annual impairment test of goodwill as at 31 December. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units.

Impairment is determined by assessing the recoverable amount of the cash-generating unit (group of cash-generating units) to which the goodwill relates. Where the recoverable amount of the cash-generating unit (group of cash-generating units) is less than the carrying amount, an impairment loss is recognised. An impairment loss recognised for goodwill is not reversed in a subsequent period.

Where goodwill forms part of a cash-generating unit (group of cash-generating units) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

### **Property, plant and equipment and depreciation**

Property, plant and equipment, other than construction in progress, are stated at cost less accumulated depreciation and any accumulated impairment losses.

The cost of an item of property, plant and equipment comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditure incurred after items of property, plant and equipment have been put into operation, such as repairs and maintenance, is normally charged to the income statement in the period in which it is incurred. In situations where the recognition criteria are satisfied, the expenditure for a major inspection is capitalised in the carrying amount of the asset as a replacement. Where significant parts of property, plant and equipment are required to be replaced at intervals, the Group recognises such parts as individual assets with specific useful lives and depreciation.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### **Property, plant and equipment and depreciation** *(Continued)*

Depreciation is calculated on the straight-line basis to write off the cost of each item of property, plant and equipment to its estimated residual value over its estimated useful life. The estimated useful lives of different categories of property, plant and equipment are as follows:

|  |   |
|--|---|
| Buildings                                | 15 to 35 years  |
| Leasehold improvements                   | Over the lease terms or 5 years, whichever is shorter |
| Sewage and water pipelines               | 10 to 20 years  |
| Machinery                                | 5 to 10 years   |
| Furniture, fixtures and office equipment | 5 to 10 years   |
| Motor vehicles                           | 3 to 10 years   |

Where parts of an item of property, plant and equipment have different useful lives, the cost of that item is allocated on a reasonable basis among the parts and each part is depreciated separately.

Residual values, useful lives and the depreciation method are reviewed, and adjusted if appropriate, at least at each financial year/period end.

An item of property, plant and equipment and any significant part initially recognised is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss on disposal or retirement recognised in the income statement in the period the asset is derecognised is the difference between the net sales proceeds and the carrying amount of the relevant asset.

Construction in progress represents sewage and water pipelines, buildings, structures, and machinery under construction or installation, and construction materials. Construction in progress is stated at cost less any accumulated impairment losses, and is not depreciated. Cost comprises direct costs of construction, installation and testing as well as capitalised borrowing costs on related borrowed funds during the period of construction or installation. Construction in progress is reclassified to the appropriate category of property, plant and equipment when completed and ready for use.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### **Operating leases**

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. Where the Group is the lessor, rentals receivable under the operating leases are credited to the income statement on the straight-line basis over the lease terms. Where the Group is the lessee, rentals payable under the operating leases are charged to the income statement on the straight-line basis over the lease terms.

Prepaid land premiums under operating leases are initially stated at cost and subsequently amortised on the straight-line basis over the lease terms.

### **Service concession arrangements**

#### *Consideration given by the grantor*

A financial asset (receivable under service concession arrangement) is recognised to the extent that (a) the Group has an unconditional right to receive cash or another financial asset from or at the direction of the grantor for the construction services rendered and/or the consideration paid and payable by the Group for the right to charge users of the public service; and (b) the grantor has little, if any, discretion to avoid payment, usually because the agreement is enforceable by law. The Group has an unconditional right to receive cash if the grantor contractually guarantees to pay the Group (a) specified or determinable amounts or (b) the shortfall, if any, between amounts received from users of the public service and specified or determinable amounts, even if the payment is contingent on the Group ensuring that the infrastructure meets specified quality of efficiency requirements. The financial asset (receivable under service concession arrangement) is accounted for in accordance with the policy set out for "Investments and other financial assets" below.

An intangible asset (operating concession) is recognised to the extent that the Group receives a right to charge users of the public service, which is not an unconditional right to receive cash because the amounts are contingent on the extent that the public uses the service. The intangible asset (operating concession) is accounted for in accordance with the policy set out for "Intangible assets (other than goodwill)" below.

If the Group is paid partly by a financial asset and partly by an intangible asset, in which case, each component of the consideration is accounted for separately and the consideration received or receivable for both components shall be recognised initially at the fair value of the consideration received or receivable.

#### *Construction or upgrade services*

Revenue and costs relating to construction or upgrade services are accounted for in accordance with the policy set out for "Construction contracts" below.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### **Service concession arrangements** *(Continued)*

#### *Operating services*

Revenue and costs relating to operating services are accounted for in accordance with the policy for “Revenue recognition” below.

#### *Contractual obligations to restore the infrastructure to a specified level of serviceability*

The Group has contractual obligations which it must fulfil as a condition of its licence, that is (a) to maintain the sewage and water treatment plants it operates to a specified level of serviceability and/or (b) to restore the plants to a specified condition before they are handed over to the grantor at the end of the service concession arrangement. These contractual obligations to maintain or restore the sewage and water treatment plants, except for upgrade element, are recognised and measured in accordance with the policy set out for “Provisions” below.

### **Intangible assets (other than goodwill)**

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is the fair value as at the date of acquisition. The useful lives of intangible assets are assessed to be either finite or indefinite.

Intangible assets with finite lives are subsequently amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at each financial year/period end.

Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash-generating unit level. Such intangible assets are not amortised. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is accounted for on a prospective basis.

An intangible asset is derecognised on disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss on disposal or retirement recognised in the income statement in the period the intangible asset is derecognised is the difference between the net sales proceeds and the carrying amount of the relevant intangible asset.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### **Intangible assets (other than goodwill)** *(Continued)*

#### *Operating concessions*

Operating concessions represent the rights to operate sewage and water treatment plants and are stated at cost less accumulated amortisation and any accumulated impairment losses. Amortisation is provided on the straight-line basis over the respective periods of the operating concessions granted to the Group of 20 to 40 years.

#### *Patents*

Purchased patents are stated at cost less accumulated amortisation and any accumulated impairment losses. Amortisation is provided on the straight-line basis over their estimated useful lives of 10 years.

#### *Computer software*

Computer software is stated at cost less accumulated amortisation and any accumulated impairment losses. Amortisation is provided on the straight-line basis over the estimated useful life of 5 years.

#### *Research and development costs*

All research costs are charged to the income statement as incurred.

Expenditure incurred on projects to develop new products is capitalised and deferred only when the Group can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale, its intention to complete and its ability to use or sell the asset, how the asset will generate future economic benefits, the availability of resources to complete the project and the ability to measure reliably the expenditure during the development. Product development expenditure which does not meet these criteria is expensed when incurred.



# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### **Impairment of non-financial assets other than goodwill**

Where an indication of impairment exists, or when annual impairment testing for an asset is required (other than goodwill, deferred tax assets, financial assets, inventories and amounts due from contract customers), the asset's recoverable amount is estimated. An asset's recoverable amount is the higher of the asset's or cash-generating unit's value in use and its fair value less costs to sell, and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case the recoverable amount is determined for the cash-generating unit to which the asset belongs.

An impairment loss is recognised only if the carrying amount of an asset exceeds its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. An impairment loss is charged to the income statement in the period in which it arises.

An assessment is made at the end of each reporting period as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such an indication exists, the recoverable amount is estimated. A previously recognised impairment loss of a non-financial asset other than goodwill is reversed only if there has been a change in the estimates used to determine the recoverable amount of that asset, but not to an amount higher than the carrying amount that would have been determined (net of any depreciation/amortisation) had no impairment loss been recognised for the asset in prior periods. A reversal of such an impairment loss is credited to the income statement in the period in which it arises.

### **Investments and other financial assets**

#### *Initial recognition and measurement*

Financial assets within the scope of HKAS 39 are classified as financial assets at fair value through profit or loss, loans and receivables and an available-for-sale investment, as appropriate. The Group determines the classification of its financial assets at initial recognition. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs.

All regular way purchases and sales of financial assets are recognised on the trade date, that is, the date that the Group commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### **Investments and other financial assets** *(Continued)*

#### *Subsequent measurement*

The subsequent measurement of financial assets depends on their classification as follows:

- (a) Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss are financial assets held for trading. Financial assets are classified as held for trading if they are acquired for the purpose of sale in the near term. Gains or losses on investments held for trading are recognised in the income statement. Financial assets at fair value through profit or loss are carried in the statement of financial position at fair value with changes in fair value recognised in “Other income and gains, net” or “Other operating expenses, net” in the income statement. These net fair value changes do not include any dividends on these financial assets, which are recognised in accordance with the policy set out for “Revenue recognition” below.

- (b) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, such assets are subsequently measured at amortised cost using the effective interest rate method less any allowance for impairment. Amortised cost is calculated taking into account any discount or premium on acquisition and includes fees or costs that are an integral part of the effective interest rate. The effective interest rate amortisation is included in “Revenue” or “Other income and gains, net”, as appropriate, in the income statement. The loss arising from impairment is recognised in “Other operating expenses, net” in the income statement.

- (c) Available-for-sale investment

Available-for-sale investment is a non-derivative financial asset in an unlisted equity investment that is designated as available for sale. After initial recognition, the available-for-sale investment is stated at cost less any accumulated impairment losses as the fair value of the unlisted investment cannot be reliably measured, which is because (a) the variability in the range of reasonable fair value estimates is significant for that investment or (b) the probabilities of the various estimates within the range cannot be reasonably assessed and used in estimating fair value.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### **Impairment of financial assets**

The Group assesses at the end of each reporting period whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred “loss event”) and that loss event has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that a debtor or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and observable data indicating that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

#### *Financial assets carried at amortised cost*

For financial assets carried at amortised cost, the Group first assesses individually whether objective evidence of impairment exists for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset’s carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not yet been incurred). The present value of the estimated future cash flows is discounted at the financial asset’s original effective interest rate (i.e., the effective interest rate computed at initial recognition). If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate.

The carrying amount of the asset is reduced either directly or through the use of an allowance account and the amount of the loss is recognised in the income statement. Interest income continues to be accrued on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. Loans and receivables together with any associated allowance are written off when there is no realistic prospect of future recovery.

If, in a subsequent period, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a future write-off is later recovered, the recovery is credited to “Other operating expenses, net” in the income statement.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### **Impairment of financial assets** *(Continued)*

#### *Available-for-sale investment carried at cost*

If there is objective evidence that an impairment loss has been incurred on the unlisted equity investment that is not carried at fair value because its fair value cannot be reliably measured, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. Impairment losses on this asset are not reversed.

### **Derecognition of financial assets**

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised when:

- the rights to receive cash flows from the asset have expired;
- the Group has transferred its rights to receive cash flows from the asset, or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a "pass-through" arrangement; and either (a) the Group has transferred substantially all the risks and rewards of the asset, or (b) the Group has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Group has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset. In that case, the Group also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Group has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### **Financial liabilities (loans and borrowings)**

#### *Initial recognition and measurement*

Financial liabilities within the scope of HKAS 39 are all classified as loans and borrowings. The Group determines the classification of its financial liabilities at initial recognition. All financial liabilities are recognised initially at fair value less directly attributable transaction costs.

#### *Subsequent measurement*

After initial recognition, loans and borrowings are subsequently measured at amortised cost, using the effective interest rate method unless the effect of discounting would be immaterial, in which case they are stated at cost. Gains and losses are recognised in the income statement when the liabilities are derecognised as well as through the effective interest rate method amortisation process.

Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the effective interest rate. The effective interest rate amortisation is included in "Finance costs" in the income statement.

### **Financial guarantee contracts**

Financial guarantee contracts issued by the Group are those contracts that require a payment to be made to reimburse the holder for a loss it incurs because the specified debtor fails to make a payment when due in accordance with the terms of a debt instrument. A financial guarantee contract is recognised initially as a liability at its fair value, adjusted for transaction costs that are directly attributable to the issue of the guarantee. Subsequent to initial recognition, the Group measures the financial guarantee contract at the higher of: (i) the amount of best estimate of the expenditure required to settle the present obligation at the end of the reporting period and (ii) the amount initially recognised less, when appropriate, cumulative amortisation.

### **Convertible bonds**

The component of convertible bonds that exhibits characteristics of a liability is recognised as a liability in the statement of financial position, net of transaction costs. On issuance of convertible bonds, the fair value of the liability component is determined using a market rate for an equivalent non-convertible bond; and this amount is carried as a non-current liability on the amortised cost basis until extinguished on conversion or redemption. The remainder of the proceeds is allocated to the conversion option (the equity component) that is recognised and included in shareholders' equity, net of transaction costs. The carrying amount of the conversion option is not remeasured in subsequent years.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### **Convertible bonds** *(Continued)*

Transaction costs are apportioned between the liability and equity components of the convertible bonds based on the allocation of proceeds to the liability and equity components when the instruments are initially recognised.

Upon the exercise of the conversion options, the resulting ordinary shares issued are recorded by the Company as additional share capital at the nominal value of the ordinary shares issued, and the excess of the total carrying amount of the liability and equity components of the convertible bonds over the nominal value of the ordinary shares issued is recorded in the share premium account. When the convertible bonds are redeemed, the carrying amount of the equity component is transferred to retained profits as a movement in reserves and any difference between the amount paid and the carrying amount of the liability component is recognised in the income statement. Where the conversion option remains unexercised at the expiry date, any remaining balance of the equity component of the convertible bonds will be transferred to retained profits as a movement in reserves. No gain or loss is recognised in the income statement upon conversion or expiration of the conversion option.

### **Derecognition of financial liabilities**

A financial liability is derecognised when the obligation under the liability is discharged or cancelled, or expires.

When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and a recognition of a new liability, and the difference between the respective carrying amounts is recognised in the income statement.

### **Offsetting of financial instruments**

Financial assets and financial liabilities are offset and the net amount is reported in the statement of financial position if, and only if, there is currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liabilities simultaneously.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### Fair value of financial instruments

The fair value of financial instruments that are traded in active markets is determined by reference to quoted market prices or dealer price quotations (bid price for long positions and ask price for short positions), without any deduction for transaction costs. For financial instruments where there is no active market, the fair value is determined using appropriate valuation techniques. Such techniques include using recent arm's length market transactions; reference to the current market value of another instrument which is substantially the same; a discounted cash flow analysis; and other valuation models.

### Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined on the weighted average basis. Net realisable value is based on the estimated selling prices less any estimated costs to be incurred to completion and disposal.

### Construction contracts

Contract revenue comprises (i) the agreed contract amount and appropriate amounts from variation orders, claims and incentive payments in respect of Build-Transfer ("BT") contracts and (ii) construction revenue recognised under Build-Operate-Transfer ("BOT") contracts. Contract costs incurred comprise direct materials, the costs of subcontracting, direct labour and an appropriate proportion of variable and fixed construction overheads.

Revenue from BT contracts is recognised on the percentage-of-completion method, measured by reference to the proportion of costs incurred to date to the estimated total cost of the relevant contract.

Revenue from the construction of a sewage treatment plant under the terms of BOT contracts (service concession agreements) is estimated on a cost-plus basis with reference to a prevailing market rate of gross margin at the date of the agreement applicable to similar construction services rendered in similar location, and is recognised on the percentage-of-completion method, measured by reference to the proportion of costs incurred to date to the estimated total cost of the relevant contract.

Provision is made for foreseeable losses as soon as they are anticipated by management.

Where contract costs incurred to date plus recognised profits less recognised losses exceed progress billings, the surplus is treated as an amount due from contract customers.

Where progress billings exceed contract costs incurred to date plus recognised profits less recognised losses, the surplus is treated as an amount due to contract customers.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### **Contracts for services**

Contract revenue on the rendering of services comprises the agreed contract amount. Costs of rendering services comprise labour and other costs of personnel directly engaged in providing the services and attributable overheads.

Revenue from the rendering of services is recognised based on the percentage of completion of the transaction, provided that the revenue, the costs incurred and the estimated costs to completion can be measured reliably. The percentage of completion is established by reference to the costs incurred to date as compared to the total costs to be incurred under the transaction. Where the outcome of a contract cannot be measured reliably, revenue is recognised only to the extent that the expenses incurred are eligible to be recovered.

Provision is made for foreseeable losses as soon as they are anticipated by management.

Where contract costs incurred to date plus recognised profits less recognised losses exceed progress billings, the surplus is treated as an amount due from contract customers.

Where progress billings exceed contract costs incurred to date plus recognised profits less recognised losses, the surplus is treated as an amount due to contract customers.

### **Cash and cash equivalents**

For the purpose of the consolidated statement of cash flows, cash and cash equivalents comprise cash on hand and demand deposits, and short term highly liquid investments that are readily convertible into known amounts of cash, are subject to an insignificant risk of changes in value, and have a short maturity of generally within three months when acquired, less bank overdrafts which are repayable on demand and form an integral part of the Group's cash management.

For the purpose of the statements of financial position, cash and cash equivalents comprise cash on hand and at banks, including term deposits, and assets similar in nature to cash, which are not restricted as to use.



# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### Provisions

A provision is recognised when a present obligation (legal or constructive) has arisen as a result of a past event and it is probable that a future outflow of resources will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation.

When the effect of discounting is material, the amount recognised for a provision is the present value at the end of the reporting period of the future expenditures expected to be required to settle the obligation. The increase in the discounted present value amount arising from the passage of time is included in "Finance costs" in the income statement.

### Income tax

Income tax comprises current and deferred tax. Income tax relating to items recognised outside the income statement is recognised outside the income statement, either in other comprehensive income or directly in equity.

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period, taking into consideration interpretations and practices prevailing in the countries in which the Group operates.

Deferred tax is provided, using the liability method, on all temporary differences at the end of the reporting period between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised for all taxable temporary differences, except:

- where the deferred tax liability arises from the initial recognition of goodwill or an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries and an associate, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### **Income tax** *(Continued)*

Deferred tax assets are recognised for all deductible temporary differences, carryforward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward of unused tax credits and unused tax losses can be utilised, except:

- where the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries and an associate, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred tax assets are reassessed at the end of each reporting period and are recognised to the extent that it has become probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### Government grants

Government grants are recognised at their fair value where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with. When the grant relates to an expense item, it is recognised as income over the periods necessary to match the grant on a systematic basis to the costs that it is intended to compensate. Where the grant relates to an asset, the fair value is credited to a deferred income account and is released to the income statement over the expected useful life of the relevant asset by equal annual instalments.

Where the Group receives government loans granted with no or at a below-market rate of interest for the construction of a qualifying asset, the initial carrying amount of the government loans is determined using the effective interest rate method, as further explained in the accounting policy for “Financial liabilities (loans and borrowings)” above. The benefit of the government loans granted with no or at a below-market rate of interest, which is the difference between the initial carrying value of the loans and the proceeds received, is treated as a government grant and released to the income statement over the expected useful life of the relevant asset by equal annual instalments.

### Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Group and when the revenue can be measured reliably, on the following bases:

- (a) from construction contracts, on the percentage-of-completion basis, as further explained in the accounting policy for “Construction contracts” above;
- (b) from the rendering of services, on the percentage-of-completion basis, as further explained in the accounting policy for “Contracts for services” above;
- (c) from licensing of technical know-how, when the related technique has been delivered and accepted;
- (d) from the sale of water and goods, when the significant risks and rewards of ownership have been transferred to the buyer, provided that the Group maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the water and goods sold;

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### Revenue recognition *(Continued)*

- (e) rental income, on a time proportion basis over the lease terms;
- (f) interest income, on an accrual basis using the effective interest rate method by applying the rate that exactly discounts the estimated future cash receipts through the expected life of the financial instrument or a shorter period, when appropriate, to the net carrying amount of the financial asset;
- (g) profit and loss from the trading of listed investments, on the trade dates; and
- (h) dividend income, when the right to receive payment has been established.

### Employee benefits – Pension schemes

The Group has joined a number of defined contribution pension schemes organised by certain PRC provincial or municipal governments for certain of its employees, the assets of which are held separately from those of the Group. Contributions made are based on a percentage of the eligible employees' salaries and are charged to the income statement as they become payable, in accordance with the rules of the pension schemes. The employer contributions vest fully once made.

For those employees that have not yet joined a pension scheme, the Group has accrued for the estimated future pension costs based on a percentage of their salaries. The related assets for the purpose of discharging such liabilities are not separately held from those of the Group.

The Group also operates a defined contribution Mandatory Provident Fund retirement benefits scheme in Hong Kong (the "MPF Scheme") under the Hong Kong Mandatory Provident Fund Schemes Ordinance, for those employees who are eligible to participate in the MPF Scheme. Contributions are made based on a percentage of the employees' basic salaries and are charged to the income statement as they become payable in accordance with the rules of the MPF Scheme. The assets of the MPF Scheme are held separately from those of the Group in an independently administered fund. The Group's employer contributions vest fully with the employees when contributed into the MPF Scheme.

# NOTES TO FINANCIAL STATEMENTS

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## 3.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### **Borrowing costs**

Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds. Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, i.e., assets that necessarily take a substantial period of time to get ready for their intended use or sale, are capitalised as part of the cost of those assets. The capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs capitalised. All other borrowing costs are expensed in the period in which they are incurred.

### **Foreign currencies**

These financial statements are presented in Hong Kong dollar, which is the Company's functional and presentation currency. Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency. Foreign currency transactions recorded by the entities in the Group are initially recorded using their respective functional currency rates ruling at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rates of exchange ruling at the end of the reporting period. All differences are taken to the income statement. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

The functional currency of the subsidiaries and the associate established in Mainland China is Renminbi ("RMB"). As at the end of the reporting period, the assets and liabilities of these entities are translated into the presentation currency of the Company at the exchange rate ruling at the end of the reporting period and their income statements are translated into Hong Kong dollars at the weighted average exchange rate for the year/period. The resulting exchange differences are recognised in other comprehensive income and accumulated in the exchange fluctuation reserve. On disposal of a foreign operation, the component of the exchange fluctuation reserve relating to that particular foreign operation is recognised in the income statement.

Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on the acquisition date are treated as assets and liabilities of the foreign operation and translated at the closing rate.

For the purpose of the consolidated statement of cash flows, the cash flows of the subsidiaries established in Mainland China are translated into Hong Kong dollars at the exchange rates ruling at the dates of the cash flows. Frequently recurring cash flows of these subsidiaries which arise throughout the year/period are translated into Hong Kong dollars at the weighted average exchange rate for the year/period.

# NOTES TO FINANCIAL STATEMENTS

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## 4. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES

The preparation of the Group's financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent liabilities, at the end of the reporting period. However, uncertainty about these assumptions and estimates could result in outcomes that could require a material adjustment to the carrying amounts of the assets or liabilities affected in the future.

The major judgements, estimates and assumptions that have the most significant effect on the amounts recognised in the financial statements and have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are set out below:

### **Classification between operating concessions and receivables under service concession arrangements**

As explained in note 3.4 to the financial statements, if the Group is paid for the construction services partly by a financial asset and partly by an intangible asset, it is necessary to account separately for each component of the operator's consideration. The consideration received or receivable for both components shall be recognised initially at the fair value of the consideration received or receivable.

The segregation of the consideration for a service concession arrangement between the financial asset component and the intangible asset component, if any, requires the Group to make an estimate of a number of factors, which include, inter alia, expected future sewage treatment volume of the relevant sewage treatment plant over its service concession period, future guaranteed receipts and unguaranteed receipts, and also to choose a suitable discount rate in order to calculate the present value of those cash flows. The carrying amounts of the operating concessions and receivables under service concession arrangements carried as assets in the consolidated statement of financial position as at 31 December 2009 were HK\$399,132,000 (2008: HK\$429,589,000) and HK\$2,054,265,000 (2008: HK\$1,373,656,000), respectively. Further details of which are set out in note 17 to the financial statements.

### **Determination of fair value of contract revenue in respect of the construction services rendered**

Revenue from the construction of a sewage treatment plant under the terms of a BOT contract is estimated on a cost-plus basis with reference to a prevailing market rate of gross margin at the date of agreement applicable to similar construction services rendered in similar location, and is recognised on the percentage-of-completion method, measured by reference to the proportion of costs incurred to date to the estimated total cost of the relevant contract.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 4. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES *(Continued)*

### **Determination of fair value of contract revenue in respect of the construction services rendered**

*(Continued)*

The construction margin is determined from the gross profit margins of market comparables by identifying relevant peer groups, which are listed in various stock exchanges in the world. Criteria for selection included:

- (i) the peer firm must be doing business on construction of infrastructure, majoring in sewage treatment facilities in the PRC; and
- (ii) information of the peer firm must be available and from a reliable source.

### **Percentage of completion of construction work and service contracts**

The Group recognises revenue for construction work and service contracts according to the percentage of completion of the individual contract of construction or service work. The Group's management estimates the percentage of completion of construction and service work based on the actual cost incurred over the total budgeted cost, where corresponding contract revenue is also estimated by management. Because of the nature of the activity undertaken in construction and service contracts, the date at which the activity is entered into and the date when the activity is completed usually fall into different accounting periods. The Group reviews and revises the estimates of both contract revenue and contract costs in the budget prepared for each construction contract and service contract as the contract progresses.

### **Estimate of water consumption**

Determination of the revenue for the distribution and sale of water may include an estimation of the water supplied to customers for whom actual meter reading is not available. The estimation is done mainly based on the past consumption records and the recent consumption pattern of individual customers.

The actual consumption could deviate from those estimates.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 4. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES *(Continued)*

### **Provision for major overhauls of sewage and water treatment plants to a specified level of serviceability**

The Group have contractual obligations which it must fulfil as a condition of its licence and that is (a) to maintain the sewage and water treatment plants it operates to a specified level of serviceability and/or (b) to restore the plants to a specified condition before they are handed over to the grantor at the end of the service concession arrangement. These contractual obligations to maintain or restore infrastructure, except for any upgrade element, are recognised and measured in accordance with HKAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, i.e., at the best estimate of the expenditure that would be required to settle the present obligation at the end of the reporting period. The estimation of the expenditure requires the Group to estimate the expected future cash outlays on major overhauls of the sewage and water treatment plants over the service concession periods and also to choose a suitable discount rate in order to calculate the present value of those cash flows. The carrying amount of the provision for major overhauls carried as a liability in the consolidated statement of financial position as at 31 December 2009 was HK\$91,792,000 (2008: HK\$69,006,000), further details of which are set out in note 33 to the financial statements.

### **Useful lives and residual values of property, plant and equipment, and intangible assets (other than goodwill)**

The Group's management determines the useful lives, residual values and related depreciation/amortisation charges for the Group's property, plant and equipment, and intangible assets. This estimate is based on the historical experience of the actual useful lives and residual values of property, plant and equipment, and intangible assets of similar nature and functions. It could change significantly as a result of technical innovations and competitor actions in response to severe industry cycles. Management will increase the depreciation/amortisation charges where useful lives or residual values are less than previously estimated, or it will write off or write down technically obsolete or non-strategic assets that have been abandoned or sold. Actual economic lives may differ from estimated useful lives. Periodic review could result in a change in depreciable/amortisable lives and therefore depreciation/amortisation in the future periods. The carrying amounts of property, plant and equipment, and intangible assets (other than goodwill) carried as assets in the consolidated statement of financial position as at 31 December 2009 were HK\$232,027,000 (2008: HK\$13,414,000) and HK\$402,425,000 (2008: HK\$431,245,000), respectively. Further details of which are set out in notes 14, 17 and 18 to the financial statements.

### **Impairment of goodwill**

The Group determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the value in use of the cash-generating units to which the goodwill is allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating units and also to choose a suitable discount rate in order to calculate the present value of those cash flows. The carrying amount of goodwill carried as assets in the consolidated statement of financial position as at 31 December 2009 was HK\$1,575,451,000 (2008: HK\$1,466,915,000), details of which are set out in note 16 to the financial statements.



# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 4. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES *(Continued)*

### **Impairment of property, plant and equipment, and intangible assets (other than goodwill)**

The carrying amounts of items of property, plant and equipment, and intangible assets are reviewed for impairment when events or changes in circumstances indicate the carrying amounts may not be recoverable in accordance with the accounting policy as disclosed in note 3.4 to these financial statements. The recoverable amount is the higher of its fair value less costs to sell and value in use, and calculations of which involve the use of estimates. In estimating the recoverable amounts of assets, various assumptions, including future cash flows to be associated with the non-current assets and discount rates, are made. If future events do not correspond to such assumptions, the recoverable amounts will need to be revised, and this may have an impact on the Group's results of operations or financial position.

### **Impairment of receivables under service concession arrangements, trade receivables and other receivables**

The policy for provision for impairment of receivables under service concession arrangements, trade receivables and other receivables of the Group is based on the evaluation of collectability and ageing analysis of accounts and on management's estimation. A considerable amount of estimation is required in assessing the ultimate realisation of these receivables, including the current creditworthiness and the past collection history of each debtor. If the financial conditions of debtors were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. The carrying amounts of receivables under service concession arrangements, trade receivables and other receivables carried as assets in the consolidated statement of financial position as at 31 December 2009 were HK\$2,054,265,000 (2008: HK\$1,373,656,000), HK\$150,902,000 (2008: HK\$9,029,000) and HK\$915,769,000 (2008: HK\$421,423,000), respectively. Further details of which are set out in notes 17, 24 and 25 to the financial statements.

### **Current tax and deferred tax**

The Group is subject to income taxes in Hong Kong and Mainland China. The Group carefully evaluates tax implications of its transactions in accordance with prevailing tax regulations and makes tax provision accordingly. However, judgement is required in determining the Group's provision for income taxes as there are many transactions and calculations of which the ultimate tax determination is uncertain during the ordinary course of business. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact on the income tax and deferred tax provision in the periods in which such determination is made. The carrying amount of current tax payable carried as liabilities in the consolidated statement of financial position as at 31 December 2009 was HK\$26,770,000 (2008: HK\$17,328,000).

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 4. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES *(Continued)*

### **Current tax and deferred tax** *(Continued)*

Deferred tax assets relating to certain temporary differences and tax losses are not recognised as management considered these losses were arisen in subsidiaries that have been loss-making for some time and it is not considered probable that taxable profits will be available against which the tax losses can be utilised. Where the expectations are different from the original estimates, such differences will impact the recognition of deferred tax assets and tax in the periods in which such estimates have been changed. The carrying amount of deferred tax assets and liabilities carried as assets and liabilities in the consolidated statement of financial position as at 31 December 2009 were HK\$31,071,000 (2008: HK\$27,112,000) and HK\$100,305,000 (2008: HK\$59,707,000), respectively, details of which are set out in note 35 to the financial statements.

## 5. OPERATING SEGMENT INFORMATION

For management purpose, the Group's operating businesses are structured and managed separately according to the nature of their operations and the products and services they provide. Each of the Group's operating segments represents a strategic business unit that offers products and services which are subject to risks and returns that are different from those of the other operating segments. Particulars of the Group's reportable operating segments are summarised as follows:

- (a) the sewage treatment and construction services segment engages in the construction and operation of sewage treatment plants and related facilities;
- (b) the water supply services segment engages in the operation of water supply and the provision of related services;
- (c) the sewage technical services segment engages in the provision of consultancy services and the licensing of technical know-how that are related to sewage treatment;
- (d) the sale of sewage treatment facilities segment engages in the trading of sewage treatment facilities and machinery and the provision of related services; and
- (e) the corporate and others segment comprises the trading of computer and related products and the corporate income and expense items.

Management monitors the results of its operating segments separately for the purpose of making decisions about resources allocation and performance assessment. Segment performance is evaluated based on the profit for the year/period of each reportable operating segment, which is measured consistently with the Group's profit for the year/period.

Segment assets of each of the reportable operating segments are separately managed by each of the individual operating segment.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 5. OPERATING SEGMENT INFORMATION *(Continued)*

Year ended 31 December 2009

|   | Sewage<br>treatment and<br>construction<br>services<br><i>HK\$'000</i> | Water<br>supply<br>services<br><i>HK\$'000</i> | Sewage<br>technical<br>services<br><i>HK\$'000</i> | Sale of<br>sewage<br>treatment<br>facilities<br><i>HK\$'000</i> | Corporate<br>and others<br><i>HK\$'000</i> | Total<br><i>HK\$'000</i> |
|---|--|--|--|---|--|--------------------------|
| Segment revenue   | 1,505,615  | 60,462   | 69,156   | 94,780  | -  | 1,730,013                |
| Cost of sales   | (1,100,452)  | (37,365)                                       | (5,607)  | (70,659)  | -  | (1,214,083)              |
| Gross profit  | <u>405,163</u>   | <u>23,097</u>                                  | <u>63,549</u>                                      | <u>24,121</u>   | <u>-</u>                                   | <u>515,930</u>           |
| Profit/(loss) from operating activities                                   | 363,963  | 10,398   | 58,291   | 24,121  | (58,823)                                   | 397,950                  |
| Imputed interest on convertible bonds                                     | -  | -  | -  | -   | (43,864)                                   | (43,864)                 |
| Other finance costs   | (77,513)   | (3,755)  | -  | -   | -  | (81,268)                 |
| Total finance costs   | <u>(77,513)</u>  | <u>(3,755)</u>                                 | <u>-</u>   | <u>-</u>  | <u>(43,864)</u>                            | <u>(125,132)</u>         |
| Share of profit of an associate   | -  | -  | -  | -   | 4,565                                      | 4,565                    |
| Profit/(loss) before tax  | 286,450  | 6,643  | 58,291   | 24,121  | (98,122)                                   | 277,383                  |
| Income tax  | (43,252)   | 1,863  | (7,248)  | -   | -  | (48,637)                 |
| Segment profit/(loss) for the year  | <u>243,198</u>   | <u>8,506</u>                                   | <u>51,043</u>                                      | <u>24,121</u>   | <u>(98,122)</u>                            | <u>228,746</u>           |
| Profit/(loss) for the year attributable to<br>shareholders of the Company | <u>201,076</u>   | <u>6,722</u>                                   | <u>51,699</u>                                      | <u>24,121</u>   | <u>(90,907)</u>                            | <u>192,711</u>           |
| Segment assets  | <u>5,429,428</u>   | <u>226,496</u>                                 | <u>699,974</u>                                     | <u>-</u>  | <u>1,067,819</u>                           | <u>7,423,717</u>         |
| Other segment information:  |  |  |  |   |  |                          |
| Depreciation  | 7,266  | 5,727  | 562  | -   | 815  | 14,370                   |
| Amortisation of operating concessions                                     | 17,878   | 1,548  | -  | -   | -  | 19,426                   |
| Amortisation of other intangible assets                                   | 4  | -  | 196  | -   | 56   | 256                      |
| Impairment/(reversal of impairment) of<br>segment assets, net             | 339  | (426)  | 7,043  | -   | 113  | 7,069                    |
| Provision for major overhauls   | 20,495   | 280  | -  | -   | -  | 20,775                   |
| Capital expenditure*  | <u>96,882</u>  | <u>5,612</u>                                   | <u>282</u>   | <u>-</u>  | <u>4,428</u>                               | <u>107,204</u>           |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 5. OPERATING SEGMENT INFORMATION *(Continued)*

Period from 1 July 2007 to 31 December 2008

|   | Sewage<br>treatment and<br>construction<br>services<br><i>HK\$'000</i> | Water<br>supply<br>services<br><i>HK\$'000</i> | Sewage<br>technical<br>services<br><i>HK\$'000</i> | Corporate<br>and others<br><i>HK\$'000</i> | Total<br><i>HK\$'000</i> |
|---|--|--|--|--|--------------------------|
| Segment revenue   | 269,567  | 6,087  | 51,071   | 10,956                                     | 337,681                  |
| Cost of sales   | <u>(167,090)</u>   | <u>(2,318)</u>                                 | <u>(2,677)</u>                                     | <u>(10,793)</u>                            | <u>(182,878)</u>         |
| Gross profit  | <u>102,477</u>   | <u>3,769</u>                                   | <u>48,394</u>                                      | <u>163</u>                                 | <u>154,803</u>           |
| Profit/(loss) from operating activities                                     | 86,868   | 3,637  | 42,347   | (16,632)                                   | 116,220                  |
| Imputed interest on convertible bonds                                       | –  | –  | –  | (35,426)                                   | (35,426)                 |
| Other finance costs   | <u>(23,273)</u>  | <u>(1,574)</u>                                 | <u>–</u>   | <u>–</u>                                   | <u>(24,847)</u>          |
| Total finance costs   | <u>(23,273)</u>  | <u>(1,574)</u>                                 | <u>–</u>   | <u>(35,426)</u>                            | <u>(60,273)</u>          |
| Share of loss of an associate   | <u>–</u>   | <u>–</u>                                       | <u>–</u>   | <u>(811)</u>                               | <u>(811)</u>             |
| Profit/(loss) before tax  | 63,595   | 2,063  | 42,347   | (52,869)                                   | 55,136                   |
| Income tax  | <u>(11,240)</u>  | <u>(16)</u>                                    | <u>(900)</u>                                       | <u>(78)</u>                                | <u>(12,234)</u>          |
| Segment profit/(loss) for the period  | <u>52,355</u>  | <u>2,047</u>                                   | <u>41,447</u>                                      | <u>(52,947)</u>                            | <u>42,902</u>            |
| Profit/(loss) for the period attributable to<br>shareholders of the Company | <u>43,703</u>  | <u>1,269</u>                                   | <u>38,312</u>                                      | <u>(52,300)</u>                            | <u>30,984</u>            |
| Segment assets  | <u>3,766,919</u>   | <u>43,656</u>                                  | <u>905,976</u>                                     | <u>99,607</u>                              | <u>4,816,158</u>         |
| Other segment information:  |  |  |  |  |                          |
| Depreciation  | 742  | 98   | 278  | 112  | 1,230                    |
| Amortisation of operating concessions                                       | 5,412  | 387  | –  | –  | 5,799                    |
| Amortisation of other intangible assets                                     | –  | –  | 78   | –  | 78                       |
| Impairment/(reversal of impairment) of<br>segment assets, net               | 1,953  | –  | (69)   | –  | 1,884                    |
| Provision for major overhauls   | 7,216  | 69   | –  | –  | 7,285                    |
| Capital expenditure*  | <u>592</u>   | <u>16</u>                                      | <u>552</u>   | <u>3,953</u>                               | <u>5,113</u>             |

\* Capital expenditure consists of additions to property, plant and equipment, operating concessions and other intangible assets, excluding assets from the acquisition of subsidiaries.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 5. OPERATING SEGMENT INFORMATION *(Continued)*

### Geographical information

Since over 90% of the Group's revenue from external customers is generated in the PRC and over 90% of the assets of the Group are located in the PRC, in the opinion of the directors, no geographic information is presented.

### Information about a major customer

Revenue of approximately HK\$176,059,000 (period ended 31 December 2008: HK\$35,828,000) was derived from the construction service provided by the sewage treatment and construction services segment to a single customer.

## 6. REVENUE, OTHER INCOME AND GAINS, NET

Revenue, which is also the Group's turnover, represents: (1) an appropriate proportion of contract revenue of construction contracts and service contracts relating to sewage treatment, net of business tax and government surcharges; (2) the aggregate of the invoiced value of water sold and the estimated value of unbilled water distributed based on the consumption recorded by water meter readings, net of value-added tax, business tax and government surcharges; (3) the value of consultancy fees and licence fees, net of business tax and government surcharges; (4) the net invoiced value of goods sold, net of value-added tax and government surcharges and after allowances for returns and trade discounts; and (5) the imputed interest income on service concession arrangements.

An analysis of the Group's revenue, other income and gains, net, is as follows:

|                             | Year ended<br>31 December<br>2009<br>HK\$'000 | Period from<br>1 July 2007 to<br>31 December<br>2008<br>HK\$'000 |
|-----------------------------|---|--|
| <b>Revenue</b>              |   |  |
| Sewage treatment services * | 439,784                                       | 138,224  |
| Construction contracts *    | 1,065,831                                     | 131,343  |
| Sale of water               | 60,462  | 6,087  |
| Consultancy services        | 34,342  | 23,881   |
| Licence fees                | 34,814  | 27,190   |
| Sale of goods               | 94,780  | 10,956   |
|                             | <b>1,730,013</b>                              | <b>337,681</b>   |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 6. REVENUE, OTHER INCOME AND GAINS, NET *(Continued)*

|   | Year ended<br>31 December<br>2009<br>HK\$'000 | Period from<br>1 July 2007 to<br>31 December<br>2008<br>HK\$'000 |
|---|---|--|
| <b>Other income</b>   |   |  |
| Bank interest income  | 5,789   | 9,193  |
| Gross rental income <sup>#</sup>  | 117   | 268  |
| Pipeline installation income  | 545   | 179  |
| Dividend income from financial assets<br>at fair value through profit or loss     | –   | 137  |
| Government grants <sup>§</sup>  | 2,369   | –  |
| Sludge treatment income   | 12,791  | –  |
| Others  | 2,602   | 133  |
|   | <u>24,213</u>                                 | <u>9,910</u>   |
| <b>Gains, net</b>   |   |  |
| Gain on disposal of financial assets at fair value<br>through profit or loss, net | –   | 718  |
| Gain on disposal of subsidiaries <i>(note 40)</i>                                 | –   | 760  |
| Foreign exchange differences, net   | 1,965   | –  |
|   | <u>1,965</u>                                  | <u>1,478</u>   |
| Other income and gains, net   | <u>26,178</u>                                 | <u>11,388</u>  |

\* *Imputed interest income under service concession arrangements amounting to HK\$176,033,000 (period ended 31 December 2008: HK\$60,241,000) and HK\$1,440,000 (period ended 31 December 2008: HK\$2,398,000) are included in the revenue derived from "Sewage treatment services" and "Construction contracts" above, respectively.*

# *The Group leased certain areas of buildings, which form part of the operating assets transferred to the Group by the grantors in respect of the Group's sewage and water treatment operations, to third parties under operating lease arrangements and accordingly, earned rental income therefrom for the year. Further details of the operating lease arrangements are set out in note 43(a) to the financial statements.*

§ *The government grants represented government subsidies received for the construction of a sewage treatment plant and for the alleviation of the Group's suffering from the earthquake and related aftershocks in Sichuan Province, the PRC, in May 2008. There are no unfulfilled conditions or contingencies relating to these grants.*

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 7. PROFIT FROM OPERATING ACTIVITIES

The Group's profit from operating activities is arrived at after charging/(crediting):

|  |              | Year ended<br>31 December<br>2009<br>HK\$'000 | Period from<br>1 July 2007 to<br>31 December<br>2008<br>HK\$'000 |
|--|--------------|---|--|
|  | <i>Notes</i> | <i>HK\$'000</i>                               | <i>HK\$'000</i>  |
| Cost of sewage treatment services rendered   |              | 142,691                                       | 47,889   |
| Cost of construction contracts   |              | 939,883                                       | 113,402  |
| Cost of water sold   |              | 35,817  | 2,318  |
| Cost of consultancy services rendered  |              | 3,219   | 2,651  |
| Cost of licensing  |              | 2,388   | 26   |
| Cost of goods sold   |              | 70,659  | 10,793   |
| Depreciation   | 14           | 14,370  | 1,230  |
| Amortisation of prepaid land premiums  | 15           | 331   | –  |
| Amortisation of operating concessions *  | 17           | 19,426  | 5,799  |
| Amortisation of other intangible assets *  | 18           | 256   | 78   |
| Minimum lease payments under operating leases<br>of land and buildings                           |              | 4,384   | 1,878  |
| Auditors' remuneration   |              | 4,300   | 3,207  |
| Employee benefit expense (including directors' remuneration (note 9)):                           |              |   |  |
| Salaries, allowances and benefits in kind  |              | 64,988  | 24,532   |
| Net pension scheme contributions   |              | 6,498   | 917  |
| Welfare and other expenses   |              | 15,185  | 3,397  |
|  |              | <b>86,671</b>                                 | <b>28,846</b>  |
| Loss on disposal of items of property,<br>plant and equipment, net                               |              | 53  | 17   |
| Loss on disposal of other intangible assets  |              | 75  | –  |
| (Gain)/loss on disposal of subsidiaries  | 40           | 2,922   | (760)  |
| Loss on disposal of an associate   |              | 326   | –  |
| Impairment/(reversal of impairment) of receivables<br>under service concession arrangements, net | 17           | (408)   | 1,748  |
| Impairment of amounts due from contract<br>customers   | 23           | 6,273   | –  |
| Impairment/(reversal of impairment) of<br>trade receivables, net                                 | 24(c)        | 612   | (69)   |
| Impairment of other receivables, net   | 25(b)        | 592   | 205  |
| Provision for major overhauls  | 33           | 20,775  | 7,285  |
| Foreign exchange differences, net  |              | (1,965)                                       | 5,262  |

\* The amortisation of operating concessions and other intangible assets for the year are included in "Cost of sales" and "Administrative expenses" on the face of the consolidated income statement, respectively.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 8. FINANCE COSTS

|   |              | Group                             |  |
|---|--------------|-----------------------------------|--|
|   |              | Year ended<br>31 December<br>2009 | Period from<br>1 July 2007 to<br>31 December<br>2008 |
|   | <i>Notes</i> | <i>HK\$'000</i>                   | <i>HK\$'000</i>                                      |
| Interest on bank loans and other loans<br>wholly repayable within five years                        |              | 84,670                            | 28,061   |
| Interest in other loans   |              | 875                               | 799  |
| Imputed interest on convertible bonds   | 31           | 43,863                            | 35,426   |
| Interest on a finance lease   |              | 1,015                             | 643  |
|   |              | <hr/>                             | <hr/>  |
| Total interest expenses   |              | 130,423                           | 64,929   |
| Increase in discounted amounts of provision for<br>major overhauls arising from the passage of time | 33           | 2,011                             | 595  |
|   |              | <hr/>                             | <hr/>  |
| Total finance costs   |              | 132,434                           | 65,524   |
| Less: Interest included in cost of<br>construction contracts  |              | (7,302)                           | (5,251)  |
|   |              | <hr/>                             | <hr/>  |
|   |              | <b>125,132</b>                    | <b>60,273</b>  |



# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 9. DIRECTORS' REMUNERATION

Directors' remuneration for the year/period, disclosed pursuant to The Rules Governing the Listing of Securities on the Stock Exchange and Section 161 of the Hong Kong Companies Ordinance, is as follows:

|   | Group  |   |
|---|--|---|
|   | Year ended<br>31 December<br>2009<br><i>HK\$'000</i> | Period from<br>1 July 2007 to<br>31 December<br>2008<br><i>HK\$'000</i> |
| Fees:                                     |  |   |
| Executive directors                       | 1,022  | 1,273   |
| Independent non-executive directors       | 488  | 432   |
|   | <u>1,510</u>   | <u>1,705</u>  |
| Other emoluments for executive directors: |  |   |
| Salaries, allowances and benefits in kind | 3,699  | 1,153   |
| Pension scheme contributions              | 36   | 27  |
|   | <u>3,735</u>   | <u>1,180</u>  |
|   | <u>5,245</u>   | <u>2,885</u>  |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 9. DIRECTORS' REMUNERATION *(Continued)*

### (a) Independent non-executive directors

The fees paid to independent non-executive directors were as follows:

|                             | Year ended<br>31 December<br>2009<br><i>HK\$'000</i> | Period from<br>1 July 2007 to<br>31 December<br>2008<br><i>HK\$'000</i> |
|-----------------------------|--|---|
| Mr. Shea Chun Lok, Quadrant | 68   | 108   |
| Mr. Zhang Gaobo             | 120  | 78  |
| Mr. Guo Rui                 | 100  | 58  |
| Ms. Hang Shijun             | 100  | 42  |
| Mr. Wang Kaijun             | 100  | 42  |
| Mr. Chan Wai Kwong, Peter   | -  | 50  |
| Mr. So Kwok Keung           | -  | 45  |
| Mr. Ngai Chi Yung           | -  | 9   |
| Mr. Chan Yiu Kwong          | -  | -   |
|                             | <b>488</b>   | <b>432</b>  |

There were no other emoluments payable to the independent non-executive directors during the year (period ended 31 December 2008: Nil).

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 9. DIRECTORS' REMUNERATION (Continued)

### (b) Executive directors

|                         | Fees            | Salaries,<br>allowances<br>and benefits<br>in kind | Pension<br>scheme<br>contributions | Total<br>remuneration |
|-------------------------|-----------------|--|------------------------------------|-----------------------|
|                         | <i>HK\$'000</i> | <i>HK\$'000</i>                                    | <i>HK\$'000</i>                    | <i>HK\$'000</i>       |
| <b>Year ended</b>       |                 |  |                                    |                       |
| <b>31 December 2009</b> |                 |  |                                    |                       |
| Mr. Zhang Honghai       | -               | -  | -                                  | -                     |
| Mr. Liu Kai             | -               | -  | -                                  | -                     |
| Mr. E Meng              | 100             | -  | -                                  | 100                   |
| Mr. Jiang Xinhao        | 100             | -  | -                                  | 100                   |
| Mr. Hu Xiaoyong         | 100             | 1,477  | 12                                 | 1,589                 |
| Mr. Wang Taoguang       | 100             | -  | -                                  | 100                   |
| Mr. Wu Xiaoming         | 147             | -  | -                                  | 147                   |
| Mr. Zhou Min            | 100             | 1,233  | 12                                 | 1,345                 |
| Mr. Li Haifeng          | 100             | 989  | 12                                 | 1,101                 |
| Ms. Qi Xiaohong         | 100             | -  | -                                  | 100                   |
| Mr. Ju Yadong           | 100             | -  | -                                  | 100                   |
| Mr. Zhang Tiefu         | 75              | -  | -                                  | 75                    |
|                         | <b>1,022</b>    | <b>3,699</b>                                       | <b>36</b>                          | <b>4,757</b>          |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 9. DIRECTORS' REMUNERATION *(Continued)*

### (b) Executive directors *(Continued)*

|                         | Fees            | Salaries,<br>allowances<br>and benefits<br>in kind | Pension<br>scheme<br>contributions | Total<br>remuneration |
|-------------------------|-----------------|--|------------------------------------|-----------------------|
|                         | <i>HK\$'000</i> | <i>HK\$'000</i>                                    | <i>HK\$'000</i>                    | <i>HK\$'000</i>       |
| <b>Period ended</b>     |                 |  |                                    |                       |
| <b>31 December 2008</b> |                 |  |                                    |                       |
| Mr. Zhang Honghai       | –               | –  | –                                  | –                     |
| Mr. Liu Kai             | 92              | –  | –                                  | 92                    |
| Mr. E Meng              | 92              | –  | –                                  | 92                    |
| Mr. Jiang Xinhao        | 57              | –  | –                                  | 57                    |
| Mr. Hu Xiaoyong         | 42              | 460  | 5                                  | 507                   |
| Mr. Wang Taoguang       | 42              | –  | –                                  | 42                    |
| Mr. Wu Xiaoming         | 42              | –  | –                                  | 42                    |
| Mr. Zhou Min            | 42              | 384  | 5                                  | 431                   |
| Mr. Li Haifeng          | 42              | 309  | 5                                  | 356                   |
| Ms. Qi Xiaohong         | 66              | –  | –                                  | 66                    |
| Mr. Ju Yadong           | 66              | –  | –                                  | 66                    |
| Mr. Flynn Xuxian Huang  | –               | –  | –                                  | –                     |
| Ms. Guan Mei            | –               | –  | –                                  | –                     |
| Mr. Chase J Wong        | 690             | –  | 12                                 | 702                   |
|                         | <u>1,273</u>    | <u>1,153</u>                                       | <u>27</u>                          | <u>2,453</u>          |

There was no arrangement under which a director waived or agreed to waive any remuneration during the year (period ended 31 December 2008: Nil).

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 10. FIVE HIGHEST PAID EMPLOYEES

The five highest paid employees during the year included four (period ended 31 December 2008: three) directors, details of whose remuneration are set out in note 9 above. Details of the remuneration of the remaining one (period ended 31 December 2008: two) non-director, highest paid employee for the year/period is as follows:

|   | <b>Year ended<br/>31 December<br/>2009<br/>HK\$'000</b> | Period from<br>1 July 2007 to<br>31 December<br>2008<br>HK\$'000 |
|---|---|--|
| Salaries, allowances and benefits in kind | 594   | 1,214  |
| Pension scheme contributions              | 12  | 29   |
|   | <b>606</b>  | 1,243  |

The remuneration of the two non-director, highest paid employees for the period ended 31 December 2008 each fell within the range of nil to HK\$1,000,000.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 11. INCOME TAX

No provision of Hong Kong profits tax has been made for the year ended 31 December 2009 as the Group did not generate any assessable profits arising in Hong Kong during the year (period ended 31 December 2008: Nil).

The income tax provision in respect of operations in Mainland China is calculated at the applicable tax rates on the estimated assessable profits for the year/period based on existing legislation, interpretations and practices in respect thereof. In accordance with the relevant tax rules and regulations of the PRC, certain of the Company's subsidiaries enjoy income tax exemptions and reductions, by reason that these companies are engaged in the operations of sewage treatment.

|   | Group   |  |
|---|---|--|
|   | Year ended<br>31 December<br>2009<br>HK\$'000 | Period from<br>1 July 2007 to<br>31 December<br>2008<br>HK\$'000 |
| Current – PRC:                                    |   |  |
| Hong Kong   | –   | –  |
| Mainland China                                    | 20,004  | 3,905  |
| Underprovision/(overprovision) in prior periods * | (8,003)                                       | 78   |
| Deferred ( <i>note 35</i> )                       | <u>36,636</u>                                 | <u>8,251</u>   |
| Total tax charge for the year/period              | <u>48,637</u>                                 | <u>12,234</u>  |

\* *Income tax exemptions were granted to certain subsidiaries of the Group by relevant provincial tax bureaus in Mainland China during the year ended 31 December 2009 in respect of their assessable profits for the period ended 31 December 2008. Accordingly, their respective income taxes provided in the period ended 31 December 2008 were reversed during the year.*

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 11. INCOME TAX (Continued)

A reconciliation of the tax expense applicable to profit before tax at the statutory rates for the jurisdictions in which the Company and its subsidiaries are domiciled to the tax expense at the effective tax rates, and a reconciliation of the applicable rates (i.e., the statutory tax rates) to the effective tax rates, are as follows:

### Group – Year ended 31 December 2009

|  | Hong Kong       |              | Mainland China |             | Total          |             |
|--|-----------------|--------------|----------------|-------------|----------------|-------------|
|  | HK\$'000        | %            | HK\$'000       | %           | HK\$'000       | %           |
| Profit/(loss) before tax   | <u>(62,859)</u> |              | <u>340,242</u> |             | <u>277,383</u> |             |
| Tax at the statutory tax rate  | (10,371)        | 16.5         | 85,060         | 25.0        | 74,689         | 26.9        |
| Lower tax rates of specific provinces<br>or enacted by local authorities | -               | -            | (8,915)        | (2.6)       | (8,915)        | (3.2)       |
| Tax concession enjoyed   | -               | -            | (27,513)       | (8.1)       | (27,513)       | (9.9)       |
| Adjustments in respect of current tax of<br>previous periods             | -               | -            | (8,003)        | (2.4)       | (8,003)        | (2.9)       |
| Profit attributable to an associate                                      | -               | -            | (1,141)        | (0.3)       | (1,141)        | (0.4)       |
| Income not subject to tax  | (403)           | 0.6          | (2,396)        | (0.7)       | (2,799)        | (1.0)       |
| Expenses not deductible for tax  | 8,267           | (13.1)       | 8,554          | 2.5         | 16,821         | 6.1         |
| Tax losses utilised from previous periods                                | -               | -            | (279)          | (0.1)       | (279)          | (0.1)       |
| Tax losses not recognised as deferred<br>tax assets                      | <u>2,507</u>    | <u>(4.0)</u> | <u>3,270</u>   | <u>1.0</u>  | <u>5,777</u>   | <u>2.0</u>  |
| Tax charge at the Group's effective rate                                 | <u>-</u>        | <u>-</u>     | <u>48,637</u>  | <u>14.3</u> | <u>48,637</u>  | <u>17.5</u> |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 11. INCOME TAX (Continued)

### Group – Period ended 31 December 2008

|  | Hong Kong |        | Mainland China |       | Total    |        |
|--|-----------|--------|----------------|-------|----------|--------|
|  | HK\$'000  | %      | HK\$'000       | %     | HK\$'000 | %      |
| Profit/(loss) before tax   | (36,300)  |        | 91,436         |       | 55,136   |        |
| Tax at the statutory tax rate  | (5,988)   | 16.5   | 22,859         | 25.0  | 16,871   | 30.6   |
| Lower tax rates of specific provinces<br>or enacted by local authorities | –         | –      | (4,534)        | (5.0) | (4,534)  | (8.2)  |
| Tax concession enjoyed   | –         | –      | (8,877)        | (9.7) | (8,877)  | (16.1) |
| Adjustments in respect of current tax of<br>previous periods             | –         | –      | 78             | 0.1   | 78       | 0.1    |
| Loss attributable to an associate  | –         | –      | 203            | 0.2   | 203      | 0.4    |
| Income not subject to tax  | (5,747)   | 15.8   | (1,814)        | (2.0) | (7,561)  | (13.7) |
| Expenses not deductible for tax  | 6,052     | (16.6) | 2,593          | 2.9   | 8,645    | 15.6   |
| Tax losses utilised from previous periods                                | (15)      | –      | –              | –     | (15)     | –      |
| Tax losses not recognised as deferred<br>tax assets                      | 5,698     | (15.7) | 1,726          | 1.9   | 7,424    | 13.5   |
| Tax charge at the Group's effective rate                                 | –         | –      | 12,234         | 13.4  | 12,234   | 22.2   |

## 12. PROFIT FOR THE YEAR/PERIOD ATTRIBUTABLE TO SHAREHOLDERS OF THE COMPANY

The consolidated profit attributable to shareholders of the Company for the year ended 31 December 2009 includes a loss of HK\$62,505,000 (period ended 31 December 2008: HK\$47,168,000), which has been dealt with in the financial statements of the Company (*note 29(b)*).

## 13. EARNINGS PER SHARE ATTRIBUTABLE TO SHAREHOLDERS OF THE COMPANY

The calculation of basic earnings per share amounts is based on the profit for the year/period attributable to shareholders of the Company, and the weighted average number of ordinary shares in issue during the year/period.



# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 13. EARNINGS PER SHARE ATTRIBUTABLE TO SHAREHOLDERS OF THE COMPANY

(Continued)

The calculation of diluted earnings per share amounts is based on the profit for the year/period attributable to shareholders of the Company, adjusted to reflect the effect of the deemed conversion of all dilutive convertible bonds, and the weighted average number of ordinary shares assumed to have been issued on the deemed conversion of all dilutive convertible bonds into ordinary shares. All convertible bonds of the Company outstanding during the year ended 31 December 2009 had a dilutive effect on the basic earnings per share amount for the year. Except for the Tranche 1 Bond (as defined in the circular of the Company dated 3 May 2007) issued by the Company on 27 July 2007, all other convertible bonds of the Company outstanding in the prior period had either an anti-dilutive effect or no diluting effect on the basic earnings per share amount for the period ended 31 December 2008.

The calculation of the basic and diluted earnings per share amounts is based on the following data:

|  | Year ended<br>31 December<br>2009<br><i>HK\$'000</i> | Period from<br>1 July 2007 to<br>31 December<br>2008<br><i>HK\$'000</i> |
|--|--|---|
| <b>Earnings</b>  |  |   |
| Profit for the year/period attributable to shareholders of the Company, used in the basic earnings per share calculation     | 192,711  | 30,984  |
| Interest on dilutive convertible bonds   | 43,864   | 6,210   |
|  | <u>236,575</u>                                       | <u>37,194</u>   |
| Profit for the year/period attributable to shareholders of the Company, used in the diluted earnings per share calculation   | 236,575  | 37,194  |
| <b>Number of ordinary shares</b>   |  |   |
| Weighted average number of ordinary shares in issue during the year/period, used in the basic earnings per share calculation | 3,152,955,623  | 811,259,728   |
| Effect of dilution of dilutive convertible bonds<br>– weighted average number of ordinary shares                             | 1,264,943,280  | 188,818,182   |
| Weighted average number of ordinary shares,<br>used in the diluted earnings per share calculation                            | 4,417,898,903  | 1,000,077,910   |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 14. PROPERTY, PLANT AND EQUIPMENT

### Group

|  | Buildings<br>HK\$'000 | Leasehold<br>improvements<br>HK\$'000 | Machinery,<br>and sewage<br>and water<br>pipelines<br>HK\$'000 | Furniture,<br>fixtures<br>and office<br>equipment<br>HK\$'000 | Motor<br>vehicles<br>HK\$'000 | Construction<br>in progress<br>HK\$'000 | Total<br>HK\$'000 |
|--|-----------------------|---------------------------------------|--|---|-------------------------------|---|-------------------|
| <b>Year ended 31 December 2009</b>                     |                       |                                       |  |   |                               |   |                   |
| At 31 December 2008 and<br>1 January 2009:             |                       |                                       |  |   |                               |   |                   |
| Cost   | -                     | 979                                   | -  | 7,624   | 13,786                        | -                                       | 22,389            |
| Accumulated depreciation                               | -                     | (645)                                 | -  | (2,794)   | (5,536)                       | -                                       | (8,975)           |
| Net carrying amount                                    | -                     | 334                                   | -  | 4,830   | 8,250                         | -                                       | 13,414            |
| Net carrying amount:                                   |                       |                                       |  |   |                               |   |                   |
| At 1 January 2009                                      | -                     | 334                                   | -  | 4,830   | 8,250                         | -                                       | 13,414            |
| Acquisition of subsidiaries (note 39)                  | 39,331                | -                                     | 13,616   | 1,464   | 1,645                         | 115,512                                 | 171,568           |
| Additions  | -                     | 63                                    | 1,668  | 3,844   | 4,523                         | 51,176                                  | 61,274            |
| Transfer from construction in progress                 | 98,129                | -                                     | 65,260   | 99  | 277                           | (163,765)                               | -                 |
| Depreciation provided during the year                  | (5,031)               | (172)                                 | (4,938)  | (1,639)   | (2,590)                       | -                                       | (14,370)          |
| Disposals  | -                     | -                                     | (53)   | -   | -                             | -                                       | (53)              |
| Exchange realignment                                   | 34                    | -                                     | 20   | 2   | 2                             | 136                                     | 194               |
| At 31 December 2009                                    | 132,463               | 225                                   | 75,573   | 8,600   | 12,107                        | 3,059                                   | 232,027           |
| At 31 December 2009:                                   |                       |                                       |  |   |                               |   |                   |
| Cost   | 153,982               | 1,041                                 | 95,579   | 13,741  | 22,111                        | 3,059                                   | 289,513           |
| Accumulated depreciation                               | (21,519)              | (816)                                 | (20,006)   | (5,141)   | (10,004)                      | -                                       | (57,486)          |
| Net carrying amount                                    | 132,463               | 225                                   | 75,573   | 8,600   | 12,107                        | 3,059                                   | 232,027           |
| <b>Period from 1 July 2007 to<br/>31 December 2008</b> |                       |                                       |  |   |                               |   |                   |
| At 1 July 2007:  |                       |                                       |  |   |                               |   |                   |
| Cost   | -                     | 134                                   | -  | 200   | -                             | -                                       | 334               |
| Accumulated depreciation                               | -                     | (101)                                 | -  | (162)   | -                             | -                                       | (263)             |
| Net carrying amount                                    | -                     | 33                                    | -  | 38  | -                             | -                                       | 71                |
| Net carrying amount:                                   |                       |                                       |  |   |                               |   |                   |
| At 1 July 2007   | -                     | 33                                    | -  | 38  | -                             | -                                       | 71                |
| Acquisition of subsidiaries (note 39)                  | -                     | 417                                   | -  | 3,605   | 6,017                         | -                                       | 10,039            |
| Additions  | -                     | -                                     | -  | 1,584   | 3,007                         | -                                       | 4,591             |
| Depreciation provided during the period                | -                     | (114)                                 | -  | (367)   | (749)                         | -                                       | (1,230)           |
| Disposals  | -                     | -                                     | -  | (17)  | -                             | -                                       | (17)              |
| Exchange realignment                                   | -                     | (2)                                   | -  | (13)  | (25)                          | -                                       | (40)              |
| At 31 December 2008                                    | -                     | 334                                   | -  | 4,830   | 8,250                         | -                                       | 13,414            |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 14. PROPERTY, PLANT AND EQUIPMENT *(Continued)*

### Company

|  | Furniture,<br>fixtures and<br>office equipment<br><i>HK\$'000</i> | Motor<br>vehicles<br><i>HK\$'000</i> | Total<br><i>HK\$'000</i> |
|--|---|--------------------------------------|--------------------------|
| <b>Year ended 31 December 2009</b>                     |   |                                      |                          |
| At 31 December 2008 and<br>1 January 2009:             |   |                                      |                          |
| Cost   | 26  | 490                                  | 516                      |
| Accumulated depreciation                               | (1)   | (49)                                 | (50)                     |
| Net carrying amount                                    | 25  | 441                                  | 466                      |
| Net carrying amount:                                   |   |                                      |                          |
| At 1 January 2009                                      | 25  | 441                                  | 466                      |
| Additions  | 8   | –                                    | 8                        |
| Depreciation provided during the year                  | (6)   | (147)                                | (153)                    |
| At 31 December 2009                                    | 27  | 294                                  | 321                      |
| At 31 December 2009:                                   |   |                                      |                          |
| Cost   | 25  | 441                                  | 466                      |
| Accumulated depreciation                               | 2   | (147)                                | (145)                    |
| Net carrying amount                                    | 27  | 294                                  | 321                      |
| <b>Period from 1 July 2007 to<br/>31 December 2008</b> |   |                                      |                          |
| At 1 July 2007:  |   |                                      |                          |
| Cost and net carrying amount                           | –   | –                                    | –                        |
| Net carrying amount:                                   |   |                                      |                          |
| At 1 July 2007   | –   | –                                    | –                        |
| Additions  | 26  | 490                                  | 516                      |
| Depreciation provided during the period                | (1)   | (49)                                 | (50)                     |
| At 31 December 2008                                    | 25  | 441                                  | 466                      |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 15. PREPAID LAND PREMIUMS

### Group

|  | Year ended<br>31 December<br>2009<br>HK\$'000 | Period from<br>1 July 2007 to<br>31 December<br>2008<br>HK\$'000 |
|--|---|--|
| Carrying amount at beginning of year/period    | –   | –  |
| Acquisition of subsidiaries ( <i>note 39</i> ) | 28,005  | –  |
| Amortisation provided during the year/period   | (331)   | –  |
| Exchange realignment                           | 30  | –  |
| Carrying amount at end of year/period          | 27,704  | –  |
| Portion classified as current assets           | (644)   | –  |
| Non-current portion                            | 27,060  | –  |

The leasehold land of the Group are all located in Mainland China and held under medium term leases.

## 16. GOODWILL

### Group

|  | Year ended<br>31 December<br>2009<br>HK\$'000 | Period from<br>1 July 2007 to<br>31 December<br>2008<br>HK\$'000 |
|--|---|--|
| Cost and net carrying amount:                  |   |  |
| At beginning of year/period                    | 1,466,915                                     | –  |
| Acquisition of subsidiaries ( <i>note 39</i> ) | 20,607  | 1,466,760  |
| Acquisition of minority interests              | 87,925  | –  |
| Exchange realignment                           | 4   | 155  |
| At end of year/period                          | 1,575,451                                     | 1,466,915  |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 16. GOODWILL (Continued)

### Impairment testing of goodwill

The carrying amounts of the goodwill acquired through acquisitions, which have been allocated to the relevant business units of the following individual business operations of the Group for impairment testing, are summarised as follows:

|  | Group            |                  |
|--|------------------|------------------|
|  | 2009             | 2008             |
|  | HK\$'000         | HK\$'000         |
| Sewage treatment and construction services segment | 1,202,299        | 1,129,522        |
| Water supply services segment                      | 13,912           | –                |
| Sewage technical services segment                  | 359,240          | 337,393          |
|  | <b>1,575,451</b> | <b>1,466,915</b> |

The recoverable amounts of the relevant business units in each of the above operating segments have been determined by reference to business valuations performed by CB Richard Ellis Limited, independent professionally qualified valuers, on a fair value less costs to sell estimation using cash flow projections which are based on financial forecast approved by senior management covering a period of ten years and based on the assumption that the sizes of the operations remain constant perpetually. The discount rate applied to the cash flow projections for the first ten-year period is 11%, which is determined by reference to the average rates for the similar industries and the business risk of the relevant business unit. A growth rate of 3% is used for the perpetual period.

Based on the impairment testing of goodwill, in the opinion of the directors, no impairment provision is considered necessary for the Group's goodwill as at 31 December 2009.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 16. GOODWILL *(Continued)*

### Impairment testing of goodwill *(Continued)*

*Key assumptions used in fair value less costs to sell estimation*

The following describes each key assumption adopted by management in the preparation of the cash flow projections for the purpose of impairment testing of goodwill:

- Budgeted turnover
  - in respect of the revenue from the sewage treatment and construction services segment, and the water supply services segment, the budgeted turnover is based on the projected sewage treatment and water sales volume.
  - in respect of the revenue from the sewage technical services segment, the budgeted turnover is based on the expected growth rate of the market.
- Budgeted gross margins
  - in respect of the sewage treatment and construction services segment, and the water supply services segment, the basis used to determine the latest sewage treatment and water selling price up to the date of valuation report.
  - the basis used to determine the value assigned to the budgeted gross margins is the average gross margins achieved in the year immediately before the budget year, increased for expected efficiency improvements.
- Business environment
  - There have been no major changes in the existing political, legal and economic conditions in the Mainland China.
  - Under the service concession arrangements, the Group has been granted with priority for renewal of operating rights of sewage and water treatment plants. Given its historical performance record and its long-established relationship with the grantor, the Group has key advantages over other operators. In addition, the high investment cost has also created an entry barrier for new competitors. Therefore, in the opinion of the directors, the operating rights of sewage and water treatment plants shall be renewed at expiry, and therefore the sizes of the operations of the sewage treatment and water distribution operations are expected to remain constant perpetually which enables the Group to generate income perpetually.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 17. SERVICE CONCESSION ARRANGEMENTS

The Group has entered into a number of service concession arrangements with certain governmental authorities in Mainland China on a BOT or a Transfer-Operate-Transfer (“TOT”) basis in respect of its sewage and water treatment businesses. These service concession arrangements generally involve the Group as an operator (i) constructing sewage and water treatment plants for those arrangements on a BOT basis; (ii) paying a specific amount for those arrangements on a TOT basis; (iii) operating and maintaining the sewage and water treatment plants at a specified level of serviceability on behalf of the relevant governmental authorities for periods ranging from 20 to 40 years (the “service concession periods”), and the Group will be paid for its services over the relevant periods of the service concession arrangements at prices stipulated through a pricing mechanism. The Group is generally entitled to use all the property, plant and equipment of the sewage and water treatment plants, however, the relevant governmental authorities as grantors will control and regulate the scope of services the Group must provide with the sewage and water treatment plants, and retain the beneficial entitlement to any residual interest in the sewage and water treatment plants at the end of the term of the service concession periods. Each of these service concession arrangements is governed by a contract and, where applicable, supplementary agreements entered into between the Group and the relevant governmental authority in Mainland China that set out, inter alia, performance standards, mechanisms for adjusting prices for the services rendered by the Group, specific obligations levied on the Group to restore the sewage and water treatment plants to a specified level of serviceability at the end of the service concession periods, and arrangements for arbitrating disputes.

At 31 December 2009, the Group had 43 service concession arrangements on sewage treatment and 2 service concession arrangements on water treatment and distribution with various governmental authorities in Mainland China and a summary of the major terms of principal service concession arrangements are set out as follows:

| No. | Name of subsidiary as operator | Name of sewage and water treatment plant | Location                             | Name of grantor | Type of service concession arrangement | Practical processing capacity m <sup>3</sup> /day | Service concession period  |
|-----|--------------------------------|--|--------------------------------------|-----------------|--|---|----------------------------|
| 1.  | 江油中科成污水淨化有限公司                  | 江油市污水處理廠一期                               | Jianguyou, Sichuan Province, the PRC | 江油市人民政府         | BOT                                    | 25,000  | 30 years from 2002 to 2032 |
| 2.  | 江油中科成污水淨化有限公司                  | 江油市污水處理廠二期                               | Jianguyou, Sichuan Province, the PRC | 江油市人民政府         | BOT                                    | 25,000  | 30 years from 2007 to 2037 |
| 3.  | 成都雙流中科成污水淨化有限公司                | 雙流縣污水處理廠                                 | Shuangliu, Sichuan Province, the PRC | 雙流縣人民政府         | BOT                                    | 25,000  | 20 years from 2004 to 2024 |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 17. SERVICE CONCESSION ARRANGEMENTS (Continued)

| No. | Name of subsidiary as operator | Name of sewage and water treatment plant | Location                               | Name of grantor | Type of service concession arrangement | Practical processing capacity m <sup>3</sup> /day | Service concession period  |
|-----|--------------------------------|--|--|-----------------|--|---|----------------------------|
| 4.  | 成都雙流中科成污水淨化有限公司                | 雙流縣污水處理廠(二期)                             | Shuangliu, Sichuan Province, the PRC   | 雙流縣人民政府         | BOT                                    | 25,000  | 20 years from 2004 to 2024 |
| 5.  | 綿陽中科成污水淨化有限公司                  | 綿陽市塔子壩污水處理廠一期                            | Mianyang, Sichuan Province, the PRC    | 綿陽市人民政府         | TOT                                    | 100,000   | 30 years from 2002 to 2032 |
| 6.  | 綿陽中科成污水淨化有限公司                  | 綿陽市塔子壩污水處理廠二期                            | Mianyang, Sichuan Province, the PRC    | 綿陽市人民政府         | BOT                                    | 50,000  | 30 years from 2004 to 2034 |
| 7.  | 綿陽中科成污水淨化有限公司                  | 綿陽市塔子壩污水處理廠三期                            | Mianyang, Sichuan Province, the PRC    | 綿陽市人民政府         | BOT                                    | 50,000  | 30 years (Not yet started) |
| 8.  | 長沙中科成污水淨化有限公司                  | 長沙市金霞污水處理廠                               | Changsha, Hunan Province, the PRC      | 長沙市公用事業管理局      | TOT                                    | 180,000   | 20 years from 2004 to 2024 |
| 9.  | 青島膠南中科成污水淨化有限公司                | 膠南市污水處理廠                                 | Jiaonan, Shandong Province, the PRC    | 膠南市城鄉建設局        | BOT                                    | 60,000  | 20 years from 2006 to 2026 |
| 10. | 青島中科成污水淨化有限公司                  | 山東省膠州市污水處理廠                              | Jiaozhou, Shandong Province, the PRC   | 山東省膠州市城鄉建設局     | BOT                                    | 50,000  | 20 years from 2004 to 2024 |
| 11. | 青島膠州北控水務有限公司                   | 山東省膠州市污水處理廠                              | Jiaozhou, Shandong Province, the PRC   | 山東省膠州市城鄉建設局     | BOT                                    | 50,000  | 20 years (Not yet started) |
| 12. | 荷澤中科成污水淨化有限公司                  | 荷澤市污水處理廠                                 | Heze, Shandong Province, the PRC       | 荷澤市建設局          | TOT                                    | 80,000  | 25 years from 2007 to 2032 |
| 13. | 廣州中業污水處理有限公司                   | 廣州市花都區新華污水處理廠一期擴建工程                      | Guangzhou, Guangdong Province, the PRC | 廣州市花都區市政園林管理局   | BOT                                    | 100,000   | 25 years from 2008 to 2033 |



# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 17. SERVICE CONCESSION ARRANGEMENTS (Continued)

| No. | Name of subsidiary as operator | Name of sewage and water treatment plant | Location                               | Name of grantor | Type of service concession arrangement | Practical processing capacity m <sup>3</sup> /day | Service concession period  |
|-----|--------------------------------|--|--|-----------------|--|---|----------------------------|
| 14. | 廣州中業污水處理有限公司                   | 廣州市花都区新華污水處理廠(二期)                        | Guangzhou, Guangdong Province, the PRC | 廣州市花都区市政園林管理局   | BOT                                    | 99,000  | 25 years from 2009 to 2034 |
| 15. | 廣州中科成污水淨化有限公司                  | 廣州南沙開發區黃閣污水處理廠                           | Guangzhou, Guangdong Province, the PRC | 廣州南沙開發區建設局      | BOT                                    | 50,000  | 22 years from 2004 to 2026 |
| 16. | 廣州中科成污水淨化有限公司                  | 廣州南沙開發區黃閣污水處理廠(二期)                       | Guangzhou, Guangdong Province, the PRC | 廣州南沙開發區建設局      | BOT                                    | 50,000  | 22 years from 2004 to 2026 |
| 17. | 台州市路橋中科成污水淨化有限公司               | 路橋污水處理廠一期                                | Taizhou, Zhejiang Province, the PRC    | 台州市建設規劃局路橋分局    | TOT                                    | 40,000  | 27 years from 2006 to 2033 |
| 18. | 台州市路橋中科成污水淨化有限公司               | 路橋污水處理廠二期                                | Taizhou, Zhejiang Province, the PRC    | 台州市建設規劃局路橋分局    | BOT                                    | 50,000  | 27 years from 2006 to 2033 |
| 19. | 濟南中科成水質淨化有限公司                  | 濟南高新區水質淨化一廠一期                            | Jinan, Shandong Province, the PRC      | 濟南高新技術產業開發區中心   | TOT                                    | 10,000  | 30 years from 2008 to 2038 |
| 20. | 濟南中科成水質淨化有限公司                  | 濟南高新區水質淨化一廠二期                            | Jinan, Shandong Province, the PRC      | 濟南高新技術產業開發區中心   | BOT                                    | 40,000  | 30 years (Not yet started) |
| 21. | 佛山市三水中科成水質淨化有限公司               | 佛山市三水區中心工業園南部污水處理廠                       | Foshan, Guangdong Province, the PRC    | 佛山市三水工業園區管理委員會  | BOT                                    | 50,000  | 22 years (Not yet started) |
| 22. | 永州市北控污水淨化有限公司                  | 永州市下河綫污水處理廠                              | Yongzhou, Hunan Province, the PRC      | 永州市公用事業管理局      | BOT                                    | 50,000  | 30 years from 2008 to 2038 |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 17. SERVICE CONCESSION ARRANGEMENTS (Continued)

| No. | Name of subsidiary as operator                                       | Name of sewage and water treatment plant | Location                              | Name of grantor | Type of service concession arrangement | Practical processing capacity m <sup>3</sup> /day | Service concession period  |
|-----|--|--|---------------------------------------|-----------------|--|---|----------------------------|
| 23. | 永州市北控污水淨化有限公司  | 永州市道縣污水處理廠                               | Yongzhou, Hunan Province, the PRC     | 永州市道縣人民政府       | BOT                                    | 20,000  | 30 years from 2009 to 2039 |
| 24. | 永州市北控污水淨化有限公司  | 永州市江永縣污水處理廠                              | Yongzhou, Hunan Province, the PRC     | 永州市江永縣人民政府      | BOT                                    | 10,000  | 30 years from 2009 to 2039 |
| 25. | 永州市北控污水淨化有限公司  | 永州市新田縣污水處理廠                              | Yongzhou, Hunan Province, the PRC     | 永州市新田縣人民政府      | BOT                                    | 10,000  | 30 years from 2009 to 2039 |
| 26. | 深圳北控創新投資有限公司 ("Bei Kong Chuang Xin", formerly known as 深圳華強創新投資有限公司) | 深圳市橫嶺污水處理廠(二期)                           | Shenzhen, Guangdong Province, the PRC | 深圳市水務局          | TOT                                    | 400,000   | 20 years (Not yet started) |
| 27. | 深圳華強豐泰投資有限公司   | 深圳市龍崗區橫嶺污水處理廠                            | Shenzhen, Guangdong Province, the PRC | 深圳市龍崗區人民政府      | BOT                                    | 200,000   | 25 years from 2003 to 2028 |
| 28. | 濱州華強西海水務有限公司   | 濱州市西海供水工程 <sup>#</sup>                   | Binzhou, Shandong Province, the PRC   | 濱州市人民政府         | BOT                                    | 50,000  | 40 years from 2006 to 2046 |
| 29. | 台州黃岩北控水務污水淨化有限公司   | 台州市黃岩區污水處理廠                              | Huang Yan, Zhejiang Province, the PRC | 台州市黃岩區建設局       | TOT                                    | 80,000  | 30 years from 2009 to 2039 |
| 30. | 成都青白江中科成污水淨化有限公司   | 成都市青白江區污水處理廠                             | Chengdu, Sichuan Province, the PRC    | 成都市青白江區人民政府     | TOT                                    | 100,000   | 25 years from 2009 to 2034 |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 17. SERVICE CONCESSION ARRANGEMENTS (Continued)

| No. | Name of subsidiary as operator  | Name of sewage and water treatment plant | Location                                  | Name of grantor | Type of service concession arrangement | Practical processing capacity m <sup>3</sup> /day | Service concession period  |
|-----|---------------------------------|--|---|-----------------|--|---|----------------------------|
| 31. | 齊齊哈爾市北控污水淨化有限公司                 | 齊齊哈爾市富拉爾基區污水處理廠                          | Qi Qi Har, Heilongjiang Province, the PRC | 齊齊哈爾市環境保護局      | BOT                                    | 100,000   | 30 years (Not yet started) |
| 32. | 清鎮市北控水務有限公司                     | 貴陽清鎮朱家河一期污水處理廠                           | Guizhou, Yunnan Province, the PRC         | 清鎮市建設局          | TOT                                    | 25,000  | 30 years from 2009 to 2039 |
| 33. | 清鎮市北控水務有限公司                     | 貴陽清鎮朱家河二期污水處理廠                           | Guizhou, Yunnan Province, the PRC         | 清鎮市建設局          | BOT                                    | 27,500  | 30 years from 2009 to 2039 |
| 34. | 錦州市北控水務有限公司 ("Jinzhou Beikong") | 錦州市一期污水處理廠                               | Jinzhou, Liaoning Province, the PRC       | 錦州市公用事業與房產局     | TOT                                    | 100,000   | 30 years from 2009 to 2039 |
| 35. | 錦州市北控水務有限公司 ("Jinzhou Beikong") | 錦州市二期污水處理廠                               | Jinzhou, Liaoning Province, the PRC       | 錦州市公用事業與房產局     | BOT                                    | 100,000   | 30 years (Not yet started) |
| 36. | 錦州市北控水務有限公司 ("Jinzhou Beikong") | 錦州市再生水項目 <sup>#</sup>                    | Jinzhou, Liaoning Province, the PRC       | 錦州市公用事業與房產局     | BOT                                    | 180,000   | 30 years (Not yet started) |

# Except for these service concession arrangements being on water treatment and distribution, all other service concession arrangements of the Group are on sewage treatment.

The above table lists the service concession arrangements of the Group which, in the opinion of the directors, principally affected the results for the year/period or formed a substantial portion of the net assets of the Group. To give details of other service concession arrangements would, in the opinion of the directors, result in particulars of excessive length.

Pursuant to the service concession agreements signed, the Group are granted the rights to use the property, plant and equipment of the sewage and water treatment plants and related land, which are generally registered under the names of the relevant companies in the Group, during the service concession periods, but the Group is generally required to surrender these property, plant and equipment to the grantors at a specified level of serviceability at the end of the respective service concession periods. At 31 December 2009, the Group was in the process of applying for the changing of registration of the title certificates with respect to certain land use rights and buildings of certain sewage treatment plants to which the Group's service concession arrangements relate. The directors of the Company are of the opinion that the Group is entitled to the lawful and valid occupation or use of these buildings and land to which the above-mentioned land use rights relate, and that the Group would not have any legal barriers in obtaining the proper title certificates.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 17. SERVICE CONCESSION ARRANGEMENTS (Continued)

As further explained in the accounting policy for “Service concession arrangements” set out in note 3.4 to the financial statements, the consideration paid by the Group for a service concession arrangement is accounted for as an intangible asset (operating concession) or a financial asset (receivable under service concession arrangement) or a combination of both, as appropriate. The following is the summarised information of the intangible asset component (operating concession) and the financial asset component (receivable under service concession arrangement) with respect to the Group’s service concession arrangements:

### Operating concessions

#### Group

|   | Year ended<br>31 December<br>2009<br>HK\$'000 | Period from<br>1 July 2007 to<br>31 December<br>2008<br>HK\$'000 |
|---|---|--|
| At beginning of year/period:  |   |  |
| Cost  | 483,337                                       | –  |
| Accumulated amortisation  | (53,748)                                      | –  |
| Net carrying amount   | <u>429,589</u>                                | <u>–</u>   |
| Net carrying amount:  |   |  |
| At beginning of year/period   | 429,589                                       | –  |
| Acquisition of subsidiaries (note 39)                                 | –   | 436,105  |
| Additions   | 44,043  | –  |
| Amortisation provided during the year/period                          | (19,426)                                      | (5,799)  |
| Reclassification to receivables under service concession arrangements | (55,086)                                      | –  |
| Exchange realignment  | 12  | (717)  |
| At end of year/period   | <u>399,132</u>                                | <u>429,589</u>   |
| At end of year/period:  |   |  |
| Cost  | 467,714                                       | 483,337  |
| Accumulated amortisation  | (68,582)                                      | (53,748)   |
| Net carrying amount   | <u>399,132</u>                                | <u>429,589</u>   |

At 31 December 2009, certain sewage treatment concession rights of the Group in a then aggregate net carrying amount of HK\$85,376,000 (2008: HK\$98,529,000), together with certain of the property, plant and equipment of the related sewage treatment plants, are pledged to secure certain bank loans granted to the Group (note 30(b)(i)).

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 17. SERVICE CONCESSION ARRANGEMENTS *(Continued)*

### Receivables under service concession arrangements

|   | Group            |           |
|---|------------------|-----------|
|   | 2009             | 2008      |
|   | HK\$'000         | HK\$'000  |
| Receivables under service concession arrangements | 2,061,249        | 1,382,478 |
| Impairment <i>(note (b))</i>                      | (6,984)          | (8,822)   |
|   | <b>2,054,265</b> | 1,373,656 |
| Portion classified as current assets              | (137,443)        | (135,347) |
|   | <b>1,916,822</b> | 1,238,309 |

#### Notes:

- (a) In respect of the Group's receivables under service concession arrangements, the various group companies have different credit policies, depending on the requirements of the locations in which they operate. Aged analysis of receivables under service concession arrangements are closely monitored in order to minimise any credit risk associated with the receivables.

An aged analysis of the Group's receivables under service concession arrangements as at the end of the reporting period, based on the invoice date and net of impairment, is as follows:

|                 | Group            |           |
|-----------------|------------------|-----------|
|                 | 2009             | 2008      |
|                 | HK\$'000         | HK\$'000  |
| Billed:         |                  |           |
| Within 3 months | 90,285           | 55,751    |
| 4 to 6 months   | 34,923           | 42,121    |
| 7 to 12 months  | 11,151           | 35,661    |
| 1 to 2 years    | 1,084            | 1,814     |
|                 | <b>137,443</b>   | 135,347   |
| Unbilled        | <b>1,916,822</b> | 1,238,309 |
|                 | <b>2,054,265</b> | 1,373,656 |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 17. SERVICE CONCESSION ARRANGEMENTS *(Continued)*

### Receivables under service concession arrangements *(Continued)*

Notes: *(Continued)*

- (b) The movements in the provision for impairment of the Group's receivables under service concession arrangements during the year/period are as follows:

|   | Group   |  |
|---|---|--|
|   | Year ended<br>31 December<br>2009<br>HK\$'000 | Period from<br>1 July 2007 to<br>31 December<br>2008<br>HK\$'000 |
| At beginning of year/period   | 8,822   | –  |
| Acquisition of subsidiaries   | –   | 7,072  |
| Impairment/(reversal of impairment) during the year/period<br>recognised in the income statement, net <i>(note 7)</i> | (408)   | 1,748  |
| Amount written off as uncollectable   | (1,430)                                       | –  |
| Exchange realignment  | –   | 2  |
| At end of year/period   | <b>6,984</b>                                  | <b>8,822</b>   |

The above provision for impairment of receivables under service concession arrangements as at 31 December 2009 was made against the whole balances of the receivables under service concession arrangements collectively as at that date. The Group does not hold any collateral or other credit enhancements over these balances.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 17. SERVICE CONCESSION ARRANGEMENTS *(Continued)*

### Receivables under service concession arrangements *(Continued)*

Notes: *(Continued)*

(b) *(Continued)*

An aged analysis of the billed receivables under service concession arrangements that are neither individually nor collectively considered to be impaired is as follows:

|                               | Group          |                |
|-------------------------------|----------------|----------------|
|                               | 2009           | 2008           |
|                               | HK\$'000       | HK\$'000       |
| Neither past due nor impaired | 43,020         | 23,071         |
| Less than 1 month past due    | 12,883         | 35,869         |
| 1 to 3 months past due        | 44,331         | 31,073         |
| 4 to 6 months past due        | 29,487         | 18,522         |
| 7 months to 1 year past due   | 6,575          | 25,043         |
| Over 1 year past due          | 1,147          | 1,769          |
|                               | <b>137,443</b> | <b>135,347</b> |

Receivables classified as non-current were neither past due nor impaired.

The above receivables were mainly due from governmental authorities in Mainland China as grantors in respect of the Group's sewage treatment business.

Based on past experience, the directors of the Company are of the opinion that no provision for impairment is necessary in respect of these balances as there has not been a significant change in credit quality and the balances are still considered fully recoverable. The Group does not hold any collateral or other credit enhancements over these balances.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 18. OTHER INTANGIBLE ASSETS

### Group

|  | Patents<br><i>HK\$'000</i> | Computer<br>software<br><i>HK\$'000</i> | Total<br><i>HK\$'000</i> |
|--|----------------------------|---|--------------------------|
| <b>Year ended 31 December 2009</b>                     |                            |   |                          |
| At 31 December 2008 and 1 January 2009:                |                            |   |                          |
| Cost   | 555                        | 1,628                                   | 2,183                    |
| Accumulated amortisation                               | (449)                      | (78)                                    | (527)                    |
| Net carrying amount                                    | 106                        | 1,550                                   | 1,656                    |
| Net carrying amount:                                   |                            |   |                          |
| At 1 January 2009                                      | 106                        | 1,550                                   | 1,656                    |
| Acquisition of subsidiaries ( <i>note 39</i> )         | –                          | 81                                      | 81                       |
| Additions  | –                          | 1,887                                   | 1,887                    |
| Amortisation provided during the year                  | (56)                       | (200)                                   | (256)                    |
| Disposals  | –                          | (75)                                    | (75)                     |
| At 31 December 2009                                    | 50                         | 3,243                                   | 3,293                    |
| At 31 December 2009:                                   |                            |   |                          |
| Cost   | 555                        | 3,521                                   | 4,076                    |
| Accumulated amortisation                               | (505)                      | (278)                                   | (783)                    |
| Net carrying amount                                    | 50                         | 3,243                                   | 3,293                    |
| <b>Period from 1 July 2007<br/>to 31 December 2008</b> |                            |   |                          |
| At 1 July 2007:  |                            |   |                          |
| Cost and net carrying amount                           | –                          | –                                       | –                        |
| Net carrying amount:                                   |                            |   |                          |
| At 1 July 2007   | –                          | –                                       | –                        |
| Acquisition of subsidiaries ( <i>note 39</i> )         | 133                        | 1,086                                   | 1,219                    |
| Additions  | –                          | 522                                     | 522                      |
| Amortisation provided during the period                | (26)                       | (52)                                    | (78)                     |
| Exchange realignment                                   | (1)                        | (6)                                     | (7)                      |
| At 31 December 2008                                    | 106                        | 1,550                                   | 1,656                    |



# NOTES TO FINANCIAL STATEMENTS

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## 19. INTERESTS IN SUBSIDIARIES

|   | Notes | Company          |                  |
|---|-------|------------------|------------------|
|   |       | 2009             | 2008             |
|   |       | HK\$'000         | HK\$'000         |
| Unlisted shares or investments, at cost |       | 2,374,007        | 1,943,342        |
| Due from subsidiaries                   | (a)   | 866,240          | 942,352          |
| Due to subsidiaries                     | (a)   | (502,016)        | –                |
|   |       | <b>2,738,231</b> | <b>2,885,694</b> |

Notes:

- (a) The amounts due from/to subsidiaries are unsecured, interest-free and have no fixed terms of repayment.
- (b) Particulars of the principal subsidiaries are as follows:

| Company name   | Place of incorporation/ registration and operations | Nominal value of issued and paid-up capital/ registered capital | Percentage of attributable equity interest held by |       | Principal activities                       |
|--|---|---|--|-------|--|
|  |   |   | Company  | Group |  |
| Beijing Enterprises Z.K.C. Environmental Co., Ltd. ("BE-ZKC", formerly known as Z.K.C Environmental Group Co., Ltd.) | PRC/ Mainland China                                 | RMB286,969,071  | –  | 99.21 | Consultancy service and investment holding |
| 深圳北控創新投資有限公司   | PRC/ Mainland China                                 | RMB300,000,000  | –  | 88.27 | Investment holding                         |
| 深圳華強豐泰投資有限公司   | PRC/ Mainland China                                 | RMB70,000,000   | –  | 70.61 | Sewage treatment                           |
| 綿陽中科成污水淨化有限公司  | PRC/ Mainland China                                 | RMB40,000,000   | –  | 99.21 | Sewage treatment                           |
| 長沙中科成污水淨化有限公司  | PRC/ Mainland China                                 | RMB50,000,000   | –  | 89.29 | Sewage treatment                           |
| 廣州中業污水處理有限公司   | PRC/ Mainland China                                 | RMB85,000,000   | –  | 99.21 | Sewage treatment                           |
| 江油中科成污水淨化有限公司  | PRC/ Mainland China                                 | RMB8,000,000  | –  | 99.21 | Sewage treatment                           |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 19. INTERESTS IN SUBSIDIARIES (Continued)

Notes: (Continued)

(b) (Continued)

| Company name         | Place of incorporation/<br>registration<br>and operations | Nominal value of<br>issued and<br>paid-up capital/<br>registered capital | Percentage of<br>attributable equity<br>interest held by |       | Principal<br>activities |
|----------------------|---|--|--|-------|-------------------------|
|                      |   |  | Company  | Group |                         |
| 成都雙流中科成污水淨化<br>有限公司  | PRC/<br>Mainland China                                    | RMB10,000,000  | –  | 79.37 | Sewage<br>treatment     |
| 青島膠南中科成污水淨化<br>有限公司  | PRC/<br>Mainland China                                    | RMB30,000,000  | –  | 99.21 | Sewage<br>treatment     |
| 青島中科成污水淨化有限公司        | PRC/<br>Mainland China                                    | RMB20,000,000  | –  | 99.21 | Sewage<br>treatment     |
| 廣州中科成污水淨化有限公司        | PRC/<br>Mainland China                                    | RMB30,000,000  | –  | 99.21 | Sewage<br>treatment     |
| 青島上馬中科成污水淨化<br>有限公司  | PRC/<br>Mainland China                                    | RMB15,000,000  | –  | 99.21 | Sewage<br>treatment     |
| 成都華陽中科成污水淨化<br>有限公司  | PRC/<br>Mainland China                                    | RMB9,000,000   | –  | 99.21 | Sewage<br>treatment     |
| 台州市路橋中科成污水淨化<br>有限公司 | PRC/<br>Mainland China                                    | RMB55,500,000  | –  | 99.21 | Sewage<br>treatment     |
| 成都龍泉中科成污水淨化<br>有限公司  | PRC/<br>Mainland China                                    | RMB27,600,000  | –  | 99.21 | Sewage<br>treatment     |
| 菏澤中科成污水淨化有限公司        | PRC/<br>Mainland China                                    | RMB30,000,000  | –  | 99.21 | Sewage<br>treatment     |
| 濟南中科成水質淨化有限公司        | PRC/<br>Mainland China                                    | RMB20,000,000  | –  | 99.21 | Sewage<br>treatment     |
| 彭州中科成污水淨化有限公司        | PRC/<br>Mainland China                                    | RMB28,000,000  | –  | 99.21 | Sewage<br>treatment     |
| 佛山市三水中科成水質淨化<br>有限公司 | PRC/<br>Mainland China                                    | RMB76,000,000  | –  | 99.21 | Sewage<br>treatment     |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 19. INTERESTS IN SUBSIDIARIES (Continued)

Notes: (Continued)

(b) (Continued)

| Company name   | Place of incorporation/<br>registration<br>and operations | Nominal value of<br>issued and<br>paid-up capital/<br>registered capital | Percentage of<br>attributable equity<br>interest held by |                 | Principal<br>activities                    |
|--|---|--|--|-----------------|--|
|  |   |  | Company  | Group           |  |
| 北控水務(廣西)有限公司 <sup>□</sup>  | PRC/<br>Mainland China                                    | HK\$30,000,000   | –  | 100             | Investment<br>holding                      |
| 永州市北控污水淨化有限公司 <sup>□</sup>   | PRC/<br>Mainland China                                    | HK\$73,130,000   | 100  | 100             | Sewage<br>treatment                        |
| 濱州華強西海水務有限公司   | PRC/<br>Mainland China                                    | RMB50,000,000  | –  | 73.97           | Water<br>supply                            |
| 沾化華強水務環保有限公司   | PRC/<br>Mainland China                                    | RMB10,000,000  | –  | 81.83           | Sewage<br>treatment                        |
| 北控水務(中國)投資有限公司 <sup>□</sup>  | PRC/<br>Mainland China                                    | US\$32,600,000   | 100  | 100             | Investment<br>holding                      |
| 雲南中科城投水務有限公司 <sup>△</sup>  | PRC/<br>Mainland China                                    | RMB400,000,000   | –  | 50 <sup>†</sup> | Investment<br>holding                      |
| 錦州市北控水務有限公司 <sup>△</sup>   | PRC/<br>Mainland China                                    | RMB105,355,240   | 80   | 80              | Sewage<br>treatment<br>and water<br>supply |
| 齊齊哈爾市北控污水淨化<br>有限公司 <sup>△</sup>   | PRC/<br>Mainland China                                    | RMB56,000,000  | –  | 100             | Sewage<br>treatment                        |
| 清鎮市北控水務有限公司 <sup>△</sup>   | PRC/<br>Mainland China                                    | RMB10,000,000  | –  | 60              | Sewage<br>treatment                        |
| 北京北控污水淨化及回用<br>有限公司 <sup>△</sup>   | PRC/<br>Mainland China                                    | RMB26,360,000  | –  | 100             | Sewage<br>treatment                        |
| 廣西貴港北控水務有限公司 <sup>△</sup><br>("Guigang Water", formerly known<br>as 貴港市供水有限責任公司) | PRC/<br>Mainland China                                    | RMB33,184,898  | –  | 66.67           | Sewage<br>treatment and<br>water supply    |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 19. INTERESTS IN SUBSIDIARIES *(Continued)*

*Notes: (Continued)*

(b) *(Continued)*

<sup>†</sup> *This entity is accounted for as a subsidiary by virtue of the Company's control over it.*

<sup>Ω</sup> *These entities are registered as wholly-foreign-owned enterprises under the PRC Law.*

<sup>§</sup> *Acquired/incorporated during the year.*

The above table lists the subsidiaries of the Company which, in the opinion of the directors, principally affected the results for the year or formed a substantial portion of the net assets of the Group. To give details of other subsidiaries would, in the opinion of the directors, result in particulars of excessive length.

During the year, the Group acquired a 66.67% equity interest in Guigang Water. Guigang Water and its subsidiaries are principally engaged in the operations of sewage treatment and water supply, and the provision of related water supply services in Guigang Municipality, Guangxi Province, the PRC.

In addition, on 15 August 2009, the Group acquired the sewage and water treatment business previously operated by a government authority in Mainland China by the establishment of Jinzhou Beikong, in which the Group holds a 80% equity interest, with the government authority (the "Jinzhou JV Partner").

Further details of the above acquisition transactions are included in note 39 to the financial statements.

During the year, the Group disposal of its entire interest in 四川中科成投資管理有限公司 ("Sichuan ZKC Investment Management"), a then 86.86% indirectly-owned subsidiary of the Company, further details of which are included in note 40 to the financial statements.

# NOTES TO FINANCIAL STATEMENTS

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## 20. INTEREST IN AN ASSOCIATE

The associate of the Group as at 31 December 2008 was a 23% equity interest in 中信產業基金管理有限公司 (“Zhongxin Chanye”), which is established in Mainland China and engaged in fund management. Pursuant to two share transfer agreements both dated 23 March 2009 entered into between BE-ZKC, Sichuan ZKC Investment Management (a then indirectly-owned subsidiary of the Company) and a related company, BE-ZKC disposed of the entire 23% equity interest in Zhongxin Chanye (an associate of BE-ZKC prior to the completion of the above transaction) to Sichuan ZKC Investment Management and the related company for a total cash consideration of RMB23,000,000. Upon the disposal of Sichuan ZKC Investment Management as further detailed in notes 19 and 40 to the financial statements, Zhongxin Chanye ceased to be an associate of the Group during the year.

The following tables illustrate the summarised financial information of the Group’s associate:

|  | 2009<br><i>HK\$'000</i>  | 2008<br><i>HK\$'000</i>  |
|--|--|--|
| <b>Share of the associate’s assets and liabilities</b> |  |  |
| Non-current assets                                     | –  | 7  |
| Current assets   | –  | 25,312   |
| Current liabilities                                    | –  | (6)  |
| Net assets   | –  | 25,313   |
|  | <b>Year ended<br/>31 December<br/>2009<br/><i>HK\$'000</i></b> | <b>Period from<br/>1 July 2007 to<br/>31 December<br/>2008<br/><i>HK\$'000</i></b> |
| <b>Share of the associate’s results</b>                |  |  |
| Revenue  | 10,449   | 259  |
| Total expenses   | (4,776)  | (1,070)  |
| Profit/(loss) before tax                               | 5,673  | (811)  |
| Income tax   | (1,108)  | –  |
| Profit/(loss) for the year/period                      | 4,565  | (811)  |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 21. AVAILABLE-FOR-SALE INVESTMENT

The available-for-sale investment of the Group is a 4.08% equity interest in 四川省水處理及資源化工程技術研究中心, which is an unlisted equity investment in Mainland China.

The investment was not stated at fair value but at cost less any accumulated impairment losses because it does not have a quoted market price in an active market and hence, in the opinion of the directors, the range of reasonable fair value estimates is significant and the probabilities of the various estimates cannot be reasonably assessed.

## 22. INVENTORIES

|                       | Group        |              |
|-----------------------|--------------|--------------|
|                       | 2009         | 2008         |
|                       | HK\$'000     | HK\$'000     |
| Raw materials         | 6,129        | 3,179        |
| Low value consumables | 1,010        | 954          |
|                       | <u>7,139</u> | <u>4,133</u> |

## 23. AMOUNTS DUE FROM CONTRACT CUSTOMERS

|   | Group            |                |
|---|------------------|----------------|
|   | 2009             | 2008           |
|   | HK\$'000         | HK\$'000       |
| Contract costs incurred plus recognised profit less recognised losses to date | 1,141,903        | 200,462        |
| Impairment ( <i>note</i> )  | (6,273)          | –              |
|   | <u>1,135,630</u> | <u>200,462</u> |
| Portion classified as current assets  | (49,930)         | (200,462)      |
| Non-current portion   | <u>1,085,700</u> | <u>–</u>       |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 23. AMOUNTS DUE FROM CONTRACT CUSTOMERS *(Continued)*

*Note:* The movement in provision for impairment of amounts due from contract customers during the year/period is as follows:

|   | Year ended<br>31 December<br>2009<br><i>HK\$'000</i> | Period from<br>1 July 2007 to<br>31 December<br>2008<br><i>HK\$'000</i> |
|---|--|---|
| At beginning of year/period   | –  | –   |
| Impairment during the year/period recognised<br>in the income statement <i>(note 7)</i> | <u>6,273</u>   | –   |
| At end of year/period   | <u>6,273</u>   | –   |

Included in the above provision for impairment of amounts due from contract customers is a full provision for an individually impaired amount due from a contract customer, in which the contract customer is in delinquency in principal payment, and the entire carrying amount before provision is not expected to be recovered. The Group does not hold any collateral or other credit enhancement over the balance.

## 24. TRADE RECEIVABLES

|                                      | Group                   |                         | Company                 |                         |
|--------------------------------------|-------------------------|-------------------------|-------------------------|-------------------------|
|                                      | 2009<br><i>HK\$'000</i> | 2008<br><i>HK\$'000</i> | 2009<br><i>HK\$'000</i> | 2008<br><i>HK\$'000</i> |
| Trade receivables                    | 152,123                 | 9,638                   | 85,693                  | –                       |
| Impairment <i>(note (c))</i>         | <u>(1,221)</u>          | <u>(609)</u>            | <u>–</u>                | <u>–</u>                |
| Portion classified as current assets | 150,902                 | 9,029                   | 85,693                  | –                       |
|                                      | <u>(99,192)</u>         | <u>(9,029)</u>          | <u>(85,693)</u>         | <u>–</u>                |
| Non-current portion                  | 51,710                  | –                       | –                       | –                       |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 24. TRADE RECEIVABLES *(Continued)*

*Notes:*

- (a) The Group's trade receivables arise from the construction services for a BT contract, sewage technical services, sale of water and related water supply services and sale of sewage treatment facilities. The Group's trading terms with its customers are mainly on credit and each customer has a maximum credit limit. The various group companies have different credit policies, depending on the requirements of their markets in which they operate and the businesses they engage in. The credit period granted to customers is generally one month to three months, except for a customer with instalment period extended up to 25 years. The Group seeks to maintain strict control over its outstanding receivables and has a credit control department to minimise credit risk. Overdue balances are reviewed regularly by senior management. Trade receivables are non-interest-bearing.

An aged analysis of the trade receivables as at the end of the reporting period, based on the invoice date and net of impairment, is as follows:

|                                     | Group            |                  | Company          |                  |
|-------------------------------------|------------------|------------------|------------------|------------------|
|                                     | 2009<br>HK\$'000 | 2008<br>HK\$'000 | 2009<br>HK\$'000 | 2008<br>HK\$'000 |
| Within 3 months                     | 62,763           | 8,789            | 50,239           | –                |
| 4 to 6 months                       | 324              | –                | –                | –                |
| 7 to 12 months                      | 35,667           | –                | 35,454           | –                |
| 1 to 2 years                        | 438              | 240              | –                | –                |
| Balance with extended credit period | 51,710           | –                | –                | –                |
|                                     | <b>150,902</b>   | <b>9,029</b>     | <b>85,693</b>    | <b>–</b>         |

- (b) Included in the trade receivables of the Group and the Company as at 31 December 2009 were HK\$85,693,000 due from 北京北控環保工程技術有限公司 and 北控水務集團(海南)有限公司, both being fellow subsidiaries of the Company, arising from the sale of sewage treatment facilities carried out in the ordinary course of business of the Group. The balances with the fellow subsidiaries were unsecured, interest-free and repayable within credit periods similar to those offered by the Group to its major customers.

Further details of the transactions with the aforesaid two fellow subsidiaries are set out in the Company's circulars dated 18 August 2009 and 13 January 2010.



# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 24. TRADE RECEIVABLES (Continued)

Notes: (Continued)

(c) The movements in the Group's provision for impairment of trade receivables during the year/period are as follows:

|  | Group   |  |
|--|---|--|
|  | Year ended<br>31 December<br>2009<br>HK\$'000 | Period from<br>1 July 2007 to<br>31 December<br>2008<br>HK\$'000 |
| At beginning of year/period  | 609   | –  |
| Acquisition of subsidiaries  | –   | 677  |
| Impairment/(reversal of impairment) during the year/period<br>recognised in the income statement, net (note 7) | 612   | (69)   |
| Exchange realignment   | –   | 1  |
| At end of year/period  | <b>1,221</b>                                  | 609  |

The above provision for impairment of trade receivables was made against the whole balances of trade receivables collectively as at that date. The Group does not hold any collateral or other credit enhancements over these balances.

An aged analysis of the billed trade receivables as at the end of the reporting period that are neither individually nor collectively considered to be impaired is as follows:

|                               | Group            |                  | Company          |                  |
|-------------------------------|------------------|------------------|------------------|------------------|
|                               | 2009<br>HK\$'000 | 2008<br>HK\$'000 | 2009<br>HK\$'000 | 2008<br>HK\$'000 |
| Neither past due nor impaired | 108,491          | 8,407            | 50,239           | –                |
| Less than 1 month past due    | 606              | –                | –                | –                |
| 1 to 3 months past due        | 5,375            | 382              | –                | –                |
| 4 to 6 months past due        | 324              | –                | –                | –                |
| 7 months to 1 year past due   | 35,668           | –                | 35,454           | –                |
| Over 1 year past due          | 438              | 240              | –                | –                |
|                               | <b>150,902</b>   | 9,029            | <b>85,693</b>    | –                |

Receivables that were neither past due nor impaired mainly related to the construction services for a BT contract with instalment period extended up to 25 years. Receivables that were past due but not impaired relate to a number of independent customers that have a good track record with the Group. Based on past experience, the directors of the Company are of the opinion that no provision for impairment is necessary in respect of these balances as there has not been a significant change in credit quality and the balances are still considered fully recoverable. The Group does not hold any collateral or other credit enhancements over these balances.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 25. PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

|                                      | Group            |           | Company          |          |
|--------------------------------------|------------------|-----------|------------------|----------|
|                                      | 2009             | 2008      | 2009             | 2008     |
|                                      | HK\$'000         | HK\$'000  | HK\$'000         | HK\$'000 |
| Prepayments                          | 5,202            | 516       | 417              | –        |
| Deposits and other debtors           | 877,761          | 249,923   | 586,296          | 200      |
| Advances to suppliers                | 21,932           | 47,170    | –                | –        |
| Due from related parties (note 26)   | 14,062           | 124,888   | –                | –        |
|                                      | <b>918,957</b>   | 422,497   | <b>586,713</b>   | 200      |
| Impairment (note (b))                | <b>(3,188)</b>   | (1,074)   | –                | –        |
|                                      | <b>915,769</b>   | 421,423   | <b>586,713</b>   | 200      |
| Portion classified as current assets | <b>(710,579)</b> | (302,099) | <b>(586,713)</b> | (200)    |
|                                      | <b>205,190</b>   | 119,324   | –                | –        |

Notes:

- (a) The Group's deposits and other debtors as at 31 December 2009 included, inter alia, the following:
- (i) various tender deposits of RMB525,310,000 (equivalent to HK\$596,672,000) (2008: RMB30,650,000 (equivalent to HK\$34,812,000)) in aggregate paid by the Group for the bidding of potential sewage treatment projects. These deposits are classified as current assets.
  - (ii) an instalment of RMB154,000,000 (equivalent to HK\$175,000,000) paid to a government authority in Mainland China for the procurement of a concession right to operate a sewage treatment plant in Shenzhen on a TOT basis. The balance is classified as a non-current asset.
  - (iii) cash advances of RMB11,092,000 (equivalent to HK\$12,599,000) (2008: RMB41,107,000 (equivalent to HK\$46,689,000)) in aggregate made to a contract customer of the Group in connection with a contract of service dated 8 May 2008 entered into between the two parties, pursuant to which the Group is providing (i) construction management services to the customer regarding the construction of a sewage treatment plant in Mainland China by the customer; and (ii) funding at the maximum amount of RMB60 million (equivalent to HK\$68 million) to the customer to finance the construction of the sewage treatment plant. Notwithstanding that any advances made had been due for repayment on 25 April 2009, in the opinion of the directors, no impairment against these advances is considered necessary. The balance is classified as a current asset.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 25. PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES *(Continued)*

*Notes: (Continued)*

(a) *(Continued)*

(iv) a deposit of RMB10,150,000 (equivalent to HK\$11,528,000) (2008: RMB10,150,000 (equivalent to HK\$11,528,000)) paid for the purchase of an office building in Chengdu, Sichuan Province, the PRC. The balance is classified as a non-current asset.

(v) a deposit of RMB8,000,000 (equivalent to HK\$9,086,000) (2008: RMB8,000,000 (equivalent to HK\$9,086,000)) paid to guarantee the performance of all obligations under a lease arrangement for the purchase of certain equipment. The balance is classified as a non-current asset and further details of the lease arrangement are set out in note 32 to the financial statements.

(b) The movements in the provision for impairment of other receivables during the year/period are as follows:

|  | Group  |   |
|--|--|---|
|  | Year ended<br>31 December<br>2009<br><i>HK\$'000</i> | Period from<br>1 July 2007 to<br>31 December<br>2008<br><i>HK\$'000</i> |
| At beginning of year/period  | 1,074  | –   |
| Acquisition of subsidiaries  | 1,522  | 786   |
| Impairment during the year/period recognised in<br>the income statement, net <i>(note 7)</i> | 592  | 205   |
| Exchange realignment   | –  | 83  |
| At end of year/period  | <b>3,188</b>   | 1,074   |

The above provision for impairment of other receivables was made against the whole balances of other receivables collectively as at that date. The Group does not hold any collateral or other credit enhancements over these balances.

# NOTES TO FINANCIAL STATEMENTS

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## 26. DUE FROM/TO RELATED PARTIES/A SHAREHOLDER

- (a) The amounts due from related parties are unsecured, interest-free and have no fixed terms of repayment.
- (b) Particulars of the amounts due from related parties, disclosed pursuant to Section 161B of the Hong Kong Companies Ordinance, are as follows:

| Name                  | 31 December<br>2009<br>HK\$'000 | Maximum<br>amount<br>outstanding<br>during the year<br>HK\$'000 | 1 January<br>2009<br>HK\$'000 |
|-----------------------|---------------------------------|---|-------------------------------|
| Group                 |                                 |   |                               |
| 成都太然投資有限公司 *          | —                               | 14,195  | 14,195                        |
| Other related parties | 14,062                          |   | 110,693                       |
|                       | <u>14,062</u>                   |   | <u>124,888</u>                |

\* Mr. Hu Xiaoyong, a director of the Company, has a beneficial interest in this company.

# NOTES TO FINANCIAL STATEMENTS

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## 26. DUE FROM/TO RELATED PARTIES/A SHAREHOLDER *(Continued)*

- (c) Included in the amounts due from related parties of the Group as at 31 December 2008 was an amount of RMB86,908,000 (equivalent to HK\$98,716,000) due from 鴻橋投資有限公司 (“Hong Qiao”, a company established in Mainland China holding a 40% equity interest in Bei Kong Chuang Xin), which represented the remaining unsettled portion of the purchase consideration paid to the vendor on behalf of Hong Qiao by the Group pursuant to the Assignment of Equity Interest Agreement (as defined in the Company’s circular dated 6 October 2008) entered into between the Group and Hong Qiao in connection with the acquisition of Bei Kong Chuang Xin in 2008. During the year, the amount was settled by the deduction in the same amount of the capital contributed by Hong Qiao in Bei Kong Chuang Xin in accordance with a share transfer agreement entered into between the Group and Hong Qiao on 30 June 2009. Following the completion of the transaction during the year, the Group’s equity interest in Bei Kong Chuang Xin increased from 60% to 88.97% while the profit sharing ratio remains to be 60%. Further details of the acquisition of Bei Kong Chuang Xin in the prior period are disclosed in note 39(c)(ii) to the financial statements.
- (d) The amount due to a shareholder of the Group and the Company as at 31 December 2008 was the outstanding consideration payable in connection with the Group’s acquisition of 100% equity interest in Monico Investments Limited (“Monico”), as further detailed in note 39(c)(i) to the financial statements. The amount was fully settled by the Group during the year.

## 27. RESTRICTED CASH AND PLEDGED DEPOSITS AND CASH AND CASH EQUIVALENTS

|   | Group            |                  | Company          |                  |
|---|------------------|------------------|------------------|------------------|
|   | 2009<br>HK\$'000 | 2008<br>HK\$'000 | 2009<br>HK\$'000 | 2008<br>HK\$'000 |
| Cash and bank balances  | 845,783          | 671,240          | 8,697            | 15,376           |
| Cash equivalents  | 1,457            | 1,392            | –                | –                |
| Time deposits   | 43,640           | 170,370          | –                | –                |
|   | <b>890,880</b>   | 843,002          | <b>8,697</b>     | 15,376           |
| Less: Restricted cash and<br>pledged deposits <i>(note (a))</i> | <b>(14,019)</b>  | (8,066)          | –                | –                |
| Cash and cash equivalents                                       | <b>876,861</b>   | 834,936          | <b>8,697</b>     | 15,376           |

# NOTES TO FINANCIAL STATEMENTS

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## 27. RESTRICTED CASH AND PLEDGED DEPOSITS AND CASH AND CASH EQUIVALENTS

(Continued)

Notes:

- (a) The Group's restricted cash and pledged deposits as at 31 December 2009 included the following:
- (i) RMB6,500,000 (equivalent to HK\$7,383,000) (2008: Nil) pledged to banks for the issuance of guarantees by the banks to the grantors in respect of the specific performance of the duties by the Group under the relevant service concession agreements; and
  - (ii) RMB5,842,000 (equivalent to HK\$6,636,000) (2008: RMB101,000 (equivalent to HK\$115,000)) pledged to banks to secure certain banking facilities granted to the Group (*note 30(b)*).

In addition to the above, as at 31 December 2008, RMB7,000,000 (equivalent to HK\$7,951,000) was pledged to certain government authorities in Mainland China as a condition to place tenders for sewage treatment projects.

- (b) At 31 December 2009, the cash and bank balances and time deposits of the Group denominated in RMB amounted to HK\$865,386,000 (2008: HK\$827,043,000). The RMB is not freely convertible into other currencies, however, under Mainland China's Foreign Exchange Control Regulations and Administration of Settlement, Sale and Payment of Foreign Exchange Regulations, the Group is permitted to exchange RMB for other currencies through banks authorised to conduct foreign exchange business.
- (c) The bank balances and pledged deposits are deposited with creditworthy banks with no recent history of defaults.

## 28. SHARE CAPITAL

|  | 2009<br>HK\$'000 | 2008<br>HK\$'000 |
|--|------------------|------------------|
| Authorised:  |                  |                  |
| 15,000,000,000 (2008: 15,000,000,000) ordinary shares of HK\$0.10 each                   | <u>1,500,000</u> | <u>1,500,000</u> |
| Issued and fully paid:   |                  |                  |
| 3,482,196,992 (2008: 2,405,073,357) ordinary shares of HK\$0.10 each ( <i>note (a)</i> ) | <u>348,219</u>   | <u>240,507</u>   |

# NOTES TO FINANCIAL STATEMENTS

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## 28. SHARE CAPITAL *(Continued)*

A summary of the movements in the Company's issued share capital during the year ended 31 December 2009 and the period ended 31 December 2008 is as follows:

|  | <i>Notes</i> | Number of<br>ordinary shares<br>in issue | Issued capital<br><i>HK\$'000</i> | Share<br>premium<br>account<br><i>HK\$'000</i> | Total<br><i>HK\$'000</i> |
|--|--------------|--|-----------------------------------|--|--------------------------|
| At 1 July 2007   |              | 83,285,449                               | 8,328                             | –  | 8,328                    |
| Share placement  | <i>(a)</i>   | 247,000,000                              | 24,700                            | 74,100   | 98,800                   |
| Allotment of shares for the acquisition<br>of Gainstar Limited | <i>(b)</i>   | 559,787,908                              | 55,979                            | 694,137  | 750,116                  |
| Shares issued upon conversion of<br>convertible bonds          | <i>(c)</i>   | 1,515,000,000                            | 151,500                           | 460,211  | 611,711                  |
| Share issue expenses   |              | <u>–</u>                                 | <u>–</u>                          | <u>(2,968)</u>                                 | <u>(2,968)</u>           |
| At 31 December 2008 and<br>1 January 2009                      |              | 2,405,073,357                            | 240,507                           | 1,225,480                                      | 1,465,987                |
| Issue of new shares  | <i>(b)</i>   | 226,683,106                              | 22,668                            | 281,087  | 303,755                  |
| Shares issued upon conversion of<br>convertible bonds          | <i>(c)</i>   | <u>850,440,529</u>                       | <u>85,044</u>                     | <u>310,811</u>                                 | <u>395,855</u>           |
| At 31 December 2009  |              | <u>3,482,196,992</u>                     | <u>348,219</u>                    | <u>1,817,378</u>                               | <u>2,165,597</u>         |

*Notes:*

- (a) Pursuant to a subscription agreement (the "Shang Hua Subscription Agreement") dated 21 January 2008 entered into between BEHL, BE Environmental and the Company, 247,000,000 new ordinary shares of the Company were allotted and issued to BE Environmental at a subscription price of HK\$0.40 per ordinary share for a total cash consideration, before any issuance expenses, of HK\$98,800,000, for the purpose of providing additional working capital to the Group.

# NOTES TO FINANCIAL STATEMENTS

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## 28. SHARE CAPITAL *(Continued)*

*Notes: (Continued)*

- (b) Pursuant to an acquisition agreement (the “BE-ZKC Acquisition Agreement”) entered into between, among others, the Company, Besto Holdings Limited (“Besto”), Tenson Investment Limited (“Tenson”) and Newton Finance Holdings Limited (“Newton”) (collectively the “BE-ZKC Vendors”) on 3 June 2008, 226,683,106 (period ended 31 December 2008: 559,787,908) new ordinary shares of the Company were issued during the year ended 31 December 2009 as part of the consideration for the acquisition of a 100% equity interest in Gainstar Limited, which holds indirectly a 88.43% equity interest in BE-ZKC. The fair value of these ordinary shares, determined by reference to the closing quoted market price of the Company’s ordinary shares on the Stock Exchange at the date of acquisition of 1 August 2008, amounted to HK\$303,755,000 (period ended 31 December 2008: HK\$750,116,000). Following the allotment of these ordinary shares during the year ended 31 December 2009, all ordinary shares to be issued as consideration under the BE-ZKC Acquisition Agreement have been issued. Further details of the transaction are set out in note 39(c)(i) to the financial statements and the Company’s circular dated 30 June 2008 (the “BE-ZKC Acquisition Circular”).

Immediately following the acquisition of Gainstar Limited by the Group, Besto, Tenson and Newton became major shareholders of the Company. Tenson is beneficially owned as to 52.62% and 44.94% by Messrs. Hu Xiaoyong and Zhou Min, directors of the Company, respectively. Newton is beneficially owned as to 50% by Mr. Wang Taoguang, another director of the Company.

- (c) During the year ended 31 December 2009, convertible bonds of the Company with an aggregate principal amount of approximately HK\$373,654,000 (period ended 31 December 2008: HK\$606,000,000) were converted by certain bondholders into 850,440,529 (period ended 31 December 2008: 1,515,000,000) new ordinary shares of the Company in total at a conversion price of HK\$0.40 or HK\$0.69 per ordinary share, as appropriate. The difference of approximately HK\$310,811,000 (period ended 31 December 2008: HK\$460,211,000) between nominal value of the ordinary shares issued and the then aggregate carrying amounts of the liability and equity components of the relevant convertible bonds at the dates of conversions was transferred to the Company’s share premium account.

## 29. RESERVES

### (a) Group

- (i) The amounts of the Group’s reserves and the movements therein for the current year and the prior period are presented in the consolidated statement of changes in equity on page 44 of the financial statements.
- (ii) The Group’s contributed surplus account represents the difference between the nominal value of the shares and the share premium account of the subsidiaries acquired pursuant to the group reorganisation undertaken in prior years, over the nominal value of the Company’s ordinary shares issued in exchange therefor.
- (iii) The PRC reserve funds are reserves set aside in accordance with the PRC Companies Law or the Law of the PRC on Joint Ventures Using Chinese and Foreign Investment as applicable to the Group’s subsidiaries. None of the Group’s PRC reserve funds as at 31 December 2009 were distributable in the form of cash dividends.



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## 29. RESERVES (Continued)

### (b) Company

|   | Notes     | Share<br>premium<br>account<br>HK\$'000 | Contributed<br>surplus<br>HK\$'000 | Convertible<br>bond equity<br>reserve<br>HK\$'000 | Accumulated<br>losses<br>HK\$'000 | Total<br>HK\$'000 |
|---|-----------|---|------------------------------------|---|-----------------------------------|-------------------|
| At 1 July 2007  |           | -                                       | 60,859                             | -   | (37,689)                          | 23,170            |
| Share issue expenses and<br>other comprehensive loss for<br>the period, net of tax of nil |           | (2,968)                                 | -                                  | -   | -                                 | (2,968)           |
| Loss for the period   |           | -                                       | -                                  | -   | (47,168)                          | (47,168)          |
| Total comprehensive loss<br>for the period  |           | (2,968)                                 | -                                  | -   | (47,168)                          | (50,136)          |
| Share placement   | 28(a)     | 74,100                                  | -                                  | -   | -                                 | 74,100            |
| Allotment of shares for the acquisition<br>of Gainstar Limited                            | 28(b)     | 694,137                                 | -                                  | -   | -                                 | 694,137           |
| Issue of convertible bonds  | 31        | -                                       | -                                  | 364,524   | -                                 | 364,524           |
| Conversion of convertible bonds   | 28(c), 31 | 460,211                                 | -                                  | (120,780)   | -                                 | 339,431           |
| At 31 December 2008 and<br>1 January 2009   |           | 1,225,480                               | 60,859                             | 243,744   | (84,857)                          | 1,445,226         |
| Loss for the year and total<br>comprehensive loss for the year                            |           | -                                       | -                                  | -   | (62,505)                          | (62,505)          |
| Allotment of shares for the acquisition<br>of Gainstar Limited                            | 28(b)     | 281,087                                 | -                                  | -   | -                                 | 281,087           |
| Issue of convertible bonds  | 31        | -                                       | -                                  | 52,439  | -                                 | 52,439            |
| Conversion of convertible bonds   | 28(c), 31 | 310,811                                 | -                                  | (79,197)  | -                                 | 231,614           |
| At 31 December 2009   |           | 1,817,378                               | 60,859                             | 216,986   | (147,362)                         | 1,947,861         |

The Company's contributed surplus account represents the excess of the fair value of the shares of the subsidiaries acquired pursuant to the group reorganisation undertaken in prior years, over the nominal value of the Company's shares in exchange therefor. Under the Bermuda Companies Act 1981, the Company may make distribution to its members out of contributed surplus subject to the Company's Bye-laws and provided that immediately following the distribution of dividends, the Company will be in a position to pay off its debts as and when they fall due in the ordinary course of business.

# NOTES TO FINANCIAL STATEMENTS

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## 30. BANK AND OTHER BORROWINGS

|  | Group              |                  | Company          |          |
|--|--------------------|------------------|------------------|----------|
|  | 2009               | 2008             | 2009             | 2008     |
|  | HK\$'000           | HK\$'000         | HK\$'000         | HK\$'000 |
| Bank loans:                                  |                    |                  |                  |          |
| Secured                                      | 1,417,404          | 1,155,949        | –                | –        |
| Unsecured                                    | 969,416            | –                | 501,446          | –        |
|  | <u>2,386,820</u>   | <u>1,155,949</u> | <u>501,446</u>   | <u>–</u> |
| Other loans, unsecured                       | 224,348            | 43,160           | –                | –        |
| Total bank and other borrowings              | <u>2,611,168</u>   | <u>1,199,109</u> | <u>501,446</u>   | <u>–</u> |
| Analysed into:                               |                    |                  |                  |          |
| Bank loans repayable:                        |                    |                  |                  |          |
| Within one year                              | 1,229,343          | 201,224          | 501,446          | –        |
| In the second year                           | 170,973            | 137,159          | –                | –        |
| In the third to fifth years,<br>inclusive    | 476,196            | 420,309          | –                | –        |
| Beyond five years                            | 510,308            | 397,257          | –                | –        |
|  | <u>2,386,820</u>   | <u>1,155,949</u> | <u>501,446</u>   | <u>–</u> |
| Other loans repayable:                       |                    |                  |                  |          |
| Within one year                              | 61,603             | 11,017           | –                | –        |
| In the second year                           | 13,708             | 4,203            | –                | –        |
| In the third to fifth years,<br>inclusive    | 53,377             | 12,607           | –                | –        |
| Beyond five years                            | 95,660             | 15,333           | –                | –        |
|  | <u>224,348</u>     | <u>43,160</u>    | <u>–</u>         | <u>–</u> |
| Total bank and other borrowings              | <u>2,611,168</u>   | <u>1,199,109</u> | <u>501,446</u>   | <u>–</u> |
| Portion classified<br>as current liabilities | <u>(1,290,946)</u> | <u>(212,241)</u> | <u>(510,446)</u> | <u>–</u> |
| Non-current portion                          | <u>1,320,222</u>   | <u>986,868</u>   | <u>–</u>         | <u>–</u> |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 30. BANK AND OTHER BORROWINGS *(Continued)*

Notes:

- (a) The carrying amounts of the Group's and the Company's bank and other borrowings are denominated in the following currencies:

|      | Group            |                  | Company          |                  |
|------|------------------|------------------|------------------|------------------|
|      | 2009<br>HK\$'000 | 2008<br>HK\$'000 | 2009<br>HK\$'000 | 2008<br>HK\$'000 |
| HK\$ | 501,446          | –                | 501,446          | –                |
| RMB  | 2,033,644        | 1,199,109        | –                | –                |
| US\$ | 76,078           | –                | –                | –                |
|      | <b>2,611,168</b> | <b>1,199,109</b> | <b>501,446</b>   | <b>–</b>         |

- (b) Certain of the Group's bank loans are secured by:
- (i) mortgages over sewage treatment concession rights, land use rights and certain operating facilities of the sewage treatment plants which are under the management of the Group pursuant to the relevant service concession agreements signed with the grantors. These land use rights and operating facilities are normally registered under the names of the relevant entities in the Group and are required to be returned to the grantors at the end of the respective service concession periods (*note 17*);
  - (ii) guarantees given by the Company and/or its subsidiaries;
  - (iii) a pledge over the Group's 60% equity interest in Bei Kong Chuang Xin; and/or
  - (iv) pledges over certain of the Group's bank balances of HK\$6,636,000 (2008: HK\$115,000) in aggregate (*note 27(a)*).
- (c) HK\$13,630,000 of the Group's unsecured bank loans as at 31 December 2009 were guaranteed by the Jinzhou JV Partner.
- (d) HK\$3,067,000 of the Group's unsecured other loans as at 31 December 2008 were guaranteed by a government authority in Mainland China. These loans were fully settled by the Group during the year.
- (e) Except for an interest-free government loan of HK\$6,815,000 (2008: HK\$6,815,000), and certain bank and other loans with an aggregate carrying amount of HK\$103,403,000 (2008: a bank loan of HK\$68,148,000) which bear fixed interest rates between 2.96% to 7.47% per annum (2008: 7.47% per annum), all the Group's bank and other loans bear interest at floating interest rates.

# NOTES TO FINANCIAL STATEMENTS

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## 31. CONVERTIBLE BONDS

The Company issued an aggregate of seven batches of convertible bonds during the year ended 31 December 2009 and the period ended 31 December 2008, the summary information of which is set out as follows:

### Group and Company

|  | Tranche 1  | Tranche 2  | Firm       | First      | Second     | ZKC         | ZKC         |
|--|------------|------------|------------|------------|------------|-------------|-------------|
|  | Bond*      | Bond*      | Bonds*     | Option     | Option     | Convertible | Convertible |
|  | (note (a)) | (note (a)) | (note (b)) | Bond*      | Bond*      | Bonds 1*    | Bonds 2*    |
|  | (note (a)) | (note (a)) | (note (b)) | (note (b)) | (note (b)) | (note (c))  | (note (c))  |
| Issuance date                              | 27/7/2007  | 31/3/2008  | 4/3/2008   | 17/7/2008  | 17/7/2008  | 24/7/2008   | 6/4/2009    |
| Maturity date                              | 26/7/2010  | 30/3/2011  | 3/3/2011   | 16/7/2011  | 16/7/2011  | 23/7/2013   | 23/7/2013   |
| Original principal amount (HK\$'000)       | 100,000    | 100,000    | 200,000    | 300,000    | 200,000    | 589,304     | 238,696     |
| Coupon rate                                | Zero       | Zero       | Zero       | Zero       | Zero       | Zero        | Zero        |
| Conversion price per ordinary share (HK\$) | 0.40       | 0.40       | 0.40       | 0.40       | 0.40       | 0.69        | 0.69        |

\* As defined in the respective circulars of the Company in connection with the issuance of the convertible bonds (see notes below).

Each batch of these convertible bonds is bifurcated into a liability component and an equity component for accounting purpose as further described in the accounting policy for "Convertible bonds" set out in note 3.4 to the financial statements. The following tables summarise the movements in the principal amounts, liability and equity components of the Company's convertible bonds during the year ended 31 December 2009 and the period ended 31 December 2008:

### Group and Company

|  | Tranche 1  | Tranche 2  | Firm       | First      | Second     | ZKC         | ZKC         | Total     |
|--|------------|------------|------------|------------|------------|-------------|-------------|-----------|
|  | Bond       | Bond       | Bonds      | Option     | Option     | Convertible | Convertible |           |
|  | HK\$'000   | HK\$'000   | HK\$'000   | HK\$'000   | HK\$'000   | HK\$'000    | HK\$'000    | HK\$'000  |
|  | (note (a)) | (note (a)) | (note (b)) | (note (b)) | (note (b)) | (note (c))  | (note (c))  |           |
| <b>Principal amount outstanding</b>    |            |            |            |            |            |             |             |           |
| At 1 July 2007                         | -          | -          | -          | -          | -          | -           | -           | -         |
| Issue of convertible bond              | 100,000    | 100,000    | 200,000    | 300,000    | 200,000    | 589,304     | -           | 1,489,304 |
| Conversion to ordinary shares          | (66,000)   | (20,000)   | (20,000)   | (300,000)  | (200,000)  | -           | -           | (606,000) |
| At 31 December 2008 and 1 January 2009 | 34,000     | 80,000     | 180,000    | -          | -          | 589,304     | -           | 883,304   |
| Issue of convertible bonds             | -          | -          | -          | -          | -          | -           | 238,696     | 238,696   |
| Conversion to ordinary shares          | (34,000)   | (80,000)   | (180,000)  | -          | -          | (34,245)    | (45,409)    | (373,654) |
| At 31 December 2009                    | -          | -          | -          | -          | -          | 555,059     | 193,287     | 748,346   |

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## 31. CONVERTIBLE BONDS (Continued)

### Group and Company (Continued)

|   | Tranche 1  | Tranche 2  | Firm       | First      | Second     | ZKC         | ZKC         |           |
|---|------------|------------|------------|------------|------------|-------------|-------------|-----------|
|   | Bond       | Bond       | Bonds      | Option     | Option     | Convertible | Convertible | Total     |
|   | HK\$'000   | HK\$'000   | HK\$'000   | HK\$'000   | HK\$'000   | HK\$'000    | HK\$'000    | HK\$'000  |
|   | (note (a)) | (note (a)) | (note (b)) | (note (b)) | (note (b)) | (note (c))  | (note (c))  |           |
| <b>Liability component</b>  |            |            |            |            |            |             |             |           |
| At 1 July 2007  | -          | -          | -          | -          | -          | -           | -           | -         |
| Issue of convertible bonds  | 82,724     | 78,707     | 160,228    | 239,315    | 159,543    | 404,263     | -           | 1,124,780 |
| Imputed interest expense (note 8)   | 6,210      | 4,357      | 9,782      | 375        | 740        | 13,962      | -           | 35,426    |
| Transfer to share capital and share premium accounts upon conversion to ordinary shares (note 28(c))            | (58,155)   | (16,157)   | (16,646)   | (239,690)  | (160,283)  | -           | -           | (490,931) |
| At 31 December 2008 and 1 January 2009  | 30,779     | 66,907     | 153,364    | -          | -          | 418,225     | -           | 669,275   |
| Issue of convertible bonds  | -          | -          | -          | -          | -          | -           | 186,257     | 186,257   |
| Imputed interest expense (note 8)   | 710        | 2,087      | 3,084      | -          | -          | 30,569      | 7,413       | 43,863    |
| Transfer to share capital and share premium accounts upon conversion to ordinary shares (note 28(c))            | (31,489)   | (68,994)   | (156,448)  | -          | -          | (24,326)    | (35,401)    | (316,658) |
| At 31 December 2009   | -          | -          | -          | -          | -          | 424,468     | 158,269     | 582,737   |
| <b>Equity component (included in convertible bond equity reserve)</b>   |            |            |            |            |            |             |             |           |
| At 1 July 2007  | -          | -          | -          | -          | -          | -           | -           | -         |
| Issue of convertible bonds  | 17,276     | 21,293     | 39,772     | 60,685     | 40,457     | 185,041     | -           | 364,524   |
| Transfer to share capital and share premium accounts upon conversion to ordinary shares (notes 28(c) and 29(b)) | (11,402)   | (4,259)    | (3,977)    | (60,685)   | (40,457)   | -           | -           | (120,780) |
| At 31 December 2008 and 1 January 2009  | 5,874      | 17,034     | 35,795     | -          | -          | 185,041     | -           | 243,744   |
| Issue of convertible bonds  | -          | -          | -          | -          | -          | -           | 52,439      | 52,439    |
| Transfer to share capital and share premium accounts upon conversion to ordinary shares (notes 28(c) and 29(b)) | (5,874)    | (17,034)   | (35,795)   | -          | -          | (10,753)    | (9,741)     | (79,197)  |
| At 31 December 2009   | -          | -          | -          | -          | -          | 174,288     | 42,698      | 216,986   |

# NOTES TO FINANCIAL STATEMENTS

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## 31. CONVERTIBLE BONDS *(Continued)*

*Notes:*

- (a) Tranche 1 Bond and Tranche 2 Bond were issued to Pioneer Wealth Limited, a shareholder of the Company, pursuant to a convertible bond subscription agreement dated 12 April 2007 for the purpose of financing future investments in water treatment businesses in the PRC (as amended) and providing additional working capital (as amended) to the Group. Further details of these convertible bonds are set out in the Company's circulars dated 3 May 2007 and announcements dated 27 July 2007, 31 March 2008 and 12 June 2008.
- (b) The Firm Bonds, the First Option Bond and the Second Option Bond were issued to BE Environmental, the immediate holding company, pursuant to a subscription agreement dated 21 January 2008 entered into between BEHL, BE Environmental and the Company for the purpose of financing investment and development of water treatment and environmental business and providing additional working capital to the Group. Further details of these convertible bonds are set out in the Company's circular dated 18 February 2008.
- (c) ZKC Convertible Bonds 1 and ZKC Convertible Bonds 2 were issued to the BE-ZKC Vendors as part of the consideration for the acquisition of the 100% equity interest in Gainstar Limited, which holds indirectly a 88.43% equity interest in BE-ZKC, pursuant to the BE-ZKC Acquisition Agreement. Further details of the ZKC Convertible Bonds 1 and ZKC Convertible Bonds 2 are set out in the BE-ZKC Acquisition Circular.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 32. FINANCE LEASE PAYABLE

The purchase of certain equipment, which forms part of a sewage treatment plant constructed by the Group, was financed by a finance lease arrangement with an original lease term of 5 years. Pursuant to the lease agreement, a deposit of RMB8,000,000 (equivalent to HK\$9,086,000) is required to be placed at the lessor as a guarantee in respect of the arrangement, which will be refunded from the lessor upon the completion of all obligations by the Group under the lease arrangement (*note 25(a)(v)*).

At 31 December 2009, the total future minimum lease payments under the finance lease and their present values were as follows:

| Group                                     | Minimum<br>lease<br>payments<br>2009<br>HK\$'000 | Minimum<br>lease<br>payments<br>2008<br>HK\$'000 | Present value<br>of minimum<br>lease payments<br>2009<br>HK\$'000 | Present value<br>of minimum<br>lease payments<br>2008<br>HK\$'000 |
|---|--|--|---|---|
| Amounts payable:                          |  |  |   |   |
| Within one year                           | 7,055  | 6,953  | 5,676   | 5,311   |
| In the second year                        | 4,975  | 6,633  | 4,743   | 5,816   |
| In the third year                         | –  | 4,975  | –   | 4,743   |
| Total minimum finance lease payments      | 12,030   | 18,561   | 10,419  | 15,870  |
| Future finance charges                    | (1,611)  | (2,691)  |   |   |
| Total net finance lease payable           | 10,419   | 15,870   |   |   |
| Portion classified as current liabilities | (5,676)  | (5,311)  |   |   |
| Non-current portion                       | 4,743  | 10,559   |   |   |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 33. PROVISION FOR MAJOR OVERHAULS

Pursuant to the service concession agreements entered into by the Group, the Group has contractual obligations to maintain the sewage and water treatment plants it operates to a specified level of serviceability and/or to restore the plants to a specified condition before they are handed over to the grantors at the end of the service concession periods. These contractual obligations to maintain or restore the sewage and water treatment plants, except for any upgrade element, are recognised and measured in accordance with HKAS 37, i.e., at the best estimate of the expenditure that would be required to settle the present obligation at the end of the reporting period. The future expenditure on these maintenance and restoration costs is collectively referred to as "major overhauls". The estimation basis is reviewed on an ongoing basis, and revised where appropriate.

The movements in the provision for the major overhauls of sewage and water treatment plants during the year/period, are as follows:

|  | Group   |  |
|--|---|--|
|  | Year ended<br>31 December<br>2009<br>HK\$'000 | Period from<br>1 July 2007 to<br>31 December<br>2008<br>HK\$'000 |
| At beginning of year/period  | 69,006  | –  |
| Acquisition of subsidiaries ( <i>note 39</i> )                                       | –   | 61,447   |
| Additional provision   | 20,775  | 7,285  |
| Increase in discounted amounts arising<br>from the passage of time ( <i>note 8</i> ) | 2,011   | 595  |
| Exchange realignment   | –   | (321)  |
| At end of year/period  | 91,792  | 69,006   |

## 34. DEFERRED INCOME

Deferred income of the Group represented subsidies received from third parties, fresh water customers and government authorities in respect of the Group's sewage treatment businesses and the construction of a sewage treatment plant. The subsidies are interest-free and not required to be repaid, and are recognised in the consolidated income statement on the straight-line basis over the expected useful life of the relevant assets.



# NOTES TO FINANCIAL STATEMENTS

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## 35. DEFERRED TAX

Net deferred tax assets/(liabilities) recognised in the consolidated statement of financial position are as follows:

|                          | Group            |                  |
|--------------------------|------------------|------------------|
|                          | 2009<br>HK\$'000 | 2008<br>HK\$'000 |
| Deferred tax assets      | 31,071           | 27,112           |
| Deferred tax liabilities | (100,305)        | (59,707)         |
|                          | <b>(69,234)</b>  | <b>(32,595)</b>  |

The components of deferred tax assets and liabilities and the movements during the year/period are as follows:

### Group

|  | Notes | Fair value<br>adjustments<br>arising from<br>acquisition of<br>subsidiaries<br>HK\$'000 | Impairment<br>and<br>provision<br>HK\$'000 | Provision<br>for major<br>overhauls<br>HK\$'000 | Temporary<br>difference<br>related to<br>service<br>concession<br>arrangements<br>HK\$'000 | Losses<br>available for<br>offsetting<br>against<br>future<br>taxable<br>profits<br>HK\$'000 | Net<br>deferred<br>tax assets/<br>(liabilities)<br>HK\$'000 |
|--|-------|---|--|---|--|--|---|
| At 1 July 2007   |       | -   | -  | -   | -  | -  | -   |
| Acquisition of subsidiaries  | 39    | 49,909  | 2,066                                      | 14,613  | (91,291)   | -  | (24,703)  |
| Net deferred tax credited/(charged) to<br>the income statement during the period | 11    | -   | 432  | 1,970   | (10,653)   | -  | (8,251)   |
| Exchange realignment   |       | 30  | -  | (78)  | 407  | -  | 359   |
| At 31 December 2008 and 1 January 2009   |       | 49,939  | 2,498                                      | 16,505  | (101,537)  | -  | (32,595)  |
| Net deferred tax credited/(charged) to<br>the income statement during the year   | 11    | -   | 151  | 5,696   | (46,923)   | 4,440  | (36,636)  |
| Exchange realignment   |       | -   | -  | -   | -  | (3)  | (3)   |
| At 31 December 2009  |       | 49,939  | 2,649                                      | 22,201  | (148,460)  | 4,437  | (69,234)  |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 35. DEFERRED TAX *(Continued)*

*Notes:*

- (a) At 31 December 2009, deferred tax assets have not been recognised in respect of unused tax losses of HK\$28,274,000 (2008: HK\$41,437,000) as they have been arisen in the Company and certain subsidiaries that have been loss-making for some time and it is not probable that taxable profits will be available against which such tax losses can be utilised. Out of this amount, unrecognised tax losses of HK\$13,080,000 (2008: HK\$6,904,000) will expire in one to five years.
- (b) Pursuant to the new PRC Corporate Income Tax Law, a 10% withholding tax is levied on dividends declared to foreign investors from the foreign investment enterprises established in Mainland China. The requirement is effective from 1 January 2008 and applies to earnings after 31 December 2007. A lower withholding tax rate may be applied if there is a tax treaty between Mainland China and jurisdiction of the foreign investors. For the Group, the applicable rate is 5% or 10%. The Group is therefore liable to withholding taxes on dividends distributed by those subsidiaries established in Mainland China in respect of earnings generated from 1 January 2008.

Deferred tax has not been recognised for withholding taxes that would be payable on the unremitted earnings that are subject to withholding taxes of the Group's subsidiaries established in Mainland China. In the opinion of the directors, it is not probable that these subsidiaries will distribute such earnings in the foreseeable future. The aggregate amount of temporary differences associated with investments in subsidiaries in Mainland China for which deferred tax liabilities have not been recognised totalled approximately HK\$132,093,000 at 31 December 2009 (2008: HK\$91,212,000).

- (c) In the opinion of the directors, there are no income tax consequences regarding the Company's convertible bonds issued during the current year and the prior period and hence, no deferred tax liabilities have been provided in respect to these convertible bonds.

# NOTES TO FINANCIAL STATEMENTS

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## 36. TRADE PAYABLES

An aged analysis of the trade payables as at the end of the reporting period, based on the invoice date, is as follows:

|                    | Group          |               | Company       |          |
|--------------------|----------------|---------------|---------------|----------|
|                    | 2009           | 2008          | 2009          | 2008     |
|                    | HK\$'000       | HK\$'000      | HK\$'000      | HK\$'000 |
| Within 3 months    | 387,843        | 45,965        | 21,159        | –        |
| 4 to 6 months      | 14,559         | 12,911        | 8,900         | –        |
| 7 months to 1 year | 15,978         | 2,561         | 4,226         | –        |
| 1 to 2 years       | 12,670         | 12,508        | –             | –        |
| 2 to 3 years       | 6,169          | 4,390         | –             | –        |
| Over 3 years       | 8,008          | 6,860         | –             | –        |
|                    | <b>445,227</b> | <b>85,195</b> | <b>34,285</b> | <b>–</b> |

The trade payables are non-interest-bearing and unsecured and are normally settled on 60-day terms.

## 37. OTHER PAYABLES AND ACCRUALS

|   | Notes | Group            |                  | Company        |                  |
|---|-------|------------------|------------------|----------------|------------------|
|   |       | 2009             | 2008             | 2009           | 2008             |
|   |       | HK\$'000         | HK\$'000         | HK\$'000       | HK\$'000         |
| Accruals                                  |       | 56,754           | 22,706           | 5,107          | 4,277            |
| Other liabilities                         |       | 428,003          | 134,008          | –              | –                |
| Other taxes payables                      | 38    | 7,176            | 1,358            | –              | –                |
| Due to a shareholder                      | 26(d) | –                | 542,451          | –              | 542,451          |
| Due to related parties                    | 26    | 28,172           | 1,010            | –              | –                |
|   |       | <b>520,105</b>   | <b>701,533</b>   | <b>5,107</b>   | <b>546,728</b>   |
| Portion classified as current liabilities |       | <b>(482,551)</b> | <b>(632,205)</b> | <b>(5,107)</b> | <b>(546,728)</b> |
| Non-current portion                       |       | <b>37,554</b>    | <b>69,328</b>    | <b>–</b>       | <b>–</b>         |

# NOTES TO FINANCIAL STATEMENTS

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## 37. OTHER PAYABLES AND ACCRUALS *(Continued)*

The Group's other liabilities as at 31 December 2009 included, inter alia, the following:

- (a) outstanding considerations in the amounts of RMB3,680,000 (equivalent to HK\$4,180,000) (2008: RMB33,680,000 (equivalent to HK\$38,255,000)) and RMB41,159,000 (equivalent to HK\$46,750,000) (2008: RMB41,159,000 (equivalent to HK\$46,750,000)), payable to the Mianyang Government for the transfer and construction of sewage treatment facilities under a TOT agreement and a BOT arrangement, respectively. The outstanding considerations are repayable in four annual instalments of RMB15,000,000 and the last instalment of RMB14,839,000 being due for repayment in 2012. During the year ended 31 December 2009, annual instalments for the prior year and current year of RMB15,000,000 each were settled by the Group.
- (b) outstanding consideration of HK\$111,755,000 payable to a third party for the acquisition of 100% equity interest in Chinese Profit Investment Limited, which held a 7.21% equity interest in BE-ZKC. The transaction was completed in 2009 and the balance is fully repayable in 2010.
- (c) outstanding considerations in the amounts of RMB100,000,000 (equivalent to HK\$113,585,000) and RMB42,000,000 (equivalent HK\$47,706,000) payable to Huangyan Government and Qingzhen Government for the transfers of sewage treatment facilities to the Group under TOT arrangements. The balances are fully repayable in 2010.

Other payables are non-interest-bearing and have an average term of three months.

## 38. OTHER TAXES PAYABLES

|                 | Group        |              |
|-----------------|--------------|--------------|
|                 | 2009         | 2008         |
|                 | HK\$'000     | HK\$'000     |
| Business tax    | 1,015        | 211          |
| Value-added tax | 2,519        | 239          |
| Others          | 3,642        | 908          |
|                 | <b>7,176</b> | <b>1,358</b> |

# NOTES TO FINANCIAL STATEMENTS

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## 39. BUSINESS COMBINATIONS

Except for the property, plant and equipment, prepaid land premiums and receivables under service concession arrangements with respective carrying amounts of HK\$159,362,000, HK\$25,773,000 and HK\$126,110,000 immediately before the acquisitions (2008: operating concessions with an aggregate carrying amount of HK\$626,772,000), the fair values of the identifiable assets and liabilities of the subsidiaries acquired during the year as at their respective dates of acquisition have no significant differences from their respective carrying amounts, and are set out as follows:

|   | Notes | Year ended 31 December 2009                |  |                   | Period from<br>1 July 2007 to<br>31 December<br>2008 |
|---|-------|--|--|-------------------|--|
|   |       | Guigang<br>Water<br>HK\$'000<br>(note (a)) | Jinzhou<br>Beikong<br>HK\$'000<br>(note (b)) | Total<br>HK\$'000 | Total<br>HK\$'000<br>(note (c))                      |
| Net assets acquired:                              |       |  |  |                   |  |
| Property, plant and equipment                     | 14    | 169,754                                    | 1,814  | 171,568           | 10,039   |
| Prepaid land premiums                             | 15    | 28,005                                     | –  | 28,005            | –  |
| Operating concessions                             | 17    | –  | –  | –                 | 436,105  |
| Other intangible assets                           | 18    | –  | 81   | 81                | 1,219  |
| Interest in an associate                          |       | –  | –  | –                 | 26,268   |
| Available-for-sale investment                     |       | –  | –  | –                 | 457  |
| Deferred tax assets                               | 35    | –  | –  | –                 | 28,730   |
| Inventories                                       |       | 2,517                                      | 1,696  | 4,213             | 2,896  |
| Amounts due from contract customers               |       | –  | 112,201                                      | 112,201           | 110,177  |
| Receivables under service concession arrangements |       | –  | 134,874                                      | 134,874           | 1,355,950  |
| Trade receivables                                 |       | 3,776                                      | –  | 3,776             | 9,630  |
| Prepayments, deposits and other receivables       |       | 3,404                                      | 4,735  | 8,139             | 91,553   |
| Cash and cash equivalents                         |       | 6,161                                      | 116,257                                      | 122,418           | 301,692  |
| Trade payables                                    |       | (1,781)                                    | (38,862)                                     | (40,643)          | (105,397)  |
| Other payables and accruals                       |       | (55,795)                                   | (12,048)                                     | (67,843)          | (223,515)  |
| Income tax payable                                |       | (103)                                      | –  | (103)             | (15,746)   |
| Bank and other borrowings                         |       | (71,133)                                   | (184,722)                                    | (255,855)         | (970,463)  |
| Finance lease payable                             |       | –  | –  | –                 | (16,675)   |
| Provision for major overhauls                     | 33    | –  | –  | –                 | (61,447)   |
| Deferred income                                   |       | (16,254)                                   | –  | (16,254)          | (1,184)  |
| Deferred tax liabilities                          | 35    | –  | –  | –                 | (53,433)   |
| Minority interests                                |       | (22,848)                                   | (27,221)                                     | (50,069)          | (228,327)  |
|   |       | 45,703                                     | 108,805                                      | 154,508           | 698,529  |
| Goodwill on acquisition                           | 16    | 13,912                                     | 6,695  | 20,607            | 1,466,760  |
|   |       | 59,615                                     | 115,500                                      | 175,115           | 2,165,289  |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 39. BUSINESS COMBINATIONS *(Continued)*

|  | Year ended 31 December 2009 |   |   | Period from<br>1 July 2007 to<br>31 December<br>2008 |
|--|-----------------------------|---|---|--|
|  | Notes                       | Guigang<br>Water<br>HK\$'000<br><i>(note (a))</i> | Jinzhou<br>Beikong<br>HK\$'000<br><i>(note (b))</i> | Total<br>HK\$'000<br><i>(note (c))</i>               |
| Satisfied by:                                |                             |   |   |  |
| Cash   |                             | 56,837  | 115,500   | 172,337  |
| New ordinary shares of the Company           |                             | -   | -   | -  |
| New convertible bonds                        |                             | -   | -   | -  |
| Costs associated with the acquisitions       |                             | 2,778   | -   | 2,778  |
|  |                             | <u>59,615</u>                                     | <u>115,500</u>                                      | <u>175,115</u>                                       |
| Profit for the year/period since acquisition |                             | <u>4,794</u>                                      | <u>23,999</u>                                       | <u>28,793</u>  |
|  |                             |   |   | 266,947  |
|  |                             |   |   | 1,053,871  |
|  |                             |   |   | 828,000  |
|  |                             |   |   | 16,471   |
|  |                             |   |   | 2,165,289  |
|  |                             |   |   | 76,793   |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 39. BUSINESS COMBINATIONS *(Continued)*

An analysis of the net inflow of cash and cash equivalents in respect of the acquisition of subsidiaries is as follows:

|   | Year ended 31 December 2009          |                                      |                      | Period from<br>1 July 2007 to<br>31 December<br>2008 |
|---|--------------------------------------|--------------------------------------|----------------------|--|
|   | Guigang                              | Jinzhou                              | Total                | Total  |
|   | Water                                | Beikong                              |                      |  |
|   | <i>HK\$'000</i><br><i>(note (a))</i> | <i>HK\$'000</i><br><i>(note (b))</i> |                      |  |
| Cash consideration  | (56,837)                             | –                                    | <b>(56,837)</b>      | (266,947)  |
| Cash injected by the Group as<br>capital contribution                                       | –                                    | (115,500)                            | <b>(115,500)</b>     | –  |
| Cash and bank balances acquired   | 6,161                                | 116,257                              | <b>122,418</b>       | 301,692  |
| Cash paid for costs associated with<br>the acquisition                                      | (2,778)                              | –                                    | <b>(2,778)</b>       | (16,471)   |
| Cash consideration prepaid<br>in the prior period <i>(note (a))</i>                         | <u>56,837</u>                        | <u>–</u>                             | <u><b>56,837</b></u> | <u>–</u>   |
| Net inflow of cash and cash<br>equivalents in respect of<br>the acquisition of subsidiaries | <u>3,383</u>                         | <u>757</u>                           | <u><b>4,140</b></u>  | <u>18,274</u>  |

Had the above business combinations taken place at the beginning of the year, the Group's profit for the year would have been HK\$228,356,000 (period ended 31 December 2008: HK\$220,149,000) and the Group's revenue (comprising turnover and other income and gains, net) would have been HK\$1,759,060,000 (period ended 31 December 2008: HK\$972,335,000).

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 39. BUSINESS COMBINATIONS *(Continued)*

*Notes:*

- (a) Pursuant to the share transfer agreement entered into between the Group and 貴港市人民政府國有資產監督管理委員會 (State-owned Assets Supervision and Administration Commission of People's Government of Guigang Municipality) on 17 November 2008 and as approved by the Group's shareholders at a special general meeting held on 19 January 2009, the Group acquired a 66.67% equity interest in Guigang Water at a cash consideration of RMB50,001,600 (equivalent to HK\$56,837,000). The consideration was paid in advance by the Group during the period ended 31 December 2008 and was included in deposits and other debtors as at 31 December 2008. Guigang Water and its subsidiaries are principally engaged in the operations of sewage treatment, water treatment and distribution and the provision of related services in Guigang Municipality, Guangxi Province, the PRC. Further details of the acquisition are set out in the Company's circular dated 31 December 2008.
- (b) Pursuant to a joint venture agreement (the "Jinzhou Joint Venture Agreement") entered into between the Group and the Jinzhou JV Partner on 30 June 2009, Jinzhou Beikong was established by the Group and the Jinzhou JV Partner for the purpose of operating sewage and water treatment plants under a service concession agreement (the "Jinzhou Sewage and Water Concessions") granted to Jinzhou Beikong. Jinzhou Beikong was established with an initial registered capital of RMB127,179,000, which was satisfied as to RMB101,743,000 (equivalent to HK\$115,500,000) in cash by the Group and as to RMB25,436,000 in the form of the Jinzhou Sewage and Water Concessions and related liabilities by the Jinzhou JV Partner. The transaction was completed on 15 August 2009 and the transaction was accounted for as a business combination in accordance with HKFRS 3.
- (c) The subsidiaries acquired during the period ended 31 December 2008 comprised the BE-ZKC Group and Bei Kong Chuang Xin and its subsidiaries (the "Bei Kong Chuang Xin Group"). A summary information of these acquisitions is set out as follows:
- (i) Pursuant to the BE-ZKC Acquisition Agreement entered into between, among others, the Group and the BE-ZKC Vendors on 3 June 2008 and as approved by the Group's shareholders at a special general meeting held on 15 July 2008, the Group acquired from the BE-ZKC Vendors the entire issued share capital of Gainstar Limited, an investment holding company holding indirectly an aggregate of an 88.43% equity interest in BE-ZKC Environmental after the completion of its acquisition of Monico (see below). Gainstar Limited and its subsidiaries (the "BE-ZKC Group") are principally engaged in the operations of sewage treatment and the provision of related services in Mainland China. The acquisition was completed on 1 August 2008.



# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 39. BUSINESS COMBINATIONS *(Continued)*

*Notes: (Continued)*

(c) *(Continued)*

(i) *(Continued)*

In accordance with the BE-ZKC Acquisition Agreement, the total consideration for the acquisition, subject to adjustments in certain circumstances, amounted to HK\$1,370,665,000, of which HK\$975,557,782 (the "Gainstar Consideration") was payable to the BE-ZKC Vendors for the transfer of the entire issued share capital of Gainstar Limited to the Group and the remaining balance of HK\$395,107,218 (the "Monico Consideration") was payable to Tenson or its nominees for the transfer of the entire issued share capital of Monico to Gainstar Limited.

The Gainstar Consideration, which had been fully settled in the prior period, was satisfied by the allotment and issuance of 559,787,908 new ordinary shares of the Group and the issue of the ZKC Convertible Bonds 1 with an aggregate principal amount of HK\$589,304,125 by the Company to the ZKC Vendors. The fair value of the Gainstar Consideration amounted to approximately HK\$1,339,420,000, being the aggregate amount of the fair value of the 559,787,908 consideration shares of approximately HK\$750,116,000 (determined based on the closing price of the Company's ordinary shares on the Stock Exchange on the date of acquisition of 1 August 2008) and the nominal value of the ZKC Convertible Bonds 1 issued.

The Monico Consideration was settled during the year ended 31 December 2009 by the allotment and issuance of 226,683,106 new ordinary shares of the Group and the issue of the ZKC Convertible Bonds 2 with an aggregate principal amount of HK\$238,695,875 by the Company to Tenson or its nominees. The fair value of the Monico Consideration amounted to approximately HK\$542,451,000, being the aggregate amount of the fair value of the 226,683,106 consideration shares of approximately HK\$303,755,000 (determined based on the closing price of the Company's ordinary shares on the Stock Exchange on the date of acquisition of 1 August 2008) and the nominal value of the ZKC Convertible Bonds 2 issued.

Further details of this acquisition are set out in the BE-ZKC Acquisition Circular.

(ii) Pursuant to a share transfer agreement entered into between, among others, BE-ZKC, Hong Qiao and two third parties independent to the Group on 8 September 2008 (the "Bei Kong Chuang Xin Acquisition Agreement"), the Group acquired a 60% equity interest in Bei Kong Chuang Xin from the two third parties at a total cash consideration of RMB235,362,074 (equivalent to HK\$266,947,000), which was fully settled during the period ended 31 December 2008. The Bei Kong Chuang Xin Group is principally engaged in the operations of sewage treatment, water treatment and distribution and the provision of related services in Mainland China. The acquisition was completed on 28 September 2008.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 40. DISPOSAL OF SUBSIDIARIES

|  | Year ended<br>31 December<br>2009<br>HK\$'000<br>(note (a)) | Period from<br>1 July 2007 to<br>31 December<br>2008<br>HK\$'000<br>(note (b)) |
|--|---|--|
| Net assets disposed of:                          |   |  |
| Interest in an associate                         | 27,281  | –  |
| Cash and bank balances                           | 242   | 1,664  |
| Prepayments, deposits and other receivables      | 1,963   | 10,875   |
| Minority interests                               | (3,846)   | –  |
|  | <u>25,640</u>   | 12,539   |
| Exchange fluctuation reserve realised            | –   | (1,887)  |
| Gain/(loss) on disposal of subsidiaries (note 7) | (2,922)   | 760  |
|  | <u>22,718</u>   | 11,412   |
| Satisfied by cash                                | <u>22,718</u>   | 11,412   |

An analysis of the net inflow of cash and cash equivalents in respect of the disposal of subsidiaries is as follows:

|  | Year ended<br>31 December<br>2009<br>HK\$'000 | Period from<br>1 July 2007 to<br>31 December<br>2008<br>HK\$'000 |
|--|---|--|
| Cash consideration   | 22,718  | 11,412   |
| Consideration satisfied by offsetting current account (note 41(b))                 | (1,768)                                       | –  |
| Cash and bank balances disposal of   | (242)   | (1,664)  |
| Net inflow of cash and cash equivalents in respect of the disposal of subsidiaries | <u>20,708</u>                                 | 9,748  |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 40. DISPOSAL OF SUBSIDIARIES *(Continued)*

During the year ended 31 December 2009 and the period ended 31 December 2008, the Group had the following transactions for the disposal of subsidiaries:

- (a) During the year ended 31 December 2009, the Group disposed of its entire equity interest in Sichuan ZKC Investment Management, a non wholly-owned subsidiary indirectly held by the Company, to certain related parties (the "Sichuan ZKC Investment Management Purchasers") for an aggregate cash consideration of RMB20,000,000 (equivalent to HK\$22,718,000). Sichuan ZKC Investment Management was engaged in investment holding at the date of disposal.
- (b) Pursuant to a sale and purchase agreement dated 27 May 2008, the Group disposed of its entire equity interest in Shanghai Classic Limited, a then wholly-owned subsidiary of the Company, to an independent third party for a cash consideration of HK\$11,412,000. Shanghai Classic Limited and its subsidiary, 上海建開國際貿易有限公司, did not actively engage in any business at the date of disposal.

## 41. NOTE TO THE CONSOLIDATED STATEMENT OF CASH FLOWS

### Major non-cash transactions

Apart from the transaction detailed in notes 26(c) and 28(c) to the financial statements, the Group had the following major non-cash transactions of investing and financing activities during the year ended 31 December 2009 and the period ended 31 December 2008:

- (a) The Gainstar Consideration for the acquisition of Gainstar Limited was settled by way of the issue of new ordinary shares of the Company and convertible bonds by the Company during the year ended 31 December 2009 and the period ended 31 December 2008, details of which are set out in note 39(c)(i) to the financial statements.
- (b) Pursuant to a deed of setoff entered into between the Group and the Sichuan ZKC Investment Management Purchasers, part of the cash consideration of RMB1,567,000 (equivalent to HK\$1,768,000) receivable from the Sichuan ZKC Investment Management Purchasers in respect of the disposal of Sichuan ZKC Investment Management was offset against the current accounts between the parties.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 42. CONTINGENT LIABILITIES

At 31 December 2009, the Group did not have any significant contingent liabilities (2008: Nil).

At 31 December 2009, corporate guarantees of RMB714,000,000 (equivalent to HK\$810,995,000) (2008: a corporate guarantee of RMB324,000,000 (equivalent to HK\$367,999,000)) were given by the Company to the banks in connection with bank loans of an equivalent amount granted to the subsidiaries of the Company.

## 43. OPERATING LEASE ARRANGEMENTS

### (a) As lessor

The Group leases certain portion of buildings (which the Group has the right to use under service concession agreements) under operating lease arrangements, with the leases negotiated for a term of 7 years (2008: 3 to 4 years). The terms of the leases generally also require the tenants to pay security deposits and to provide for periodic rent adjustments.

At 31 December 2009, the Group had total future minimum lease receivables under non-cancellable operating leases with its tenants falling due as follows:

|   | Group        |            |
|---|--------------|------------|
|   | 2009         | 2008       |
|   | HK\$'000     | HK\$'000   |
| Within one year                         | 207          | 282        |
| In the second to fifth years, inclusive | 981          | 517        |
| After 5 years                           | 600          | –          |
|   | <b>1,788</b> | <b>799</b> |

At 31 December 2009, the Company did not have any operating lease arrangements as lessor (2008: Nil).

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 43. OPERATING LEASE ARRANGEMENTS *(Continued)*

### (b) As lessee

The Group leases a piece of land, a motor vehicle and certain office properties under operating lease arrangements with the leases negotiated for terms ranging from 1 to 45 years.

At 31 December 2009, the Group had total future minimum lease payments under non-cancellable operating leases falling due as follows:

|   | Group         |               |
|---|---------------|---------------|
|   | 2009          | 2008          |
|   | HK\$'000      | HK\$'000      |
| Within one year                         | 1,726         | 1,734         |
| In the second to fifth years, inclusive | 1,963         | 3,024         |
| After five years                        | 8,362         | 8,580         |
|   | <u>12,051</u> | <u>13,338</u> |

At 31 December 2009, the Company did not have any operating lease commitments as lessee (2008: Nil).

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 44. COMMITMENTS

In addition to the operating lease commitment detailed in note 43(b) above, the Group had the following commitments as at the end of the reporting period:

|  | Group          |                |
|--|----------------|----------------|
|  | 2009           | 2008           |
|  | HK\$'000       | HK\$'000       |
| Purchase of operating concession of a sewage treatment plant:                                |                |                |
| Contracted, but not provided for   | <u>405,026</u> | <u>–</u>       |
| Purchase of plant and equipment, and a land use right under service concession arrangements: |                |                |
| Authorised, but not contracted for   | 11,884         | 77,839         |
| Contracted, but not provided for   | <u>363,359</u> | <u>110,368</u> |
| Contracted, but not provided for   | <u>375,243</u> | <u>188,207</u> |
| Total capital commitments  | <u>780,269</u> | <u>188,207</u> |

At 31 December 2009, the Company had a capital commitment of HK\$676,389,000 (2008: HK\$154,988,000) in respect of its capital contributions to subsidiaries, which are contracted but not provided for.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 45. RELATED PARTY DISCLOSURES

- (a) Other than the transactions and balances detailed in notes 24, 25, 26, 28, 31 and 37 to the financial statements, the Group had no other transactions and outstanding balances with related parties during the year ended 31 December 2009 and the period ended 31 December 2008.
- (b) Compensation of key management personnel of the Group

|   | 2009<br><i>HK\$'000</i> | 2008<br><i>HK\$'000</i> |
|---|-------------------------|-------------------------|
| Short term employee benefits                        | 5,209                   | 2,858                   |
| Pension scheme contributions                        | 36                      | 27                      |
| Total compensation paid to key management personnel | <u>5,245</u>            | <u>2,885</u>            |

Further details of directors' emoluments are included in note 9 to the financial statements.

## 46. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's principal financial instruments comprise bank and other borrowings, convertible bonds, and cash and bank balances. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various other financial assets and liabilities such as trade receivables, deposits and other receivables, trade payables, other payables and amounts due from/to related parties/a shareholder which arise directly from its operations.

The main risks arising from the Group's financial instruments are interest rate risk, foreign currency risk, credit risk and liquidity risk. The directors of Company review and agree policies for managing each of these risks and they are summarised below.

### Interest rate risk

Interest rate risk is the risk that the value and the future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Group is exposed to both fair value and cash flow rate risks. The Group's exposure to market risk for changes in interest rates relates primarily to the Group's long term debt obligations.

Banks loans, convertible bonds, cash and bank balances are stated at amortised cost and not revalued on a periodic basis. Floating rate interest income and expenses are credited/charged to the income statement as earned/incurred.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 46. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

### Interest rate risk (Continued)

The following tables set out the carrying amounts, by maturity, of the Group's financial instruments as at the end of the reporting period that are exposed to interest rate risk:

|                           | Within<br>1 year or<br>on demand<br><i>HK\$'000</i> | More than<br>1 year but<br>less than<br>2 years<br><i>HK\$'000</i> | More than<br>2 years but<br>less than<br>3 years<br><i>HK\$'000</i> | More than<br>3 years but<br>less than<br>4 years<br><i>HK\$'000</i> | More than<br>4 years but<br>less than<br>5 years<br><i>HK\$'000</i> | More than<br>5 years<br><i>HK\$'000</i> | Total<br><i>HK\$'000</i> | Effective<br>interest<br>rate<br>% |
|---------------------------|---|--|---|---|---|---|--------------------------|------------------------------------|
| <b>31 December 2009</b>   |   |  |   |   |   |   |                          |                                    |
| Floating rate:            |   |  |   |   |   |   |                          |                                    |
| Cash and cash equivalents | 833,221   | -  | -   | -   | -   | -                                       | 833,221                  | 0.36                               |
| Bank and other borrowings | 1,226,581   | 184,114  | 191,939   | 158,547   | 159,450   | 532,045                                 | 2,452,676                | 4.73                               |
| Fixed rate:               |   |  |   |   |   |   |                          |                                    |
| Cash and cash equivalents | 43,640  | -  | -   | -   | -   | -                                       | 43,640                   | 1.63                               |
| Bank and other borrowings | 57,550  | 568  | 826   | 826   | 18,242  | 73,665                                  | 151,677                  | 5.64                               |
| Convertible bonds         | -   | -  | -   | 582,737   | -   | -                                       | 582,737                  | 7.32                               |
| <b>31 December 2008</b>   |   |  |   |   |   |   |                          |                                    |
| Floating rate:            |   |  |   |   |   |   |                          |                                    |
| Cash and cash equivalents | 663,174   | -  | -   | -   | -   | -                                       | 663,174                  | 0.35                               |
| Bank and other borrowings | 137,279   | 141,362  | 153,838   | 150,766   | 128,311   | 412,591                                 | 1,124,147                | 7.01                               |
| Fixed rate:               |   |  |   |   |   |   |                          |                                    |
| Cash and cash equivalents | 171,762   | -  | -   | -   | -   | -                                       | 171,762                  | 2.67                               |
| Bank and other borrowings | 68,148  | -  | -   | -   | -   | -                                       | 68,148                   | 7.47                               |
| Convertible bonds         | -   | 30,779   | 220,271   | -   | 418,225   | -                                       | 669,275                  | 7.78                               |

At 31 December 2009, it is estimated that a general decrease/increase of 100 basis points in interest rate of average balances of bank and other loans, cash and bank balances during the year/period, with all other variables held constant, would increase/decrease the Group's profit before tax for the year ended 31 December 2009 by approximately HK\$10,385,000 (period ended 31 December 2008, increase/decrease the Group's profit before tax by approximately HK\$2,158,000).

The sensitivity analysis above has been determined assuming that the change in interest rates had occurred at the respective end of the reporting periods and had been applied to the exposure to interest rate risk for non-derivative financial instruments in existence at these dates. The 100 basis point decrease or increase represents management's assessment of a reasonably possible change in interest rates over the period until the next annual end of the reporting period.



# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 46. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(Continued)*

### Foreign currency risk

Foreign currency risk is the risk that the value of a financial instrument will fluctuate because of changes in foreign exchange rates. As a result of its significant investment operations in Mainland China, the Group's statement of financial position can be affected significantly by movements in the RMB/HK\$ exchange rate.

The following table demonstrates the sensitivity at the end of the reporting period to a reasonably possible change in RMB/HK\$ exchange rate, with all other variables held constant, of the Group's profit before tax and the Group's equity.

|   | Increase/<br>(decrease)<br>in profit<br>before tax<br><i>HK\$'000</i> | Increase/<br>(decrease)<br>in equity<br><i>HK\$'000</i> |
|---|---|---|
| <b>31 December 2009</b>                           |   |   |
| If Hong Kong dollar weakens against RMB by 5%     | 16,480  | 125,354   |
| If Hong Kong dollar strengthens against RMB by 5% | (16,480)  | (125,354)   |
| <b>31 December 2008</b>                           |   |   |
| If Hong Kong dollar weakens against RMB by 5%     | 4,400   | 42,173  |
| If Hong Kong dollar strengthens against RMB by 5% | (4,400)   | (42,173)  |

The Group has minimal transactional currency exposure which arises from sales or purchases by an operating unit in currencies other than unit's functional currency.

### Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation.

The Group does not have any significant credit risk as credit given to any individual or corporate entity is not significant. The main credit risk exposure to the Group arises from default or delinquency in principal payment of trade receivables, receivables under service concession arrangements and amounts due from contract customers. In respect of trade receivables, receivables under service concession arrangements and amounts due from contract customers, the Group trades mainly with municipal governments in different provinces which do not have significant credit risk. In addition, trade receivable balances, receivables under services concession arrangements and amounts due from contract customers are monitored on an ongoing basis, in the opinion of directors, the credit risk is not significant.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 46. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

### Credit risk (Continued)

With respect to credit risk arising from the other major financial assets of the Group, which comprise deposits and other receivables, amounts due from related parties and cash and cash equivalents, the Group's exposure to credit risk arises from default of the counterparties, with a maximum exposure equal to the carrying amounts of these instruments.

### Liquidity risk

Due to the capital intensive nature of the Group's business, the Group ensures that it maintains sufficient cash and credit lines to meet its liquidity requirements. The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of bank loans, other interest-bearing loans and convertible bonds. In the opinion of the directors of the Company, most of the borrowings that mature within one year can be renewed, and hence the Group expects to have adequate sources of funding to finance the Group and manage its liquidity position.

The maturity profile of the Group's financial liabilities as at each end of the reporting periods based on the contracted undiscounted payments, was as follows:

|                         | On demand     | Within<br>1 year | More than<br>1 year but<br>less than<br>2 years | More than<br>2 years but<br>less than<br>3 years | More than<br>3 years but<br>less than<br>4 years | More than<br>4 years but<br>less than<br>5 years | More than<br>5 years | Total            |
|-------------------------|---------------|------------------|---|--|--|--|----------------------|------------------|
|                         | HK\$'000      | HK\$'000         | HK\$'000  | HK\$'000   | HK\$'000   | HK\$'000   | HK\$'000             | HK\$'000         |
| <b>31 December 2009</b> |               |                  |   |  |  |  |                      |                  |
| Bank loans              | -             | 1,319,984        | 233,434   | 232,024  | 190,202  | 182,511  | 525,113              | 2,683,268        |
| Other loans             | 22,845        | 41,223           | 21,109  | 19,700   | 18,055   | 34,542   | 97,776               | 255,250          |
| Trade payables          | -             | 445,227          | -   | -  | -  | -  | -                    | 445,227          |
| Other liabilities       | -             | 390,449          | 18,401  | 19,154   | -  | -  | -                    | 428,004          |
| Finance lease payable   | -             | 5,676            | 4,743   | -  | -  | -  | -                    | 10,419           |
| Due to related parties  | 1,057         | 26,742           | -   | -  | -  | -  | -                    | 27,799           |
| Convertible bonds       | -             | -                | -   | -  | 582,737  | -  | -                    | 582,737          |
|                         | <u>23,902</u> | <u>2,229,301</u> | <u>277,687</u>                                  | <u>270,878</u>                                   | <u>790,994</u>                                   | <u>217,053</u>                                   | <u>622,889</u>       | <u>4,432,704</u> |
| <b>31 December 2008</b> |               |                  |   |  |  |  |                      |                  |
| Bank loans              | -             | 275,076          | 198,595   | 200,945  | 187,440  | 155,536  | 446,939              | 1,464,531        |
| Other loans             | 6,815         | 6,614            | 6,345   | 6,076  | 5,807  | 5,537  | 15,933               | 53,127           |
| Trade payables          | -             | 85,195           | -   | -  | -  | -  | -                    | 85,195           |
| Other liabilities       | 15,863        | 48,817           | 18,400  | 17,037   | 33,891   | -  | -                    | 134,008          |
| Finance lease payable   | -             | 5,311            | 5,816   | 4,743  | -  | -  | -                    | 15,870           |
| Due to a shareholder    | -             | 542,451          | -   | -  | -  | -  | -                    | 542,451          |
| Due to related parties  | 1,010         | -                | -   | -  | -  | -  | -                    | 1,010            |
| Convertible bonds       | -             | -                | 30,779  | 220,271  | -  | 418,225  | -                    | 669,275          |
|                         | <u>23,688</u> | <u>963,464</u>   | <u>259,935</u>                                  | <u>449,072</u>                                   | <u>227,138</u>                                   | <u>579,298</u>                                   | <u>462,872</u>       | <u>2,965,467</u> |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 46. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(Continued)*

### Fair values

The following table sets out a comparison by category of carrying amounts and fair values of the Group's financial instruments that are carried in the financial statements at other than fair values. The fair values of these financial instruments have been calculated by discounting the expected future cash flows at prevailing interest rates:

|   | Carrying amount |           | Fair value |           |
|---|-----------------|-----------|------------|-----------|
|   | 2009            | 2008      | 2009       | 2008      |
|   | HK\$'000        | HK\$'000  | HK\$'000   | HK\$'000  |
| Financial assets:   |                 |           |            |           |
| Non-current receivables under service concession arrangements | 1,916,822       | 1,238,309 | 1,916,822  | 1,238,309 |
| Non-current other receivables                                 | 1,973           | 13,173    | 1,973      | 13,173    |
| Financial liabilities:  |                 |           |            |           |
| Non-current bank and other borrowings:                        |                 |           |            |           |
| Floating rate borrowings                                      | 1,226,095       | 986,868   | 1,226,095  | 986,868   |
| Fixed rate borrowings   | 94,127          | –         | 79,907     | –         |
| Convertible bonds   | 582,737         | 669,275   | 610,184    | 713,028   |
| Finance lease payable   | 4,743           | 10,559    | 4,743      | 10,559    |

*Note:* The carrying amounts of financial assets and liabilities which are due to be received or settled within one year are reasonable approximation of their respective fair values, and accordingly, no disclosure of the fair values of these financial instruments is made. In addition, as disclosed in note 21 to the financial statements, the available-for-sale investment of the Group is not stated at fair value but at cost less any accumulated impairment losses because fair value of which cannot be reasonably assessed and therefore no disclosure of the fair value of this financial instrument is made.

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 46. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(Continued)*

### Capital management

The primary objectives of the Group's capital management are to safeguard the Group's ability to continue as a going concern, so that it can continue to provide returns to shareholders and benefits to other stakeholders, and to provide an adequate return to shareholders by pricing products and services commensurately with the level of risk.

The Group manages its capital structure and makes adjustments to it in the light of changes in economic conditions. In order to maintain or adjust the capital structure, the Group may issue new shares to increase capital or sell assets to reduce debt.

The Group monitors capital using the gearing ratio. This ratio is calculated based on net debt and total equity. Net debt is calculated as total interest-bearing bank and other borrowings and convertible bonds (as shown in the statement of financial position) less cash and cash equivalents. The gearing ratios at 31 December 2009 and 2008 were as follows:

|               | 2009<br><i>HK\$'000</i> | 2008<br><i>HK\$'000</i> |
|---------------|-------------------------|-------------------------|
| Net debt      | <u>2,310,228</u>        | <u>1,033,448</u>        |
| Total equity  | <u>3,011,816</u>        | <u>1,997,957</u>        |
| Gearing ratio | <u>77%</u>              | <u>52%</u>              |

# NOTES TO FINANCIAL STATEMENTS

31 December 2009

## 47. FINANCIAL INSTRUMENTS BY CATEGORY

Other than an unlisted equity investment being classified as an available-for-sale investment as disclosed in note 21 to the financial statements, all financial assets and liabilities of the Group and the Company as at 31 December 2009 and 31 December 2008 were loans and receivables, and financial liabilities stated at amortised cost, respectively.

## 48. EVENT AFTER THE REPORTING PERIOD

On 27 January 2010, convertible bonds with an aggregate principal amount of HK\$68,150,381 have been converted by certain bondholders in exchange for 98,768,668 new ordinary shares of the Company. As a result of the conversions, the issued capital of the Company has been increased from HK\$348,219,699 divided into 3,482,196,992 shares to HK\$358,096,566 divided into 3,580,965,660 shares.

## 49. COMPARATIVE AMOUNTS

As further explained in note 3.2 to the financial statements, due to the adoption of HKFRS 8 during the current year, the presentation of operating segment information in the financial statements has been revised to comply with the new requirements. In addition, certain comparative amounts have been reclassified and restated to conform to the current year's presentation.

## 50. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on 31 March 2010.

# FIVE YEAR FINANCIAL SUMMARY

31 December 2009

A summary of the results and of the assets, liabilities and total equity of the Group for the last five financial years, as extracted from the audited financial statements and the annual report of the Company for the period ended 31 December 2008, is set out below:

## RESULTS

|  | Year ended 30 June |                  |                  | Period from<br>1 July<br>2007 to<br>31 December<br>2008 | Year ended<br>31 December<br>2009 |
|--|--------------------|------------------|------------------|---|-----------------------------------|
|  | 2005<br>HK\$'000   | 2006<br>HK\$'000 | 2007<br>HK\$'000 | 2008<br>HK\$'000<br>(note)                              | 2009<br>HK\$'000                  |
| Revenue                                | 66,036             | 35,786           | 19,899           | 337,681   | 1,730,013                         |
| Operating profit/(loss)                | (3,515)            | (3,202)          | (2,620)          | 55,947  | 272,818                           |
| Share of profit/(loss) of an associate | -                  | -                | -                | (811)   | 4,565                             |
| Amortisation of goodwill               | (12,400)           | -                | -                | -   | -                                 |
| Profit/(loss) before tax               | (15,915)           | (3,202)          | (2,620)          | 55,136  | 277,383                           |
| Income tax                             | (48)               | 14               | 53               | (12,234)  | (48,637)                          |
| Profit/(loss) for the year/period      | (15,963)           | (3,188)          | (2,567)          | 42,902  | 228,746                           |
| ATTRIBUTABLE TO:                       |                    |                  |                  |   |                                   |
| Shareholders of the Company            | (15,963)           | (3,188)          | (2,567)          | 30,984  | 192,711                           |
| Minority interests                     | -                  | -                | -                | 11,918  | 36,035                            |
|  | (15,963)           | (3,188)          | (2,567)          | 42,902  | 228,746                           |

## ASSETS, LIABILITIES AND TOTAL EQUITY

|   | 30 June          |                  |                  | 31 December      |                  |
|---|------------------|------------------|------------------|------------------|------------------|
|   | 2005<br>HK\$'000 | 2006<br>HK\$'000 | 2007<br>HK\$'000 | 2008<br>HK\$'000 | 2009<br>HK\$'000 |
| Total assets  | 36,750           | 34,096           | 32,115           | 4,816,158        | 7,423,717        |
| Total liabilities                                     | (3,309)          | (744)            | (679)            | (2,818,201)      | (4,411,901)      |
| NET ASSETS  | 33,441           | 33,352           | 31,436           | 1,997,957        | 3,011,816        |
| REPRESENTED BY:                                       |                  |                  |                  |                  |                  |
| Equity attributable to shareholders<br>of the Company | 33,441           | 33,352           | 31,436           | 1,758,301        | 2,622,905        |
| Minority interests                                    | -                | -                | -                | 239,656          | 388,911          |
| TOTAL EQUITY  | 33,441           | 33,352           | 31,436           | 1,997,957        | 3,011,816        |

Note:

Pursuant to an ordinary resolution passed at the Company's special general meeting held on 4 March 2008, the Company changed its financial year end date from 30 June to 31 December with effect from 4 March 2008 to align the financial year end date with that of Beijing Enterprises Holdings Limited, an intermediate holding company whose shares are listed on the Stock Exchange.





北控水務集團有限公司  
BEIJING ENTERPRISES WATER GROUP LIMITED

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