*for identification purpose only

China Water Industry Group Limited
中國水業集團有限公司*

(Incorporated in the Cayman Islands with limited liability)

Stock Code : 1129

Annual Report 2010

CONTENTS

CORPORATION INFORMATION

BOARD OF DIRECTORS

Executive Directors

Mr. Li Yu Gui *(Chairman)*
Mr. Yang Bin *(Chief Executive Officer)*
Ms. Chu Yin Yin, Georgiana
Mr. Li Wen Jun
Mr. Tang Hui Ping, Paul (Appointed on 1 January 2011)
Mr. Liu Bai Yue *(Chief Operating Officer)*
(Resigned on 1 January 2011)
Mr. Zhong Wen Sheng *(Managing Director)*
(Resigned on 4 January 2010)

Independent Non-Executive Directors

Mr. Chang Kin Man
Mr. Wu Tak Lung
Mr. Gu Wen Xuan

AUDIT COMMITTEE

Mr. Chang Kin Man *(Chairman)*
Mr. Wu Tak Lung
Mr. Gu Wen Xuan

REMUNERATION COMMITTEE

Mr. Chang Kin Man *(Chairman)*
Mr. Wu Tak Lung
Mr. Li Wen Jun (Appointed on 4 January 2010)
Mr. Zhong Wen Sheng (Resigned on 4 January 2010)

INVESTMENT COMMITTEE

Mr. Li Yu Gui *(Chairman)*
Mr. Yang Bin
Mr. Chang Kin Man
Mr. Li Wen Jun (Appointed on 4 January 2010)
Mr. Tang Hui Ping, Paul (Appointed on 30 March 2011)
Mr. Liu Bai Yue (Resigned on 1 January 2011)
Mr. Zhong Wen Sheng (Resigned on 4 January 2010)

COMPANY SECRETARY

Ms. Chu Yin Yin, Georgiana

PRINCIPAL BANKERS

PRC

Agricultural Bank of China
Bank of China
Industrial and Commercial Bank of China Limited

Hong Kong

Bank of China (Hong Kong) Limited
Chiyu Banking Corporation Limited
DBS Bank (Hong Kong) Limited
The Hongkong and Shanghai Banking Corporation Limited
Hang Seng Bank Limited

LEGAL ADVISERS TO HONG KONG LAWS

Robertsons Solicitors & Notaries
William W. L. Fan & Company

AS TO CAYMAN ISLANDS LAWS

Conyers Dill & Pearman

AUDITORS

SHINEWING (HK) CPA Limited

INTERNAL CONTROL REVIEW ADVISER

SHINEWING Risk Services Limited

PRINCIPAL SHARE REGISTRAR AND TRANSFER OFFICE

Butterfield Fulcrum Group (Cayman) Limited
Butterfield House, 68 Fort Street
P.O. Box 609
Grand Cayman KY1-1107
Cayman Islands

HONG KONG BRANCH SHARE REGISTRAR TRANSFER OFFICE

Union Registrars Limited
18/F., Fook Lee Commercial Centre, Town Place
33 Lockhart Road
Wanchai, Hong Kong

HEAD OFFICE AND PRINCIPAL PLACE OF BUSINESS

Room 1207, 12th Floor
West Tower, Shun Tak Centre
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STOCK CODE

1129

CHAIRMAN'S STATEMENT

On behalf of the board of directors (the "Board"), I am pleased to present to the shareholders the annual results of China Water Industry Group Limited (the "Company") and its subsidiaries (collectively referred to as the "Group") for the year ended 31 December 2010.

RESULTS

In 2010, the capital market was still stringent despite the overall gradual recovery of the world economy. As a result, the business expansion of the Group was encumbered to some extent. For its principal businesses, the Group continued its effort to strengthen the management of its subsidiaries and endeavoured to increase the amounts of water supply and sewage treatment on its existing capacity, and continued to explore the potential for various cost reductions, thus achieving a relatively significant growth in the income and gross profit from its principal businesses. Although the disposal of its interests in an associate and convertible bonds brought a loss to the Company, the amount of its loss this year decreased HK$192.69 million significantly to HK$149.80 million, representing a decrease of 56.3% from HK$342.49 million in the previous year. The Group's revenue in 2010 amounted to HK$238.77 million, representing an increase of 18.1% from HK$202.11 million in the previous year, and its gross profit amounted to HK$97.08 million, representing an increase of 33.2% from HK$72.87 million in the previous year.

Continuing operations

Water supply business

In 2010, the Group's water supply business consisted of 6 water supply plants which were located in Jiangxi Province, Anhui Province, Shandong Province and Hainan Province. The total daily water supply capacities were approximately 1,960,000 tonnes contributing revenue of HK$87.96 million during the year, representing 36.8% of the Group's total revenue. The price of water supply ranged from HK$1.21 to HK$2.21 per tonne.

Sewage treatment business

Sewage treatment business consisted of 2 sewage treatment plants which were located in Jiangxi Province and Shandong Province. The daily disposal sewage capacities were approximately 110,000 tonnes per day contributing revenue of HK$18.08 million during the year, representing 7.6% of the Group's total revenue. The price of sewage treatment ranged from HK$0.57 to HK$0.92 per tonne.

Construction of water supply and sewage treatment infrastructure

Construction service comprised water meter installation, construction of pipelines and pipelines repairing. This was the Group's major source of revenue contributing HK$132.73 million during the year, representing 55.6% of the Group's total revenue.

Discontinuing operations

iMerchants Limited ("iMerchants") was engaged in the business of investments in financial products and manufacturing and trading of ceramic sewage whose shares are listed on the Growth Enterprise Market. From October 2010, iMerchants ceased to be a subsidiary of Company, its whole businesses were reclassified to discontinued operations. Detail of iMerchants is set out under headings of "Discontinued operations of iMerchants" in Management Discussion and Analysis.

CHAIRMAN'S STATEMENT

PROSPECTS

The 21st century is considered a "century to tackle water shortage" by many. The severity and importance of water shortage have become a widespread consensus among the society and have been brought to the attention of the Central Government and local governments of China at all levels. For this reason, the water industry will become one of China's fastest growing industries in future.

It is explicitly stated in the Chinese Central Government's No. 1 Document in 2011 that "water is the origin of life, the cornerstone of production and the foundation of ecology". This short sentence stresses the importance of water for mankind. Article 26 in the Document unambiguously declares: "Water price reform will be proactively pushed forward, price escalation system will be gradually adopted in the excess volume of water consumed by industrial and service sectors, and the difference in water prices between water-consuming sectors and other sectors will be widened. Urban water prices will be reasonably adjusted, and the water price escalation system will be introduced steadily." Just like the saying: "the early bird catches the fish", all participants in the water industry have perceived these opportunities and are well-prepared for its future development. While enjoying the achievements but at the same time experiencing hardship and anxiety in this transformation process, they are once again encouraged in an unprecedented way. The problem of water prices, a restraining factor for the development of water industry, now looks poised to be resolved as the overall water price reform has reached a consensus among the State's decision-makers. With years of preparations in policies, considerations in public opinions and developments in technologies, the reform will hopefully be put into practice very soon. It will lay a solid foundation for the growth of our principal businesses.

In the past year, the Chinese economy maintained an admirable growth. As the Chinese government and civil society have shown greater concern for environmental protection industries, the infrastructure industry, including the water supply and sewage treatment sectors, has ascertained benefit from this trend. 2011 is the first year of the "Twelfth Five-year Plan" period, as disclosed in the outlines of the "Twelfth Five-year Plan" promulgated by the Chinese government, the energy conservation and environmental projects are among the list of pillar industries. It even clearly points out that "the role of industrial policy shall be exerted to the effect that more investments shall be attracted to the fields associated with people's likelihood, social welfare, agriculture and villages, technical innovation, ecological protection and resource conservation." Fixed asset investments for China's water industry have grown over 25% for 4 consecutive years. According to the estimates of relevant experts, the whole PRC water industry has a total market value of approximately RMB350 billion in 2010, and will increase to RMB750 billion by 2015. Apparently, the PRC water industry is greeting an unprecedented opportunity for rapid development.

CHAIRMAN'S STATEMENT

During the past few years, under the leadership of the Board and with the concerted efforts of all our staff, the Group made achievements in business expansion, industrial layout, principal business scale, enterprise management and other aspects, and possessed a certain influence in the industry by relying on the extensive management experiences of the Group's leadership. Especially in 2010, the principal business of the Group recorded substantial growth in both revenue and profitability. To ensure high-quality safe water supply and qualified sewage treatment, the Group successfully transformed one of its sewage treatment plants into an enterprise that met the grade 1A of national waste water discharge standard; continued to implement the identified sewage treatment projects; created additional income beyond principal business; implemented strategic partnership with certain central enterprises with international and domestic influence; and continued to develop new business and so on. All these achievements demonstrate that the Group has firmly seized the historical opportunities under the new circumstances and laid a solid foundation for future development.

Looking ahead, the Group will continue to strengthen its strict scientific management on existing projects, so as to enhance economic efficiency; will continue to actively seek water projects with good investment return and growth potential; will further finance through various channels and attract strategic investors, and to implement as soon as possible the specific projects identified with strategic partners; will continue to achieve the Group's prescribed water investment objectives, that is, a water supply capacity of 10 million tons per day and a sewage treatment capacity of 2 million tons per day, and better profitability through merger and acquisition, investment and water supply and treatment related construction. Furthermore, the Group will strive to achieve its strategic target of becoming a nationwide leading water group in the near future, while working hard to yield substantial returns for shareholders and investors.

APPRECIATION

Finally, I would like to take this opportunity to express my gratitude to my fellow directors, management teams and employees for their contributions and dedication to the development of the Group and my deep thanks to our shareholders, customers, suppliers and business partners for their continuous support over the years.

Li Yu Gui
Chairman

Hong Kong, 30 March 2011

MANAGEMENT DISCUSSION AND ANALYSIS

FINANCIAL PERFORMANCE

RESULTS

Financial results

The Group recorded a consolidated net loss of HK$149.80 million for the year. Comparing with the net loss in the previous year of HK$342.49 million, this represented a significant recovery of HK$192.69 million. This was mainly due to a decrease of HK$176.08 million from change in fair value of the Convertible Bonds ("CB"), and an improvement of HK$27.65 million from a loss to a gain in value relating to the disposal of available-for-sale investments. The main contributing factors to the net loss for the current year can be summarized as follows:

– loss of HK$79.45 million on deemed partial disposal of an associate,
– loss of HK$28.33 million from the change in fair value of CB issued in previous years,
– impairment loss of HK$30.50 million recognized on available-for-sale investments, and
– impairment loss of HK$40.26 million recognized on goodwill.

The loss before the accounting treatments of the change in fair value of CB and the two impairment losses is HK$50.71 million.

Revenue and gross profit for the continuing operation

Upon the deemed partial disposal of iMerchants from a subsidiary to an associate, the Group has only one single business operation involving the provision of water supply, sewage treatment and construction of water supply and sewage treatment infrastructures. For the year ended 31 December 2010, the Group achieved a continuing growth in revenue and gross profit, which amounted to HK$238.77 million and HK$97.08 million respectively. This represented a growth of 18.1% in revenue and 33.2% in gross profit as compared to the last year. The main revenue and gross profit contributors for the year were Yichun Water Industry Co., Ltd. ("Yichun Water") and Yingtan Water Supply Co., Ltd. ("Yingtan Water"), which collectively accounted for 68.3% of the consolidated revenue and 86.1% of gross profit respectively. The financial analysis of revenue and gross profit is as follows:

	Revenue				**Gross Profit**			
	2010		2009		**2010**		2009	
	HK$'M	**%**	*HK$'M*	%	***HK$'M***	**%**	*HK$'M*	%
Water supply services	**87.96**	**36.8%**	84.21	41.7%	**29.47**	**30.4%**	27.01	37.1%
Sewage treatment services	**18.08**	**7.6%**	18.54	9.2%	**6.07**	**6.3%**	6.90	9.5%
Construction services	**132.73**	**55.6%**	99.36	49.1%	**61.54**	**63.3%**	38.95	53.4%
Total	**238.77**		202.11		**97.08**		72.86	

MANAGEMENT DISCUSSION AND ANALYSIS

Other operating income

Other operating income increased by HK$11.33 million to HK$14.65 million. The increase was mainly due to interest received of HK$5.39 million from the Bureau of Yingtan City, sewage turnover compensation paid by the PRC government of HK$1.30 million and reversal of impairment loss of trade and other receivable of HK$0.92 million.

Selling and distribution costs and administrative expenses

Selling and distribution costs as well as administrative expenses recorded an aggregate amount of HK$70.07 million (2009: HK$70.21 million). These expenses mainly consisted of staff costs, legal and profession fees, rent and rates and depreciation.

Loss on deemed partial disposal of an associate

From October to December 2010, the equity interest of iMerchants owned by the Group had further reduced by 12.66% to 36.57% as a result the amounts of iMerchant's net asset value shared by the Group decreased from HK$308.95 million to HK$229.50 million. The difference of HK$79.45 million was recognized as loss in the Consolidated Statement of Comprehensive Income.

Net Gain on disposal of available-for-sale investments

Net gain from the disposal of available-for-sale investments rose substantially by HK$27.65 million to HK$4.93 million (2009: loss of HK$22.72 million). The major contribution was an amount of HK$3.22 million by selling equity investments held by iMerchants.

Impairment loss recognized on available-for-sale investments

This loss of HK$30.50 million arose from the fair value of the equity investment at the end of the reporting period being less than investment cost. Pursuant to the HKFRS, the equity investment is determined to be impaired when there is a significant or prolonged decline in the fair value of that investment below its cost, this is considered to be objective evidence of impairment. The respective cumulative loss previously accumulated in the investment revaluation reserve is reclassified to loss and are recognized in Consolidated Statement of Comprehensive Income.

Impairment loss recognized in respect of goodwill

During the year ended 31 December 2010, the Group recognized an impairment loss of goodwill of HK$40.26 million (2009: HK$66.07 million), which was mainly from the acquisition of Blue Mountain Hong Kong Group Limited. The impairment loss incurred as the present value of estimated future cash flows expected to arise from the cash-generating unit less than the respective carrying amount of the unit. The carrying amount included the carrying value of goodwill and the net asset value.

Finance costs

Finance costs of HK$9.53 million were mainly interest payments to banks and other borrowings of HK$8.11 million and to the convertible bondholders of HK$0.97 million (2009: HK$11.99 million).

MANAGEMENT DISCUSSION AND ANALYSIS

Share of loss from associates

The Group had two associated companies, iMerchants and Jinan Hongquan Water Production Co., Ltd. ("Jinan Hongquan"). In October 2010, the status of iMerchants was changed from a subsidiary to an associate of the Group. The Group held 36.57% equity interest in iMerchants, and shared the loss of HK$7.53 million from October to December 2010. During the year, the Group shared 35% loss from Jinan Hongquan of HK$0.58 million.

Discontinued operation of iMerchants

iMerchants was engaged in the business of investments in financial products and manufacturing and trading of ceramic sewage materials business. On 8 April 2009, iMerchants through its wholly-owned subsidiary of Growwise Holdings Limited, entered into a sale and purchase agreement with Rightshine Holdings Limited, to acquire the entire issued share capital of Supreme Luck International Limited ("Supreme Luck") at a consideration of HK$900,000,000. Upon completion of the acquisition, 61,522,160 Consideration Shares and 2,938,477,840 Convertible Preference Shares with a par value of HK$0.2 each as a partial consideration were allotted and issued to the Vendor by the iMerchants on 23 October 2009. During the year, the Convertible Preference Shares holders exercised their rights to convert into ordinary shares of iMerchants. There were a total of 3,439,800,000 shares issued at HK$0.04 each upon the conversion of preference shares. After the conversion, the equity interest of iMerchants owned by the Group had reduced further to 36.57% from 67.23%. iMerchants ceased to be a subsidiary of the Group and iMerchants' financial results were not consolidated into the Group's financial results and its businesses were classified in discontinued operation. From January to September 2010, iMerchants was a subsidiary of the Group and its financial result during this period was analysed as follows:

		Period ended 30.9.2010 ***HK$'M***	Year ended 31.12.2009 *HK$'M*
Revenue	(a)	**114.72**	8.94
Gross profit		**112.33**	4.82
Loss on the discontinued operations	(b)	**(230.55)**	(55.13)
Gain on deemed disposal of subsidiary	(c)	**258.23**	–
Gain on deemed partial disposal of subsidiary		**–**	21.32
		27.68	(33.81)

(a) The revenue was mainly the management fees attributable for the signed management contract between Supreme Luck with Shenzhen Careall Capital Investment Co., Ltd. dated 19 August 2009.

(b) Included in the loss of 2010, HK$245.64 million of impairment loss recognized on an intangible asset. Pursuant to the HKFRS, if the recoverable amount of intangible asset is estimated to be less than its carrying amounts, the difference is deemed as impairment loss and recognized as an expense in profit and loss.

(c) During the year, the Group's equity interest of iMerchants was diluted to 36.57% from 67.23%. Pursuant to the HKFRS, the Group was deemed to have disposed 30.66% of iMerchants and a gain thereon of HK$258.23 million was recognized.

LIQUIDITY AND FINANCIAL RESOURCES

As at 31 December 2010, the Group recorded cash and bank balance including cash held at financial institutions of HK$138.02 million (compared with HK$277.86 million on 31 December 2009). The decrease was mainly due to repayment of a portion of the issued CB and advances to independent third parties. The Group has had steady cash flow generating from the water supply and sewage treatment business segments.

The Group's consolidated non-current assets decreased by HK$827.10 million to HK$1,075.73 million (2009: HK$1,902.83 million). The decrease was mainly due to the intangible assets of HK$915.30 million being disposed of along with the deemed disposal of iMerchants during the year. This intangible asset was obtained through the acquisition of Supreme Luck by iMerchants in 2009.

The trade and other receivables including loans receivable in the current asset increased by HK$74.30 million to HK$148.90 million. The increase was mainly due to (i) reclassification the deposit paid of HK$50.90 million for acquisition of subsidiaries to loans receivable and (ii) loans to independent third parties. The deposit paid of HK$50.90 million was included in the loans receivable of HK$68.21 million which was due from Top Vision Management Limited ("Top Vision"). The Group considered to off-set HK$43.5 million as part of the consideration in the acquisition of sewage treatment plants from Top Vision. The responsible director has submitted the application of share transfer relating to the acquisition of the sewage treatment plants to the Administration for Industry and Commerce* (工商行政管理局), the PRC. As the procedures for the change of shareholding are complicated and require the approval from several PRC government authorities. The Board expects that the share transfer will be completed in 2 months.

Total liabilities of the Group as at 31 December 2010 were HK$791.59 million (compared with HK$937.12 million on 31 December 2009). They mainly comprised of the CB of HK$400.19 million (2009: HK$585.17 million), bank and other borrowings of HK$142.87 million (2009: HK$135.64 million), and government grants of HK$64.07 million (2009: HK$60.04 million). The CB were denominated in HK dollars, while others were denominated in Renminbi and the interest rates of which were fixed. The maturity profile for loans and other borrowings of the Company are set out in the notes 29 and 30 of the financial statements.

The Group's gearing ratio as at 31 December 2010 was 55.8% (2009: 41.1%). The ratio was calculated by dividing total liabilities of HK$791.59 million over total assets of the Group of HK$1,419.64 million.

At as 31 December 2010, the Group had net current liabilities of HK$303.57 million (2009: net current liabilities of HK$306.62 million). The current portion of CB amounting to HK$397.19 million represented 61.3% of the total current liabilities. During the year, the Company successfully restructured the existing CB with bondholders and entered into two Definitive Agreements on 13 August 2010 and 24 September 2010. The bondholders agreed to the Company to pay a partial of the CB in a series of installments commencing in August 2010 and ending in August 2012, and to issue New Bonds for the remaining CB balance. Details of CB are set out under headings of "Issue of new HK$ New Bonds in 2010" and "Restructuring of convertible bonds issued in 2007". To meet these debt obligations, the board considered various fund raising alternatives to strengthen the capital base of the Company. The Board is confident that the Group will be able to meet its financial obligation as and when they fall due and has sufficient working capital to support future operational needs.

MANAGEMENT DISCUSSION AND ANALYSIS

CAPITAL RAISING AND USE OF PROCEEDS

On 9 August 2010, the Company entered into a top-up placing agreement with existing shareholders and placing agent, pursuant to which, the Company placed out 265,476,000 new ordinary share of HK$0.1 each at a placing price of HK$0.108 per share. The placing was completed on 12 August 2010. The net proceed from the placing was approximately HK$28 million after deducting related expenses. At the same date, the Company entered into a new placing agreement with the placing agent, pursuant to which, the Company placed out 275,796,000 new ordinary share of HK$0.1 each in the Company at a placing price of HK$0.108 per share. The placing was completed on 30 November 2010. The net proceed from the placing was approximately HK$29 million after deducting related expenses. The proceeds from the fund raising exercises were for general working capital purposes.

Subsequent to year 2010, three CB holders exercised their rights and converted the aggregate principle CB amount of HK$31 million into 206,666,664 shares. Details of the conversion were announced in the Next Day Disclosure Returns on 3 March 2011, 15 March 2011 and 28 March 2011.

During the year, the Group incurred capital expenditures amounting to HK$71.50 million (2009: HK$207.21 million) for acquisition of concession intangible assets.

MAJOR EVENTS DURING THE YEAR UNDER REVIEW

Termination to acquire of subsidiaries

On 18 September 2009, Swift Surplus Holdings Limited ("Swift Surplus") entered into the Sales and Purchase Agreement with Sihui South China Waterworks Development Co., Ltd.* ("Sihui South China") (四會市華南水務發展有限公司), Shenzhen City South China Waterworks Group Co., Ltd.* ("Shenzhen City South China") (深圳市華南水務集團有限公司) and Da Xin Waterworks Management (Huizhou) Co., Ltd.* ("Da Xin Waterworks") (達信水務管理（惠州）有限公司), pursuant to which the Swift Surplus has conditionally agreed to acquire 70% of the registered capital of Foshan City Gaoming Huaxin Sewage Treatment Company Ltd.* ("Gaoming Huaxin") (佛山市高明區華信污水處理有限公司); 70% of the registered capital of Tangshan City Hongxiang Waterworks Limited* ("Hongxiang") (唐山市鴻翔水務有限公司); 100% interest of Boluo Phase II Project Company ("Boluo Phase II") (博羅二期項目公司) respectively, at a consideration of HK$170 million. The Group has paid HK$50.90 million as a deposit for the acquisition and the remaining amount will be paid upon the completion of the transaction. Since the conditions precedent to the acquisition have not been fulfilled on or before the extended long stop date on 31 October 2010, the relevant parties entered into the Termination Agreement on 29 November 2010 to cancel this acquisition with immediate effect. The deposit paid amounting to HK$50.90 million was assigned as loan to the holding company of the Vendors, Top Vision. The Directors are of view that the termination will not cause any material adverse impact on the existing business of the Group.

Acquisition of subsidiaries

On 1 December 2010, Mark Profit Group Holdings Limited ("Mark Profit"), a wholly owned subsidiary of the Company, entered into the Sales and Purchase Agreement with Top Vision and Da Xin Waterworks pursuant to which the Mark Profit has conditionally agreed to acquire 70% of the registered capital of Gaoming Huaxin; 100% of the registered capital of Sihui South China, 100% interest of Boluo Da Xin Sewage Treatment Company Ltd.* ("Boluo Daxin") (博羅達信污水處理有限公司) respectively, at a consideration of HK$50 million. The consideration of HK$6.5 million will be paid in cash for refundable deposit before completion and the remaining balance of HK$43.5 million will be offset by the loan which was owed by Top Vision. The acquisition has not been completed as of this report date. The responsible director has submitted the application of share transfer relating to the acquisition of the sewage treatment plants to the Administration for Industry and Commerce* (工商行政管理局), the PRC. As the procedures for the change of shareholding are complicated and require the approval from several PRC government authorities. The Board expects that the share transfer will be completed in 2 months. Upon completion of acquisition, additional 3 sewage treatment plants will add to the Group.

MANAGEMENT DISCUSSION AND ANALYSIS

Changed from the investment in a subsidiary to investment in an associate

From June to October 2010, the Convertible Preference Shares holders exercised their rights to convert the Convertible Preference Shares into ordinary shares of iMerchants. There were totally 3,439,800,000 iMerchants shares at HK$0.04 each issued upon the conversion of preference shares. After the conversion, the equity interest of iMerchants owned by the Group has reduced further from 67.23% to 36.57%. From the beginning of October 2010, iMerchants is an associate of the Group.

Issue of new HK$ New Bonds in 2010

On 13 August 2010, the Company entered into a series of Definitive Agreements ("DA1") with investors who collectively held approximately 79% of the existing CB (the "Majority Investors"). New CB due in 2012 in the aggregate principal amount of HK$337 million were issued as a consideration of settling the Majority Investors' interests in existing CB. The new CB comprised a portion of HK$175 million Repurchase Bonds which could neither be converted nor redeemed into ordinary share of the Company, and could not be traded. The remaining portion of new CB of HK$162 million could be converted at the opinion of the Majority Investors at a conversion price of HK$0.15 per ordinary share at any time on or after 15 October 2010 and up to the close of business on 9 August 2012.

Restructuring of convertible bonds issued in 2007

On 24 September 2010, the Company entered into another series Definitive Agreements ("DA2") with investors who collectively holding the remaining approximately 21% of the existing CB (the "Minority Investors"). Pursuant to the DA2, the terms and conditions of the existing CB were restructured with the following key terms:

1. Redemptions by installments: The existing CB held by the Minority Investors could be redeemed for a total consideration of approximately HK$128 million in cash (excluding interest costs and discounts for early repayment), payable in a series of installments commencing from October 2010 and ending in July 2012.

2. Revised maturity date: The original maturity date, being 3 August 2012, was brought forward to 31 July 2012.

3. Removal of the Company Sweep-up call option: The Company's sweep-up call option to early redeem the existing CB if and when at least 90% of the existing CB had already been converted, redeemed or purchased and cancelled had been removed.

4. Revised further indebtedness covenant: The original limitation on further indebtedness has been revised so that as long as the New Bonds are outstanding, the Group should not incur any further debts for which there was any recourse to the Company without the prior written consent of the holders representing over 50% in principal amount of the existing CB then outstanding unless the aggregate principal amounts of such further debt incurred after 3 August 2007 was less than US$50 million.

Save for the abovementioned key terms, the existing CB would substantially have the same terms and conditions stated in the bond purchase agreement dated 30 July 2007 and in particular, the prevailing conversion price for existing CB remained at HK$1.136 and the existing conversion price adjustments preserved.

Letter of Intent

On 13 December 2010, Neutral Crown Holdings Limited ("Neutral Crown"), a wholly owned subsidiary of the Company, entered into a non-legally binding Letter of Intent with Vendors, pursuant to which Neutral Crown intends to acquire eight sewage treatment plants in Zhaoqing City, Guangdong Province, the PRC, at a consideration not more than HK$200 million and Vendors agree to sell the entire equity interest of Li Lai Investment Holdings Limited ("Li Lai"). Li Lai has owned an indirectly wholly-owned subsidiary namely Guangdong Zhong Tian Heng Ji Environment Protection Investment Co., Ltd.* which has obtained the concessions of eight sewage treatment plants. Up to the report date, no sales and purchase agreement has been signed.

Supplemental build operate transfer

On 31 August 2010, Jining City Haiyuan Water Treatment Company Limited* ("Jining Haiyuan"), an indirect subsidiary of the Company, entered into a supplemental build operate transfer agreement with the government of Jinxiang county, Jining city ("Supplemental BOT Agreement"). Pursuant to the Supplemental BOT Agreement, Jining Haiyuan shall further invest in the expansion and upgrades of the Plant ("Project") such that the discharged water quality shall improve from grade 1B standard to grade 1A standard in the PRC and the sewage charges shall increase from Renminbi 0.80 to Renminbi 1.19 per tonne, Jinxiang county government has also agreed to grant exemptions from various administrative charges. The upgraded plant has been put into operation at the end of the year.

PENDING LITIGATION

(i) Technostore Limited, a subsidiary of the Company

On 30 May 2007, a Petition was filed under sections 168A and 177 of the Company Ordinance (Cap. 32) to wind-up Technostore Limited ("Technostore"), a company in which the Company held 50.01% of the issued shares. The Petition was commenced by Mr. Mao Chi Fai ("Petitioner"), the minority shareholder of Technostore holding 49.99% of the issued shares.

Following court hearings regarding the winding-up proceeding in the preceding year, on 29 August 2008, the court made an order to appoint Kenny Tam & Company, Certified Public Accountant as a liquidator of Technostore. The Liquidator, Happy Hour Limited and Mr. Mao Chi Fai to become members in the Committee of Inspection ("COI"). In October 2009, all stocks of Technostore with costs valued at approximately HK$2.2 million transferred by the Official Receiver's Office to the Liquidator were disposed at the consideration of around HK$0.62 million by public tender. As of the report date, the latest development in the liquidation process reported by the Liquidator was that preferential and ordinary dividends were distributed in November 2010. Further a sum of less than HK$1,000 was realized from the bank accounts of Technostore. The Liquidator has further indicated that it anticipates that statements of accounts containing further details of the distribution have been submitted to the Official Receiver's Office for approval and shall be circulated once approved by the Official Receiver. The matter is still in the liquidation process up to the report date and is being handled by the Official Receiver's Office. The directors of the Company believe that no material future outflows resources from the Group is expected and sufficient provision on assets related to Technostore have been provided. It is unlikely that there will be a material adverse financial impact on the Group.

(ii) Super Sino Investment Limited, an indirect wholly-owned subsidiary of the Company

On 6 November 2007, the People's Government of Danzhou and Super Sino Investment Limited ("Super Sino") entered into an assets and liabilities transfer agreement, pursuant to which the assets and liabilities of Danzhou City Water Company* (儋州市自來水公司) were transferred to Super Sino. On 26 June 2008, Agricultural Bank of China Danzhou Branch instituted proceedings with Hainan Intermediate People's Court against Danzhou City Water Company, Super Sino and the People's Government of Danzhou (a third party) regarding the abovementioned transfer of the relevant liabilities, claiming for the principal of RMB26 million and the interest thereon of RMB43.17 million repayable by Danzhou City Water Company and Super Sino (as defendants). On 13 November 2009, the First Intermediate People's Court of Hainan Province issued a civil verdict, pursuant to which Super Sino was ordered to fully repay the loan principal of RMB26 million together with the interest thereon. On 17 December 2009, the Plaintiff made an appeal to the Higher People's Court of Hainan Province court seeking the fulfilment of the guarantee responsibility of Danzhou Urban Development Corporation. On 15 December 2010, Higher People's Court of Hainan Province issued verdict, pursuant to which all the shares of Danzhou City Water owned by Super Sino (the "shares") have been freezed from 15 December 2010 to 14 December 2012. The Company cannot transfer or dispose of the shares during the period.

According to the legal advice, the directors of the Company are of the opinion that the verdict will not impair the control of the Group over Danzhou City Water due to the following reason:

(1) Super Sino is still the legal owner of Danzhou City Water during the year ended 31 December 2010 and up to the reporting date.

(2) As Danzhou City Water is engaged in the business of provision of water in the PRC which requires special license from the respective the PRC government authorities. The procedures for the change of shareholding is complicated and require the approval from several the PRC government authorities.

As at the reporting date, the directors of the Company are discussing the settlement arrangement with the Plaintiff and there is no demand for settlement from the Plaintiff at the moment. The principal of the said loan and the interest thereon have been included in the consolidated financial statements of the Group. The directors of the Company are of the view that the aforesaid litigation is unlikely to have any significant material financial impact on the Group.

Save and except for this, the Company is not aware of any other significant proceedings instituted against the Company.

FOREIGN EXCHANGE RISK

The Group's exposure to foreign exchange risk is minimal as most of the Group's subsidiaries operate in the PRC and most of the transactions, assets and liabilities are denominated in Renminbi. Accordingly, the Group does not have derivative financial instruments to hedge its foreign currency risks.

MANAGEMENT DISCUSSION AND ANALYSIS

PLEDGE OF ASSETS

The Group's bank loans and other loans of HK$35.42 million in total as at 31 December 2010 (2009: HK$36.74 million were secured by:

(i) Charges over property, plant and equipment in which their carrying amount was HK$2.19 million (2009: HK$2.19 million);

(ii) Charges over prepaid lease payments in relation to land use right in which their aggregate carrying amount was HK$10.28 million (2009: HK$12.88 million); and

(iii) Charges over concession intangible assets in relation to exclusive operating rights for provision of water supply and sewage treatment service to the public users in which their aggregate carrying amount was HK$19.24 million (2009: HK$19.39 million).

CONTINGENT LIABILITIES

As at 31 December 2010, the group did not have any significant contingent liabilities (2009: Nil)

CAPITAL COMMITMENTS

As at 31 December 2010, the Group has the capital commitments contracted but not provided for acquisition of property, plant and equipment approximately HK$7.08 million (2009: HK$7.51 million).

EMPLOYEES AND REMUNERATION POLICES

As at 31 December 2010, the Group has employed approximately 898 full-time employees (2009: 884 full-time employees). Most of them stationed in the PRC while the remaining in Hong Kong. The remuneration package of the employees is determined by various factors including the employees' experience and performance, the market condition, industry practice and applicable employment law.

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

DIRECTORS

Executive Directors

Mr. Li Yu Gui ("Mr. Li"), aged 65, was appointed as the Chairman and Executive Director of the Company in October 2007. Currently, he also serves as the Secretary General of the Guangdong Water Supply Association* (廣東省城鎮供水協會). Mr. Li has accumulated more than 30 years of experience in the organization and management of middle-to-large scale city water treatment plants as well as the construction of water supply facilities. Prior to joining the Company, Mr. Li had been the Chief Officer of the Infrastructure Department of the Guangzhou Utilities Authority* (廣州市公用事業局基本建設處), the General Manager of Guangzhou Water Supply Company* (廣州市自來水公司), the Vice Chairman of the National Water Supply Association* (全國城鎮供水協會) and the Chairman of the board of directors of the Guangdong Water Supply Association* (廣東省城鎮供水協會). During his tenure in the Guangzhou Water Supply Company, he had successively organized several large scale water supply construction projects, in which Mr. Li had taken a leading and directive role, collectively supply 4 million tones drinkable water to Guangzhou city per day.

Mr. Yang Bin ("Mr. Yang"), aged 37, was appointed as Executive Director of the Company in December 2008 and the Chief Executive Officer in June 2009. Mr. Yang is currently an Executive Director of iMerchants Limited (Stock code: 08009), an associate of the Company and the shares of which are listed on the Growth Enterprise Market of The Stock Exchange. Mr. Yang was graduated from the college of Jiu-jiang, Jiangxi Province, the PRC. He has also completed his studies in Economy Administration in Distance Learning College of The Party School of the Central Committee of the Communist Party of China. Mr. Yang joined the Company in 2007 as a deputy general manager in charge of the Operation Division of the Company. He has over 10 years' working experience in water industry. Before joining the Company, Mr. Yang was a General Manager Assistant of Jiangxi Shangrao City Water Supply Company* (江西省上饒市自來水公司) where he was mainly responsible for marketing and promoting water supply business to the urban residents of Shangrao City, the People's Republic of China (the "PRC")as well as designing and constructing water supply piping network.

Ms. Chu Yin Yin, Georgiana ("Ms. Chu"), aged 40, was appointed as the Executive Director and Company Secretary of the Company in October 2006. Ms. Chu holds a Bachelor's Degree of Business Administration in Accountancy and a Master's Degree of Corporate Governance. She is a fellow member of both the Hong Kong Institute of Certified Public Accountants, the Association of the Chartered Certified Accountants and a member of the Institute of Chartered Accountants in England and Wales. Ms. Chu is also an associate of the Institute of Chartered Secretaries and Administrators and a member of the Hong Kong Institute of Company Secretaries. Prior to joining the Company, she has over 15 years' extensive experience by working in an international audit firm and other listed companies.

Mr. Li Wen Jun ("Mr. Li"), aged 52, was appointed as the Executive Director of the Company in June 2009. Mr. Li is currently an Executive Director of iMerchants Limited (Stock code: 08009), an associate of the Company and the shares of which are listed on the Growth Enterprise Market of The Stock Exchange. Mr. Li was graduated from Department of Chemical Machinery of South China University of Technology. He has passed the national training and examination organised by the State Council of the PRC in respect of the overseas delegated engineer and he has also passed the national training and examination for managers and factory director. Mr. Li has more than 25 years of extensive experience in chemical engineering and management of the chemical industry in the PRC. Mr. Li has also conducted various research and development projects in relation to organic chemistry majoring in research on treatment of sewage by (BAF) Biological Aerated Filter.

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

Mr. Tang Hui Ping, Paul ("Mr. Tang"), aged 56, was appointed as an Executive Director in January 2011. He is currently an Chief Internal Auditor and Deputy General Manager since 2009. Mr. Tang holds a Bachelor Degree in Accountancy from the South Central University of Finance & Economic, Politics & Law, China and a Master's Degree in Business Administration from the Oklahoma City University, United States of America. He is a member of Certified Management Accountant of Australia in 2000. Mr. Tang has more than 27 years extensive experience in the finance & accounting field in the PRC, Hong Kong and Canada.

Independent Non-executive Directors

Mr. Chang Kin Man ("Mr. Chang"), aged 47, was appointed as the Independent Non-executive Director of the Company in June 2006. Mr. Chang is currently an Independent Non-executive Director of Birmingham International Holdings Limited (stock code: 2309) which is listed on the Main Board of the Stock Exchange, and iMerchants Limited (stock code: 8009), an associate of the Company and which is listed on the Growth Enterprise Market operated by the Stock Exchange. He is a certified public accountant in Hong Kong and a fellow member of The Association of Chartered Certified Accountants and an associate member of the Hong Kong Institute of Certified Public Accountants. Mr. Chang holds a Bachelor's Degree in Economics and a Master's Degree in Applied Finance. Mr. Chang has extensive experience in corporate finance and in accounting field. He worked for an international accounting firm and a number of public listed companies for more than 15 years.

Mr. Wu Tak Lung ("Mr. Wu"), aged 45, was appointed as the Independent Non-executive Director of the Company in June 2006. Mr. Wu is currently an Independent Non-executive Director of AUPU Group Holding Company Limited (stock code:477) and Neo-Neon Holdings Limited (stock code: 1868) which are listed on the Main Board of the Stock Exchange, and AKM Industrial Company Limited (stock code: 8298) and iMerchants Limited (stock code: 8009) which are listed on the Growth Enterprise Market operated by the Stock Exchange. Mr. Wu is a fellow member of The Association of Chartered Certified Accountants, The Hong Kong Institute of Chartered Secretaries and The Taxation Institute of Hong Kong. Mr. Wu is also a full Member of the Hong Kong Securities Institute and an associate member of The Hong Kong Institute of Certified Accountants. Mr. Wu received a Bachelor's Degree in Business Administration from the Hong Kong Baptist University and a Master's Degree in Business Administration from the University of Manchester and the University of Wale. Mr. Wu is a Vice-President of The Association of Chartered Certified Accountant and President of The Taxation Institute of Hong Kong. He is also a Vice-President of Hong Kong Guangdong Youth Exchange Promotion Association, a Council Member of Kiangsu and Chekiang Shanghai Resident (HK) Association and an Honorary Associate of the School of Business of the Hong Kong Baptist University.

Mr. Gu Wen Xuan ("Mr. Gu"), aged 68, was appointed as the Independent Non-executive Director of the Company in November 2006, Mr. Gu had been the Deputy Director General of The Department of Urban Planning of The Ministry of Construction of the PRC and taking a leading role in other related bureau. During his working for the government bureau, Mr. Gu was responsible for urban planning and in charge of the designs of various infra-structures (which includes the planning and designs of water supply-related projects) for the urban cities in the PRC. Mr. Gu had accumulated over 15 years of experience in urban planning. Mr. Gu obtained his Bachelor degree in Geography and Master's Degree of Science in Regional Planning from The Beijing Normal University. Mr. Gu has been qualified as a Research Fellow of the Seal of the Evaluation Committee of Professional Titles and also a State Certified Planner of The Ministry of Construction of the PRC.

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

SENIOR MANAGEMENT OF THE GROUP

Mr. Gu Ling Bo ("Mr. Gu"), aged 42, joined the Company as the General Manager in December 2006. He holds a Bachelor's Degree in Radiation Chemistry from Sichuan University, the People's Republic of China (the "PRC") and a Master's Degree in Business Administration from the New York Institute of Technology, USA. Currently, Mr. Gu is the Vice Executive President of Jiangxi Yichun Water Industry Co., Ltd. ("Yichun Water") (江西宜春市供水有限公司) since 2004 and also being the Managing Director of Jiangxi Yichun Fangke Sewage Treatment Company Limited* ("Yichun Fangke") (江西宜春市方科污水處理有限公司) since 2005. He has successfully reorganized the management team of Yichun Water and brought a remarkable profit growth to Yichun Water under his governance. Mr. Gu has more than 10 years extensive expertise and experiences in corporate development and project management.

Ms. Lam Man Yee, Maria ("Ms. Lam"), aged 39, was appointed as the Financial Controller of the Company in December 2006 and is responsible for Financial Management and Corporate Administration. Ms. Lam holds a Bachelor's Degree in Accountancy. She is an associate member of Hong Kong Institute of Certified Public Accountant and an associate member of Association of International Accountants. Before joining the Group in December 2006, she had over 10 years of working experience in auditing, internal auditing, financial accounting and management accounting.

Mr. Zhang Yan Qing ("Mr. Zhang"), aged 42, joined the Company as a Deputy General Manager in December 2006. Mr. Zhang holds a Master's Degree in Business Administration from Hefei University of Technology. Before joining Company, Mr. Zhang was a financial controller of Yichun Water since 2004. He has over 10 years' extensive experience in the financial accounting and management accounting.

Mr. Liu Peng Cheng ("Mr. Liu"), aged 38, had resigned as the Executive Director and Deputy Chairman of the Company in May 2009 but remain serves as a General Manager of the Engineering Department of the Company. Mr. Liu holds a Bachelor of Science Degree in Physics from the Shenzhen University. Before joining the Company, he was the Chief Marketing Executive in Southern China Region of Anhui Guo Zhen Environmental Energy Savings Technology Company Limited* (安徽國禎環保節能科技有限公司), which is a sizeable enterprise in the People's Republic of China (the "PRC") engaging in environmental protection industry. Mr. Liu has extensive expertise and more than 10 years experience in water and water related industries. He had been responsible for the design and constructing of various water supply and sewage treatment factories in the PRC.

Mr. Liu Bai Yue ("Mr. Liu"), aged 60, resigned as the Chief Operating Officer and Executive Director and other directorship in subsidiaries of the Company in January 2011. Upon his resignation, Mr. Liu was appointed as a consultant to the Company. Mr. Liu graduated from the School of Adult Education, China University of Political Science and Law. He is a registered practicing certified enterprise legal advisor as well as an arbitrator of the Guangzhou Arbitration Commission in the PRC. Prior to joining the Company, Mr. Liu was head of the financial department, asset management department and legal department of GDH Limited, the Hong Kong representative office of People's Government of Guangdong Province and held various positions including the Chairman of the Board and Managing Director of its certain companies from 1986 to 2006. Mr. Liu has over 20 years of experience in handling and management of international trade, investment, corporate restructure and merger and acquisition.

Mr. Zhong Wen Sheng ("Mr. Zhong"), aged 44, had resigned as the Managing Director and General Manager of the Company in January 2010 and April 2010 respectively. He graduated from the Sichuan University with a Master's Degree in National Economic Management. Mr. Zhong has over 15 years of experience in the corporate finance, management, and treasury control, especially in the China water and related industries. Prior to joining the Company, he was the General Manager in-charging the Corporate Finance Department and the Financial Controller of the Shenzhen Head Office of China Water Affairs Group Limited (Stock Code:855), a company listed on the main board of the Stock Exchange of Hong Kong.

CORPORATE GOVERNANCE REPORT

OVERVIEW

The directors of the Company are committed to achieving and maintaining high standards of corporate governance to ensure that all decisions are made in good faith, in the best interest of shareholders and in long-term shareholders value.

The corporate governance standards of the Company are built on the principles of independence, accountability, transparency and fairness. Throughout the financial year ended 31 December 2010, the Company has complied with the code provisions set out in the Code of Corporate Governance Practices (the "Code") contained in Appendix 14 of the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited (the "Listing Rules") which was in force prior to 1 January 2005.

CORPORATE GOVERNANCE PRACTICE

A Directors

A.1 Board of Directors

- The Company has held 39 Board meetings in the year of 2010. Directors have been consulted to advice the agenda of the Board meeting. Sufficient notice of the Board meeting has been given to the Directors.

- Directors may attend meetings in person or through other means of telephone, electronic or other communication facilities in accordance with the minutes of the Board. The Board Committees are recorded in sufficient details and kept by the company secretary for inspection at any reasonable time on reasonable notice by any Director.

- Directors were supplied with adequate and relevant information in a timely manner to enable them forming decision in the relevant meetings. Every Director is aware that he/she should give sufficient time and attention to the affairs of the Company. Agreed procedures are in place providing to the member of the Board and/or committee to seek independent professional advice at the Company's expenses to assist them to discharge their duties.

- Where a substantial shareholder or a Director had a conflict of interest in a matter to be considered by the Board which the Board has determined to be material, a Board meeting was held instead of by way of circulation and with the presence of Independent Non-executive Directors.

- There was in place a Directors' and Officers' Liabilities Insurance cover in respect of legal actions against Directors and senior management arising out of corporate activities.

- The Board holds meetings on a regular basis and will meet on other occasions when a board-level decision on a particular matter is required. The Board also monitors and controls financial performance in pursuit of the Group's strategic objectives. The names of the directors during the financial year and their individual attendance of is set out below:

Name	Number of Board Meetings Attended/Total
Total numbers of meetings held during the year of 2010	39
Executives Directors:	
Mr. Li Yu Gui *(Chairman)*	32/39
Mr. Yang Bin *(Chief Executive Officer)*	39/39
Ms. Chu Yin Yin, Georgiana	27/39
Mr. Li Wen Jun	39/39
Mr. Liu Bai Yue *(Chief Operating Officer)* (Resigned on 1 January 2011)	22/39
Mr. Zhong Wen Sheng *(Managing Director)* (Resigned on 4 January 2010)	0/39
Independent Non-Executive Directors:	
Mr. Chang Kin Man	39/39
Mr. Wu Tak Lung	12/39
Mr. Gu Wen Xuan	38/39

A.2 Chairman and Chief Executive Officer

- The Chairman of the Group is Mr. Li Yu Gui ("Mr. Li") and the Chief Executive Officer ("CEO") of the Group is Mr. Yang Bin ("Mr. Yang"). The roles of Chairman and CEO are separate and not performed by the same individual to ensure a balance of power and authority. Their responsibilities are clearly defined and set out in writing.

- The Chairman provides leadership and is responsible for the effective functioning of the Board in accordance with good corporate governance practice. With the support of the senior management, the Chairman is also responsible for ensuring that the Directors receive adequate, complete and reliable information in a timely manner and appropriate briefing on issues arising at board meeting.

- The CEO focuses on implementing objectives, policies and strategies approved and delegated by the Board. He is in charge of the Company's day-to-day management and operations. He is also responsible for developing strategic plans and formulating the company practices and procedures, business objectives and risk assessment for the Board's approval.

A.3 Board Composition

- The composition of the Board is shown on page 18 of this report. The Board comprises a total of 8 members including 5 Executive Directors and 3 Independent Non-Executive Directors. Members of the Board have different professional and relevant industry experiences and background so as to bring in valuable contributions and advices for the development of the Group's business.

- During the year, the Board at all times met the requirements of the Listing Rules relating to having at least 3 independent non-executive Directors and two of them are qualified accountants.

- The Company has received written confirmation from each Independent Non-Executive Director of their independence to the Group. The Group considered all of Independent Non-Executive Directors meets the independence guidelines set out in Rule 3.13 of the Listing Rules and are independent in accordance with the terms of the guidelines.

- The names of the directors and their respective biographies are set out on pages 15 to 17 of this annual report.

A.4 Appointment, re-election and removal

- The Company does not have a nomination committee, and the power to nominate or appoint additional directors is vested in the Board according to the articles of association of the Company, in addition to the power of the shareholders to nominate any person to become a director of the Company in accordance with the articles of association of the Company.

- The Board takes the responsibility to review the Board composition, monitoring the appointment and succession planning of Directors and assessing the independence of Independent Non-executive Directors. During the year, the Board held 2 meetings including for the approval of the resignation of Managing Director and Chief Operating Officer and for the appointment of executive Director. The names of the directors during the financial year and their individual attendance of is set out below:

Name	Number of Board Meetings Attended/Total
Total numbers of meetings held during the year of 2010	2
Executives Directors:	
Mr. Li Yu Gui *(Chairman)*	2/2
Mr. Yang Bin *(Chief Executive Officer)*	2/2
Ms. Chu Yin Yin, Georgiana	2/2
Mr. Li Wen Jun	2/2
Mr. Liu Bai Yue *(Chief Operating Officer)* *(Resigned on 1 January 2011)*	1/2
Mr. Zhong Wen Sheng *(Managing Director)* *(Resigned on 4 January 2010)*	0/2
Independent Non-Executive Directors:	
Mr. Chang Kin Man	2/2
Mr. Wu Tak Lung	1/2
Mr. Gu Wen Xuan	2/2

- The Board from time to time considers replenishing the composition of the Board whenever the Company requires to meet the business demand, opportunities and challenges and to comply with the laws and regulations. The nomination procedures basically follow the articles of association which empowers the Board from time to time and at any time to appoint any person as a director either to fill a casual vacancy or as an additional to the Board. The Directors will select and evaluate the balance of skills, qualification, knowledge and experience of the candidate to the directorship as may be required by the Company from time to time by such means as the Company may deems fit. The Directors shall consider the candidate from a wide range of backgrounds, on his/her merits and against objective criteria set out by the Board and taking into consideration his/her time devoted to the position. Up to the reporting date, Mr. Tang Hui Ping, Paul ("Mr. Tang") was appointed as director after carried out the above process of selecting and procedures by the Board. Mr. Tang should be subject to election by shareholders in the coming Annual General Meeting ("AGM") after his appointment.

- At every AGM, one-third of the Directors for the time being or, if their number is not a multiple of three or a multiple of three, then the number nearest to but not less than one-third shall retire from office by rotation provided that every Directors, including those appointed for a specific term shall be subject to retirement by rotation at least once every three years. A retiring Director shall be eligible for re-election to fill a casual vacancy until the next general meeting or the next annual general meeting.

- All Independent Non-Executive Directors of the Company were not appointed for a specific term but they are subject to retirement by rotation and re-election at annual general meetings of the Company in line with the Company's Articles of Association.

- In order to enable shareholders of the Company to make an informed decision on the re-election of Directors, the biographical details demonstrating qualification, experience, expertise, skills and other directorships held in listed companies of the retiring Directors were set out in the AGM circular which was dispatched to the shareholders of the Company accompanied with Annual Report 2010.

- For those directors who resigned from office, the announcement relating to the director's resignation had stated the reasons given by the director for his resignation and a statement to confirm no disagreement with the Company that need to be brought to the attention of shareholders of the Company and The Stock Exchange of Hong Kong Limited (the "Stock Exchange")

A.5 Responsibilities of the Directors

- The Company ensures that every newly appointed Director should receive a comprehensive information package containing business activities and operation of the Group, the Directors' responsibilities and duties and other statutory requirement upon his appointment. The Company Secretary is responsible for keeping all Directors updated on the Listing Rules and other statutory requirement.

- Independent Non-Executive Directors were well aware of their functions and had been actively providing their independent advices at the Board meetings, take the lead where potential conflicts of interest arise and scrutinize the Company's performance.

- Independent Non-Executive Directors are also members of the Audit, Remuneration and Investment Committee.

- There were satisfactory attendances and active participations at the Board meetings, the Board Committee meetings and the general meetings by the Directors.

- The Company has adopted the full set of Model Code set out in Appendix 10 of the Listing Rules as the code of the conduct for securities transactions by directors (the "Model Code"). The prohibitions on securities dealing and disclosure requirements in the Model Code apply to specified individuals including the Group's senior management and also persons who are privy to price sensitive information of the Group. Having made specific enquiry of all directors, the Board confirms that the director of the Company have complied with the Model Code regarding directors' securities transactions during the year and up to the date of publication of the Annual Report.

A.6 Supply of and access to information

- The Company's senior management regularly supplies the Board and its Committees with adequate information in a timely manner to enable them to make informed decisions.

- For Board meetings and the Board Committee meetings, the agenda accompanying with Board papers were sent to all Directors at least 3 days before the intended date of the Board meetings or Board Committee meetings. Queries raised by the Directors would be responded promptly by the relevant management.

B Remuneration of directors and Senior Management

The Company has established a remuneration committee since 29 June 2005 with written terms of reference in consistence with the Corporate Governance Code. During the year under review, the members of remuneration committee comprised Mr. Chang Kin Man (Independent Non-executive Director) who acts as Committee Chairman, Mr. Wu Tak Lung (Independent Non-executive Director) and Mr. Li Wen Jun (Executive Director).

(a) The primary duties of the remuneration committee include the following:

i. To make recommendation to the board on the Company's policy and structure for all remuneration of directors and senior management;

ii. To determine the remuneration packages of executive Directors and senior management, according to the major scope, responsibilities and duties, importance of position of the directors and the senior management as well as the remuneration level of the related position in the market, including benefit in kind, pension rights and compensation payments which include compensation payable for loss or termination of their office or appointment.

iii. To review and approve performance-based remuneration by reference to corporate goals and objectives resolved by the board from time or time.

iv. To review and approve the compensation payable to executive directors and senior management in connection with any loss or termination of their office or appointment to ensure that such compensation is determined in accordance with relevant contractual terms and that such compensation is otherwise fair and not excessive for the Company.

v. To ensuring that no director or any of his associates shall be involved in any decisions as to their own remuneration.

vi. To advising shareholders on how to vote with respect to any service contracts of directors that requires shareholders' approval under the Listing Rules.

(b) The emolument policy of the employees of the Group was set up by the Remuneration Committee on the basis of their merit, qualification and competence.

(c) The emolument of the directors of the Company are determined by the Remuneration Committee, having regard to the Group's operating results, individual performance and comparable market statistics.

(d) The Remuneration Committee would consult the Chairman or CEO the proposals relating to the remuneration of other Executive Directors. The Remuneration Committee may have access to external professional advice if considered necessary.

(e) Further details on the emolument policy and the basis of determining the emolument payable to the Directors are set out in the page 84 of this annual report.

(f) The Group's stock option scheme as described on page 35 of this annual report is adopted as the Group's long-term incentive scheme.

(g) The Remuneration Committee held 2 meeting during the year to review and approve the remuneration of Executive Directors including Independent Non-Executive Directors and senior management. The attendance record of individual members is set out below:

Name	Number of Meetings Attended/Total
Independent Non-Executive Directors:	
Mr. Chang Kin Man *(Chairman)*	2/2
Mr. Wu Tak Lung	2/2
Executive Director:	
Mr. Li Wen Jun	2/2

C Accountability and Audit

C.1 Financial Reporting

- Management was required to provide detailed reports and explanation to enable the Board to make an informed assessment of the financial and other information put before for approval.

- The directors acknowledged their responsibility for preparing the financial statements of the Company for the year ended 31 December 2010. The Board must ensure that the financial statements of the Group are prepared so as to give a true and fair view of the financial status of the Group.

- The Board is responsible for presenting a balanced, clear and understandable assessment of annual and interim reports, price-sensitive announcements and other disclosures required under the Listing Rules and other regulatory requirement.

- A statement by the independent auditor of the Company about their reporting responsibilities is included in the Report of the Auditors on page 38 of this annual report.

C.2 Internal Control

- The Board acknowledges its responsibility in maintaining sound and effective internal control system for the Group to safeguard investments of the shareholders and assets of the Company at all times. The system of internal controls aims to help achieving the Group's business objectives, safeguarding assets and maintaining proper accounting records for provision of reliable financial information. However, the design of the system is to provide reasonable, but not absolute, assurance against material misstatement in the financial statements or loss of assets and to manage rather than eliminate risks of failure when business objectives are being sought.

- In addition, a policy and procedure regarding the Publication Price-Sensitive Information is established, setting out the guiding principles, procedures and internal controls for the handling and dissemination of price-sensitive information in a timely manner.

- The scope of internal audit covers key areas such as the Company operation, investments, corporate governance and financial management. The work results and suggestions of the Internal Audit Department are reported by the Chief Internal Auditor directly to the Audit Committee for consideration, then makes recommendations to the management of the Company and reports to the Board in respect thereof.

- During the year, the Board has through the Chief Internal Auditor and SHINEWING Risk Services Limited, an independent accountancy firm, conducted an annual review on the Group's internal control systems, including but not limited to financial, operational and compliance controls and risk management functions. The Board is of the view that the internal control system of the Group are effective and adequate, no material deficiencies have been identified.

- The annual review of the adequacy of resources, qualifications or experience of staff of the Company's accounting and financial reporting function and their training programs and budget will be conducted in 2011. The Chief Internal Auditor will carry out this evaluation on annual basis and report the review result to the Audit Committee. The financial department of the Company is managed by the qualified accountant and accountants of the subsidiaries have good experience in financial accounting and management accounting. The Board believed that the Company has sufficient qualifications and experience staff in accounting and financial reporting function.

C.3 Audit Committee

The Audit Committee of the Company was established since 29 June 2005 with specific written terms of reference which are of no less exacting terms than those stipulated in Code provision The Audit Committee comprises 3 Independent Non-executive Directors, namely Mr. Chang Kin Man (Committee Chairman), Mr. Wu Tak Lung and Mr. Gu Wen Xuan. Mr. Chang and Mr. Wu both are certified public accountants for many years. The major duties of the Audit Committee include:

(a) to make recommendations to the Board on the appointment, reappointment and removal of the external auditor and to approve the remuneration and the terms of engagement of the external auditor;

(b) to oversight the Company's financial controls, internal control and risk management systems;

(c) to co-ordinate between the internal and external auditors, to monitor the performance of both internal and external auditors and to ensure that the internal audit function is adequately resourced and has appropriate standing within the Company, and to review and monitor the effectiveness of the internal audit function;

(d) to review the interim and final results of the Group prior to recommending them to the Board for approval;

(e) to ensure compliance with applicable statutory accounting and reporting requirements, legal and regulatory requirements, an internal rules and procedures approved by the Board;

(f) to review the adequacy of resources, qualifications or experience of staff of the Company's accounting and financial reporting function and their training programs and budget.

For the year under review, the Audit Committee held 2 meetings included the review of the final results for the year ended 31 December 2010 and interim accounts for 30 June 2010. The Group's annual report for the year ended 31 December 2010 has been reviewed by the Audit Committee. The individual attendance records of each member are as follows:

Name	Number of Meetings Attended/Total
Independent Non-Executive Directors:	
Mr. Chang Kin Man *(Chairman)*	2/2
Mr. Wu Tak Lung	2/2
Mr. Gu Wen Xuan	2/2

D. Delegation by the Board

D.1 Management functions

- When the Board delegates aspects of its management and administration functions to the management, it has given clear directions as to the powers of management, in particular, with respect to the circumstance where management shall report back and obtain prior approval from the Board before making decisions or entering into any commitments on behalf of the Company.

- The segregation of duties and responsibilities between the Board and the management has been defined as follows:

  The duties of the Board include:

  – Formulating the Company's operational strategies and management policies and establishing corporate governance and internal control system;

  – Setting the objectives and targets of the Company; and

  – Monitoring performance of management and providing guidance to the management.

  The duties of the management include:

  – Reviewing the business and operation performance;

  – Ensuring adequate fundings; and

  – Monitoring performance of the management of the Group.

D.2 Board Committees

The Company has set up three committees including an Audit Committee, a Remuneration Committee and an Investment Committee of the Board with respective terms of reference which clearly defined its authority and duties. The Chairman of Board Committees reported to the Board their work, findings and recommendations at the Board meetings.

D.3 Investment Committee

The Investment Committee of the Company was established since 18 December 2008, consisted of 5 directors, namely Mr. Li Yu Gui (Committee Chairman), Mr. Liu Bai Yue, Mr. Yang Bin, Mr. Li Wen Jun and Mr. Chang Kin Man. The role of Investment Committee is to oversee the Company's strategic and investment policy on a regular basis and to advise the Board on the investment of the Company including asset allocation and new investment proposal. The Investment Committee held 3 meeting during the year. The attendance record of individual members is set out below:

Name	Number of Meetings Attended/Total
Executive Directors	
Mr. Li Yu Gui *(Chairman)*	3/3
Mr. Yang Bin	3/3
Mr. Li Wen Jun	3/3
Mr. Liu Bai Yue (Resigned on 1 January 2011)	3/3
Independent Non-Executive Directors:	
Mr. Chang Kin Man	3/3

E Communication with Shareholders

E.1 Effective communication

- The annual general meetings of the Company provide a forum for communication between the shareholders and the Board. The Chairman of the Board as well as chairmen of the Audit Committee and Remuneration Committee, or in their absence, other members of the respective committees, are available to answer questions at the shareholders' meetings. The annual report together with annual general meeting circular is distributed to all the shareholders at least 20 clear business days before the AGM and at least 10 clear business days in case of all other general meetings.

- Separate resolutions are proposed at shareholders' meetings on each substantial issue, including the election of individual directors.

- The Company continues to enhance communications and relationships with its investors. Designated Directors or senior management maintains regular dialogue with investors and analysis to keep them abreast of the Company's developments. Enquiries from investors are dealt with in an informative and timely manner.

E.2 Voting by poll

The rights of shareholders and the procedures for demanding a poll on resolutions at shareholders' meetings are contained in the Company's articles of association. Details of such rights to demand a poll and the poll procedures are included in all circulars to shareholders and will be explained during the proceedings of meetings.

Poll results were published on the website of the Stock Exchange at www.hkex.com.hk as well as the Company's website at www.chinawaterind.com.

AUDITORS' REMUNERATION

For the financial year, SHINEWING (HK) CPA Limited and its an associate, the auditors of the Company, the fee paid or payable to the auditor for audit service provided to the Group is approximately HK$1,000,000 and for non-audit service provided is approximately HK$613,550 mainly for the purpose of reviewing internal control system and performing due diligence for the acquisition transaction. The auditors' remuneration has been duly approved by the audit committee and there was no disagreement between the Board and the audit committee on the selection and appointment of auditor.

COMPLIANCE WITH THE CODE ON CORPORATE GOVERNANCE PRACTICES

The Company has complied with the Code throughout the financial year ended 31 December 2010 except for deviations from the code provision A4.1 and C2.2 as below:

- Pursuant to A4.1 of the CG Code, Non-Executive Directors should be appointed for a specific term, subject to re-election while all directors should be subject to retirement by rotation at least once every three years. All Independent Non-Executive Directors of the Company were not appointed for a specific term but they are subject to retirement by rotation and re-election at annual general meetings of the Company in line with the Company's Articles of Association.

- Pursuant to C2.2 of the CG code, the Board's annual review should consider the adequacy of resources, qualifications and experience of staff of the Company's accounting and financial reporting function, and their training programmes and budget. The Company has not undertaken this review but the financial department of the Company is managed by the qualified accountant and accountants of the subsidiaries have at least 5 years working experience in financial and accounting field. The Board believes that the Company has sufficient qualifications and experience staff in accounting and financial reporting function. The Company understands the importance to comply with the code provision C2.2 so the Chief Internal Auditor will carry out this evaluation on annual basis and report the review result to the Audit Committee.

The Company considers that sufficient measures have been taken to ensure that the Company's corporate governance practices are no less exacting than those in the CG Code.

REPORT OF THE DIRECTORS

The Broad of Directors of the Company, present their report together with the audited consolidated financial statements of the company and its subsidiaries (collectively, the "Group") for the year ended 31 December 2010.

PRINCIPAL ACTIVITIES AND ANALYSIS OF OPERATIONS

The principal activity of the Company is investment holding. The principal activities of the Group in the continuing operations, including: (i) provision of water supply (ii) sewage treatment and (iii) construction of water supply and sewage treatment infrastructure.

During the year under review, the discontinued operations included: (i) investments in financial and investment products and (ii) manufacturing and trading of ceramic sewage materials. Both of the above-mentioned operations were operated by iMerchants.

With effect from October 2010, the equity interest in iMerchants owned by the Group was diluted to 36.57%. The investments in iMerchants were then reclassified from an investment in a subsidiary to investment in an associate. Upon the deemed partial disposal of iMerchants from a subsidiary to an associate, the operations of iMerchants were classified as discontinued operations of the Group.

SEGMENT INFORMATION

The analysis of the Group's principal activities of the group during the financial year are set out in note 7 to the consolidated financial statements.

RESULTS

The results of the Group for the year ended 31 December 2010 are set out in the consolidated statement of comprehensive income on pages 41 to 42.

DIVIDENDS

The Directors do not recommend the payment of a final dividend for the year ended 31 December 2010. (2009: Nil)

MAJOR CUSTOMERS AND SUPPLIERS

For the year ended 31 December 2010, the aggregate amount of turnover attribute to the Group's five largest customers was less than 30% of the total value of the Group's turnover. The Group's purchase to the five largest suppliers accounted for less than 30% of the total value of the Group's purchase.

At no time during the year have the Directors, their associates or any shareholder of the Company (which to the knowledge of the Directors owns more than 5% of the Company's share capital) had any interest in these major customers or suppliers.

PROPERTY, PLANT AND EQUIPMENT

Details of movements in the property, plant and equipment of the group during the year are set out in note 16 to the consolidated financial statements.

REPORT OF THE DIRECTORS

SHARE CAPITAL, SHARE OPTIONS AND CONVERTIBLE BONDS

Details of the movements in the Company's share capital, share options and convertible bonds during the year are set out in notes 34, 48, and 33 to the consolidated financial statements, respectively.

RESERVES AND DISTRIBUTIVE RESERVES

Details of movements in the reserves of the group during the year are set out in the consolidated statement of changes in equity on pages 45 to 46.

BANK BORROWINGS AND BANKING FACILITIES

Particulars of bank loans of the Group as at 31 December 2010 are set out in note 29 to the consolidated financial statements.

FIVE YEARS FINANCIAL SUMMARY

A summary of the results and of the assets and liabilities of the group for the last five financial years is set out on page 142.

DIRECTORS

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

Executives Directors:

Mr. Li Yu Gui *(Chairman)*	
Mr. Yang Bin *(Chief Executive Officer)*	
Ms. Chu Yin Yin, Georgiana	
Mr. Li Wen Jun	
Mr. Tang Hui Ping, Paul	(Appointed on 1 January 2011)
Mr. Liu Bai Yue *(Chief Operating Officer)*	(Resigned on 1 January 2011)
Mr. Zhong Wen Sheng *(Managing Director)*	(Resigned on 4 January 2010)

Independent Non-Executive Directors:

Mr. Chang Kin Man
Mr. Wu Tak Lung
Mr. Gu Wen Xuan

In accordance with article 108(A) of the Company's Articles of Association, one-third of the Directors for the time being or, if their number is not a multiple of three or a multiple of three, then the number nearest to but not exceeding one-third shall retire from the office by rotation at least once every three years, Mr. Yang Bin, Mr. Chang Kin Man and Mr. Wu Tak Lung will retire from office by rotation and will offer themselves for re-election at the AGM.

In accordance with article 112 of the Company's Articles of Association, at any time to appoint directors either to fill a causal vacancy or as an addition to the Board, they shall retire from office at the forthcoming AGM and shall be eligible for re-election. Mr. Tang Hui Ping, Paul shall hold office only until the AGM and will offer himself for re-election at the AGM.

REPORT OF THE DIRECTORS

DIRECTORS' BIOGRAPHICAL DETAILS

Biographical details of the directors of the Company are set out on pages 15 to 17 of the annual report.

EMOLUMENT POLICY

A Remuneration Committee is set up for reviewing the Group's emolument policy and structure for all remuneration of the directors and senior management of the Group, having regard to the group's operating results, individual performance and comparable market practices.

The Company has adopted a Share Option Scheme as incentive to Directors and eligible employees, details of the scheme are set out as "Share Option Scheme" below.

DIRECTORS' SERVICE CONTRACTS

As at 31 December 2010, none of the Directors has entered into any service contracts with the Company or any of its subsidiaries within one year without payment of compensation, other than normal statutory obligations and does not have specific terms of appointment but is subject for retirement and for re-elections at the forthcoming AGM as required by the articles of association of the Company.

DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS IN SECURITIES

As at 31 December 2010, the interests and short positions of each Director and Chief Executive of the Company, or their associates in the shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of the Securities and Futures Ordinance ("**SFO**") which (a) had been notified of the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions in which Directors have taken or deemed to have under such provisions of the SFO) or which (b) were required pursuant to section 352 of the SFO, to be entered in the register referred to therein; or which (c) were required, pursuant to the Model Code for Securities Transactions by Directors of Listed Companies (the "Model Code") contained in Appendix 10 to the Listing Rules to be notified to Company and the Stock Exchange were as follows:

(i) Interest in the Shares

Name of director	Nature of interest	Number of issued ordinary shares held	Total interest	Percentage of the issued share capital of the Company
Chu Yin Yin, Georgiana	Beneficial owner	5,432,000	5,432,000 (L)	0.17%
Yang Bin	Interest of controlled corporation	450,479,000	450,479,000 (L) *(Note)*	13.87%

For the purpose of this section, the shareholding percentage in the Company is calculated on the basis of 3,247,651,000 Shares in issue as at 31 December 2010.

The letter "L" denotes a long position in shares of the Company

Note: These China Water Shares are held by Boost Skill Investments Limited (as to 265,479,000 China Water Shares) and its wholly owned subsidiaries, Favor Jumbo Investments Limited (as to 130,000,000 China Water Shares) and Sure Ability Limited (as to 55,000,000 China Water Shares). Mr. Yang Bin, an executive Director is interested in 60% of the equity interest in Boost Skill Investments Limited.

(ii) Interest in underlying Shares

Name of director	Exercise Price (HK$)	Exercise Period	Number of underlying Shares (under share options of the Company)	Approximate shareholding % (Note)
Chu Yin Yin, Georgiana	0.335	11 January 2007 to 10 January 2017	3,000,000	0.09

Note: For the purpose of this section, the shareholding percentage in the Company is calculated on the basis of 3,247,651,000 Shares in issue as at 31 December 2010.

Save as disclosed above, as at 31 December 2010, none of the Directors or Chief Executive of the Company had any interest or short position in any shares, underlying shares or debenture of the Company or any of its associated corporations (within meaning of the SFO) which (a) were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which Directors have taken or deemed to have under such provisions of SFO) or (b) were required pursuant to section 352 of the SFO, to be entered in the register referred to therein; or which (c) were required, pursuant to the Model Code to be notified to Company and the Stock Exchange.

SUBSTANTIAL SHAREHOLDERS

As at 31 December 2010, the following persons and entities, other than a Director or Chief Executive of the Company disclosed under the section "Directors' and Chief Executive's interests in Securities" above) had interest or short positions in the shares and underlying shares of the Company as recorded in the register required to be kept under Section 336 of SFO:

Name of shareholder	Capacity	Number of issued Shares held	Approximate Percentage of the issued share capital of the Company
Li Jian Ping	Interest of controlled corporation	450,479,000 *(Note 1)*	13.87%
Boost Skill Investments Limited	Interest of controlled corporation	185,000,000 *(Note 2)*	5.70%
	Beneficial owner	265,479,000	8.17%
Abax Arhat Fund	Interest of controlled corporation	228,873,239 *(Note 3)*	7.05%
Abax Claremont Ltd.	Interest of controlled corporation	228,873,239 *(Note 3)*	7.05%
Abax Global Capital	Interest of controlled corporation	228,873,239 *(Note 3)*	7.05%
Abax Global Opportunities Fund	Interest of controlled corporation	228,873,239 *(Note 3)*	7.05%
Abax Lotus Ltd.	Beneficial owner	228,873,239 *(Note 3)*	7.05%
Abax Upland Fund, LLC	Interest of controlled corporation	228,873,239 *(Note 3)*	7.05%
Citigroup Inc.	Person having a security interest in shares	241,333,333	7.43%

Note 1: These China Water Shares are held by Boost Skill Investments Limited (as to 265,479,000 China Water Shares), Favor Jumbo Investments Limited (as to 130,000,000 China Water Shares) and Sure Ability Limited (as to 55,000,000 China Water Shares). Mr. Yang Bin, an executive Director, and Mr. Li Jian Ping is interested in 60% and 40% respectively of the equity interest in Boost Skill Investments Limited.

Note 2: These China Water Shares are held by Favor Jumbo Investments Limited (as to 130,000,000 China Water Shares) and Sure Ability Limited (as to 55,000,000 China Water Shares). Favor Jumbo Investments Limited and Sure Ability Limited are wholly-owned subsidiaries of Boost Skill Investments Limited.

REPORT OF THE DIRECTORS

Note 3: These 228,873,239 underlying Shares are those Shares which would be issued upon exercise of the convertible rights attaching to the convertible bonds issued by the Company as disclosed in the announcement of the Company dated 31 July 2007. As the issued share capital of Abax Lotus Ltd. is held indirectly or directly by Abax Arhat Fund, Abax Claremont Ltd., Abax Global Capital, Abax Global Opportunities Fund and Abax Upland Fund, LLC, they are deemed to be interested in the underlying Shares under SFO.

Note 4: The shareholding percentage in China Water is calculated on the basis of 3,247,651,000 China Water Shares in issue as at 31 December 2010.

Save as disclosed above, as at 31 December 2010, the Company has not been notified of any person or entity who had interests and short position in the shares and underlying shares of the Company as recorded in the register required to be kept under Section 336 of the SFO.

DIRECTORS' RIGHTS TO ACQUIRES OR DEBENTURES

Save as disclosed under the heading "Share Option Scheme" below, at no time during the year were the rights to acquire benefits by means of the acquisition of shares in or debentures of the Company granted to any Director or Chief Executive of the Company or their respective spouse or children under 18 years of age, or were any such rights exercised by them; or was the Company and its 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 contract of significance to which the Company or its subsidiaries was a party, in which a Director of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

MANAGEMENT CONTRACTS

No contracts concerning the management and administration of the whole or any substantial part of the business of the Company were entered into or in the year under review.

CONNECTED TRANSACTIONS

During the year, no contracts concerning the management and administration of the whole or any substantial part of the business of the Company were entered into or in the year under review.

RELATED PARTY TRANSACTIONS

Details of the related party transactions of the Group are set out in note 52 to the financial statements.

DIRECTORS' INTERESTS IN COMPLETING BUSINESS

During the year and up to the date of this report, none of the Directors are considered to have an interest in a business which competes or is likely to compete, either directly or indirectly, with the business of the Group, pursuant to the Listing Rules, other than those business of which directors were appointed as directors to represent the interest of the Company and/or the Group.

SHARE OPTION SCHEME

The Company had adopted share option scheme on 17 January 2002 (the "Scheme") and the Scheme will expire on 16 January 2012, for which the details are set out in note 48 to the consolidated financial statements.

Details of the movements in the share options during the year ended 31 December 2010 under the Scheme are as follows:

Name or category of participant	Date of grant	Outstanding as at 1 January 2010	Granted during the year	Exercised during the year	Lapsed during the year	Outstanding as at 31 December 2010	Exercisable period	Exercise Price per share of the Company *HK$*
Directors								
Chu Yin Yin, Georgiana	11 January 2007	3,000,000	–	–	–	3,000,000	11 January 2007 to 10 January 2017	0.335
Liu Bai Yue	17 January 2007	5,000,000	–	–	–	5,000,000	17 January 2007 to 16 January 2017	0.420
		8,000,000				8,000,000		
Other eligible participant *(Note)*	11 January 2007	10,000,000	–	–	(10,000,000)	–	11 January 2007 to 10 January 2017	0.335
Total as at 31 December 2010		**18,000,000**	**–**	**–**	**–**	**8,000,000**		

Note: Mr. Sze Chun Ning, Vincent resigned all positions in the Group in May 2010, the share options granted to him were lapsed.

PRE-EMPTIVE RIGHTS

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

REPORT OF THE DIRECTORS

PURCHASES, REDEMPTIONS OR SALES OF COMPANY'S LISTED SECURITIES

There were no purchases, redemptions or sales of the Company's listed securities by the Company or any of its subsidiaries during the year.

RETIREMENT SCHEMES

The Group's subsidiary in the PRC participates in a central pension scheme ("CPS") operated by the PRC government. The subsidiaries are required to contribute a certain percentage of the relevant the PRC employees' salaries to the CPS. The Group's subsidiary in Hong Kong has also participated in a mandatory provident fund scheme for its staff based in Hong Kong pursuant to the Mandatory Provident Fund Schemes Ordinance. Save as disclosed, the Group was not required to operate any other of retirement benefits of its employees during the year.

POST BALANCE SHEET EVENTS

There was no post balance sheet events occurring after the reporting period.

SUFFICIENT OF PUBLIC FLOAT

As far as the information publicly available to the company is concerned and to the best knowledge of the Directors of the Company, at least 25% of the Company's issued share capital were held by members of the public as at the date of this report.

AUDIT COMMITTEE

In accordance with the requirements of the Listing Rules, the Group established an Audit Committee comprising three Independent Non-Executive Directors of the Company. The Audit Committee of the Company has reviewed the unaudited consolidated financial statements for the year ended 31 December 2010. Information on the work of Audit Committee and its composition are set out in the Report of the corporate Governance on page 25 of this Annual Report.

CORPORATE GOVERNANCE

The Company's corporate governance principles and practices are set out in the Corporate Governance Report on pages 18 to 28 of this Annual Report.

MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

The Company has adopted the full set of Model Code set out in Appendix 10 of the Listing Rules as the code of the conduct for securities transactions by directors (the "Model Code"). The prohibitions on securities dealing and disclosure requirements in the Model Code apply to specified individuals including the Group's senior management and also persons who are privy to price sensitive information of the Group. Having made specific enquiry of all directors, the Board confirmed that directors of the Company had complied with the Model Code regarding directors' securities transactions during the year and up to the date of publication of the Annual Report.

CONFIRMATION OF INDEPENDENCE

The Company has received from each of the Independent Non-Executive Director an annual confirmation of independence pursuant to Rule 3.13 of the Listing Rules and considers all the Independent Non-Executive Directors to be independent.

AUDITORS

SHINEWING (HK) CPA Limited ("SHINEWING") retire and, being eligible, offer themselves for reappointment. A resolution for their reappointment of SHINEWING as auditors of the Company will be proposed at the forthcoming annual general meeting.

By order of the Board
Li Yu Gui
Chairman

Hong Kong, 30 March 2011

INDEPENDENT AUDITOR'S REPORT

信永中和 ShineWing

SHINEWING (HK) CPA Limited
43/F., The Lee Gardens
33 Hysan Avenue
Causeway Bay, Hong Kong

TO THE MEMBERS OF
CHINA WATER INDUSTRY GROUP LIMITED
(Incorporated in the Cayman Islands with limited liability)

We were engaged to audit the consolidated financial statements of China Water Industry Group Limited (the "Company") and its subsidiaries (collectively referred to as the "Group") set out on pages 41 to 141, which comprise the consolidated statement of financial position as at 31 December 2010, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

DIRECTORS' RESPONSIBILITY FOR THE CONSOLIDATED FINANCIAL STATEMENTS

The directors of the Company are responsible for the preparation of consolidated financial statements that give a true and fair view 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, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these consolidated financial statements based on our audit and to report our opinion solely to you, as a body, in accordance with our agreed terms of engagement, 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 about whether the consolidated financial statements are free from material misstatement.

However, because of the matters described in the basis for disclaimer of opinion section, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

BASIS FOR DISCLAIMER OF OPINION

Scope limitation – Loans receivables

As explained in note 25 to the consolidated financial statements, included in loans receivables was an amount of approximately HK$68,206,000 amounting to HK$50,901,000 was paid by the Group in the year of 2009 as deposit for the acquisition of certain equity interests in three companies which were established in the People's Republic of China (the "Acquisition"). The Acquisition was terminated by Swift Surplus Holdings Limited, a wholly-owned subsidiary of the Group, during the year ended 31 December 2010 and the deposit paid was then assigned as loan to the holding company of the vendors. Further details are set out in note 23 to the consolidated financial statements. We have not been provided with sufficient evidence to satisfy ourselves as to whether the loan balance would be recovered in full. There are no other satisfactory audit procedures that we could adopt to ascertain the impairment loss amount, if any, and the carrying value of the aforesaid loan receivables as at 31 December 2010 being fairly stated in the consolidated statement of financial position.

Any adjustment to the above as at 31 December 2010 was found to be necessary would have a consequential impact on the Group's net assets as at 31 December 2010 and on the consolidated loss for the year then ended and the related disclosure thereof in the consolidated financial statements.

Fundamental uncertainty relating to the going concern basis

As explained in note 2 to the consolidated financial statements, which indicates that the Group incurred a consolidated loss attributable to owners of the Company of approximately HK$92,685,000 for the year ended 31 December 2010 and had a consolidated net current liabilities of approximately HK$303,574,000 as at 31 December 2010, the consolidated financial statements have been prepared on a going concern basis, the validity of which is dependent upon future funding available.

The consolidated financial statements do not include any adjustments that would result from the unavailability of future funding. We consider that appropriate disclosures have been made. However, the uncertainty surrounding the outcome of future funding available raises significant doubt about the Group's ability to continue as a going concern.

The consolidated financial statements do not include any adjustments that may be necessary should the future funding be unavailable. We consider that appropriate disclosures have been made in the consolidated financial statements concerning this situation, but we consider that this fundamental uncertainty relating to whether the going concern basis is appropriate is so extreme that we have disclaimed our opinion.

INDEPENDENT AUDITOR'S REPORT

Disclaimer of opinion: disclaimer on view given by the consolidated financial statements

Because of the significance of the matters described in the basis for disclaimer of opinion paragraph, we do not express an opinion on the consolidated financial statements as to whether they give a true and fair view of the state of affairs of the Group as at 31 December 2010 and of the Group's loss and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards. In all other respects, in our opinion, the consolidated financial statements have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

SHINEWING (HK) CPA Limited
Certified Public Accountants
Ip Yu Chak
Practising Certificate Number: P04798

Hong Kong
30 March 2011

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2010

	Notes	2010 HK$'000	2009 HK$'000 (Restated)
Continuing operation			
Revenue	6	**238,771**	202,108
Cost of sales		**(141,693)**	(129,243)
Gross profit		**97,078**	72,865
Other operating income	8	**14,650**	3,320
Selling and distribution expenses		**(7,667)**	(6,632)
Administrative expenses		**(62,400)**	(63,578)
Finance costs	9	**(9,534)**	(11,993)
Change in fair value of convertible bonds	33	**(28,326)**	(204,404)
Change in fair value of derivative financial instruments	33	**(4,135)**	–
Extinguishment loss of convertible bonds	33	**(1,521)**	–
Loss on redemption of convertible bonds	33	**(10,542)**	–
Loss on deemed partial disposal of an associate		**(79,449)**	–
Gain on disposal of subsidiaries	42(a)	**–**	7,504
Loss on disposal of a business	42(b)	**–**	(4,760)
Net gain (loss) on disposal of available-for-sale investments		**4,928**	(22,721)
Net gain on disposal of listed trading securities		**–**	1,729
Impairment loss recognised on trade and other receivables		**(880)**	(7,671)
Impairment loss recognised on available-for-sale investments		**(30,502)**	–
Impairment loss recognised on goodwill	20	**(40,258)**	(66,069)
Share of results of an associate		**(8,109)**	2,183
Loss before tax		**(166,667)**	(300,227)
Income tax expense	10	**(10,813)**	(8,448)
Loss for the year from continuing operation	11	**(177,480)**	(308,675)
Discontinued operations	12		
Profit (loss) for the year from discontinued operations		**27,684**	(33,810)
Loss for the year		**(149,796)**	(342,485)
Other comprehensive (expenses) income for the year			
Exchange difference arising on translation		**14,030**	3,057
Exchange reserve released upon disposal/deemed disposal of a subsidiary		**42**	(5,028)
Change in fair value of available-for-sale investments		**(30,873)**	10,265
Release of investment revaluation reserve upon disposal of available-for-sale investments		**(694)**	70,520
Share of other comprehensive income of associates		**2,163**	681
Other comprehensive (expenses) income for the year		**(15,332)**	79,495
Total comprehensive expenses for the year		**(165,128)**	(262,990)

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2010

	Notes	2010 *HK$'000*	2009 *HK$'000* (Restated)
(Loss) profit for the year attributable to:			
Owners of the Company			
From continuing operation		**(205,043)**	(328,359)
From discontinued operations		**112,358**	(25,880)
Loss for the year attributable to owners of the Company		**(92,685)**	(354,239)
Non-controlling interests			
From continuing operation		**27,563**	19,684
From discontinued operations		**(84,674)**	(7,930)
(Loss) profit for the year attributable to non-controlling interests		**(57,111)**	11,754
		(149,796)	(342,485)
Total comprehensive (expense) income attributable to:			
Owners of the Company		**(113,420)**	(284,909)
Non-controlling interests		**(51,708)**	21,919
		(165,128)	(262,990)
Loss per share (HK cents)	*15*		
From continuing and discontinued operations			
Basic and diluted		**(3.27)**	(15.68)
From continuing operation			
Basic and diluted		**(7.24)**	(14.53)

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

At 31 December 2010

	Notes	2010 HK$'000	2009 HK$'000
Non-current assets			
Property, plant and equipment	16	**97,598**	103,164
Prepaid lease payments	17	**40,621**	42,854
Concession intangible assets	18	**483,829**	416,718
Intangible asset	19	**–**	915,301
Goodwill	20	**142,373**	250,995
Available-for-sale investments	21	**29,898**	65,040
Interest in associates	22	**281,407**	57,853
Deposit paid for acquisition of subsidiaries	23	**–**	50,901
		1,075,726	1,902,826
Current assets			
Inventories	24	**26,748**	13,304
Trade and other receivables	25	**148,900**	74,600
Prepaid lease payments	17	**1,150**	1,181
Derivative financial instruments	33	**10,239**	–
Amounts due from customers for contract works	28	**18,864**	10,884
Cash held at financial institutions	26	**37,724**	212,474
Bank balances and cash	26	**100,291**	65,383
		343,916	377,826
Current liabilities			
Trade and other payables	27	**163,572**	138,959
Amounts due to customers for contract works	28	**592**	657
Bank borrowings	29	**34,240**	33,017
Other loans	30	**39,885**	33,813
Amounts due to non-controlling shareholders of a subsidiary	31	**6,216**	8,258
Loan from an associate	32	**2,419**	–
Convertible bonds	33	**397,187**	466,739
Tax payables		**3,379**	3,000
		647,490	684,443
Net current liabilities		**(303,574)**	(306,617)
Total assets less current liabilities		**772,152**	1,596,209

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

At 31 December 2010

	Notes	2010 HK$'000	2009 HK$'000
Capital and reserves			
Share capital	34	**324,765**	270,638
Share premium and reserves		**124,128**	190,659
Equity attributable to owners of the Company		**448,893**	461,297
Non-controlling interests		**179,164**	882,237
Total equity		**628,057**	1,343,534
Non-current liabilities			
Bank borrowings	29	**21,253**	23,909
Other loans	30	**47,487**	44,902
Convertible bonds	33	**3,000**	–
Convertible bonds of a subsidiary	36	**–**	118,427
Government grants	37	**64,074**	60,040
Deferred tax liabilities	38	**8,281**	5,397
		144,095	252,675
		772,152	1,596,209

The consolidated financial statements on pages 41 to 141 were approved and authorised for issue by the board of directors on 30 March 2011 and are signed on its behalf by:

Li Yu Gui
Chairman

Yang Bin
Chief Executive Officer

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2010

	Attributable to owners of the Company									Non-controlling interests				
	Share capital HK$'000	Share premium HK$'000	Share options reserve HK$'000	Translation reserve HK$'000	Reserve funds HK$'000 *(note 1)*	Investment revaluation reserves HK$'000	Special capital reserve HK$'000 *(note 2)*	Accumulated losses HK$'000	Sub-total HK$'000	Non-redeemable convertible preference shares of a subsidiary HK$'000 *(note 35)*	Equity component of convertible bonds of a subsidiary HK$'000	Non-controlling interests HK$'000	Sub-total HK$'000	Total HK$'000
At 1 January 2009	189,090	418,093	727	22,022	2,417	(70,676)	–	(45,594)	516,079	–	–	194,862	194,862	710,941
Loss for the year	–	–	–	–	–	–	–	(354,239)	(354,239)	–	–	11,754	11,754	(342,485)
Other comprehensive income (expense) for the year	–	–	–	(2,411)	–	71,741	–	–	69,330	–	–	10,165	10,165	79,495
Total comprehensive income for the year	–	–	–	(2,411)	–	71,741	–	(354,239)	(284,909)	–	–	21,919	21,919	(262,990)
Dividend paid to a non-controlling shareholder	–	–	–	–	–	–	–	–	–	–	–	(6,445)	(6,445)	(6,445)
Issuance of shares (net of transaction cost) *(note 34)*	81,548	164,348	–	–	–	–	–	–	245,896	–	–	–	–	245,896
Transfer	–	–	–	–	2,956	–	–	(2,956)	–	–	–	–	–	–
Issue of non-redeemable preference shares of a subsidiary *(note 35)*	–	–	–	–	–	–	(15,769)	–	(15,769)	587,696	–	(4,801)	582,895	567,126
Issue of convertible bonds of a subsidiary *(note 36)*	–	–	–	–	–	–	–	–	–	–	84,045	–	84,045	84,045
Disposal of subsidiaries/ business *(note 42)*	–	–	–	–	–	–	–	–	–	–	–	(26,583)	(26,583)	(26,583)
Deemed partial disposal of interest in a subsidiary *(note 44)*	–	–	–	–	–	–	–	–	–	–	–	31,544	31,544	31,544
At 31 December 2009	270,638	582,441	727	19,611	5,373	1,065	(15,769)	(402,789)	461,297	587,696	84,045	210,496	882,237	1,343,534

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2010

	Attributable to owners of the Company											Non-controlling interests				
	Share capital HK$'000	Share premium HK$'000	Share options reserve HK$'000	Convertible bond equity reserve HK$'000	Translation reserve HK$'000	Other reserve HK$'000 (note 3)	Reserve funds HK$'000 (note 1)	Investment revaluation reserves HK$'000	Special capital reserve HK$'000 (note 2)	Accumulated losses HK$'000	Sub-total HK$'000	Non-redeemable convertible preference shares of a subsidiary HK$'000	Equity component of convertible bonds of a subsidiary HK$'000	Non-controlling interests HK$'000	Sub-total HK$'000	Total HK$'000
At 1 January 2010	270,638	582,441	727	–	19,611	–	5,373	1,065	(15,769)	(402,789)	461,297	587,696	84,045	210,496	882,237	1,343,534
(Loss) profit for the year	–	–	–	–	–	–	–	–	–	(92,685)	(92,685)	–	–	(57,111)	(57,111)	(149,796)
Other comprehensive income (expense) for the year	–	–	–	–	10,832	–	–	(31,567)	–	–	(20,735)	–	–	5,403	5,403	(15,332)
Total comprehensive income (expenses) for the year	–	–	–	–	10,832	–	–	(31,567)	–	(92,685)	(113,420)	–	–	(51,708)	(51,708)	(165,128)
Impairment loss recognised on available-for-sales investment	–	–	–	–	–	–	–	30,502	–	–	30,502	–	–	–	–	30,502
Placing of new shares (net of transaction cost) *(note 34)*	54,127	2,765	–	–	–	–	–	–	–	–	56,892	–	–	–	–	56,892
Recognition of equity component of convertible bonds	–	–	–	15,914	–	–	–	–	–	–	15,914	–	–	–	–	15,914
Deemed partial disposal of a subsidiary	–	–	–	–	–	(2,292)	–	–	–	–	(2,292)	(17,600)	–	19,892	2,292	–
Cancellation of share options	–	–	(404)	–	–	–	–	–	–	404	–	–	–	–	–	–
Transfer	–	–	–	–	–	–	3,481	–	–	(3,481)	–	–	–	–	–	–
Deemed disposal of a subsidiary	–	–	–	–	–	2,292	–	–	15,769	(18,061)	–	(570,096)	(84,045)	8,976	(645,165)	(645,165)
Dividend paid to non-controlling shareholders	–	–	–	–	–	–	–	–	–	–	–	–	–	(8,492)	(8,492)	(8,492)
At 31 December 2010	324,765	585,206	323	15,914	30,443	–	8,854	–	–	(516,612)	448,893	–	–	179,164	179,164	628,057

Note:

1. As stipulated in the relevant laws and regulations, certain subsidiaries operating in the People's Republic of China (the "PRC") are required to maintain certain statutory reserves (the "Reserve Funds"). Appropriations to the Reserve Funds are made out of net profit as reported in the PRC statutory financial statements. The amounts of appropriations are determined by the respective board of directors. All statutory reserves are for specific purposes and are not distributable in the form of dividends.

2. On 23 October 2009, iMerchants Limited, a non-wholly owned subsidiary of the Group ("iMerchants"), whose shares are listed on the Growth Enterprise Market (the "GEM") of The Stock Exchange of Hong Kong Limited (the "Stock Exchange"), issued approximately 2,938,478,000 non-redeemable convertible preference shares (the "Convertible Preference Shares") with a par value of HK$0.2 each, as a partial consideration for the acquisition of an intangible asset through acquisition of a subsidiary (note 41). The fair value of the Convertible Preference Shares as at 23 October 2009 amounted to approximately HK$567,126,000, representing HK$0.193 per Convertible Preference Share. The discount of approximately HK$20,570,000, which represented the difference between the fair value of the non-redeemable Convertible Preference Shares as of 23 October 2009 and the par value, is charged to the special capital reserve in the equity of iMerchants. The Group's share of this reserve amounted to HK$15,769,000.

3. In June 2010, the holders of 440,000,000 Convertible Preference Shares exercised their rights to convert the Convertible Preference Shares into fully paid ordinary shares of iMerchants. After the conversion, the equity interest of iMerchants owned by the Group has reduced from 76.66% to 67.23%. The Group retained control of iMerchants subsequent to the conversion. The amount of approximately HK$2,292,000, being the difference between the carrying amount of the Convertible Preference Shares converted of approximately HK$17,600,000 and the respective increase in the interest attributable to shares held in subsidiaries of approximately HK$19,892,000, was recognised directly in equity and attributed to the owners of the Company.

CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31 December 2010

	2010 HK$'000	2009 HK$'000
OPERATING ACTIVITIES		
Loss before tax from continuing operation	**(166,667)**	(300,227)
Profit (loss) before tax from discontinued operations	**56,180**	(33,923)
Loss before taxation	**(110,487)**	(334,150)
Amortisation of concession intangible assets	**15,292**	14,864
Amortisation of an intangible asset	**46,279**	10,283
Amortisation of prepaid lease payments	**1,140**	1,362
Change in fair value of convertible bonds	**28,326**	204,404
Change in fair value of financial derivative instruments	**4,135**	–
Depreciation of property, plant and equipment	**6,928**	5,872
Finance costs	**20,122**	14,930
Loss on disposal of property, plant and equipment	**619**	54
Gain on deemed disposal of a subsidiary	**(258,229)**	–
Impairment loss recognised on trade and other receivables	**1,299**	8,444
Impairment loss recognised on goodwill	**40,258**	98,685
Impairment loss recognised on an intangible asset	**245,639**	–
Impairment loss recognised on concession intangible assets	**–**	2,222
Impairment loss recognised in respect of available-for-sale investments	**30,502**	–
Interest income	**(6,279)**	(229)
Loss on redemption of convertible bonds	**10,542**	–
Extinguishment loss of convertible bonds	**1,521**	–
Loss on deemed partial disposal of an associate	**79,449**	–
Net (gain) loss on disposal of available-for-sale investments	**(4,928)**	22,721
Reversal of impairment loss on other receivables	**(921)**	–
Share of results of an associate	**8,109**	(2,183)
Write down of inventories	**1,750**	1,682
Bad debt directly written off on other receivables	**–**	2,807
Gain on deemed partial disposal of a subsidiary	**–**	(21,323)
Gain on disposal of subsidiaries	**–**	(7,504)
Loss on disposal of concession intangible assets	**–**	309
Loss on disposal of a business	**–**	4,760
Write back of long outstanding payables	**–**	61
Operating cash flows before movements in working capital	**161,066**	28,071
Increase in inventories	**(15,522)**	(3,998)
Increase in trade and other receivables	**(113,518)**	(25,369)
Increase in amounts due from customers for contract works	**(7,980)**	(10,884)
Increase in trade and other payables	**26,906**	18,591
(Decrease) increase in amounts due to customers for contract works	**(65)**	657
Cash generated from operations	**50,887**	7,068
Income taxes paid	**(1,846)**	(7,084)
NET CASH FROM (USED IN) OPERATING ACTIVITIES	**49,041**	(16)

CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31 December 2010

	Notes	2010 HK$'000	2009 HK$'000
INVESTING ACTIVITIES			
Increase in loan receivables		**(72,859)**	–
Acquisition of concession intangible assets		**(71,508)**	(57,421)
Purchase of property, plant and equipment		**(4,957)**	(4,036)
Net cash outflow in respect of deemed disposal of a subsidiary	43	**(3,121)**	–
Net proceeds from sales of available–for–sale investments		**8,503**	52,543
Interest received		**6,279**	229
Proceeds from disposals of property, plant and equipment		**713**	555
Repayment from a non-controlling shareholder of subsidiaries		**–**	1,970
Proceeds from disposals of concession intangible assets		**196**	34
Net cash outflow in respect of the acquisition of an intangible asset through acquisition of a subsidiary	41	**–**	(98,890)
Deposit paid for acquisition of subsidiaries		**–**	(50,901)
Net cash inflow in respect of the disposal of subsidiaries/business	42	**–**	56,369
Refund of deposits for potential investment projects		**–**	20,401
Dividend from an associate		**–**	794
NET CASH USED IN INVESTING ACTIVITIES		**(136,754)**	(78,353)
FINANCING ACTIVITIES			
Issue of new shares (net of issue expenses)		**56,892**	245,896
New bank and other loans raised		**41,994**	4,099
Government grants received		**3,278**	3,766
Advance from an associate		**2,419**	–
Advance from (repayment to) non-controlling shareholders of a subsidiary		**162**	(15,451)
Redemption of convertible bonds		**(105,602)**	–
Repayment of bank borrowings and other loans		**(30,638)**	(17,852)
Interest paid		**(9,717)**	(7,146)
Dividend paid to non-controlling shareholder		**(8,492)**	(6,445)
NET CASH (USED IN) FROM FINANCING ACTIVITIES		**(49,704)**	206,867
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS		**(137,417)**	128,498
CASH AND CASH EQUIVALENTS AT 1 JANUARY		**277,857**	148,642
EFFECT OF FOREIGN EXCHANGE RATE CHANGES		**(2,425)**	717
CASH AND CASH EQUIVALENTS AT 31 DECEMBER, represented by bank balances and cash and cash held at financial institutions		**138,015**	277,857

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2010

1. GENERAL

China Water Industry Group Limited (the "Company") was incorporated in the Cayman Islands as an exempted company with limited liability and its shares are listed on The Stock Exchange of Hong Kong Limited (the "Stock Exchange"). The addresses of the registered office and principal place of business of the Company are disclosed in the "Corporate Information" section of the annual report.

The consolidated financial statements are presented in Hong Kong dollars ("HK$"). Other than those subsidiaries established in the People's Republic of China (the "PRC") whose functional currency is Renminbi ("RMB"), the functional currency of the Company and its subsidiaries (collectively referred to as the "Group") is HK$. The reason for selecting HK$ as its presentation currency is because the Company is a public company with its shares listed on the Stock Exchange.

The Company is an investment holding company. The principal activities of its subsidiaries are set out in note 53.

2. BASIS OF PREPARATION

The Group reported a consolidated loss attributable to owners of the Company of approximately HK$92,685,000 for the year ended 31 December 2010 and had a consolidated net current liabilities of approximately HK$303,574,000 as at 31 December 2010. This condition indicates the existence of a material uncertainty which may cast significant doubt on the Group's ability to continue as a going concern and therefore it may be unable to realise its assets and discharge its liability in the normal course of business. Nevertheless, the directors of the Company are of the opinion that the Group will have sufficient working capital to meet its financial obligations as and when they fall due for the next twelve months from 31 December 2010 giving that the directors of the Company will consider different sources of financing being available.

Accordingly, the directors of the Company are of the opinion that it is appropriate to prepare the consolidated financial statements on a going concern basis. Should the Group be unable to continue to operate as a going concern, adjustments would have to be made to the consolidated financial statements to write down the value of assets to their recoverable amounts, to provide for further liabilities which might arise and to reclassify non-current assets and non-current liabilities as current assets and current liabilities, respectively. The effect of these adjustments has not been reflected in the consolidated financial statements.

3. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs")

In the current year, the Group has applied the following new and revised standards, amendments and interpretations ("INTs") (herein collectively referred to as "new and revised HKFRSs"), issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA").

HKFRSs (Amendments)	Amendment to HKFRS 5 as part of Improvements to HKFRSs 2008
HKFRSs (Amendments)	Improvements to HKFRSs 2009
Hong Kong Accounting Standard ("HKAS") 27 (Revised)	Consolidated and Separate Financial Statements
HKAS 39 (Amendment)	Eligible Hedged Items
HKFRS 1 (Revised)	First-time Adoption of HKFRSs
HKFRS 1 (Amendment)	Additional Exemptions for First-time Adopters
HKFRS 2 (Amendment)	Group Cash-settled Share-based Payment Transactions
HKFRS 3 (Revised)	Business Combinations
HK – INT 5	Presentation of Financial Statements – Classification by the Borrower of a Term Loan that Contains a Repayment on Demand Clause
HK(IFRIC) – INT 17	Distributions of Non-cash Assets to Owners

Except as described below, the application of these new and revised HKFRSs had no material effect on the consolidated financial statements of the Group for the current or prior accounting periods.

HKFRS 3 (Revised 2008) Business Combinations

HKFRS 3 (Revised 2008) has been applied in the current year prospectively to business combinations of which the acquisition date is on or after 1 January 2010 in accordance with the relevant transitional provisions. Its application has affected the accounting for business combinations in the current year.

The impact of the application of HKFRS 3 (Revised 2008) is as follows:

a. HKFRS 3 (Revised 2008) allows a choice on a transaction-by-transaction basis for the measurement of non-controlling interests at the date of acquisition (previously referred to as "minority" interests) either at fair value or at the non-controlling interests' share of recognised identifiable net assets of the acquiree.

b. HKFRS 3 (Revised 2008) changes the recognition and subsequent accounting requirements for contingent consideration. Previously contingent consideration was recognised at the acquisition date only if payment of the contingent consideration was probable and it could be measured reliably; any subsequent adjustments to the contingent consideration were always made against the cost of the acquisition. Under the revised standard, contingent consideration is measured at fair value at the acquisition date; subsequent adjustments to the consideration are recognised against the cost of acquisition only to the extent that they arise from new information obtained within the measurement period (a maximum of 12 months from the acquisition date) about the fair value at the acquisition date. All other subsequent adjustments to contingent consideration classified as an asset or a liability are recognised in profit or loss.

3. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs") *(Continued)*

HKFRS 3 (Revised 2008) Business Combinations *(Continued)*

c. HKFRS 3 (Revised 2008) requires the recognition of a settlement gain or loss when the business combination in effect settles a pre-existing relationship between the Group and the acquiree.

d. HKFRS 3 (Revised 2008) requires acquisition-related costs to be accounted for separately from the business combination, generally leading to those costs being recognised as an expense in profit or loss as incurred, whereas previously they were accounted for as part of the cost of the acquisition.

HKAS 27 (Revised 2008) Consolidated and Separate Financial Statements

The application of HKAS 27 (Revised 2008) has resulted in changes in the Group's accounting policies regarding increases or decreases in ownership interests in subsidiaries of the Group. In prior years, in the absence of specific requirements in HKFRSs, increases in interests in existing subsidiaries were treated in the same manner as the acquisition of subsidiaries, with goodwill or a bargain purchase gain being recognised where appropriate. The impact of decreases in interests in subsidiaries that did not involve loss of control (being the difference between the consideration received and the carrying amount of the share of net assets disposed of) was recognised in profit or loss. Under HKAS 27 (Revised 2008), all increases or decreases in such interests are dealt with in equity, with no impact on goodwill or profit or loss.

When control of a subsidiary is lost as a result of a transaction, event or other circumstance, the revised standard requires that the Group derecognises all assets, liabilities and non-controlling interests at their carrying amount. Any retained interest in the former subsidiary is recognised at its fair value at the date the control is lost. A gain or loss on loss of control is recognised in profit or loss as the difference between the proceeds, if any, and these adjustments.

In respect of the disposal during the year of part of the Group's interest in iMerchants Limited ("iMerchants") (note 12), the impact of the change in policy has been that the loss on deemed partial disposal of a subsidiary of approximately HK$2,292,000 has been recognised directly in equity. Had the previous accounting policy been applied, this amount would have been recognised in profit or loss. Therefore the change in accounting policy has resulted in a decrease in the loss for the year ended 31 December 2010 and loss per share of 2010 of approximately HK$2,292,000 and HK$0.08 cents respectively.

In addition, under HKAS 27 (Revised 2008), the definition of non-controlling interest has been changed. Specifically, under the revised standard, non-controlling interest is defined as the equity in a subsidiary not attributable, directly or indirectly, to a parent. The application of the revised standard has resulted in non-redeemable convertible preference shares and equitable component of convertible bonds of a subsidiary, being included as part of non-controlling interest in the consolidated statement of changes in equity in 2009.

3. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs") *(Continued)*

HKAS 27 (Revised 2008) Consolidated and Separate Financial Statements *(Continued)*

Amendments to HKFRS 5 Non-current Assets Held for Sale and Discontinued Operations

The amendment to HKFRS 5 Non-current Assets Held for Sale and Discontinued Operations issued in 2009, as part of the Improvements to HKFRSs clarifies the disclosures required in respect of non-current assets (or disposal groups) classified as held for sale or discontinued operations. It states that disclosure requirements of other HKFRSs do not apply to non-current assets (or disposal groups) classified as held for sale or discontinued operations unless those HKFRSs have specific disclosure requirement in respect of such asset (or disposal groups); or the disclosures relate to the measurement of an individual asset or assets, as part of a disposal group which follows others HKFRSs and the information is not disclosed elsewhere in the consolidated financial statements.

Amendment to HKAS 17 Lease

As part of Improvements to HKFRSs issued in 2009, HKAS 17 Leases has been amended in relation to the classification of leasehold land. Before the amendment to HKAS 17, the Group was required to classify leasehold land as operating leases and to present as prepaid lease payments in the consolidated statement of financial position. The amendment to HKAS 17 has removed such a requirement. The amendment requires the classification of leasehold land should be based on the general principles set out in HKAS 17, that is, whether or not substantially all the risks and rewards incidental to ownership of a leased asset have been transferred to the lessee.

In accordance with the transitional provisions set out in the amendment to HKAS 17, the Group reassessed the classification of unexpired leasehold land at 1 January 2010 based on information that existed at the inception of the leases. In the opinion of the directors of the Company, no reclassification is considered necessary because none of the leasehold land qualifies for finance lease classification. The adoption of amendment to HKAS 17 has had no effect on the consolidated financial statements for the year ended 31 December 2010 and 2009.

Hong Kong Interpretation 5 Presentation of Financial Statements – Classification by the Borrower of a Term Loan that Contains a Repayment on Demand Clause

Hong Kong Interpretation 5 Presentation of Financial Statements – Classification by the Borrower of a Term Loan that Contains a Repayment on Demand Clause ("HK INT 5") clarifies that term loans that include a clause that gives the lender the unconditional right to call the loans at any time ("repayment on demand clause") should be classified by the borrower as current liabilities. The Group has applied HK INT 5 for the first time in the current year. HK INT 5 requires retrospective application.

In order to comply with the requirements set out in HK INT 5, the Group has changed its accounting policy on classification of term loans with a repayment on demand clause. In the past, the classification of such term loans were determined based on the agreed scheduled repayment dates set out in the loan agreements. Under HK INT 5, term loans with a repayment on demand clause are classified as current liabilities. This Interpretation did not have a material impact on the Group's financial statements for the year ended 31 December 2010 and 2009.

3. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs") *(Continued)*

The Group has not early applied the following new and revised standards, amendments or interpretations that have been issued but are not yet effective:

HKFRSs (Amendments)	Improvements to HKFRSs 2010 except of the amendments to HKFRS 3 (Revised in 2008), HKFRS 7, HKAS 1 and HKAS 28[1]
HKFRS 1 (Amendment)	Limited Exemption from Comparative HKFRS 7 Disclosures for First-time Adopters[3]
HKFRS 1 (Amendments)	Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters[5]
HKFRS 7 (Amendments)	Disclosures – Transfers of Financial Assets[5]
HKFRS 9	Financial Instruments[7]
HKAS 12 (Amendments)	Deferred Tax: Recovery of Underlying Assets[6]
HKAS 24 (Revised)	Related Party Disclosures[4]
HKAS 32 (Amendment)	Classification of Rights Issues[2]
HK(IFRIC)-INT 14 (Amendment)	Prepayments of a Minimum Funding Requirement[4]
HK(IFRIC)-INT 19	Extinguishing Financial Liabilities with Equity Instruments[3]

1 Effective for annual periods beginning on or after 1 July 2010 and 1 January 2011, as appropriate.
2 Effective for annual periods beginning on or after 1 February 2010.
3 Effective for annual periods beginning on or after 1 July 2010.
4 Effective for annual periods beginning on or after 1 January 2011.
5 Effective for annual periods beginning on or after 1 July 2011.
6 Effective for annual periods beginning on or after 1 January 2012.
7 Effective for annual periods beginning on or after 1 January 2013.

HKFRS 9 Financial Instruments (as issued in November 2009) introduces new requirements for the classification and measurement of financial assets. HKFRS 9 Financial Instruments adds requirements for financial liabilities and for derecognition.

- Under HKFRS 9, all recognised financial assets that are within the scope of HKAS 39 Financial Instruments: Recognition and Measurement are subsequently measured at either amortised cost or fair value. Specifically, debt investments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortised cost at the end of subsequent accounting periods. All other debt investments and equity investments are measured at their fair values at the end of subsequent accounting periods.

- In relation to financial liabilities, the significant change relates to financial liabilities that are designated as at fair value through profit or loss. Specifically, under HKFRS 9, for financial liabilities that are designated as at fair value through profit or loss, the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability is presented in other comprehensive income, unless the presentation of the effects of changes in the liability's credit risk in other comprehensive income would create or enlarge an accounting mismatch in profit or loss. Changes in fair value attributable to a financial liability's credit risk are not subsequently reclassified to profit or loss. Previously, under HKAS 39, the entire amount of the change in the fair value of the financial liability designated as at fair value through profit or loss was presented in profit or loss.

3. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs") *(Continued)*

HKFRS 9 of the Company is effective for annual periods beginning on or after 1 January 2013, with earlier application permitted.

The directors of the Company anticipate that HKFRS 9 that will be adopted in the Group's consolidated financial statements for the annual periods beginning 1 January 2013 and that the application of the new standard will have a significant impact on amounts reported in respect of the Group's financial assets and financial liabilities. However, it is not practicable to provide a reasonable estimate of that effect until a detailed review has been completed.

The amendments HKFRS 7 *Disclosures – Transfers of Financial Assets* increase the disclosure requirements for transactions involving transfers of financial assets. These amendments are intended to provide greater transparency around risk exposures when a financial asset is transferred but the transferor retains some level of continuing exposure in the asset. The amendments also require disclosures where transfers of financial assets are not evenly distributed throughout the period.

The directors of the Company do not anticipate that these amendments to HKFRS 7 will have a significant effect on the Group's disclosures regarding transfers of trade receivables previously effected. However, if the Group enters into other types of transfers of financial assets in the future, disclosures regarding those transfers may be affected.

HKAS 24 *Related Party Disclosures* (as revised in 2009) modifies the definition of a related party and simplifies disclosures for government-related entities.

The disclosure exemptions introduced in HKAS 24 (as revised in 2009) do not affect the Group because the Group is not a government-related entity. However, disclosures regarding related party transactions and balances in these consolidated financial statements may be affected when the revised version of the standard is applied in future accounting periods because some counterparties that did not previously meet the definition of a related party may come within the scope of the standard.

The amendments to HKAS 32 *Classification of Rights Issues address* the classification of certain rights issues denominated in a foreign currency as either an equity instrument or as a financial liability. To date, the Group has not entered into any arrangements that would fall within the scope of the amendments. However, if the Group does enter into any rights issues within the scope of the amendments in future accounting periods, the amendments to HKAS 32 will have an impact on the classification of those rights issues.

The amendments to HK(IFRIC)-Int 14 Prepayments of a Minimum Funding Requirement require entities to recognise as an economic benefit any prepayment of minimum funding requirement contributions. As the Group has no defined benefit scheme, the amendments are unlikely to have any financial impact on the Group.

3. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs") *(Continued)*

HK(IFRIC)-19 Extinguishing Financial Liabilities with Equity Instruments ("HK(IFRIC)-19") provides guidance regarding the accounting for the extinguishment of a financial liability by the issue of equity instruments. To date, the Group has not entered into transactions of this nature. However, if the Group does enter into any such transactions in the future, HK(IFRIC)-Int 19 will affect the required accounting. In particular, under HK(IFRIC)-Int 19, equity instruments issued under such arrangements will be measured at their fair value, and any difference between the carrying amount of the financial liability extinguished and the fair value of equity instruments issued will be recognised in profit or loss.

The directors of the Company anticipate that the application of the other new and revised standards, amendments or interpretations will have no material impact on the consolidated financial statements.

4. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared in accordance with HKFRSs issued by the HKICPA. In addition, the consolidated financial statements include applicable disclosures required by the Rules Governing the Listing of Securities ("Listing Rules") on the Stock Exchange and by the Hong Kong Companies Ordinance.

The consolidated financial statements have been prepared on the historical cost basis, except for certain financial instruments, which are measured at fair values, as explained in the accounting policies set out below. Historical cost is generally based on the fair value of the consideration given in exchange for goods.

The principal accounting policies are set out below:

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries). Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated statement of comprehensive income from the effective date of acquisition and up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Group.

All intra-group transactions, balances, income and expenses are eliminated in full on consolidation.

Non-controlling interests in subsidiaries are presented separately from the Group's equity therein.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Allocation of total comprehensive income to non-controlling interests

Total comprehensive income and expense of a subsidiary is attributed to the owners of the Company and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance. Prior to 1 January 2010, losses applicable to the non-controlling interests in excess of the non-controlling interests in the subsidiary's equity were allocated against the interests of the Group except to the extent that the non-controlling interests had a binding obligation and were able to make an additional investments to cover the losses.

Changes in the Group's ownership interests in existing subsidiaries

Changes in the Group's ownership interests in existing subsidiaries on or after 1 January 2010

Changes in the Group's ownership interests in subsidiaries that do not result in the Group losing control over the subsidiaries are accounted for as equity transactions. The carrying amounts of the Group's interests and the non-controlling interests are adjusted to reflect the changes in their relative interests in the subsidiaries. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognised directly in equity and attributed to owners of the Company.

When the Group loses control of a subsidiary, the profit and loss on disposal is calculated as the difference between (i) the aggregate of the fair value of the consideration received and the fair value of any retained interest and (ii) the previous carrying amount of the assets (including goodwill), and liabilities of the subsidiary and any non-controlling interests. When assets of the subsidiary are carried at revalued amounts or fair values and the related cumulative gain or loss has been recognised in other comprehensive income and accumulated in equity, the amounts previously recognised in other comprehensive income and accumulated in equity are accounted for as if the Company had directly disposed of the relevant assets (i.e. reclassified to profit or loss or transferred directly to retained earnings). The fair value of any investment retained in the former subsidiary at the date when control is lost is regarded as the fair value on initial recognition for subsequent accounting under HKAS 39 Financial Instruments: Recognition and Measurement or, when applicable, the cost on initial recognition of an investment in an associate or a jointly controlled entity.

Changes in the Group's ownership interests in existing subsidiaries prior to 1 January 2010

Increases in interests in existing subsidiaries were treated in the same manner as the acquisition of subsidiaries, with goodwill or a bargain purchase gain being recognised where appropriate. For decreases in interests in subsidiaries, regardless of whether the disposals would result in the Group losing control over the subsidiaries, the difference between the consideration received and the adjustment to the non-controlling interests was recognised in profit or loss.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Business combinations

Business combinations that took place prior to 1 January 2010

Acquisition of businesses was accounted for using the purchase method. The cost of the acquisition was measured at the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree, plus any costs directly attributable to the business combination. The acquiree's identifiable assets, liabilities and contingent liabilities that met the relevant conditions for recognition were generally recognised at their fair value at the acquisition date.

Goodwill arising on acquisition was recognised as an asset and initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the recognised amounts of the identifiable assets, liabilities and contingent liabilities recognised. If, after assessment, the Group's interest in the recognised amounts of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the combination, the excess was recognised immediately in profit or loss.

The minority interest in the acquiree was initially measured at the minority interest's proportionate share of the recognised amounts of the assets, liabilities and contingent liabilities of the acquiree.

Contingent consideration was recognised, if and only if, the contingent consideration was probable and could be measured reliably. Subsequent adjustments to contingent consideration were recognised against the cost of the acquisition.

Business combinations achieved in stages were accounted for as separate steps. Goodwill was determined at each step. Any additional acquisition did not affect the previously recognised goodwill.

Goodwill

Goodwill arising on an acquisition of a business is carried at cost less any accumulated impairment losses and is presented separately in the consolidated statement of financial position.

For the purposes of impairment testing, goodwill is allocated to each of the Group's cash-generating units (or groups of cash-generating units) that is expected to benefit from synergies of the acquisition.

A cash-generating unit to which goodwill has been allocated is tested for impairment annually, or more frequently when there is indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than its carrying amount, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit on a pro rata basis based on the carrying amount of each asset in the unit. Any impairment loss for goodwill is recognised directly in profit or loss in the consolidated statement of comprehensive income. An impairment loss recognised for goodwill is not reversed in subsequent periods.

On disposal of the relevant cash-generating unit, the attributable amount of goodwill capitalised is included in the determination of the amount of profit or loss on disposal.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Investments in subsidiaries

Investments in subsidiaries are included in the Company's statement of financial position at cost less any identified impairment loss.

Investments in associates

An associate is an entity over which the investor has significant influence and that is neither a subsidiary nor an interest in a joint venture. Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies.

The results and assets and liabilities of associates are incorporated in these consolidated financial statements using the equity method of accounting. Under the equity method, investments in associates are carried in the consolidated statement of financial position at cost as adjusted for post-acquisition changes in the Group's share of the net assets of the associates, less any identified impairment loss. When the Group's share of losses of an associate equals or exceeds its interest in that associate (which includes any long-term interests that, in substance, form part of the Group's net investment in the associate), the Group discontinues recognising its share of further losses. An additional share of losses is provided for and a liability is recognised only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of that associate.

Any excess of the cost of acquisition over the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities of the associate recognised at the date of acquisition is recognised as goodwill which is included within the carrying amount of the investment.

The requirements of HKAS 39 are applied to determine whether it is necessary to recognise any impairment loss with respect to the Group's investment in an associate. When necessary, the entire carrying amount of the investment is tested for impairment in accordance with HKAS 36 Impairment of Assets as a single asset by comparing its recoverable amount (higher of value in use and fair value less costs to sell) with its carrying amount. Any impairment loss recognised forms part of the carrying of the investment. Any reversal of that impairment loss is recognised in accordance with HKAS 36 to the extent the recoverable amount of the investment subsequently increases.

For disposal of an associate prior to 1 January 2010, the Group shall discontinue the use of the equity method from the date it ceases to have significant influence over an associate and shall account for the investment in accordance with HKAS 39 from that date, provided the associate does not become a subsidiary or a joint venture as defined in HKAS 31. The carrying amount of the investment at the date that it ceases to be an associate shall be regarded as its cost on initial measurement as a financial asset in accordance with HKAS 39.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Investments in associates *(Continued)*

From 1 January 2010 onwards, upon disposal of an associate that results in the Group losing significant influence over that associate, any retained investment is measured at fair value at that date and the fair value is regarded as its fair value on initial recognition as a financial asset in accordance with HKAS 39. The difference between the previous carrying amount of the associate attributable to the retained interest and its fair value is included in the determination of the gain or loss on disposal of the associate. In addition, the Group accounts for all amounts previously recognised in other comprehensive income in relation to that associate on the same basis as would be required if that associate had directly disposed of the related assets or liabilities. Therefore, if a gain or loss previously recognised in other comprehensive income by that associate would be reclassified to profit or loss on the disposal of the related assets or liabilities, the Group reclassifies that gain or loss from equity to profit or loss (as a reclassification adjustment) when it loses significant influence over that associate.

Dilution gains and losses arising in investments in associates are recognised in the consolidated statement of comprehensive income.

Where a group entity transacts with an associate of the Group, profits and losses resulting from the transactions with the associate are recognised in the Group's consolidated financial statements only to the extent of the interest in the associate that are not related to the Group.

Property, plant and equipment

Property, plant and equipment including buildings held for use in the production or supply of goods or services, or for administrative purposes (other than construction in progress) are stated at cost less subsequent accumulated depreciation and accumulated impairment losses, if any.

Depreciation is recognised so as to write off the cost of items of property, plant and equipment (other than construction in progress) over their estimated useful lives, using the straight-line method. The estimated useful lives and depreciation method are reviewed at the end of each reporting period, with the effect of any changes in estimate accounted for on a prospective basis.

Construction in progress for production, supply or administrative purposes are carried at cost, less any recognised impairment loss. Costs include professional fees and, for qualifying assets, borrowing costs capitalised in accordance with the Group's accounting policy. Such properties are classified to the appropriate categories of property, plant and equipment when completed and ready for intended use. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on the disposal or retirement of an item of property, plant and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in profit and loss.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Concession intangible assets

When the Group has a right to charge for usage of concession infrastructure, it recognises concession intangible assets at fair value upon initial recognition. The concession intangible assets representing water supply and sewage treatment operating rights are carried at cost less accumulated amortisation and any accumulated impairment losses.

The concession intangible assets are amortised to write off their cost, over their expected useful lives in the remaining concession period using an amortisation period which reflects the pattern in which their future economic benefits are expected to be consumed on a straight-line basis.

Costs in relation to the day-to-day servicing, repair and maintenance of the water supply and sewage treatment infrastructures are recognised as expenses in the periods in which they are incurred.

Intangible assets acquired separately

Intangible assets acquired separately and with finite useful lives are carried at costs less accumulated amortization and any accumulated impairment losses. Amortisation for intangible assets with finite useful lives is provided on a straight-line basis over their estimated useful lives.

Leasehold land and building

When a lease includes both land and building elements, the Group assesses the classification of each element as a finance or an operating lease separately based on the assessment as to whether substantially all the risks and rewards incidental to ownership of each element have been transferred to the Group. Specifically, the minimum lease payments (including any lump-sum upfront payments) are allocated between the land and the building elements in proportion to the relative fair values of the leasehold interests in the land element and building element of the lease at the inception of the lease.

To the extent the allocation of the lease payments can be made reliably, interest in leasehold land that is accounted for as an operating lease is presented as "prepaid lease payments" in the consolidated statement of financial position and is amortised over the lease term on a straight-line basis except for those that are classified and accounted for as investment properties under the fair value model. When the lease payments cannot be allocated reliably between the land and building elements, the entire lease is generally classified as a finance lease and accounted for as property, plant and equipment, unless it is clear that both elements are operating leases, in which case the entire lease is classified as an operating lease.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Construction contracts

Where the outcome of a construction contract (including construction or upgrade services of the infrastructure under a service concession arrangement) can be estimated reliably, revenue and costs are recognised by reference to the stage of completion of the contract activity at the end of the reporting period, as measured by the proportion that contract costs incurred for work performed to date bear to the estimated total contract costs, except where this would not be representative of the stage of completion. Variations in contract work, claims and incentive payments are included to the extent that the amount can be measured reliably and its receipt is considered probable.

Where the outcome of a construction contract cannot be estimated reliably, contract revenue is recognised to the extent of contract costs incurred that it is probable will be recoverable. Contract costs are recognised as expenses in the period in which they are incurred.

When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately.

Where contract costs incurred to date plus recognised profits less recognised losses exceed progress billings, the surplus is shown as amounts due from customers for contract work. For contracts where progress billings exceed contract costs incurred to date plus recognised profits less recognised losses, the surplus is shown as amounts due to customers for contract work. Amounts received before the related work is performed are included in the consolidated statement of financial position, as a liability, as advances received. Amounts billed for work performed but not yet paid by the customer are included in the consolidated statement of financial position under trade and other receivables.

Financial instruments

Financial assets and financial liabilities are recognised in the consolidated statement of financial position when a group entity becomes a party to the contractual provisions of the instruments.

Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets or financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in profit or loss.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Financial instruments *(Continued)*

Financial assets

The Group's financial assets are classified into one of the two categories, including, loans and receivables and available-for-sale financial assets. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition. All regular way purchases or sales of financial assets are recognised and derecognised on a trade date basis. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset, or, where appropriate, a shorter period to the net carrying amount on initial recognition.

Interest income is recognised on effective interest basis for the debt instruments, other than those financial assets classified as at FVTPL, of which interest income is included in net gains or losses.

Financial assets at fair value through profit or loss

Financial assets at FVTPL represented investment held for trading. A financial asset is classified as held for trading if:

- it has been acquired principally for the purpose of selling in the near future; or
- on initial recognition, it is a part of an identified portfolio of financial instruments that the Group manages together and has a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

Financial assets at FVTPL are measured at fair value, with any gains or losses arising on remeasurement recognised directly in profit or loss in the period in which they arise. The net gain or loss recognised in profit or loss excludes any dividend or interest earned on the financial assets.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Financial instruments *(Continued)*

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Subsequent to initial recognition, loans and receivables (including trade and other receivables, cash held at financial institutions and bank balance and cash) are carried at amortised cost using the effective interest method, less any identified impairment losses (see accounting policy on impairment loss on financial assets below).

Available-for-sale financial assets

Available-for-sale financial assets are non-derivatives that are either designated or not classified as financial assets at FVTPL, loans and receivables or held-to-maturity investments.

Available-for-sale financial assets are measured at fair value at the end of the reporting period. Changes in fair value are recognised in other comprehensive income and accumulated in investment revaluation reserves, until the financial asset is disposed of or is determined to be impaired, at which time, the cumulative gain or loss previously accumulated in the investment revaluation reserves is reclassified to profit or loss (see accounting policy on impairment loss on financial assets below).

Impairment loss on financial assets

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at the end of the reporting period. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the financial assets have been affected.

For an available-for-sale equity investment, a significant or prolonged decline in the fair value of that investment below its cost is considered to be objective evidence of impairment.

For all other financial assets, objective evidence of impairment could include:

– significant financial difficulty of the issuer or counterparty; or

– breach of contract, such as default or delinquency in interest or principal payments; or

– it becoming probable that the borrower will enter bankruptcy or financial re-organisation; or

– the disappearance of an active market for that financial asset because of financial difficulties.

For certain categories of financial asset, such as trade and other receivables, assets that are assessed not to be impaired individually are subsequently assessed for impairment on a collective basis. Objective evidence of impairment for a portfolio of receivables could include the Group's past experience of collecting payments, an increase in the number of delayed payments in the portfolio past the average credit period of 30 to 180 days, observable changes in national or local economic conditions that correlate with default on receivables.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Financial instruments *(Continued)*

Impairment loss on financial assets (Continued)

For financial assets carried at amortised cost, an impairment loss is recognised in the profit or loss when there is objective evidence that the asset is impaired, and is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade and other receivables, where the carrying amount is reduced through the use of an allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss. When a trade and other receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited to profit or loss.

For an available-for-sale equity investment, a significant or prolonged decline in the fair value of that investment below its cost is considered to be objective evidence of impairment.

For financial assets measured at amortised cost, if, in a subsequent period, the amount of impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment losses was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent that the carrying amount of the asset at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

Impairment losses on available-for-sale equity investments will not be reversed in profit or loss in subsequent periods. Any increase in fair value subsequent to impairment loss is recognised directly in other comprehensive income and accumulated in investment revaluation reserves.

Financial liabilities and equity instruments

Financial liabilities and equity instruments issued by a group entity are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument.

An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities. The Group's financial liabilities are generally classified into financial liabilities at FVTPL and other financial liabilities.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period.

Interest expense is recognised on an effective interest basis other than those financial liabilities designed as FVTPL, of which the interest expense is included in net gains or losses.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Financial instruments *(Continued)*

Financial liabilities at fair value through profit or loss

Financial liabilities at FVTPL has two subcategories, including financial liability held for trading and those designated at FVTPL on initial recognition.

A financial liability other than a financial liability held for trading may be designated as at FVTPL upon initial recognition if:

– such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or

– the financial liability forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Group's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or

– it forms part of a contract containing one or more embedded derivatives, and HKAS 39 permits the entire combined contract (asset or liability) to be designated as at FVTPL.

Financial liabilities at FVTPL are measured at fair value, with changes in fair value arising on remeasurement recognised directly in profit or loss in the period in which they arise. The net gain or loss recognised in profit or loss excludes any interest paid on the financial liabilities.

Other financial liabilities

Other financial liabilities including trade and other payables, amounts due to non-controlling shareholders of a subsidiary, loan from an associate, bank borrowings and other loans are subsequently measured at amortised cost, using the effective interest rate method.

Convertible bonds designated at FVTPL

Convertible bonds issued by the Group (including related embedded derivatives) are designated as FVTPL on initial recognition. At each end of the reporting period subsequent to initial recognition, the entire convertible bonds are measured at fair value, with changes in fair value recognised directly in profit or loss in the period in which they arise.

Convertible bonds contain liability and equity components

Convertible bonds issued by group entities that contain both the liability and conversion option components are classified separately into respective items on initial recognition. Conversion option that will be settled by the exchange of a fixed amount of cash or another financial asset for a fixed number of the Company's own equity instruments is classified as an equity instrument.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Financial instruments *(Continued)*

Convertible bonds contain liability and equity components (Continued)

On initial recognition, the fair value of the liability component is determined using the prevailing market interest of similar non-convertible debts. The difference between the gross proceeds of the issue of the convertible bonds and the fair value assigned to the liability component, representing the conversion option for the holder to convert the bonds into equity, is included in equity component of convertible bonds of a subsidiary.

In subsequent periods, the liability component of the convertible bonds is carried at amortised cost using the effective interest method. The equity component, representing the option to convert the liability component into ordinary shares of the respective group entity, will remain in equity component of convertible bonds of a subsidiary until the embedded option is exercised (in which case the balance stated in equity component of convertible bonds of a subsidiary will transferred to share premium). Where the option remains unexercised at the expiry date, the balance stated in equity component of convertible bonds of a subsidiary will be released to the accumulated losses. No gain or loss is recognised in profit or loss upon conversion or expiration of the option.

Transaction costs that relate to the issue of the convertible bonds are allocated to the liability and equity components in proportion to the allocation of the gross proceeds. Transaction costs relating to the equity components are charged directly to equity. Transaction costs relating to the liability components are included in the carrying amount of the liability portion and amortised over the period of the convertible bonds using the effective interest method.

Convertible bonds contain liability and equity components, and early redemption option derivative

Convertible bonds issued by the Group that contain liability, conversion option and early redemption option (which is not closely related to the host liability component) are classified separately into respective items on initial recognition. Conversion option that will be settled by the exchange of a fixed amount of cash or another financial asset for a fixed number of the Company's own equity instruments is classified as an equity instrument. At the date of issue, both the liability and early redemption option components are measured at fair value. The difference between the gross proceeds of the issue of the convertible bond and the fair values assigned to the liability and early redemption option components respectively, representing the conversion option for the holder to convert the loan notes into equity, is included in equity (convertible bond equity reserve).

In subsequent periods, the liability component of the convertible loan notes is carried at amortised cost using the effective interest method. The early redemption option is measured at fair value with changes in fair value recognised in profit or loss.

The equity component, representing the option to convert the liability component into ordinary shares of the Company, will remain in convertible bonds equity reserve until the embedded conversion option is exercised (in which case the balance stated in convertible loan notes equity reserve will be transferred to share premium). Where the conversion option remains unexercised at the expiry date, the balance stated in convertible loan notes equity reserve will be released to the retained profits. No gain or loss is recognised in profit or loss upon conversion or expiration of the conversion option.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Financial instruments *(Continued)*

Convertible bonds contain liability and equity components, and early redemption option derivatives (Continued)

Upon redemption of the convertible bond, the redemption consideration will be allocated to the liability component and equity component using the same allocation basis as when the convertible bond was originally issued.

Differences between the fair value and the carrying amount of the liability component will be recognised in the consolidated statement of comprehensive income. The difference between the redemption consideration and the fair value of the liability component will be included in equity (convertible bond reserve) and released to retained profits.

Transaction costs that relate to the issue of the convertible loan notes are allocated to the liability and conversion option components in proportion to their relative fair values. Transaction costs relating to the conversion option derivative is charged to profit or loss immediately. Transaction costs relating to the liability component are included in the carrying amount of the liability portion and amortised over the period of the convertible loan notes using the effective interest method.

Equity instruments

Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

Non-redeemable convertible preference shares of a subsidiary

Preference share capital is classified as equity if it is non-redeemable, or redeemable only at the Group's option, and any dividend is discretionary.

Embedded derivatives

Derivatives embedded in non-derivative host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contracts and the host contracts are not measured at fair value with changes in fair value recognised in profit or loss.

Derecognition

Financial assets are derecognised when the rights to receive cash flows from the assets expire or, the financial assets are transferred and the Group has transferred substantially all the risks and rewards of ownership of the financial assets. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received. On derecognition of a financial asset in its entirety, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognised directly in other comprehensive income is recognised in profit or loss.

Financial liabilities are derecognised when the obligation specified in the relevant contract is discharged, cancelled or expired. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in profit or loss.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Equity-settled share-based payment transactions

Share options granted to employees (on or before 7 November 2002, or granted after 7 November 2002 and vested before 1 January 2005)

The financial impact of share options granted is not recorded in the consolidated financial statements until such time as the options are exercised, and no charge is recognised in the profit or loss in respect of the value of options granted. Upon the exercise of the share options, the resulting shares issue are recorded as additional share capital at the nominal value of the shares, and the excess of the exercise price per share over the nominal value of the shares is recorded as share premium. Options which lapse or are cancelled prior to their exercise date are deleted from the register of outstanding options.

Share options granted to employees of the Group (after 7 November 2002 and vested on or after 1 January 2005)

The fair value of services received are determined by reference to the fair value of share options granted at the grant date is recognised as an expense in full at the grant date when the share options granted vest immediately, with a corresponding increase in equity (share options reserve).

At the end of each reporting period, the Group revises its estimates of the number of options that are expected to ultimately vest. The impact of the revision of the estimates during the vesting period, if any, is recognised in profit or loss, with a corresponding adjustment to share options reserve.

At the time when the share options are exercised, the amount previously recognised in share options reserve will be transferred to share premium. When the share options are forfeited after the vesting date or are still not exercised at the expiry date, the amount previously recognised in share option reserve will be transferred to accumulated profits (losses).

Share options granted to eligible persons

Share options issued in exchange for services are measured at fair values of services received. The fair values of services received are recognised as expenses, with a corresponding increase in equity (share options reserve), when the counterparties render services, unless the services qualify for recognition as assets.

Government grants

Government grants are not recognised until there is reasonable assurance that the Group will comply with the conditions attaching to them and that the grants will be received.

Government grants are recognised in profit or loss on a systematic basis over the periods in which the Group recognises as expenses the related costs for which the grants are intended to compensate. Government grants related to depreciable assets are recognised as deferred income in the consolidated statement of financial position and transferred to profit or loss over the useful lives of the related assets. Other government grants are recognised as revenue over the periods necessary to match them with the costs for which they are intended to compensate, on a systematic basis. Government grants that are receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to the Group with no future related costs are recognised in profit or loss in the period in which they become receivable.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Government grants *(Continued)*

The benefit of a government loan received on or after 1 January 2009 at a below-market rate of interest is treated as a government grant, measured as the difference between proceeds received and the fair value of the loan on initial recognition.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is calculated using the weighted average method.

Cash and cash equivalents

Bank balances and cash in the consolidated statement of financial position comprise cash at banks and on hand. For the purpose of the consolidated statement of cash flows, cash and cash equivalents consist of cash as defined above.

Impairment loss on tangible and intangible assets other than goodwill (see the accounting policy in respect of goodwill above)

At the end of the reporting period, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss, if any.

Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

Recoverable amount is the higher of fair value less costs to sell and value in use. 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 for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised as an expense immediately in profit or loss.

Where an impairment loss subsequently reverses, the carrying amount of the asset (or cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (or cash-generating unit) in prior years. A reversal of an impairment loss is recognised as income immediately in profit or loss.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods sold and services provided in the normal course of business, net of discounts and sales related taxes.

Revenue from sales of goods is recognised on the transfer of risks and rewards of ownership, which generally coincides with the time when the goods are delivered to customers and the title has passed.

Revenue arising from water supply is recognised based on water supplied as recorded by meter readings during the year.

Revenue from sewage treatment is recognised based on actual sewage treated from meter readings during the year.

Water supply related installation and construction income is recognised when services are rendered and income can be measured reliably.

Revenue from long-term construction contracts is recognised in accordance with the Group's accounting policy on construction contracts (see above).

Interest income from a financial asset is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts the estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount on initial recognition.

Sales of available-for-sale investments are recognised on a trade date basis.

Dividend income from investments is recognised when the shareholders' rights to receive payment have been established.

Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the consolidated statement of comprehensive income because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Taxation *(Continued)*

Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the corresponding tax base used in the computation of taxable profit. Deferred tax liabilities are generally recognised for all taxable temporary differences. Deferred tax assets are generally recognised for all deductible temporary difference to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

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

The measurement of deferred tax liabilities reflects the tax consequences that would follow from the manner in which the Group expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities. Deferred tax is recognised in profit or loss, except when it relates to items that are recognised in other comprehensive income or directly in equity, in which case the deferred tax is also recognised in other comprehensive income or directly in equity respectively. Where current tax or deferred tax arises from the initial accounting for a business combination, the tax effect is included in the accounting for the business combination.

Foreign currencies

In preparing the financial statements of each individual group entity, transactions in currencies other than the functional currency of that entity (foreign currencies) are recorded in the respective functional currency (i.e. the currency of the primary economic environment in which the entity operates) at the rates of exchanges prevailing on the dates of the transactions. At the end of the reporting period, monetary items denominated in foreign currencies are retranslated at the rates prevailing at that date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences arising on the settlement of monetary items, and on the retranslation of monetary items, are recognised in profit or loss in the period in which they arise. Exchange differences arising on the retranslation of non-monetary items carried at fair value are included in profit or loss for the period.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Foreign currencies *(Continued)*

For the purposes of presenting the consolidated financial statements, the assets and liabilities of the Group's foreign operations are translated into the presentation currency of the Group (i.e. "HK$") at the rate of exchange prevailing at the end of the reporting period, and their income and expenses are translated at the average exchange rates for the year. Exchange differences arising, if any, are recognised in other comprehensive income and accumulated in equity under the heading of the translation reserve (attributed to non-controlling interest as appropriate).

On the disposal of a foreign operation (i.e. a disposal of the Group's entire interest in a foreign operation, or a disposal involving loss of control over a subsidiary that includes a foreign operation, a disposal involving loss of joint control over a jointly controlled entity that includes a foreign operation, or a disposal involving loss of significant influence over an associate that includes a foreign operation), all of the exchange differences accumulated in equity in respect of that operation attributable to the owners of the Company are reclassified to profit or loss.

From 1 January 2010 onwards, on the disposal of a foreign operation (i.e. a disposal of the Group's entire interest in a foreign operation, or a disposal involving loss of control over a subsidiary that includes a foreign operation), all of the exchange differences accumulated in equity in respect of that operation attributable to the owners of the Company are reclassified to profit or loss. In addition, in relation to a partial disposal that does not result in the Group losing control over a subsidiary that includes a foreign operation, the proportionate share of accumulated exchange differences are re-attributed to non-controlling interests and are not recognised in profit or loss. For all other partial disposals (i.e. reductions in the Group's ownership interest in associates that do not result in the Group losing significant influence), the proportionate share of the accumulated exchange differences is reclassified to profit or loss.

Goodwill and fair value adjustments on identifiable assets acquired arising on an acquisition of a foreign operation are treated as assets and liabilities of that foreign operation and retranslated at the rate of exchange prevailing at the end of the reporting period. Exchange differences arising are recognised in the translation reserve.

Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

The Group as lessee

Operating lease payments are recognised as an expense on a straight-line basis over the term of the relevant lease.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale for which the commencement date for capitalisation is on or after 1 January 2010, are added to the cost of those assets until such time as 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 eligible for capitalisation.

All other borrowing costs are recognised in profit or loss in the period in which they are incurred.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Retirement benefits costs

Payments to the Mandatory Provident Fund Scheme are charged as an expense when employees have rendered services entitling them to the contributions.

The subsidiaries in the PRC participate in the Central Pension Scheme (the "CPS") operated by the PRC government for all of their staff. The subsidiaries are required to contribute a certain percentage of their covered payroll to the CPS to fund the benefits. The only obligation of the Group with respect to the CPS is to pay the ongoing required contributions under the CPS. Payments to the CPS are charged as expenses as they fall due in accordance with the rules of the CPS.

5. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

In the application of the Group's accounting policies, which are described in note 4, the directors of the Company are required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Critical judgments in applying the entity's accounting policies

The following are the critical judgments, apart from those involving estimations, that the directors of the Company have made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in consolidated financial statement.

Going concern basis

Although the Group had net current liabilities at the end of the reporting period, the Group manages its liquidity risk by monitoring its current and expected liquidity requirements regularly and ensuring sufficient liquid cash to meet the Group's liquidity requirements in the short and long term. Details of liquidity risk are disclosed in note 40.

Building and land use right

Despite the Group has paid the full purchase consideration as detailed in notes 16 and 17, certain of the Group's rights to use of the building and land were not granted formal titles from the relevant government authorities. The directors of the Company are of the opinions that the risks and rewards of using these assets have been transferred to the Group and the absence of formal titles to these buildings and land use rights do not impair the value of the relevant properties to the Group.

5. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY *(Continued)*

Critical judgments in applying the entity's accounting policies *(Continued)*

Control of Danzhou Qingyuan Water Industry Company Limited ("Danzhou City Water")

As detailed in note 51, all shares of Danzhou City Water owned by the Group have been freezed by High People's Court of Hainan Province during the year ended 31 December 2010. The directors of Company are of the opinion that after having sought the legal advice from the Company's lawyer, the control of Danzhou City Water is still existed, accordingly, the asset and liabilities of Danzhou City Water has been incorporated in the consolidated financial statement.

Key sources of estimation uncertainty

The following are the key assumptions concerning the future, and other key sources of estimation uncertainty at the end of the reporting period, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

Useful lives and impairment assessment of property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and identified impairment losses. The estimation of useful lives impacts the level of annual depreciation expenses recorded. Property, plant and equipment are evaluated for possible impairment on a specific asset basis or in groups of similar assets, as applicable. This process requires management's estimate of future cash flows generated by each asset or group of assets. For any instance where this evaluation process indicates impairment, the relevant asset's carrying amount is written down to the recoverable amount and the amount of the write-down is charged against the consolidated statement of comprehensive income.

Impairment loss recognised in respect of trade receivables

The Group performs ongoing credit evaluations of its customers and adjusts credit limits based on payment history and the customer's current credit-worthiness, as determined by review of their current credit information. The Group continuously monitors collections and payments from its customers and maintains a provision for estimated credit losses based upon its historical experience. Credit losses have historically been within the Group's expectations and the Group will continue to monitor the collections from customers and maintain an appropriate level of estimated credit losses. As at 31 December 2010, the carrying amount of trade receivables was approximately HK$10,973,000 (2009: HK$9,176,000) (net of impairment loss of approximately HK$5,246,000 (2009: HK$5,807,000)).

Impairment loss recognised in respect of other receivables and loans receivables

When there is objective evidence of impairment loss, the Group takes into consideration the estimation of future cash flows. The amount of the impairment 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 been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). Where the actual future cash flows are less than expected, a material impairment loss may arise. As at 31 December 2010, the carrying amounts of other receivables and loans receivables are HK$13,851,000 (2009: HK$44,914,000) and HK$123,760,000 (2009:HK$17,305,000) respectively (net of impairment loss of HK$8,903,000 (2009: HK$8,680,000) and HK$5,720,000 (2009: HK$5,720,000) respectively).

5. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY *(Continued)*

Key sources of estimation uncertainty *(Continued)*

Impairment of intangible asset and concession intangible assets

The Group determines whether an asset 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 asset is allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. A change in the estimated future cash flows and/or the discount rate applied will result in an adjustment to the estimated impairment provision previously made. As at 31 December 2009, the carrying amounts of intangible asset were HK$915,301,000 (2010: Nil). As at 31 December 2010, the carrying amounts of concession intangible asset are HK$483,829,000 (2009: HK$416,718,000) (net of impairment loss of HK$2,222,000 (2009: HK$2,222,000).

Impairment of available-for-sales investments

Management reviews the recoverability of the Group's available-for-sale investments with reference to current market environment whenever events or changes in circumstances indicate that the carrying amounts of the assets exceeds their corresponding recoverable amounts. Appropriate impairment for estimated irrecoverable amounts are recognised in profit and loss when there is objective evidence that the asset is impaired. During the year ended 31 December 2010, the impairment loss of approximately HK$30,502,000 (2009: nil) was recognised in the statement of comprehensive income.

Impairment of goodwill

Determining whether goodwill is impaired requires an estimation of the value in use of the cash-generating units to which goodwill has been allocated. The value in use calculation requires the Group to estimate the future cash flows expected to arise from the cash-generating unit and a suitable discount rate in order to calculate present value. Where the actual future cash flows are less than expected, a material impairment loss may arise. As at 31 December 2010, the carrying amounts of goodwill was approximately HK$142,373,000 (2009: HK$250,995,000) (net of impairment loss of HK$40,258,000 (2009: HK$98,685,000)). Details of impairment testing on goodwill are set out in note 20.

Fair values of convertible bonds

The fair values of the convertible bonds involve assumptions on the Company's credit spread, discount rate, expected credit rating and future cash flows. Should these assumptions change, there would be material changes to the valuation.

Revenue from construction contracts

Revenue from construction contracts of certain water supply and sewage treatment of the Group are recognised by reference to the stage of completion of the contract activity at the end of the reporting period. In recognition of profit and loss on the construction contracts, the management makes their best estimation of the future expected revenue from the contracts and future expected cost to complete the job. The estimates are determined by the management based on the current market conditions and expected time cost, material cost, other overhead expense to be incurred, expectations of future changes in the market and experience of similar transactions. Should there be a change in these estimates, then will be an impact on the amount of contract revenue or contract loss.

5. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY *(Continued)*

Key sources of estimation uncertainty *(Continued)*

Fair value of non-redeemable convertible preference shares

The best evidence of fair value is the published price quotations in an active market. In the absence of such information, the fair value is determined by an independent professional valuer. Such valuation is subject to limitations of the valuation models adopted and the uncertainty in estimates used by management in the assumptions. Should the estimates including share prices, volatility and the relevant parameters of the valuation model be changed, there would be changes in the fair value of non-redeemable convertible preference shares.

6. REVENUE

Revenue represents revenue arising from the provision of water supply services, sewage treatment services, water supply related installation and construction income and water supply and sewage treatment infrastructure construction income.

An analysis of the Group's revenue for the year from continuing operation is as follows:

	2010 ***HK$'000***	2009 *HK$'000*
Water supply services	**87,959**	84,201
Sewage treatment services	**18,078**	18,543
Water supply related installation and construction income	**100,712**	85,536
Water supply and sewage treatment infrastructure construction income	**32,022**	13,828
	238,771	202,108

7. SEGMENT INFORMATION

Information reported to the board of directors of the Company, being the chief operating decision maker, for the purposes of resource allocation and assessment of segment performance focused on types of goods and services delivered or provided.

(a)	Provision of water supply and sewage treatment as well as construction services	Provision of water supply and sewage treatment and construction of water supply and sewage treatment infrastructure
(b)	Investments in financial products	Investments in financial and investment products
(c)	All others	Mainly represents manufacturing and trading of ceramic sewage materials and others

With effect from October 2010, the equity interest in iMerchants owned by the Group was diluted to 36.57%. The investments in iMerchants were then reclassified from an investment in a subsidiary to investment in an associate. iMerchants is engaged in the business of investments in financial products and manufacturing and trading of ceramic sewage materials which was reported as a separate operating segment and a major component of the Group's other operating segment respectively for the year ended 31 December 2009. Upon the deemed partial disposal of iMerchants from a subsidiary to an associate, the operation of iMerchants was classified as discontinued operations of the Group and is described in more detail in note 12.

Segment revenues, results, assets and liabilities

Upon the deemed partial disposal of iMerchants from a subsidiary to an associate in September 2010, the Group has only one single continuing operation, namely provision of water supply and sewage treatment as well as construction services, accordingly no further segment information is presented.

Geographical information

No geographical information is presented as the Group's business is principally carried out in the PRC (country of domicile) and the Group's revenue from external customers and non-current assets are in the PRC. No geographical information for other country is of a significant size to be reported separately.

Information about major customers

For the year ended 31 December 2010 and 2009, the Group does not have any single significant customer with the transaction value over 10% of the turnover from continuing operation.

8. OTHER OPERATING INCOME

	2010 HK$'000	2009 HK$'000
Continuing operation:		
Handling charges	**1,311**	746
Interest from Bureau of Yingtan City *(note i)*	**5,394**	–
Net exchange gain	**223**	–
Loan interest income	**636**	–
Bank interest income	**249**	218
Write back of long outstanding payables	**–**	61
Government subsidies *(note ii)*	**1,301**	–
Penalty income	**351**	643
Reversal impairment loss of trade and other receivables	**921**	–
Others	**4,264**	1,652
	14,650	3,320

Notes:

(i) Interest from Bureau of Yingtan City was earned from fund provided to the relevant government authorities for construction of the sewage treatment operation. The interest rate is at 12% per annum.

(ii) The amount represented the sewage turnover compensation received by the Group from the PRC government to subsidies the Group's sewage treatment operation.

9. FINANCE COSTS

	2010 HK$'000	2009 HK$'000
Continuing operation:		
Interest on:		
– Interest on convertible bonds	**967**	963
– Imputed interest charged on convertible bonds	**201**	–
– Bank borrowings wholly repayable within five years	**2,681**	2,163
– Bank borrowings wholly repayable more than five years	**1,633**	1,762
– Other loans wholly repayable within five years	**2,353**	5,214
– Other loans wholly repayable more than five years	**1,443**	1,394
– Amounts due to non-controlling shareholders of subsidiaries	**200**	278
– Loan from an associate	**56**	219
	9,534	11,993

10. INCOME TAX EXPENSE

	2010 HK$'000	2009 HK$'000
Continuing operation:		
PRC Enterprise Income Tax ("EIT")		
– Current	**7,929**	6,316
– Under provision in prior years	**–**	294
	7,929	6,610
Deferred tax *(note 38)*	**2,884**	1,838
	10,813	8,448

No tax is payable on the profit arising in Hong Kong in both years since the assessable profit is wholly absorbed by tax losses brought forward.

Pursuant to the relevant laws and regulations in the PRC, certain subsidiaries of the Group are exempted from PRC EIT for two years from the first profit making year, followed by a 50% reduction for the next three years. Yichun Water Supply Co., Ltd, Yichun City Water Supply Engineering Limited and Jining City Haiyuan Water Treatment Company Limited were under the 50% tax reduction for both years.

Under the Law of the EIT and Implementation Regulation of the Law of the EIT, the tax rate of the other PRC subsidiaries is at 25% for both years.

10. INCOME TAX EXPENSE *(Continued)*

The income tax expense for the year can be reconciled to the loss before tax per the consolidated statement of comprehensive income as follows:

	2010	2009
	HK$'000	*HK$'000*
Loss before tax from continuing operation	**(166,667)**	(300,227)
Tax at the domestic income tax rate of 25% (2009: 25%)	**(41,667)**	(75,057)
Tax effect of share of results of associates	**2,027**	(546)
Tax effect of expenses not deductible for tax purpose	**50,295**	65,925
Tax effect of income not taxable for tax purpose	**(5,179)**	(5,547)
Effect of different tax rates of subsidiaries operating in other jurisdictions	**7,625**	22,618
Effect of tax exemption granted to PRC subsidiaries	**(3,673)**	(1,824)
Tax effect of deductible temporary differences not recognised	**244**	2,065
Utilisation of tax losses previously not recognised	**–**	(221)
Under provision for taxation in prior years	**–**	294
Deferred tax liabilities arising on undistributed profit of PRC subsidiaries from 1 January 2008 onwards	**1,141**	741
Income tax expense for the year	**10,813**	8,448

Details of deferred tax are set out in note 38.

11. LOSS FOR THE YEAR FROM CONTINUING OPERATION

Loss for the year from continuing operation has been arrived at after charging:

	Year ended 2010 HK$'000	2009 HK$'000
Amortisation of prepaid lease payments	**1,093**	1,302
Amortisation of concession intangible assets (included in cost of sales)	**13,792**	14,864
Auditors' remuneration	**1,000**	960
Bad debts directly written off on other receivables	**–**	2,807
Cost of inventories recognised as expenses	**25,674**	25,026
Depreciation of property, plant and equipment	**6,505**	5,458
Impairment loss on concession intangible assets	**–**	2,222
Write down of inventories (included in cost of sales)	**–**	1,682
Loss on disposal of concession intangible assets	**–**	309
Loss on disposal of property, plant and equipment	**619**	54
Minimum lease payment under operating leases	**1,651**	2,552
Net exchange loss	**–**	77
Staff costs excluding directors' emoluments		
– Salaries, wages and other benefits	**32,676**	33,977
– Retirement benefits scheme contributions	**7,276**	6,114
Total staff costs	**39,952**	40,091

12. DISCONTINUED OPERATIONS

On 23 October 2009, iMerchants issued approximately 2,938,478,000 non-redeemable convertible preference shares with a par value of HK$0.2 each (the "Convertible Preference Shares"), as a partial consideration for the acquisition of an intangible asset through the acquisition of a subsidiary (note 41).

In June 2010, the holders of 440,000,000 Convertible Preference Shares exercised their rights to convert the Convertible Preference Shares into fully paid ordinary shares of iMerchants. After the conversion, the equity interest of iMerchants owned by the Group has reduced from 76.66% to 67.23%. The Group retained control of iMerchants subsequent to the conversion. The amount of approximately HK$2,292,000, being the difference between the carrying amount of the Convertible Preference Shares converted of approximately HK$17,600,000 and the respective increase in the interest attributable to shares held in subsidiaries of approximately HK$19,892,000, was recognised directly in equity and attributed to the owners of the Company.

In September and October 2010, the holders of 1,308,800,000 Convertible Preference Shares exercised their rights to convert the Convertible Preference Shares into fully paid ordinary shares of iMerchants. After the conversion, the equity interest of iMerchants owned by the Group has reduced further from 67.23% to 49.23%. The investments in iMerchants were then changed from investment in a subsidiary to investment in an associate. Details of this deemed disposal is set out in note 43.

12. DISCONTINUED OPERATIONS *(Continued)*

Analysis of loss for the year from discontinued operations

iMerchants is engaged in the business of investments in financial products and manufacturing and trading of ceramic sewage. The combined results of these discontinued operations in the consolidated statement of comprehensive income and consolidated statement of cash flows are set out below. The comparative loss and cash flows from the discontinued operations have been re-presented to include those operations classified as discontinued in the current year.

The loss for the year from discontinued operations is analysed as follows:

	Notes	**Period ended 30/9/2010** ***HK$'000***	Year ended 31/12/2009 *HK$'000*
Loss on the discontinued operations for the year		**(230,545)**	(55,133)
Gain on deemed disposal of a subsidiary	*43*	**258,229**	–
Gain on deemed partial disposal of a subsidiary	*44*	**–**	21,323
		27,684	(33,810)

	Period ended 30/9/2010 ***HK$'000***	Year ended 31/12/2009 *HK$'000*
Loss for the year from discontinued operations		
Revenue	**114,720**	8,938
Cost of sales	**(2,386)**	(4,119)
Gross profit	**112,334**	4,819
Other operating income	**353**	2,065
Selling and distribution expenses	**(4,157)**	(4,565)
Administrative expenses	**(53,933)**	(21,239)
Impairment loss recognised on an intangible asset	**(245,639)**	–
Impairment loss recognised on trade and other receivables	**(419)**	(773)
Impairment loss recognised on goodwill	**–**	(32,616)
Finance costs	**(10,588)**	(2,937)
Loss before tax	**(202,049)**	(55,246)
Taxation	**(28,496)**	113
Loss for the year from discontinued operations	**(230,545)**	(55,133)

12. DISCONTINUED OPERATIONS *(Continued)*

Loss for the year from discontinued operating include the following:

	Period ended 30/9/2010 *HK$'000*	Year ended 31/12/2009 *HK$'000*
Loss before tax has been arrived at after charging:		
Amortisation of prepaid lease payments	**47**	60
Amortisation of an intangible asset	**46,279**	10,283
Depreciation of property, plant and equipment	**423**	414
Minimum lease payment under operating leases	**1,006**	1,028
Finance costs		
Interest on other loans	**384**	465
Imputed interest on convertible bonds	**10,204**	2,472
Staff costs excluding directors' emoluments		
– Salaries, wages and other benefits	**1,824**	3,108
– Retirement benefits scheme contributions	**55**	76
Total staff costs	**1,879**	3,184
Cash flows from discontinued operations		
Net cash (outflows) inflows from operation activities	**(52,771)**	103,628
Net cash inflows (outflows) from investing activities	**5,079**	(159,911)
Net cash inflows from financing activities	**1,464**	56,497
Net cash (outflows) inflows	**(46,228)**	214

13. EMOLUMENTS FOR DIRECTORS AND EMPLOYEES

(a) Directors' emoluments

The emolument paid or payable to each of the 9 (2009: 13) directors were as follows:

For the year ended 31 December 2010

Name	Fees *HK$'000*	Salaries, allowance and benefits in kind *HK$'000*	Retirement benefits scheme contributions *HK$'000*	Total *HK$'000*
Executive Directors:				
Li Yu Gui	–	390	12	402
Yang Bin	–	350	9	359
Zhong Wen Sheng[1]	–	256	–	256
Liu Bai Yue[2]	–	497	12	509
Chu Yin Yin, Georgiana	–	546	12	558
Li Wen Jun	–	300	9	309
	–	2,339	54	2,393
Independent Non-Executive Directors:				
Chang Kin Man	120	–	–	120
Wu Tak Lung	144	–	–	144
Gu Wen Xuan	120	–	–	120
	384	–	–	384
Total	384	2,339	54	2,777

1. Resigned on 4 January 2010
2. Resigned on 1 January 2011

13. EMOLUMENTS FOR DIRECTORS AND EMPLOYEES *(Continued)*

(a) Directors' emoluments *(Continued)*

For the year ended 31 December 2009

Name	Fees	Salaries, allowance and benefits in kind	Retirement benefits scheme contributions	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Executive Directors:				
Li Yu Gui	–	390	26	416
Yang Bin	–	391	12	403
Zhong Wen Sheng[1]	–	546	–	546
Liu Bai Yue	–	468	12	480
Shi De Mao[2]	–	86	–	86
Chu Yin Yin, Georgiana	–	546	12	558
Li Wen Jun[3]	–	210	7	217
Liu Peng Cheng[2]	–	–	–	–
	–	2,637	69	2,706
Non-Executive Directors:				
Huang Yuan Wen[4]	–	36	–	36
Pan Shi Ying[4]	–	36	–	36
	–	72	–	72
Independent Non-Executive Directors:				
Chang Kin Man	120	–	–	120
Wu Tak Lung	144	–	–	144
Gu Wen Xuan	120	–	–	120
	384	–	–	384
Total	384	2,709	69	3,162

1. Resigned on 4 January 2010
2. Resigned on 31 May 2009
3. Appointed on 3 June 2009
4. Resigned on 10 June 2009

13. EMOLUMENTS FOR DIRECTORS AND EMPLOYEES *(Continued)*

(a) Directors' emoluments *(Continued)*

There was no arrangement under which directors waived or agreed to waive any emoluments during the two years ended 31 December 2010.

The remuneration of directors is determined by the remuneration committee having regard to the performance of individuals and market trends.

(b) Employees' emoluments

Details of the five highest paid individuals included two (2009: four) directors whose emoluments are set out in (a) above. The emolument of the remaining three (2009: one) highest paid individual was as follow:

	2010	2009
	HK$'000	*HK$'000*
Salaries, allowance and benefits in kind	**1,295**	578
Retirement benefits scheme contributions	**110**	12
	1,405	590

Their emoluments were within the following bands:

	2010	2009
	No. of employees	No. of employees
	HK$'000	*HK$'000*
Nil to HK$1,000,000	**3**	1

No emolument was paid to the directors of the Company or the five highest paid individuals as an inducement to join or upon joining the Group or as compensation for loss of office, during the two year ended 31 December 2010 and 2009.

14. DIVIDEND

No dividend was paid or proposed during the year ended 31 December 2010, nor has any dividend been proposed since the end of the reporting period (2009: Nil).

15. LOSS PER SHARE

From continuing operation

The calculation of basic and diluted (loss) earning per share attributable to the owners of the Company for the year is based on the following data:

	2010 HK$'000	2009 HK$'000
(Loss) earning		
Loss for the year attributable to owners of the Company	**(92,685)**	(354,239)
Less: Profit (loss) for the year from discontinued operations	**112,358**	(25,880)
Loss for the purposes of basic and diluted loss per share from continuing operation	**(205,043)**	(328,359)
Number of shares	***'000***	*'000*
Weighted average number of ordinary shares for the purpose of basic and diluted loss per share	**2,832,357**	2,259,686

Note: The computation of diluted loss per share does not assume the exercise of the Company's outstanding share options as exercise price of those options is higher than the average market price of shares for the year ended 31 December 2010 and 2009.

Diluted loss per share was same as the basic loss per share for the year ended 31 December 2010 and 2009, as the effect of the conversion of the Company's outstanding share options and convertible bonds as well as the outstanding convertible bonds and non-redeemable preference shares issued by iMerchants would result in a decrease in loss per shares from continuing operation for the year ended 31 December 2010 and 2009.

From discontinued operations

Basic and diluted earnings per share for the discontinued operations is HK$3.97 cents per share (2009: Basic and diluted loss per share for discontinued operations is HK$1.15 cents per share), based on the profit for the year from the discontinued operations of approximately HK$112,358,000 (2009: loss for the year from the discontinued operations of approximately HK$25,880,000) and the denominators detailed above for both basic and diluted earnings per share.

16. PROPERTY, PLANT AND EQUIPMENT

	Buildings HK$'000	Plant and machinery HK$'000	Leasehold improvements HK$'000	Motor vehicles HK$'000	Water pipeline HK$'000	Construction in progress HK$'000	Total HK$'000
COST							
At 1 January 2009	53,676	2,049	8,837	9,636	46,700	15,021	135,919
Additions	125	763	674	959	116	1,399	4,036
Transfer	3,198	–	39	–	–	(3,237)	–
Disposals	(170)	(17)	(54)	(196)	(252)	–	(689)
Disposal of subsidiaries/business	(18,212)	(2,420)	(5,756)	(1,176)	–	(60)	(27,624)
Exchange realignment	172	33	19	81	417	102	824
At 31 December 2009 and 1 January 2010	38,789	408	3,759	9,304	46,981	13,225	112,466
Additions	928	1,112	577	2,340	–	–	4,957
Transfers	649	–	209	–	–	(858)	–
Disposals	–	(83)	(191)	(2,776)	–	–	(3,050)
Deemed disposal of a subsidiary	(6,305)	(1,024)	(369)	(115)	–	–	(7,813)
Exchange realignment	1,651	211	121	311	2,185	362	4,841
At 31 December 2010	**35,712**	**624**	**4,106**	**9,064**	**49,166**	**12,729**	**111,401**
ACCUMULATED DEPRECIATION							
At 1 January 2009	1,558	252	1,395	993	1,774	–	5,972
Provided for the year	1,687	166	592	1,609	1,818	–	5,872
Eliminated on disposals	–	–	(44)	(36)	–	–	(80)
Disposal of subsidiaries/business	(660)	(394)	(1,273)	(184)	–	–	(2,511)
Exchange realignment	12	3	3	9	22	–	49
At 31 December 2009 and 1 January 2010	2,597	27	673	2,391	3,614	–	9,302
Provided for the year	1,791	511	618	1,541	2,467	–	6,928
Eliminated on disposals	–	(14)	(108)	(1,596)	–	–	(1,718)
Deemed disposal of a subsidiary	(393)	(391)	(111)	(47)	–	–	(942)
Exchange realignment	58	15	17	27	116	–	233
At 31 December 2010	**4,053**	**148**	**1,089**	**2,316**	**6,197**	**–**	**13,803**
CARRYING VALUES							
At 31 December 2010	**31,659**	**476**	**3,017**	**6,748**	**42,969**	**12,729**	**97,598**
At 31 December 2009	36,192	381	3,086	6,913	43,367	13,225	103,164

16. PROPERTY, PLANT AND EQUIPMENT *(Continued)*

The above items of property, plant and equipment are depreciated on a straight-line basis at the following rates per annum:

Buildings	Over the shorter of the term of the lease, or 30 years
Plant and machinery	5 to 10 years
Leasehold improvements	Over the shorter of the term of the lease, or 5 to 10 years
Motor vehicles	5 years
Water pipeline	15 to 25 years

The buildings are situated in the PRC and are situated on land under medium-term land use rights.

As at 31 December 2010, the property usage permits of certain buildings have not been granted by relevant government authorities with the aggregate carrying values of approximately HK$3,178,000 (2009: HK$3,150,000). In the opinion of the directors of the Company, the absence of property usage permits to these buildings does not impair the value of the relevant buildings to the Group. The directors of the Company also believe that property usage permits to these buildings will be granted to the Group in due course.

The Group has pledged buildings with carrying amount of approximately HK$2,195,000 (2009: HK$2,186,000) to secure the bank and other borrowings granted to the Group.

17. PREPAID LEASE PAYMENTS

	2010	2009
	HK$'000	*HK$'000*
COST		
At 1 January	**46,026**	79,554
Disposal of subsidiaries/business	**–**	(33,889)
Deemed disposal of a subsidiary	**(2,830)**	–
Exchange realignment	**1,630**	361
At 31 December	**44,826**	46,026
ACCUMULATED AMORTISATION		
At 1 January	**1,991**	1,317
Provided for the year	**1,140**	1,362
Eliminated on disposals of subsidiaries/business	**–**	(699)
Eliminated on deemed disposal of a subsidiary	**(110)**	–
Exchange realignment	**34**	11
At 31 December	**3,055**	1,991
CARRYING VALUES		
At 31 December	**41,771**	44,035

The Group's prepaid lease payments in relation to land use rights are under medium-term leases in the PRC, and analysed for reporting purposes as:

	2010	2009
	HK$'000	*HK$'000*
Current assets	**1,150**	1,181
Non-current assets	**40,621**	42,854
	41,771	44,035

At 31 December 2010, legal titles to land use rights with carrying values of HK$14,756,000 (2009: HK$14,440,000) has not been granted by the relevant government authorities. The Group is in process to obtain the land use rights certificate and in the opinion of the directors of the company, the formal title of the land use rights will be granted to the Group in due course.

As at 31 December 2010, the Group had pledged prepaid lease payments with carrying amount of approximately HK$10,284,000 (2009: HK$12,881,000) to secure bank and other borrowings granted to the Group.

18. CONCESSION INTANGIBLE ASSETS

	Total
	HK$'000
COST	
At 1 January 2009	629,167
Additions	57,421
Disposals	(373)
Disposal of subsidiaries/business	(244,371)
Exchange realignment	3,698
At 31 December 2009 and 1 January 2010	445,542
Additions	71,508
Disposals	(220)
Exchange realignment	12,482
At 31 December 2010	**529,312**
ACCUMULATED AMORTISATION AND IMPAIRMENT	
At 1 January 2009	20,441
Provided for the year	14,864
Eliminated on disposal	(30)
Disposal of subsidiaries/business	(8,957)
Impairment loss recognised during the year	2,222
Exchange realignment	284
At 31 December 2009 and 1 January 2010	28,824
Provided for the year	13,792
Eliminated on disposals	(24)
Exchange realignment	2,891
At 31 December 2010	**45,483**
CARRYING VALUES	
At 31 December 2010	**483,829**
At 31 December 2009	416,718

18. CONCESSION INTANGIBLE ASSETS *(Continued)*

The subsidiaries of the Group, Yichun Water Industry Co. Limited ("Yichun Water"), Linyi Fenghuang Water industry Co., Ltd ("Linyi Fenghuang"), Danzhou Qingyuan Water Industry Company Limited ("Danzhou Qingyuan") and Yingtan Water Supply Co., Ltd ("Yingtan Water Supply") entered into service concession arrangements with the respective local government whereby the above subsidiaries are required to build the infrastructure of water supply plant and was granted with an exclusive operating right for provision of water supply services to the public users for a period of 30 years commencing from the operation of the respective water supply plant.

The subsidiaries of the Group, Yichun Fangke Sewage Treatment Company Limited ("Yichun Fangke") and Jining City Haiyuan Water Treatment Company Limited ("Jining Haiyuan") entered into service concession arrangements with the respective local government whereby the above subsidiaries are required to build the infrastructure of sewage treatment plant and was granted with an exclusive operating right for provision of sewage treatment services to the public users for a period ranging from 25 to 29 years, commencing from the operation of the respective waste treatment plant.

Amortisation for the above concession intangible assets has been provided on a straight-line basis over the remaining terms of the operating rights, ranging from 25 to 30 years, since commencement of operations. The receipt from these service concession arrangement, are contingent on the extent that public uses the services.

As at 31 December 2010, the Group had pledged concession intangible assets with carrying amount of approximately HK$19,240,000 (2009: HK$19,392,000) to secure bank borrowings granted to the Group.

As at 31 December 2009, impairment loss of approximately HK$2,222,000 has been recognised in concession intangible assets (2010: Nil). The recoverable amounts of the concession intangible assets have been determined by using value-in-use calculation by reference to the valuation performed by Asset Appraisal Limited, a qualified valuer not connected with the Group ("Asset Appraisal"). That calculation uses cash flow projections based on financial budgets approved by management covering a 5 year periods, and pre-tax discount rate of 11.28% (2009: 12.55%). Cash flows beyond the 5 year periods have been extrapolated using a steady 3% (2009: 3%) growth rate. This growth rate is based on the relevant industry growth forecasts and does not exceed the average long-term growth rate for the relevant industry.

19. INTANGIBLE ASSET

	2010 HK$'000	2009 HK$'000
COST		
At 1 January	**925,584**	–
Acquired through acquisition of a subsidiary	**–**	925,584
Deemed disposals of a subsidiary	**(925,584)**	–
At 31 December	**–**	925,584
ACCUMULATED AMORTISATION		
At 1 January	**10,283**	–
Provided for the year	**46,279**	10,283
Impairment loss recognised	**245,639**	–
Deemed disposal of a subsidiary	**(302,201)**	–
At 31 December	**–**	10,283
CARRYING VALUES		
At 31 December	**–**	915,301

The intangible asset represented the exclusive right which derived from a management agreement ("Management Agreement") to receive management fee equivalent to 70% of the net profits of Shenzhen Careall Capital Investment Co., Ltd ("Shenzhen Careall"), a company established in the PRC and being an independent third party of the Group. Under the Management Agreement, Shenzhen Careall shall irrevocably and unconditionally warrant, guarantee and undertake to and with Supreme Luck International Limited ("Supreme Luck"), a wholly-owned subsidiary of iMerchants that the net profits during the one-year period commencing from the date of the Management Agreement shall not be less than approximately HK$113,380,000 (equivalent to RMB100,000,000); the second one-year period commencing from the date of the Management Agreement shall not less than approximately HK$170,070,000 (equivalent to RMB150,000,000); and the third one-year period commencing from the date of the Management Agreement shall not less than approximately HK$226,760,000 (equivalents to RMB200,000,000). Shenzhen Careall is principally engaged in venture investment, venture investment advisory and management services, with the objective of investment in the equities of the new technology-based enterprises in the PRC. The exclusive right was acquired through the acquisition of the entire issued share capital of Supreme Luck during the year ended 31 December 2009. Details of which are set out in note 41.

The intangible asset are amortised on straight-line basis over its estimated useful lives of 15 years. Intangible assets was disposed of along with the deemed disposal of iMerchants during the year.

19. INTANGIBLE ASSET *(Continued)*

The recoverable amount of the exclusive right has been determined on the basis of value-in-use calculation with reference to a valuation performed by Grant Sherman Appraisal Limited, an independent qualified valuer not connected to the Group. The value-in-use calculations use cash flow projections of 15 years and based on financial budgets approved by management of the Company covering a 3-year period, and a discount rate of 20.36%. Cash flows beyond the 5 year periods have been extrapolated using a steady 3% growth rate. This rate of return is based on the relevant track record of Careall Capital and does not exceed the average long-term growth rate for the relevant industry. Cash flow projections during the budget period for the exclusive right is based on the budgeted sales and expected realisable profit during the budget period and the similar quality of new investments during the budget period. Expected cash inflows/outflows, which include budgeted sales of listed securities, cost of acquiring new investment portfolio and other direct costs have been determined based on past performance and management's expectations for the market development. The directors of the Company are of the opinion that the recoverable amount is less than its respective carrying amount as at the date of deemed disposal of iMerchants, accordingly an impairment loss of approximately HK$245,639,000 (2009: Nil) was recognised.

20. GOODWILL

	Provision of water supply and sewage treatment *HK$'000*	Investments in financial products *HK$'000*	Others *HK$'000*	Total *HK$'000*
COST				
At 1 January 2009	284,624	56,991	49,569	391,184
Released in deemed partial disposal of interest in a subsidiary	–	(5,580)	–	(5,580)
Released in disposal of subsidiaries *(note 42)*	(35,924)	–	–	(35,924)
At 31 December 2009	248,700	51,411	49,569	349,680
Released in a deemed disposal of a subsidiary *(note 43)*	–	(51,411)	(49,569)	(100,980)
At 31 December 2010	**248,700**	**–**	**–**	**248,700**
IMPAIRMENT				
At 1 January 2009	7,837	–	–	7,837
Released in disposal of subsidiaries *(note 42)*	(7,837)	–	–	(7,837)
Impairment loss recognised during the year	66,069	–	32,616	98,685
At 31 December 2009	66,069	–	32,616	98,685
Released in deemed disposal of a subsidiary *(note 43)*	–	–	(32,616)	(32,616)
Impairment loss recognised during the year	40,258	–	–	40,258
At 31 December 2010	**106,327**	**–**	**–**	**106,327**
CARRYING VALUES				
At 31 December 2010	**142,373**	**–**	**–**	**142,373**
At 31 December 2009	182,631	51,411	16,953	250,995

20. GOODWILL *(Continued)*

Impairment testing on goodwill

Goodwill was allocated to three individual cash generating units ("CGU"), including provision of water supply and sewage treatment, investments in financial products and others.

Goodwill from acquisition of Blue Mountain Hong Kong Group Limited ("Blue Mountain"), Danzhou Lian Shun Tong Water Pipe Company Limited* ("Danzhou Lian Shun Tong"), Onfar International Limited ("Onfar"), Jining City Haiyuan Water Treatment Company Limited* ("Jining Haiyuan") and Anhui Dang Shan Water Industry Company Ltd* ("Anhui Dang Shan") was allocated to the CGU of provision of water supply and sewage treatment. Goodwill from acquisition of iMerchants was allocated to the CGU of investments in financial products. Goodwill from acquisition of Plenty One Limited ("Plenty One"), a subsidiary of iMerchants was allocated to the CGU of others.

During the year ended 31 December 2010, the Group recognised an impairment loss with an aggregate amount of HK$40,258,000 (2009: HK$98,685,000) in relation to goodwill arising on acquisition of Blue Mountain and Onfar (2009: Danzhou Lian Shun Tong, Onfar, Jining Haiyuan, Anhui Dang Shan and Plenty One) which are allocated to the CGUs of provision of water supply and sewage treatment (2009: water supply and sewage treatment and investment products and others).

During the year ended 31 December 2010, the Group's equity interest in iMerchants was diluted and the Company's investment in iMerchants were changed from investments in a subsidiary to investment in an associate. Details of which are disclosed in note 12. The goodwill allocated to the CGU of investments in financial products and others were released for the calculation of loss on deemed disposal of a subsidiary (note 43).

The basis of the recoverable amount of the CGUs and the major underlying assumptions are summarised below:

Water supply and sewage treatment

The recoverable amount of this CGU has been determined on the basis of value-in-use calculation with reference to a valuation performed by Asset Appraisal. That calculation uses cash flow projections based on financial budgets approved by management covering a 5 year periods, and discount rate of 11.28% (2009: 12.55%). Cash flows beyond the 5 year periods have been extrapolated using a steady 3% (2009: 3%) growth rate. This growth rate is based on the relevant industry growth forecasts and does not exceed the average long-term growth rate for the relevant industry. The directors of the Company were of the opinion that the recoverable amount is less than its respective carrying amount as at 31 December 2010, accordingly an impairment loss of approximately HK$40,258,000 (2009: HK$66,069,000) was recognised.

20. GOODWILL *(Continued)*

Investment in financial products

During the year ended 31 December 2009, the recoverable amount of this CGU was determined on the basis of value-in-use calculation. That calculation uses cash flow projections based on financial budgets approved by management covering a 5 year periods (the "Forecast"), and discount rate of 12.92% (2010: Nil). Cash flows beyond the 5 year periods was extrapolated using a steady 3% (2010: Nil) growth rate. The management determined the budgeted growth rate based on past performance and its expectation on the relevant industry growth forecasts and did not exceed the average long term growth rate for the relevant industry. The directors of the Company were of the opinion, based on the Forecast and with reference to the valuation performed by Grant Sherman Appraisal Limited, a qualified valuer not connected with the Group, that the recoverable amount of this CGU exceeded it carrying amount in the consolidated statement of financial position and no impairment loss of goodwill was necessary.

Others

The recoverable amount of this CGU was determined on the basis of value-in-use calculation with reference to a valuation performed by Asset Appraisal. That calculation used cash flow projections based on financial budgets approved by management covering a 5 year periods, and discount rate of 17.58% (2010: Nil). Cash flows beyond the 5 year periods had been extrapolated using a steady 3% (2010: Nil) growth rate. This growth rate was based on the relevant industry growth forecasts and did not exceed the average long-term growth rate for the relevant industry. The directors of the Company were of the opinion that the recoverable amount was less than its respective carrying amount as at 31 December 2009, accordingly an impairment loss of approximately HK$32,616,000 (2010: Nil) was recognised.

21. AVAILABLE-FOR-SALE INVESTMENTS

	2010 ***HK$'000***	2009 *HK$'000*
Available-for-sale investments comprise:		
– Equity securities listed in Hong Kong	**29,898**	65,040

The fair values of the above listed securities are determined based on the quoted market bid prices available on the Stock Exchange. The directors considered the prolonged decrease in market price of the Hong Kong listed securities and an impairment loss of HK$30,502,000 (2009: Nil) was recognised for the year ended 31 December 2010.

22. INTEREST IN ASSOCIATES

	2010 HK$'000	2009 HK$'000
Cost of investment in associates		
Listed in Hong Kong *(Note 43)*	**308,949**	–
Loss on deemed partial disposal of an associate	**(79,449)**	–
	229,500	–
Unlisted associate in the PRC	**52,794**	52,794
Share of post-acquisition results and other comprehensive income, net of dividends received	**(887)**	5,059
	281,407	57,853
Fair value of listed investments	**216,551**	–

As at 31 December 2010 and 2009, the Group had interests in the following associate:

Name of entity	Form of business structure	Place of establishment	Proportion of equity interests held by the Group 2010	Proportion of equity interests held by the Group 2009	Principal activity
Jinan Hongquan Water Production Co., Ltd 濟南泓泉制水有限公司 ("Jinan Hongquan")	Incorporated	PRC	**35%**	35%	Provision of water supply
iMerchants	Incorporated	British Virgin Islands ("BVI")	**36.57%**	N/A	Investment in financial and investment products and technology investment

22. INTEREST IN ASSOCIATES *(Continued)*

The summarised financial information in respect of the Group's associates as at the end of the reporting period is set out below:

	2010 **HK$'000**	2009 HK$'000
Total assets	**1,223,616**	338,569
Total liabilities	**(415,948)**	(173,274)
Net assets	**807,668**	165,295
Group's share of net assets of associate	**292,694**	57,853
Revenue	**280,547**	273,921
(Loss) profit for the period/year	**(22,246)**	6,238
Group's share of results of associate for the period/year	**(8,109)**	2,183

As disclosed in note 12 to the consolidated financial statements, iMerchants became an associate of the Group in October 2010.

In October 2010, the holders of 1,691,000,000 Convertible Preference Shares exercised their rights to convert the Convertible Preference Shares into fully paid ordinary shares of iMerchants. After this deemed disposal, the equity interest of iMerchants owned by the Group has reduced further from 49.23% to 36.57%. The loss of approximately HK$79,449,000 being the decrease in the interest in associate of approximately HK$79,449,000, was recognised in the statement of consolidated comprehensive income.

23. DEPOSIT PAID FOR ACQUISITION OF SUBSIDIARIES

On 18 September 2009, Swift Surplus, a wholly-owned subsidiary of the Group, entered into an agreement with independent third parties, Sihui South China Waterworks Development Co., Ltd.* (四會市華南水務發展有限公司), Shenzhen City South China Waterworks Group Co., Ltd.* (深圳市華南水務集團有限公司) and Da Xin Waterworks Management (Huizhou) Co., Ltd.* (達信水務管理（惠州）有限公司), (collectively referred to as "Vendors"), pursuant to which Swift Surplus has conditionally agreed to acquire 70% of the registered capital of Foshan City Gaoming Huaxin Sewage Treatment Company Ltd.* (佛山市高明區華信污水處理有限公司); 70% of the registered capital of Tangshan City Hongxiang Waterworks Limited* (唐山市鴻翔水務有限公司) and 100% equity interests in Boluo phase II Project Company (博羅二期項目公司), respectively, at a total consideration of HK$170,000,000 (the "Acquisition"). As at 31 December 2009, the Group has paid HK$50,901,000 as a deposit for the acquisition and the remaining amount will be paid upon the completion of the transaction. Details of this transaction are stated in the Company's announcement dated 20 September 2009. On 29 November 2010, Swift Surplus entered into a termination agreement with the Vendor and the deposit paid of HK$50,901,000 was assigned as a loan to the holding company of the Vendor, Top Vision Management Limited ("Top Vision"). The amount was then reclassified to loan receivable during the year. Details of the termination of the acquisition are stated in the Company's announcement dated 29 November 2010.

24. INVENTORIES

	2010 HK$'000	2009 HK$'000
Raw materials	772	228
Finished goods	25,976	13,076
	26,748	13,304

25. TRADE AND OTHER RECEIVABLES

	2010 HK$'000	2009 HK$'000
Trade receivables	16,219	14,983
Less: impairment loss recognised	(5,246)	(5,807)
	10,973	9,176
Other receivables	22,754	53,594
Less: impairment loss recognised	(8,903)	(8,680)
	13,851	44,914
Loans receivables	129,480	23,025
Less: impairment loss recognised	(5,720)	(5,720)
	123,760	17,305
Deposits and prepayments	316	3,205
	148,900	74,600

Included in the loans receivables was an amount of HK$68,206,000 (2009: HK$23,025,000) due from Top Vision Management Ltd ("Top Vision"). The aforesaid balance included approximately HK$50,901,000 was transferred from the deposit paid for acquisition of subsidiaries during the year ended 31 December 2010, details are set out in note 23. The amount is unsecured, interest-free and repayable on demand. The remaining balance of HK$55,554,000 (2009: Nil) represents loan to other independent third parties which were unsecured, repayable within one year and carry interest at 5% per annum.

As at 31 December 2009, included in other receivables is an amount due from Construction Bureau of Yingtan City (鷹潭市建設局) of approximately HK$22,770,000 (equivalent to RMB20,000,000) which are unsecured, carrying on interest of 12% per annum and repayable on demand. The amount has been fully settled during the year ended 31 December 2010.

25. TRADE AND OTHER RECEIVABLES *(Continued)*

The Group allows an average credit period of 30 days to 180 days to its customers.

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

	2010	2009
	HK$'000	*HK$'000*
Within 90 days	**6,517**	3,537
91 to 180 days	**3,537**	4,889
181 to 365 days	**807**	710
Over 1 year	**112**	40
	10,973	9,176

Included in the Group's trade receivable balance are debtors with aggregate carrying amount of HK$1,267,000 (2009: HK$1,858,000) which were past due at the end of the reporting period and for which the Group has not provided for impairment loss. Ageing of trade receivables which are past due but not impaired:

	2010	2009
	HK$'000	*HK$'000*
Within 90 days	**918**	939
91 to 180 days	**136**	169
181 to 365 days	**213**	710
Over 1 year	**–**	40
Total	**1,267**	1,858

Trade receivables that were neither past due nor impaired relate to a wide range of customers for whom there was no recent history of default. The Group does not hold any collateral over these balances.

Trade receivables that were past due but not impaired related to a number of independent customers that have a good track record with the Group. Based on past experience, management believes that no impairment allowance is necessary in respect of these balances as there has not been a significant change in credit quality and the balance are still considered fully recoverable.

25. TRADE AND OTHER RECEIVABLES *(Continued)*

The movements in impairment loss of trade receivables were as follows:

	2010	2009
	HK$'000	*HK$'000*
Balance at beginning of the year	**5,807**	4,754
Deemed disposal of a subsidiary	**(1,246)**	–
Impairment loss recognised	**1,299**	1,006
Reversal of impairment loss	**(921)**	–
Exchange realignment	**307**	47
Balance at end of the year	**5,246**	5,807

Included in the impairment loss are individually impaired trade receivables with an aggregate balance of HK$5,246,000 (2009: HK$5,807,000) which are due to long outstanding. The Group does not hold any collateral over these balances.

The movements in impairment loss of other receivables were as follows:

	2010	2009
	HK$'000	*HK$'000*
Balance at beginning of the year	**8,680**	6,931
Impairment loss recognised	**–**	1,718
Amounts written off as uncollectible	**–**	(10)
Exchange realignment	**223**	41
Balance at end of the year	**8,903**	8,680

Included in the impairment loss are individually impaired other receivables with an aggregate balance of HK$8,903,000 (2009: HK$8,680,000) which are due to long outstanding. The Group does not hold any collateral over these balances.

During the year ended 31 December 2009, other receivables with an amount of HK$2,807,000 (2010: Nil) was written off directly due to the directors of the Company considered the recovery of the respective debtors were remote and irrecoverable.

26. CASH HELD AT FINANCIAL INSTITUTIONS/BANK BALANCES AND CASH

Cash held at financial institutions represents amounts of approximately HK$37,724,000 (2009: HK$212,474,000) deposited in financial institutions in Hong Kong carry interest rate ranging from 0% to 0.001% (2009: 0% to 0.001%) per annum.

Bank balances and cash comprise cash held by the Group and short-term bank deposits with an original maturity of three months or less. The deposits carry interest at prevailing market rates.

27. TRADE AND OTHER PAYABLES

The following is an aged analysis of trade payables at the end of reporting period, based on invoice date:

	2010 HK$'000	2009 HK$'000
Within 30 days	6,237	5,067
31 to 90 days	518	1,907
91 to 180 days	713	555
181 to 365 days	611	587
Over 1 year	1,018	2,464
	9,097	10,580
Other payables	79,309	61,323
Interest payables	75,166	67,056
	163,572	138,959

There was no specific credit period for payment granted by suppliers. The Group has financial risk management policies in place to ensure that all payables are settled within the timeframe agreed with the respective suppliers.

As at 31 December 2009, included in other payables with an amount of HK$1,100,000 (2010: Nil) was the deferred consideration payable arising from the acquisition of an intangible asset through acquisition of a subsidiary (note 41). The amount is required to settle within 6 months since the completion date of the acquisition.

28. AMOUNTS DUE FROM/(TO) CUSTOMERS FOR CONTRACT WORKS

	2010 HK$'000	2009 HK$'000
Contracts in progress at the end of reporting period:		
Contract costs incurred plus recognised profits to date	45,674	24,222
Less: progress billings	(27,402)	(13,995)
	18,272	10,227
Analysed for reporting purposes as:		
Amounts due from contract customers	18,864	10,884
Amounts due to contract customers	(592)	(657)
	18,272	10,227

At 31 December 2010, there were no retentions held by customers for contract work (2009: Nil).

29. BANK BORROWINGS

	2010 HK$'000	2009 HK$'000
Secured loans	**55,493**	56,926
Carrying amount repayable:		
On demand overdue balances *(notes (ii))*	**30,698**	29,601
On demand or within one year	**3,542**	3,416
More than one year but not exceeding two years	**3,542**	3,417
More than two years but not more than five years	**10,246**	10,246
More than five years	**7,465**	10,246
	55,493	56,926
Less: Amount due within one year shown under current liabilities	**(34,240)**	(33,017)
Amount due after one year	**21,253**	23,909

Notes:

(i) As at 31 December 2010, included in bank borrowings of approximately HK$24,795,000 (equivalent to RMB21,000,000) (2009: HK$27,325,000, equivalent to RMB24,000,000) which carries interest at Peoples' Bank of China Base Lending Rate plus 10% per annum and secured by a pledge over the subsidiary's revenue from the provision of sewage treatment.

(ii) As at 31 December 2010, in respect of bank borrowings with carrying amounts of approximately HK$30,698,000 (equivalent to RMB26,000,000) (2009: HK$29,601,000, equivalent to RMB26,000,000) borrowed from Agricultural Bank of China, Danzhou Branch, are overdue and are classified as current liabilities (the "Overdue Loans"). The Overdue Loans were arisen from the acquisition of a business on 31 March 2008. The Overdue Loans are secured floating-rate borrowings which carry interest at the People's Bank of China Base Lending Rate. Pursuant to the respective loan agreements, the Group is subject to additional interests for the overdue amounts which are calculated based on the overdue interest rate published by the People's Bank of China. On 26 June 2008, Agricultural Bank of China, Danzhou Branch had filed a claim against the Group for the repayment of the Overdue Loans together with the interests thereon. On 13 November 2009, a verdict was issued by the Intermediate People's Court of Hainan (the "Court"), the Group is ordered to fully repay the said bank borrowings together with the interests thereon. Details of the litigation are set out in note 51.

30. OTHER LOANS

	2010 HK$'000	2009 HK$'000
Other loans comprises of:		
Government loans *(note i)*	**80,825**	70,062
Loans from independent companies and non-bank institutions *(note ii and iii)*	**1,824**	4,099
Overdue loans *(note ii and iii)*	**4,723**	4,554
	87,372	78,715
Analysed as:		
Secured	**4,723**	6,831
Unsecured	**82,649**	71,884
	87,372	78,715
Carrying amount repayable:		
On demand overdue loans	**4,723**	4,554
On demand or within one year	**35,162**	29,259
More than one year but not exceeding two years	**7,943**	9,108
More than two years but not more than five years	**26,340**	24,431
More than five years	**13,204**	11,363
	87,372	78,715
Less: Amount due within one year shown under current liabilities	**(39,885)**	(33,813)
Amount due after one year	**47,487**	44,902

Notes:

(i) As at 31 December 2010, government loans of approximately HK$60,903,000 (2009: HK$59,725,000), HK$17,923,000 (2009: HK$9,148,000) and HK$1,999,000 (2009: HK$1,189,000) are fixed-rate borrowings, floating-rate borrowings and interest-free borrowings, respectively. The fixed-rate borrowings carry interest ranging from 2.28% to 5% (2009: 2.28% to 5%) per annum and the floating-rate borrowings carry interest at fixed deposit rate as stipulated by the People's Bank of China plus 0.3% per annum for the two years ended 31 December 2010. The government loans are repayable ranging from within one year to twelve years.

(ii) At 31 December 2010, loans from independent companies and non-bank institutions and overdue loans with an aggregate amount of approximately HK$6,547,000 (2009: HK$8,653,000) are fixed-rate borrowings carry interest ranging from 6% to 21.970% (2009: 6% to 21.970%) per annum.

(iii) At 31 December 2010, overdue loans with carrying amounts of approximately HK$4,723,000 (equivalent to RMB4,000,000) (2009: HK$4,554,000, equivalent to RMB4,000,000) and interest payable (included in other payables) of approximately HK$13,628,000 (2009: HK$12,140,000) are overdue and are classified as current liabilities (the "Overdue Other Loans"). According to the legal advice to the Company, the original lender has disposed of the rights of the Overdue Other Loans through an auction in the PRC during the year ended 31 December 2010. Up to the date of approval of this consolidated financial statements, the new owner of the Overdue Other Loans has not communicated with the Group on the settlement arrangement.

31. AMOUNTS DUE TO NON-CONTROLLING SHAREHOLDERS OF A SUBSIDIARY

The amounts are unsecured, other than an amount of approximately HK$2,587,000 (2009: HK$2,457,000) carries interest at 11.68% (2009: 14.88%) per annum, the remaining amounts are interest-free and are repayable on demand.

32. LOAN FROM AN ASSOCIATE

As at 31 December 2010, the amount of approximately HK$2,419,000 represented the loan from an associate and carried interest at 4.86% per annum and repayable within a year.

33. CONVERTIBLE BONDS

On 3 August 2007, the Company issued a redeemable convertible bonds ("CB1") in an aggregate principal amounts of HK$385,000,000. CB1 bears interest at the rate of 0.25% per annum, starting from 3 August 2007, payable semi-annually in arrear on 3 February and August each year. CB1 may be converted at the option of the CB1 holders at a conversion price of HK$1.42 per ordinary share at any time on or after 13 September 2007 and up to 27 July 2012.

The conversion price was subsequently adjusted to HK$1.136 on 3 February 2008 in accordance with the terms and conditions stated in the bond purchase agreement dated 30 July 2007.

On 3 August 2010 (the "Put Option Date"), all holders of CB1 exercised their rights to request the Company to redeem all of the CB1 at 132.21% of the principal amount together with interest accrued. Subsequently, the Company reached consensual agreements with all CB1 holders to restructure the Company's rights and obligation under the CB1 in the following manners:

Issue of new convertible bonds

On 13 August 2010, the Company entered into a definitive agreement (the "Definitive Agreement 1") with investors who collectively holding approximately 79% of CB1 (the "Majority Investors"). New convertible bonds due 2012 in the aggregate principal amount of HK$337,000,000 ("CB2") were issued as a consideration of settling the Majority Investors' interests in CB1. In relation to the aggregate principal amount of CB2, a portion of HK$175,000,000 ("Repurchase Bonds") cannot be converted into ordinary share of the Company, redeemed or disposed of, which will be repurchased by the Company in instalments. This part is included in the liability portion of CB2.

The remaining portion of CB2 with principal amount of HK$162,000,000 may be converted at the option of the CB2 holders at a conversion price of HK$0.15 per ordinary share at any time on or after 15 October 2010 and up to the close of business on 9 August 2012.

Unless previously redeemed, converted or purchased, the Company will redeem CB2 (excluding the Repurchasing Bonds), at 121.0119% of its principal amount on 16 August 2012 plus interest accrued.

The holder of each CB2 will have the right at such holder's option, to require the Company to redeem all or some only of CB2 (excluding the Repurchasing Bonds) on 16 August 2011 at 109.9938% of their principal amount together with accrued interest.

33. CONVERTIBLE BONDS *(Continued)*

Issue of new convertible bonds *(Continued)*

The Company has an early redemption option to redeem all or some only of the CB2 (excluding the Repurchasing Bonds) on or at any time prior to 16 August 2012 by serving a 15 days' prior written notice at a redemption price equal to, in the case of the redemption date falls before 16 August 2011, 133% of the principal amount of the CB2 together with accrued interest up to the redemption date or, in the case where the redemption date falls after 16 August 2011, 166% of the principal amount of the CB2 together with accrued interest up to the redemption date. The fair values of such early redemption option at the date of recognition and at 31 December 2010 of CB2 are approximately HK$14,374,000 and HK$10,239,000 respectively.

Restructuring of the CB1

On 24 September 2010, the Company entered into another definitive agreement (the "Definitive Agreement 2") with investors who collectively holding the remaining approximately 21% of CB1 (the "Minority Investors"). Pursuant to the Definitive Agreement 2, the terms and conditions of the CB1 will be restructured with the following key terms:

1. Redemptions by instalments: The CB1 held by the Minority Investors will be redeemed for a total consideration of approximately HK$128,000,000 in cash (excluding interest costs and discounts for early repayment), payable in a series of instalments commencing from October 2010 and ending in July 2012.

2. Revised maturity date: The original maturity date, being 3 August 2012, has been brought forward to 31 July 2012.

3. Removal of the Company Sweep-up call option: The Company's sweep-up call option to early redeem CB1 if and when at least 90% of the CB1 had already been converted, redeemed or purchased and cancelled has be removed.

4. Revised further indebtedness covenant: The original limitation on further indebtedness has been revised so that as long as the CB2 is outstanding, the Group should not incur any further debts for which there is any recourse to the Company without the prior written consent of the holders representing over 50% in principal amount of the CB1 then outstanding.

Save for abovementioned key terms, the CB1 will substantially have the same terms and conditions stated in the bond purchase agreement dated 30 July 2007 and in particular, the prevailing conversion price for CB1 remains at HK$1.136 and the existing conversion price adjustments have been preserved.

Further details of the Definitive Agreement 1 and Definitive Agreement 2 are set out in the circular and the announcement of the Company dated 3 September 2010 and 24 September 2010 respectively.

33. CONVERTIBLE BONDS *(Continued)*

CB1

Since the conversion price for the CB1 is subject to change in accordance with the terms and condition, the conversion will not result in settlement by the exchange of a fixed number of equity instruments. The CB1 was designated as "financial liabilities at fair value through profit or loss" which requires that CB1 to be carried at fair value at the end of the reporting period and the changes in fair values are recognised in the consolidated statement of comprehensive income.

In August 2010, the Company paid approximately HK$64,060,000 in cash and issued CB2 of approximately HK$337,000,000 for extinguishment of CB1. Further details are set out in the announcement of the Company dated 30 September 2010.

Movement of CB1 is as follows:

	2010	*2009*
	HK$'000	*HK$'000*
At the beginning of the year	**466,739**	262,335
Extinguishment loss of convertible bonds	**1,521**	–
Repayment	**(64,060)**	–
Extinguishment of CB1 and recognition of CB2	**(337,000)**	–
Change in fair value	**28,326**	204,404
At the end of the year	**95,526**	466,739

CB2

The CB2 contains the following components that are required to be separately accounted for:

(i) Liability component for the CB2 represents the present value of the contractually determined stream of future cash flows discounted at the rate interest at the date of issue with reference to the market rate for instruments of comparable credit status taking into account the credit risk of the Company as well as the amount of the CB2, but without the conversion portion. The effect interest rate of the liability component is 1% per annum.

(ii) Embedded derivative comprises of the fair value of redemption option represents the Company's option to early redeem all or part of the Convertible Bond.

(iii) The equity component represents the difference between the gross proceeds of the issue of the CB2 and the fair value assigned to the liability and early redemption option components respectively.

33. CONVERTIBLE BONDS *(Continued)*

CB2 *(Continued)*

Movement of CB2 is as follows:

	Equity component HK$'000	Liability component HK$'000	Early redemption option HK$'000	Total HK$'000
Extinguishment of CB1 and recognition of CB2	15,914	335,460	(14,374)	337,000
Imputed interest charged	–	201	–	201
Change in fair value	–	–	4,135	4,135
Cash paid for redemption	–	(41,542)	–	(41,542)
Loss on redemption	–	10,542	–	10,542
At the end of the year	15,914	304,661	(10,239)	310,336

During the year ended 31 December 2010, the Company has redeemed HK$31,000,000 of Repurchase Bonds, as a result, loss of redemption of approximately HK$10,542,000 has been recognised.

The fair value of approximately HK$95,526,000 (2009: HK$466,739,000) of CB1 is determined taking into account a valuation carried out by Asset Appraisal, using Monte Carlo Simulation Model.

The fair value of CB1 at the end of each reporting period was calculated using the market value basis. Major parameters adopted in the calculation of the fair value are summarised below:

	2010	2009
Stock price	**HK$0.136**	HK$0.232
Exercise price	**Subject to adjustment but not less than 80% of HK$1.42**	Subject to adjustment but not less than 80% of HK$1.42
Expected volatility	**52.42%**	53.02%
Risk-free rate	**0.49%**	1.117%
Option life	**1.59 years**	2.59 years

The fair value of derivative financial instruments of CB2 approximately HK$14,374,000 and HK$10,239,000 as at date of inception and 31 December 2010 respectively are determined taking into account a valuation carried out by Asset Appraisal, using Binomial model.

33. CONVERTIBLE BONDS *(Continued)*

CB2 *(Continued)*

The fair value of the conversion option derivative component of CB2 at the end of each reporting period was calculated using the market value basis. Major parameters adopted in the calculation of the fair value are summarised below:

	31 December 2010	**Date of inception**
Stock price	**HK$0.136**	HK$0.124
Exercise price	**HK$0.15**	HK$0.15
Expected volatility	**56.351%**	68.663%
Risk-free rate	**0.49%**	0.48%
Option life	**1.63 years**	1.88 years

The following is the analysis of CB1 and CB2 for financial reporting purposes:

	2010 **HK$'000**	2009 *HK$'000*
Financial liabilities at fair value through profit or loss		
CB1	**95,526**	466,739
Financial liabilities at amortised cost		
Liability component of CB2	**304,661**	–
Analysed as:		
Current liabilities	**301,661**	–
Non-current liabilities	**3,000**	–
	304,661	–
Derivative financial instruments		
Early redemption option	**10,239**	–
Equity element		
Convertible bond equity reserve	**15,914**	–

34. SHARE CAPITAL

	2010 Number of shares	2010 Amount HK$'000	2009 Number of shares	2009 Amount HK$'000
Authorised:				
Ordinary shares of HK$0.1 each				
At the beginning of the year	**10,000,000,000**	**1,000,000**	4,000,000,000	400,000
Increase during the year *(note 1)*	**–**	**–**	4,000,000,000	400,000
	10,000,000,000	**1,000,000**	8,000,000,000	800,000
Convertible preference shares of HK$0.1 each *(note 1)*	**–**	**–**	2,000,000,000	200,000
	10,000,000,000	**1,000,000**	10,000,000,000	1,000,000
Issued and fully paid:				
Ordinary shares of HK$0.1 each				
At the beginning of the year	**2,706,379,000**	**270,638**	1,890,900,000	189,090
Issue of shares *(note 2)*	**–**	**–**	815,479,000	81,548
Issue of shares upon top–up placing *(note 3)*	**265,476,000**	**26,547**	–	–
Issue of shares upon placing *(note 4)*	**275,796,000**	**27,580**	–	–
At the end of the year	**3,247,651,000**	**324,765**	2,706,379,000	270,638

34. SHARE CAPITAL *(Continued)*

Notes:

1. Pursuant to an ordinary resolution passed at the annual general meeting held on 29 June 2009, the Company's authorised share capital was increased from HK$400,000,000 to HK$1,000,000,000 by the creating of 4,000,000,000 ordinary shares of HK$0.1 each and 2,000,000,000 convertible preference shares of HK$0.1 each.

2. On 19 June 2009, pursuant to a placing and subscription agreement entered into with existing shareholders, the Company placed out 365,000,000 new ordinary shares of HK$0.1 each in the Company at a price of HK$0.33 per share. A sum of net amount approximately HK$116,906,000 after deducting related expenses of approximately HK$3,544,000, was raised and used as working capital of the Group.

   On 6 August 2009, pursuant to a placing and subscription agreement entered into with existing shareholders, the Company placed out 450,479,000 new ordinary shares of HK$0.1 each in the Company at a price of HK$0.295 per share. A sum of net amount approximately HK$128,990,000 after deducting related expenses of approximately HK$3,901,000, was raised and used as working capital of the Group.

3. On 9 August 2010, pursuant to a placing and subscription agreement entered into with existing shareholders, the Company placed out 265,476,000 new ordinary share of HK$0.1 each in the Company at a price of HK$0.108 per share. A sum of net amount approximately HK$27,851,000 after deducting related expenses of approximately HK$820,000, was raised and used as working capital of the Group.

4. On 9 August 2010, pursuant to a placing and subscription agreement entered into with existing shareholders, the Company placed out 275,796,000 new ordinary share of HK$0.1 each in the Company at a price of HK$0.108 per share. A sum of net amount approximately HK$29,041,000 after deducting related expenses of approximately HK$745,000, was raised and used as working capital of the Group.

   All new shares issued during the year ended 31 December 2010 rank pari passu in all respects with other shares in issue.

35. NON-REDEEMABLE CONVERTIBLE PREFERENCE SHARES OF A SUBSIDIARY

	Number of shares	Amount
	'000	*HK$'000*
Authorised:		
At 1 January 2009, 31 December 2009 and 1 January 2010		
Non-redeemable convertible preference shares of HK$0.2 each	4,000,000	800,000
Subdivision of share of HK$0.2 each into five shares of HK$0.04 each *(note i)*	16,000,000	–
Disposal of a subsidiary	(20,000,000)	(800,000)
At 31 December 2010, HK$0.04 each	**–**	**–**
Issued and fully paid:		
At 1 January 2009	–	–
Issue of preference shares of a subsidiary, HK$0.2 each	2,938,478	587,696
Subdivision of share of HK$0.2 each into five shares of HK$0.04 each *(note i)*	11,753,912	–
At 31 December 2009 and 1 January 2010	14,692,390	587,696
Redeemed during the year	(17,600)	(17,600)
Deemed disposal of a subsidiary *(note 43)*	(14,674,790)	(570,096)
At 31 December 2010, HK$0.04 each	**–**	**–**

Note i: Pursuant to an ordinary resolution passed by the iMerchants' shareholders at an extraordinary general meeting held on 30 October 2009, the existing issued and unissued for both ordinary and non-redeemable convertible preference shares of HK$0.2 each in the share capital of iMerchants are subdivided into 5 shares of HK$0.04 each. The authorised share capital of iMerchants was remained at HK$1,200,000,000. The share subdivision took place on 2 November 2009.

On 23 October 2009, iMerchants issued approximately 2,938,478,000 non-redeemable convertible preference shares with a par value of HK$0.2 each, as a partial consideration for the acquisition of an intangible asset through acquisition of a subsidiary (note 41).

The valuation of the convertible preference shares was carried out by Grant Sherman Appraisal Limited, an independent qualified professional valuer not connected to the Group. The inputs for the calculation of the fair value were a blockage discount rate of 40% on convertible preference shares based on the restriction that the convertible preference shares cannot be converted into ordinary shares immediately. The variables and assumptions used in computing the fair value of the convertible preference shares are based on the directors' best estimate.

35. NON-REDEEMABLE CONVERTIBLE PREFERENCE SHARES OF A SUBSIDIARY *(Continued)*

The fair value of the convertible preference shares as at 23 October 2009 amounted to approximately HK$567,126,000, representing HK$0.193 per convertible preference share. The amount of shortage was approximately HK$20,570,000 which represented the fair value was less than the par value of the non-redeemable convertible preference shares, is charged to the special capital reserves in the equity of iMerchants.

The non-redeemable convertible preference shares can be converted into ordinary shares of iMerchants at HK$0.2 per share (subject to adjustment). The conversion price was subsequently adjusted to HK$0.04 per share as a result of the share subdivision by an ordinary resolution in an extraordinary general meeting of iMerchants held on 30 October 2009. The major terms of the above-mentioned convertible preference shares are set out below:

(1) The convertible preference share holders has the right, exercisable at any time perpetual as from the date of issue, to convert the preference shares into fully paid ordinary shares, provided that (i) any conversion of the convertible preference shares does not trigger a mandatory offer obligation under Rule 36 of the Hong Kong Code on Takeovers and Mergers; (ii) the number of shares to be allotted and issued upon the exercise of the conversion rights attaching to the convertible preference shares, in aggregate with the new ordinary shares issued and new ordinary shares to be issued upon the exercise of the conversion rights attaching to the convertible bonds as held by the holders and parties acting in concert with it, represents not more than 9.9% of the then issued ordinary share capital of iMerchants; and/or (iii) the public float of the shares of iMerchants shall not less than 15% of the shares of iMerchants at any time.

(2) The convertible preference shares are transferable other than to connected persons, as defined under the Listing Rules of the GEM, of iMerchants and do not carry the right to vote. The convertible preference shares holders shall not be entitled to any dividend nor distribution.

(3) The convertible preference shares shall rank pari passu with any and all current and future preferred equity securities of the Company.

(4) The convertible preference shares are non-redeemable.

Based on their terms and conditions, the convertible preference shares have been classified as equity instrument in the consolidated statement of financial position of iMerchants.

36. CONVERTIBLE BONDS OF A SUBSIDIARY

On 23 October 2009, iMerchants issued zero-couple convertible bonds ("CB3") with an aggregate principal amount of HK$200,000,000 to vendors as a partial consideration for the acquisition of an intangible asset through acquisition of a subsidiary (note 41). CB3 entitled the holders to convert the bonds into ordinary shares of iMerchants at any time between the date of issue of the bonds and their settlement date on 23 October 2014 in multiples of HK$1,000,000 at the conversion price of HK$0.2 (subject to adjustment) per conversion share. The conversion price was subsequently adjusted to HK$0.04 per share as a result of the share subdivision of iMerchants on 30 October 2010. No conversion shall be made, if immediately upon such conversion, the bondholder and its parties acting in concert with in aggregate hold more than 9.9% of the issued share capital of iMerchants from time to time; and/or the public float of iMerchants' shares was less than 15% of the total issued shares of iMerchants. iMerchants has an early redemption option to redeem in whole or in part at par before the maturity date by serving seven days' prior written notice, any amount of the bonds remains outstanding on the maturity date shall be redeemed at its then outstanding amount. The fair value of such early redemption option at the date of issue and subsequent reporting period was insignificant.

The convertible bonds contain two components, liability and equity elements. The equity element was presented as part of non-controlling interests heading "equity component of convertible bonds of a subsidiary". The effective interest rate of the liability component was 11.52% per annum.

CB3 was disposed of along with the deemed disposal of iMerchants. Details are set out in note 43.

The movement of liability component in respect of CB3 is as follows:

	HK$'000
At date of issue	115,955
Imputed interest charged	2,472
At 31 December 2009	118,427
Imputed interest charged	10,204
Deemed disposal of a subsidiary *(note 43)*	(128,631)
At 31 December 2010	**–**

37. GOVERNMENT GRANTS

	HK$'000
At 1 January 2009	55,763
Addition	3,766
Exchange realignment	511
At 31 December 2009 and 1 January 2010	60,040
Addition	3,285
Exchange realignment	749
At 31 December 2010	**64,074**

Yichun Water has been granted by the local government of the PRC for the expansion and construction of water plants and pipelines. As at 31 December 2010 and 2009, the construction of water plants and pipelines was in progress.

38. DEFERRED TAX LIABILITIES

The following are the major deferred tax liabilities recognised and movements thereon during the current and prior years:

	Withholding tax on undistributed profits HK$'000	Service concession arrangement HK$'000	Total HK$'000
At 1 January 2009	1,321	3,043	4,364
Charge to consolidated statement of comprehensive income for the year	741	1,097	1,838
Release upon disposal of subsidiaries	(168)	(637)	(805)
At 31 December 2009 and 1 January 2010	1,894	3,503	5,397
Charge to consolidated statement of comprehensive income for the year	1,141	1,743	2,884
At 31 December 2010	**3,035**	**5,246**	**8,281**

38. DEFERRED TAX LIABILITIES *(Continued)*

At 31 December 2009, the Group had unused tax losses of HK$82,732,000 (2010: Nil) available to offset against future profits. No deferred tax asset has been recognised in respect of such losses due to the unpredictability of future profit streams.

At 31 December 2010, the Group also has other deductible temporary differences of approximately HK$21,651,000 (2009: HK$21,889,000). No deferred tax asset has been recognised in relation to such deductible temporary differences as it is not probable that taxable profit will be available against which the deductible temporary differences can be utilised.

Under the EIT law of PRC, withholding tax is imposed on dividend declared in respect of profits earned by PRC subsidiaries from 1 January 2008 onwards. For investors incorporated in Hong Kong which hold at least 25% of equity interest of those PRC companies, a preferential rate of 5% will be applied. Deferred tax has been provided for in respect of the temporary difference attributable to such profits amounting to approximately HK$60,700,000 (2009: HK$37,880,000). The Group has applied the preferential rate of 5% as all the Group's subsidiaries and an associate in the PRC are directly held by an investment holding company incorporated in Hong Kong. No deferred tax liability has been provided for the remaining of such profits of approximately HK$875,000 (2009: HK$1,123,000) as the Group is able to control the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

39. CAPITAL RISK MANAGEMENT

The Group manages its capital to ensure that entities in the Group will be able to continue as a going concern while maximising the return to stakeholders through the optimisation of the debt and equity balance.

The capital structure of the Group consists of debt, which includes various types of borrowings, cash and cash equivalents and equity attributable to equity holders of the Company, comprising issued share capital, reserves and accumulated losses.

The directors of the Company review the capital structure regularly. As part of this review, the directors of the Company consider the cost of capital and the risks associated with each class of capital. Based on the recommendations of the directors, the Group will balance its overall capital structure through the raise of bank borrowings and new shares issued.

40. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

(a) Categories of financial instruments

	2010 HK$'000	2009 HK$'000
Financial assets		
– Financial assets through profit or loss	**10,239**	–
– Loans and receivables (including cash and cash equivalents)	**305,463**	360,136
– Available-for-sale investments	**29,898**	65,040
Financial liabilities		
– At amortised cost	**577,577**	378,686
– At fair value through profit and loss	**95,526**	466,739

(b) Financial risk management objectives and policies

The Group's major financial instruments include trade and other receivables, cash held at financial institutions, bank balances and cash, trade and other payables, amount due to a non-controlling shareholder of a subsidiary, bank borrowings, other loans, loans from an associate and convertible bonds of a subsidiary. Details of these financial instruments are disclosed in respective notes. The risks associated with these financial instruments and the policies on how to mitigate these risks are set out below. The management manages and monitors these exposures to ensure appropriate measures are implemented on a timely and effective manner.

Market risk

Currency risk

Other than the subsidiaries established in the PRC whose functional currency is RMB, the Company and subsidiaries' functional currency is HK$. However, certain bank balances, cash held in financial institutions and other receivables are denominated in currencies other than HK$. Foreign currencies are also used to settle expenses for overseas operations.

	As at 31 December 2010		As at 31 December 2009	
	United States dollar ("USD")'000	RMB'000	USD'000	RMB'000
Assets	**95**	**16,250**	808	17,907

The Group currently does not have a foreign currency hedging policy but the management monitors foreign exchange exposure and will consider hedging significant foreign currency exposure should the needs arise.

40. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(Continued)*

(b) Financial risk management objectives and policies *(Continued)*

Market risk *(Continued)*

Currency risk (Continued)

The following table details the Group's sensitivity to a reasonably possible change of 5% in exchange rate of HK$ against each foreign currency while all other variables are held constant. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the end of each reporting period for a 5% (2009: 5%) change in foreign currency rates.

	USD		RMB	
	2010	2009	**2010**	2009
	HK$'000	*HK$'000*	***HK$'000***	*HK$'000*
Increase (decrease) in loss for the year, net of tax effect				
– if HK$ weakens against foreign currencies	**(31)**	(262)	**(801)**	(851)
– if HK$ strengthens against foreign currencies	**31**	262	**801**	851

A change of 5% (2009: 5%) in exchange rate of HK$ against each foreign currency does not affect other components of equity.

In management's opinion, the sensitivity analysis is not necessarily of the inherent foreign exchange risk as the year end exposure does not reflect the exposure during the year.

Interest rate risk

The Group is exposed to fair value interest rate risk in relation to fixed-rate loan receivables, other loans, amounts due to non-controlling shareholders of subsidiaries, loan from an associate (see notes 30, 31 and 32 for details) for the years ended 31 December 2010 and 2009. The Group currently does not have an interest rate hedging policy. However, the management monitors interest rate exposure and will consider other necessary actions when significant interest rate exposure is anticipated.

The Group was exposed to cash flow interest rate risk in relation to variable-rate bank borrowings and other loans (see notes 29 and 30 for details) for the year ended 31 December 2010 and 2009. It is the Group's policy to keep its borrowings at floating rate of interests so as to minimise the fair value interest rate risk.

40. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(Continued)*

(b) Financial risk management objectives and policies *(Continued)*

Interest rate risk *(Continued)*

The Group was also exposed to cash flow interest rate risk relates to bank balances and cash held at financial institutions carried at prevailing market rate. However, such exposure is minimal to the Group as the bank balance and cash held at financial institutions are all short-term in nature.

The Group's exposure to interest rate risk on financial liabilities are detailed in the liquidity risk management section of this note. The Group's cash flow interest rate risk is mainly concentrated on the fluctuation of the fixed deposit rate as stipulated by the People's Bank of China arising from the Group's RMB borrowings.

Sensitivity analysis

The sensitivity analysis below have been determined based on the exposure to interest rates for non-derivative instruments at the end of the reporting period. For variable-rate bank borrowings and other loans, the analysis is prepared assuming the amount of liability outstanding at the end of the reporting period was outstanding for the whole year.

If interest rates had been 50 basis points (2009: 50 basis points) higher/lower and all other variables were held constant, the Group's loss after tax for the year ended 31 December 2010 would increase/decrease by approximately HK$275,000 (2009: HK$252,000). This is mainly attributable to the Group's exposure to interest rates on its variable-rate bank borrowings and other loans.

Other price risk

The Group is exposed to equity price risk through its investments in listed equity securities. The managements manages this exposure by maintaining a portfolio of investments with different risks. The Group's equity price risk is mainly concentrated on equity instruments quoted in the Stock Exchange. In addition, the Group has a team to monitor the price risk and will consider hedging the risk exposure should the needs arise.

Sensitivity analysis

The sensitivity analyses below have been determined based on the exposure to equity price risks at the reporting date.

If the prices of the respective equity instruments had been 5% (2009: 5%) higher/lower, the investment revaluation reserve would increase/decrease by HK$1,495,000 (2009: HK$3,252,000) for the Group as a result of the changes in fair value of available-for-sale investments.

Equity price risk on convertible note

The Group is required to estimate the fair value of the conversion option component of the convertible bond at each end of the reporting period which therefore exposed the Group to equity security price risk.

40. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(Continued)*

(b) Financial risk management objectives and policies *(Continued)*

Interest rate risk *(Continued)*

Equity price sensitivity

The sensitivity analyses below have been determined based on the exposure to equity price risk at the reporting dates.

If the stock price inputted to the valuation model had been 5% (2009: 5%) higher/lower while all other variables were held constant, the loss for the year ended 31 December 2010 and would increase/decrease by approximately HK$1,510,000/HK$702,000 (2009: loss would decrease/increase by approximately HK$24,000/HK$101,000) for the Group, principally as a result of the changes in fair value of the convertible bond.

Credit risk

Credit risk refers to the risk that debtors will default on their obligations to repay the amounts owing to the Group, resulting in a loss to the Group. The maximum exposure to credit risk in the event that the counterparties fail to perform their obligations at end of the financial year in relation to each class of recognised financial assets in the carrying amount of those assets as stated in the consolidated statement of financial position.

The Group has no significant credit risks as it has policies in place to ensure that sales of products and services are made to customers with appropriate credit history. The Group has adopted a policy of only dealing with creditworthy counterparties. The Group only transacts with entities with good repayment history.

The Group does not have any other significant concentration of credit risk. Trade receivables consist of a large number of customers, spread across diverse industries.

The Group's concentration of credit risk by geographical locations is in the PRC, Hong Kong and Taiwan, which accounted for the entire (2009: 100%) total trade receivables as at 31 December 2010.

The credit risk on liquid funds is limited because the counterparties are banks with high credit ratings assigned by international credit-rating agencies.

For other financial assets, such as cash held at financial institutions and available-for-sale investments, the Group limited its exposure to credit risk by transacting the majority of its securities with broker-dealers and regulated exchanges with high credit rating of which the Group considered to be well established. All transactions in listed securities are settled/paid for upon delivery using approved and reputable brokers.

40. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(Continued)*

(b) Financial risk management objectives and policies *(Continued)*

Liquidity risk

The Group is exposed to liquidity risk as at 31 December 2010 as its financial assets due within one year was less than its financial liabilities due within one year. The Group had net current liabilities of approximately HK$303,574,000 (2009: HK$306,617,000) as at 31 December 2010.

The Group has planned to implement measure to improve its working capital position and net financial position. Details of which are set out in note 2.

The following table details the Group's remaining contractual maturities for its financial liabilities. For non-derivative financial liabilities, the table has been drawn up based on undiscounted cash flows of financial liabilities based on the earliest date on which the Group can be required to pay. The table includes both interest and principal cash flows.

	Overdue *HK$'000*	On demand or within one year *HK$'000*	More than one year but less than two years *HK$'000*	More than two years but less than five years *HK$'000*	More than five years *HK$'000*	Total undiscounted cash flows *HK$'000*	Carrying amounts *HK$'000*
2010							
Non-derivatives financial liabilities							
Trade and other payables	–	121,416	–	–	–	121,416	121,416
Bank borrowings and other loans	35,421	40,778	12,873	44,291	28,055	161,418	142,865
Amounts due to non-controlling shareholders of a subsidiary	–	6,216	–	–	–	6,216	6,216
Loan from an associate	–	2,419	–	–	–	2,419	2,419
Convertible bonds	–	303,104	5,251	–	–	308,355	304,661
	35,421	473,933	18,124	44,291	28,055	599,824	577,577

40. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(Continued)*

(b) Financial risk management objectives and policies *(Continued)*

Liquidity risk *(Continued)*

	Overdue *HK$'000*	On demand or within one year *HK$'000*	More than one year but less than two years *HK$'000*	More than two years but less than five years *HK$'000*	More than five years *HK$'000*	Total undiscounted cash flows *HK$'000*	Carrying amounts *HK$'000*
2009							
Non-derivatives financial liabilities							
Trade and other payables	–	116,360	–	–	–	116,360	116,360
Bank borrowings and other loans	34,155	42,039	20,667	50,990	29,015	176,866	135,641
Amounts due to non-controlling shareholders of subsidiaries	–	8,258	–	–	–	8,258	8,258
Convertible bonds of a subsidiary	–	–	–	200,000	–	200,000	118,427
	34,155	166,657	20,667	250,990	29,015	501,484	378,686

(c) Fair values

The fair value of financial assets and financial liabilities are determined as follows:

- the fair value of financial assets and financial liabilities (including derivative instruments) with standard terms and conditions and traded on active liquid markets are determined with reference to quoted market bid prices and ask prices respectively;

- the fair value of other financial assets and financial liabilities (including derivative instruments) are determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices or rates from observable current market transactions and dealer quotes for similar instruments; and

- the fair value of derivative instruments is calculated using quoted prices.

The directors of the Company consider that the carrying amounts of financial assets and financial liabilities recorded at amortised cost in the consolidated financial statements approximate their fair values.

The directors of the Company also consider that the fair value of the long-term portion of liabilities approximates to their carrying amount as the impact of discounting is not significant.

40. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(Continued)*

(d) Fair value measurement recognised in the statement of financial position

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable.

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active market for identical assets or liabilities.
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

	31 December 2010			
	Level 1	**Level 2**	**Level 3**	**Total**
	HK$'000	***HK$'000***	***HK$'000***	***HK$'000***
Financial asset through profit and loss				
Derivative financial instruments	**–**	**10,239**	**–**	**10,239**
Available-for-sale financial assets				
Listed equity securities	**29,898**	**–**	**–**	**29,898**
Financial liabilities at FVTPL				
Convertible bonds	**–**	**95,526**	**–**	**95,526**

	31 December 2009			
	Level 1	Level 2	Level 3	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Available-for-sale financial assets				
Listed equity securities	65,040	–	–	65,040
Financial liabilities at FVTPL				
Convertible bonds	–	466,739	–	466,739

There was no transfers between Level 1 and 2 in current year and prior years.

41. ACQUISITION OF AN INTANGIBLE ASSET THROUGH ACQUISITION OF A SUBSIDIARY

On 23 October 2009, iMerchants acquired the entire issued share capital of Supreme Luck from an independent third party for a total consideration of HK$925,572,000. The principal activity of Supreme Luck is an investment holding company and its major asset is an exclusive right to receive management fee from Shenzhen Careall. Shenzhen Careall is principally engaged in venture investment, venture investment advisory and management services. Shenzhen Careall mainly invests in the equities of the new technology-based enterprises in the PRC. Accordingly, the transaction has been accounted for as the acquisition of an intangible asset through acquisition of a subsidiary.

The net assets acquired in the transaction are as follows:

	2010 ***HK$'000***
Net assets acquired:	
Intangible asset	**925,584**
Other payables	**(12)**
Net assets acquired	**925,572**
Total consideration satisfied by:	
Issue of ordinary shares	**58,446**
Issue of convertible bonds *(note 36)*	**200,000**
Issue of non-redeemable convertible preference shares *(note 35)*	**567,126**
Cash	**98,890**
Deferred consideration	**1,110**
	925,572
Net cash outflow arising on acquisition:	
Cash consideration paid	**98,890**

Note: As part of the consideration for the acquisition of Supreme Luck, 61,522,160 new ordinary shares of iMerchants with par value of HK$0.2 each were issued at the price of HK$0.95. The fair value of the ordinary shares issued was determined by reference to the published price available at the date of the acquisition.

42. DISPOSAL OF SUBSIDIARIES/BUSINESS

(a) On 2 April 2009, the Group disposed of its 100% interests in Longwide Investment Limited and its subsidiaries (the "Longwide Group") and a shareholder's loan amounting to approximately HK$57,000 to Bright Blue Investments Limited, an independent third party, at a consideration of HK$50,000,000. The net assets of Longwide Group at the date of disposal were as follows:

	HK$'000
Net assets disposed of:	
Property, plant and equipment	22,191
Prepaid lease payments	33,190
Concession intangible assets	207,167
Inventories	2,008
Trade and other receivables	23,733
Bank balances and cash	3,032
Trade and other payables	(84,470)
Amount due to a non-controlling shareholder of a subsidiary	(163,074)
Amount due to a shareholder	(57)
Loan from an associate	(3,379)
Deferred tax liabilities	(735)
Minority interests	(20,248)
	19,358
Assignment of amount due to a shareholder	57
Exchange reserve realised on disposal of subsidiaries	(5,006)
Attributable goodwill	28,087
Gain on disposal	7,504
Total consideration	50,000
Satisfied by:	
Cash	50,000
Net cash inflow arising on disposal:	
Cash consideration received	50,000
Bank balances and cash disposed of	(3,032)
	46,968

42. DISPOSAL OF SUBSIDIARIES/BUSINESS *(Continued)*

(a) *(Continued)*

Note: During the year ended 31 December 2009, the Longwide Group had contributed the Group of:

	2009
	HK$'000
Turnover	8,067
Loss for the year	(3,391)
Cash inflow (outflow) from operating activities	2,731
Cash outflow from investing activities	(513)
Cash inflow from financing activities	–

42. DISPOSAL OF SUBSIDIARIES/BUSINESS *(Continued)*

(b) On 15 April 2009, the Group disposed of its assets and liabilities of a branch of Jining Haiyuan, an indirect non-wholly owned subsidiary of the Company to an independent third party at a consideration of HK$10,000,000. The assets and liabilities of the branch of Jining Haiyuan at the date of disposal were as follows:

	HK$'000
Net assets and liabilities disposed of:	
Property, plant and equipment	2,922
Concession intangible assets	28,247
Inventories	7
Trade and other receivables	1,844
Bank balances and cash	599
Trade and other payables	(12,328)
Amount due to a non-controlling shareholder of a subsidiary	(104)
Deferred tax liabilities	(70)
Minority interests	(6,335)
	14,782
Exchange reserve realised on disposal of business	(22)
Loss on disposal	(4,760)
Total consideration	10,000
Satisfied by:	
Cash	10,000
Net cash inflow arising on disposal:	
Cash consideration received	10,000
Bank balances and cash disposed of	(599)
	9,401

Note: During the year ended 31 December 2009, Jining Haiyuan branch had contributed the Group of:

	2009 *HK$'000*
Turnover	1,442
Profit for the year	321
Cash (outflow) inflow from operating activities	(260)

43. DEEMED DISPOSAL OF A SUBSIDIARY

As disclosed in note 12, the equity interest of iMerchants owned by the Group was diluted on 4 October 2010.

	HK$'000
Analysis of assets and liabilities over which control was lost:	
Property, plant and equipment	6,871
Prepaid lease payments	2,720
Intangible assets	623,383
Inventories	328
Trade and other receivables	162,600
Bank balances and cash	2,528
Cash held at financial institutions	593
Trade and other payables	(2,293)
Tax payables	(34,200)
Other loans	(4,132)
Amount due to non-controlling shareholders of a subsidiary	(2,204)
Convertible bonds of a subsidiary	(128,631)
Net assets disposed of	627,563
Gain on deemed disposal of a subsidiary:	
Fair value of interest retained in interests in associates	308,949
Exchange reserve realised on disposal of business	42
Net assets disposal of	(627,563)
Release of goodwill upon deemed disposal	(68,364)
Non-redeemable convertible preference shares of a subsidiary	570,096
Equity component of convertible bonds of a subsidiary	84,045
Non-controlling interests	(8,976)
Gain on deemed disposal	258,229
Net cash outflow arising on disposal:	
Cash held at financial institutions	(593)
Bank balances and cash disposed of	(2,528)
	(3,121)

The financial impact of the results and cash flow of iMerchants to the Group's turnover, loss for the year and cash flows during the year is disclosed in note 12.

44. DEEMED PARTIAL DISPOSAL OF INTERESTS IN A SUBSIDIARY

On 23 October 2009, iMerchants issued 61,522,160 ordinary shares at a price of HK$0.2 each as a partial consideration in respect of acquisition of Supreme Luck (note 41), resulting in the Group's interest in iMerchants being diluted from 84.98% to 76.66%. Gain on deemed partial disposal of interests in a subsidiary amounted to approximately HK$21,323,000.

45. PLEDGED OF ASSETS

Assets with the following carrying amounts have been pledged to secure bank borrowings and other loans of the Group (notes 29 and 30):

	2010	2009
	HK$'000	*HK$'000*
Prepaid lease payments	**10,284**	12,881
Property, plant and equipment	**2,195**	2,186
Concession intangible assets	**19,240**	19,392
	31,719	34,459

46. CAPITAL COMMITMENT

	2010	2009
	HK$'000	*HK$'000*
Capital commitments contracted but not provided for, in respect of acquisition of concession intangible assets and property, plant and equipment	**7,079**	7,514
Acquisition of subsidiaries	**–**	119,099

47. OPERATING LEASE COMMITMENT

The Group leases certain of its factory premises, plant and staff quarters under operating lease arrangements. Leases for properties are negotiated for terms ranging from one to five years. Rental was fixed at the inception of the lease. No provision for contingent rent and terms of renewal were established in the leases.

At the end of the reporting period, the Group had future minimum lease payments under non-cancellable operating leases which fall due as follows:

	2010 ***HK$'000***	2009 *HK$'000*
Within one year	**3,032**	3,242
In the second to fifth year, inclusive	**1,069**	803
	4,101	4,045

48. SHARE-BASED PAYMENT TRANSACTIONS

Equity-settled share option scheme

The Company's share option scheme (the "Scheme"), became effective on 17 January 2002 for the primary purpose of providing incentives to directors and eligible employees or persons and, unless otherwise cancelled or amended, will remain in force for 10 years from that date. Under the Scheme, the board of directors of the Company may grant options to eligible employees, including directors of the Company and its subsidiaries, to subscribe for shares in the Company. Additionally, the Company may, from time to time, grant share options to outside third parties for settlement in respect of goods or services provided to the Company.

At 31 December 2010, the number of shares in respect of which options had been granted and remained outstanding under the Scheme was 8,000,000 (2009: 18,000,000), representing 0.25% (2009: 0.67%) of the shares of the Company in issue at that date.

The total number of shares in respect of which options may be granted under the Scheme is not permitted to exceed 30% of the shares of the Company in issue at any point in time, without prior approval from the Company's shareholders. The number of shares issued and to be issued in respect of which options granted and may be granted to any individual in any one year is not permitted to exceed 1% of the shares of the Company in issue at any point in time, without prior approval from the Company's shareholders. Options granted to substantial shareholders or independent non-executive directors in excess of 0.1% of the Company's share capital or with a value in excess of HK$5,000,000, within one year, must be approved in advance by the Company's shareholders.

48. SHARE-BASED PAYMENT TRANSACTIONS *(Continued)*

Equity-settled share option scheme *(Continued)*

Options granted must be taken up within twelve months of the date of grant, upon payment of HK$1 per grant. Options may be exercised at any time from the date of grant of the share option to the tenth anniversary of the date of grant. The exercise price is determined by the directors of the Company, and will not be less than the higher of (i) the closing price of the Company's shares on the date of grant, (ii) the average closing price of the shares for the five business days immediately preceding the date of grant; and (iii) the nominal value of the Company's share.

The following table discloses movements of the Company's share options held by directors and other eligible persons during the year ended 31 December 2010:

Name or category of participant	Date of grant	Outstanding at 1 January 2009, 31 December 2009 and 1 January 2010	Granted during the year	Exercised during the year	Lapsed during the year	Outstanding at 31 December 2010	Exercisable period	Exercise Price per share of the Company *HK$*
Directors								
Chu Yin Yin, Georgiana	11 January 2007	3,000,000	–	–	–	3,000,000	11 January 2007 to 10 January 2017	0.335
Liu Bai Yue	17 January 2007	5,000,000	–	–	–	5,000,000	17 January 2007 to 16 January 2017	0.420
		8,000,000				8,000,000		
Other eligible persons *(Note)*	11 January 2007	10,000,000	–	–	(10,000,000)	–	11 January 2007 to 10 January 2017	0.335
Total as at 31 December 2010		**18,000,000**	**–**	**–**	**(10,000,000)**	**8,000,000**		
Weighted average exercise price		0.359	–	–	0.335	0.388		

Note: On 21 November 2008, Mr. Sze Chun Ning, Vincent ("Mr. Sze") has resigned as an Executive Director and deputy managing director of the Company but remains as a director of subsidiaries of the Company. Mr. Sze had resigned all the positions in subsidiaries in May 2010, the share options were then lapsed.

49. MAJOR NON-CASH TRANSACTIONS

During the year ended 31 December 2010, Swift Surplus entered into a termination agreement with the vendor and the deposit paid of HK$50,901,000 was assigned as a loan to the holding company of the vendor, Top Vision Management Limited ("Top Vision"), accordingly, the amount was then reclassified to loan receivable during the year ended 31 December 2010. Further details of the acquisition are set out in note 23.

During the year ended 31 December 2009, part of the consideration for the acquisition of a subsidiary comprised ordinary shares, convertible bonds and non-redeemable convertible preference shares, respectively. Further details of the acquisition are set out in note 41.

50. RETIREMENT BENEFIT SCHEME

The Group operates a Mandatory Provident Fund Scheme for all qualifying employees in Hong Kong. The assets of the schemes are held separately from those of the Group, in funds under the control of trustees. The Group contributes 5% of relevant payroll costs to the scheme, which contribution is matched by employees.

The employees of the Group's subsidiaries which operates in the PRC are required to participate in the CPS operated by the local municipal governments. These PRC subsidiaries are required to contribute 8% to 10% of its payroll costs to the CPS. The contributions are charged to the consolidated statement of comprehensive income as they become payable in accordance with the rules of the CPS.

51. LITIGATION

Super Sino, an indirectly wholly-owned subsidiary of the Company

In November 2007, the People's Government of Danzhou City and Super Sino entered into a net asset transfer agreement, pursuant to which all assets and liabilities of Danzhou City Water were transferred to Super Sino. On 26 June 2008, Super Sino was notified that Agricultural Bank of China, Danzhou Branch ("the Plaintiff") filed a claim regarding the liabilities transferred by Danzhou City Water with the Court against Danzhou City Water, Super Sino, Danzhou Urban Development Corporation and the People's Government of Danzhou City for the repayment of the loan principal of approximately HK$30,698,000 (equivalent to RMB26,000,000) (2009: HK$29,601,000 equivalent to RMB26,000,000) and the interests of approximately HK$50,972,000 (equivalent to RMB43,171,000) (2009: HK$46,494,000 equivalent to RMB40,838,000) arising from the defendants of Danzhou City Water and Super Sino to the plaintiff.

On 13 November 2009, the Court issued a civil verdict, pursuant to which Super Sino was ordered to fully repay the loan principal of RMB26,000,000 together with the interest thereon.

On 17 December 2009, the Plaintiff made an appeal to the Higher People's Court of Hainan Province court seeking the fulfilment of the guarantee responsibility of Danzhou Urban Development Corporation.

51. LITIGATION *(Continued)*

Super Sino, an indirectly wholly-owned subsidiary of the Company *(Continued)*

On 15 December 2010, Higher People's Court of Hainan Province issued verdict, pursuant to which all the shares of Danzhou City Water owned by Super Sino (the "shares") have been frozen from 15 December 2010 to 14 December 2012. The Company cannot transfer or dispose of the shares during the period. According to the legal advice, the directors of the Company are of the opinion that the verdict will not impair the control of the Group over Danzhou City Water due to the following reasons:

(1) Super Sino is still the legal owner of Danzhou City Water during the year ended 31 December 2010 and up to the date of approval of these consolidated financial statements.

(2) As Danzhou City Water is engaged in the business of provision of water in the PRC which requires special license from the respective PRC government authorities. The procedures for the change of shareholding are complicated and require the approval from several PRC government authorities.

As at the reporting date, the directors of the Company are discussing the settlement arrangement with the Plaintiff and there is no demand for settlement from the Plaintiff at the moment. The principal of the said loan and the interest thereon have been included in the consolidated financial statements of the Group. The directors of the Company are of the opinion that the power to govern the financial and operating policies of Danzhou City Water are still vest on the Group.

52. RELATED PARTY TRANSACTIONS

During the year ended 31 December 2010 and 2009, the Group entered into the following transactions with related parties:

	2010 ***HK$'000***	2009 *HK$'000*
Paid rental expenses to: Non-controlling shareholder of a subsidiary	**224**	204
Paid service expense to: Jinan Hongquan	–	100

The balance with related parties at the end of the reporting period is disclosed elsewhere in the consolidated financial statements.

52. RELATED PARTY TRANSACTIONS *(Continued)*

Compensation of key management personnel

The remuneration of directors and other members of key management during the year was as follows:

	2010 ***HK$'000***	2009 *HK$'000*
Short-term benefits	**3,744**	4,718
Post-employment benefits	**84**	107
	3,828	4,825

The remuneration of directors and key executives is determined by the remuneration committee having regard to the performance of individuals and market trends.

53. PRINCIPAL SUBSIDIARIES

Details of the principal subsidiaries at 31 December 2010 and 2009, are as follows:

Name of company	Place of incorporation/ operations	Particulars of issued and paid up share capital/ registered capital	Proportion of equity interest held by the Group 2010	2009	Principal activities
Billion City Investments Limited	British Virgin Islands ("BVI")	1 ordinary share of US$1 each	**100%**	100%	Investment holding
Super Sino Investment Limited	Hong Kong	1 ordinary share of HK$1 each	**100%**	100%	Investment holding
Danzhou Qingyuan Water Industry Company Limited*	PRC	Registered capital of HK$30,000,000	**100%**	100%	Provision of water supply
Danzhou Lian Shun Tong Water Pipe Company Limited*	PRC	Registered capital of RMB1,000,000	**100%**	100%	Provision of water supply
Onfar International Limited	BVI	100 ordinary shares of US$1 each	**100%**	100%	Investment holding
Yichun Water Supply Co., Limited	PRC	Registered capital of RMB45,500,000	**51%**	51%	Provision of water supply
Yichun Fangke Sewage Treatment Company Limited *	PRC	Registered capital of RMB20,000,000	**51%**	51%	Sewage treatment
Yichun City Water Supply Engineering Limited *	PRC	Registered capital of RMB5,000,000	**100%**	100%	Provision of water supply
Bloom Profit Investment Limited	Hong Kong	1 ordinary share of HK$1 each	**100%**	100%	Investment holding
Anhui Dang Shan Water Industry Company Limited*	PRC	Registered capital of RMB7,500,000	**100%**	100%	Provision of water supply
Victory Strategy Investment Limited	Hong Kong	1 ordinary share of HK$1 each	**100%**	100%	Not yet commenced business

53. PRINCIPAL SUBSIDIARIES *(Continued)*

Name of company	Place of incorporation/ operations	Particulars of issued and paid up share capital/ registered capital	Proportion of equity interest held by the Group 2010	2009	Principal activities
Nourish Gain Investments Limited	BVI	1 ordinary share of US$1 each	**100%**	100%	Investment holding
China Ace Investments Limited	Hong Kong	1 ordinary share of HK$1 each	**100%**	100%	Investment holding
Jining City Haiyuan Water Treatment Company Limited *	PRC	Registered capital of RMB40,000,000	**70%**	70%	Sewage treatment
China Water Industry (HK) Ltd	Hong Kong	1 ordinary share of HK$1 each	**100%**	100%	Investment holding
Linyi Fenghuang Water Industry Co., Ltd	PRC	Registered capital of RMB30,000,000	**60%**	60%	Provision of water supply
Yingtan Water Supply Co., Ltd	PRC	Registered capital of RMB66,008,000	**51%**	51%	Provision of water supply
Smart Giant Group Limited	BVI	1 ordinary share of US$1 each	**100%**	100%	Investment holding
Blue Mountain Hong Kong Group Limited	Hong Kong	HK$1	**100%**	100%	Investment holding
Bonus Raider Investments Limited	BVI	1 ordinary share of US$1 each	**100%**	100%	Investment holding
iMerchants Limited *(Note i)*	Hong Kong	3,138,885,800 HK$0.04 shares	**N/A**	76.66%	Investment in financial and investment products and technology investment

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For the year ended 31 December 2010

53. PRINCIPAL SUBSIDIARIES *(Continued)*

Name of company	Place of incorporation/ operations	Particulars of issued and paid up share capital/ registered capital	Proportion of equity interest held by the Group 2010	2009	Principal activities
iMerchants Asia Limited *(Note i)*	BVI	US$6,001,000	**N/A**	76.66%	Investment holdings, investments in financial and investment products and technology investment
Supreme Luck International Limited *(Note i)*	BVI	1 ordinary share of US$1 each	**N/A**	76.66%	Investment holding
iMerchants Consulting Limited *(Note i)*	Hong Kong	HK$1	**N/A**	76.66%	Inactive
iMerchants Service Limited *(Note i)*	BVI	US$1	**N/A**	76.66%	Inactive
Top Deluxe Limited *(Note i)*	Hong Kong	HK$1	**N/A**	76.66%	Inactive
Shine Gain Holdings Limited *(Note i)*	BVI	US$1	**N/A**	76.66%	Investment holding
Plenty One Limited *(Note i)*	BVI	US$100	**N/A**	76.66%	Investment holding
Ping Xiang City San He Lian Chuang Water Technology Company Limited* *(Note i)*	PRC	RMB5,000,000	**N/A**	61.33%	Trading of ceramists
Growwise Holding Limited *(Note i)*	BVI	1 ordinary share of US$1 each	**N/A**	76.66%	Investment holding
Top Connect Holding Limited *(Note i)*	BVI	1 ordinary share of US$1 each	**N/A**	76.66%	Not yet commenced business
Great Knight Limited *(Note i)*	BVI	1 ordinary share of US$1 each	**N/A**	76.66%	Not yet commenced business

53. PRINCIPAL SUBSIDIARIES *(Continued)*

Name of company	Place of incorporation/ operations	Particulars of issued and paid up share capital/ registered capital	Proportion of equity interest held by the Group 2010	2009	Principal activities
Swift Surplus Holdings Limited	BVI	100 ordinary share of US$1 each	**100%**	100%	Investment holding
Mark Profit Group Holdings Limited	Hong Kong	1 ordinary shares of HK$1 each	**100%**	100%	Investment holding
Guangzhou Hyde Environmental Protection Technology Co. Ltd*	PRC	RMB10,000,000	**100%**	N/A	Investment holding
Happy Hour Limited	BVI	1 ordinary share of US$1 each	**100%**	100%	Investment holding
Mascot Industries Limited	Hong Kong	2 ordinary shares of HK$1 each	**100%**	100%	Trading of watches
South Top Investment Limited	Hong Kong	1 ordinary share of HK$1 each	**100%**	100%	Inactive
Neutral Crown Holdings Limited	BVI	100 ordinary shares of US$1 each	**100%**	100%	Investment holding

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

None of the subsidiaries has issued any debt securities subsisting at the end of 2010 or at any time during the year ended 31 December 2010.

As at 31 December 2009, none of the subsidiaries had issued any debt securities subsisting. As at 31 December 2009, iMerchants had issued HK$200,000,000 of convertible bonds, in which the Group had no interest.

Notes:

(i) In October 2010, the holders of non-redeemable convertible preference shares exercised their rights to convert the preference shares in fully paid ordinary shares in iMerchants. iMerchants and it subsidiaries become an associate after the deemed disposals.

* The English names are for identification purpose only.

54. STATEMENT OF FINANCIAL POSITION OF THE COMPANY

	Notes	2010 HK$'000	2009 HK$'000
Non-current assets			
Investments in subsidiaries		**2**	2
Available-for-sale investments		**29,898**	58,890
		29,900	58,892
Current assets			
Other receivables		**427**	5,727
Loan receivables		**118,399**	17,305
Amounts due from subsidiaries	*(a)*	**827,127**	855,866
Derivative financial instruments		**10,239**	–
Cash held at financial institutions		**37,724**	165,250
Bank balances and cash		**4,844**	660
		998,760	1,044,808
Current liabilities			
Other payables		**1,803**	1,729
Convertible bonds		**397,187**	466,739
		398,990	468,468
Net current assets		**599,770**	576,340
		629,670	635,232
Capital and reserves			
Share capital		**324,765**	270,638
Reserves	*(b)*	**301,905**	364,594
Total equity		**626,670**	635,232
Non-current liability			
Convertible bonds		**3,000**	–
		629,670	635,232

Notes:

(a) Amounts due from subsidiaries

The amounts are unsecured, interest-free and repayable on demand.

54. STATEMENT OF FINANCIAL POSITION OF THE COMPANY *(Continued)*

(b) Reserves

	Share premium HK$'000	Share options reserve HK$'000	Convertible bonds equity reserve HK$'000	Investment revaluation reserves HK$'000	Accumulated losses HK$'000	Total HK$'000
At 1 January 2009	418,093	727	–	–	2,043	420,863
Loss for the year	–	–	–	–	(219,107)	(219,107)
Other comprehensive expense for the year	–	–	–	(1,510)	–	(1,510)
Issuance of shares (net of transaction cost) *(note 34)*	164,348	–	–	–	–	164,348
At 31 December 2009 and 1 January 2010	582,441	727	–	(1,510)	(217,064)	364,594
Loss for the year	–	–	–	–	(82,878)	(82,878)
Other comprehensive expense for the year	–	–	–	(28,992)	–	(28,992)
Impairment loss recognised on available–for–sale investment	–	–	–	30,502	–	30,502
Placing of new shares (net of transaction cost) *(note 34)*	2,765	–	–	–	–	2,765
Cancellation of share options	–	(404)	–	–	404	–
Recognition of equity component of convertible bonds	–	–	15,914	–	–	15,914
At 31 December 2010	585,206	323	15,914	–	(299,538)	301,905

FIVE YEARS FINANCIAL SUMMARY

	2006 HK$'000	2007 HK$'000 (restated)	2008 HK$'000	2009 HK$'000 (restated)	**2010 HK$'000**
Results					
Turnover	70,134	124,363	289,875	202,108	**238,771**
Finance costs	(494)	(2,612)	(10,280)	(11,993)	**9,534**
(Loss) profit before tax	(25,252)	(6,909)	65,746	(300,227)	**(166,667)**
Income tax expense	(336)	(1,414)	(6,937)	(8,448)	**(10,813)**
(Loss) profit for the year (including discontinued operations)	(95,742)	(11,431)	58,809	(342,485)	**(149,796)**
Discontinued operations					
(Loss) profit for the year from discontinued operations	(70,154)	(3,108)	–	(33,810)	**27,684**
Assets and liabilities					
Property, plant & equipment	64,628	54,852	129,947	103,164	**97,598**
Prepaid lease payments	–	10,143	76,443	42,854	**40,621**
Concession intangible assets	–	191,354	608,726	416,718	**483,829**
Intangible asset	–	–	–	915,301	**–**
Goodwill	1,361	77,333	383,347	250,995	**142,373**
Available-for-sale investments	–	–	59,519	65,040	**29,898**
Interest in associates	36,477	7,617	55,783	57,853	**281,407**
Deposits paid for acquisition of subsidiaries	–	567,990	–	50,901	**–**
Net current assets (liabilities)	(43,573)	132,884	(122,535)	(306,617)	**(303,574)**
	58,893	1,042,173	1,191,230	1,596,209	**772,152**
Share capital	116,450	189,090	189,090	270,638	**324,765**
Reserves	(64,722)	342,781	326,989	190,659	**124,128**
Non-redeemable convertible preference shares of a subsidiary	–	–	–	587,696	**–**
Equity component of convertible bonds of a subsidiary	–	–	–	84,045	**–**
Non-controlling interests	6,063	86,536	194,862	210,496	**179,164**
Bank borrowing due after one year	245	32,017	27,076	23,909	**21,253**
Other loans – due after one year	857	938	45,940	44,902	**47,487**
Loans from a minority shareholder	–	11,738	3,384	–	**–**
Amount due to minority shareholder of subsidiaries	–	–	81,427	–	**–**
Convertible bonds	–	326,872	262,335	–	**3,000**
Convertible bonds of a subsidiary	–	–	–	118,427	**–**
Government grants	–	50,787	55,763	60,040	**64,074**
Deferred tax liabilities	–	1,414	4,364	5,397	**8,281**
	58,893	1,042,173	1,191,230	1,596,209	**772,152**
Earnings (loss) per share					
Basic	(9.6 cents)	(1.26 cents)	(2.32 cents)	(15.68 cents)	**(3.27 cents)**
Diluted	N/A	(4.17 cents)	(0.91 cents)	(15.68 cents)	**(3.27 cents)**