金山能源集團有限公司
KING STONE ENERGY GROUP LIMITED

(Incorporated in Hong Kong with limited liability)

(Stock Code: 00663)

Annual Report 2012

Contents

CORPORATE INFORMATION

BOARD OF DIRECTORS

Executive Directors

Mr. Xu Zhendong *(Chairman)*
Mr. Zhang Wanzhong
Mr. Zong Hao
Mr. Tian Wenwei
Mr. Xu Zhuliang
Mr. Benjamin Clark Danielson

Non-Executive Director

Mr. Zhang Yongli

Independent Non-Executive Directors

Mr. Chiu Sui Keung
Mr. Li Peiming
Mr. Lee Chi Hwa, Joshua
Mr. Lu Binghui

AUDIT COMMITTEE

Mr. Chiu Sui Keung *(Chairman)*
Mr. Li Peiming
Mr. Lu Binghui

REMUNERATION COMMITTEE

Mr. Chiu Sui Keung *(Chairman)*
Mr. Tian Wenwei
Mr. Li Peiming

NOMINATION COMMITTEE

Mr. Zhang Wanzhong *(Chairman)*
Mr. Li Peiming
Mr. Chiu Sui Keung
Mr. Lee Chi Hwa, Joshua

AUTHORISED REPRESENTATIVES

Mr. Xu Zhendong
Mr. Zong Hao

COMPANY SECRETARY

Mr. Lee Tao Wai

AUDITORS

Ernst & Young
22/F, CITIC Tower
1 Tim Mei Avenue
Central, Hong Kong

LEGAL ADVISER

Michael Li & Co
19/F, Prosperity Tower
39 Queen's Road Central
Central, Hong Kong

REGISTERED OFFICE & PRINCIPAL PLACE OF BUSINESS IN HONG KONG

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99 Queen's Road Central
Hong Kong

SHARE REGISTRAR

Tricor Secretaries Limited
Level 25, Three Pacific Place
1 Queen's Road East, Hong Kong

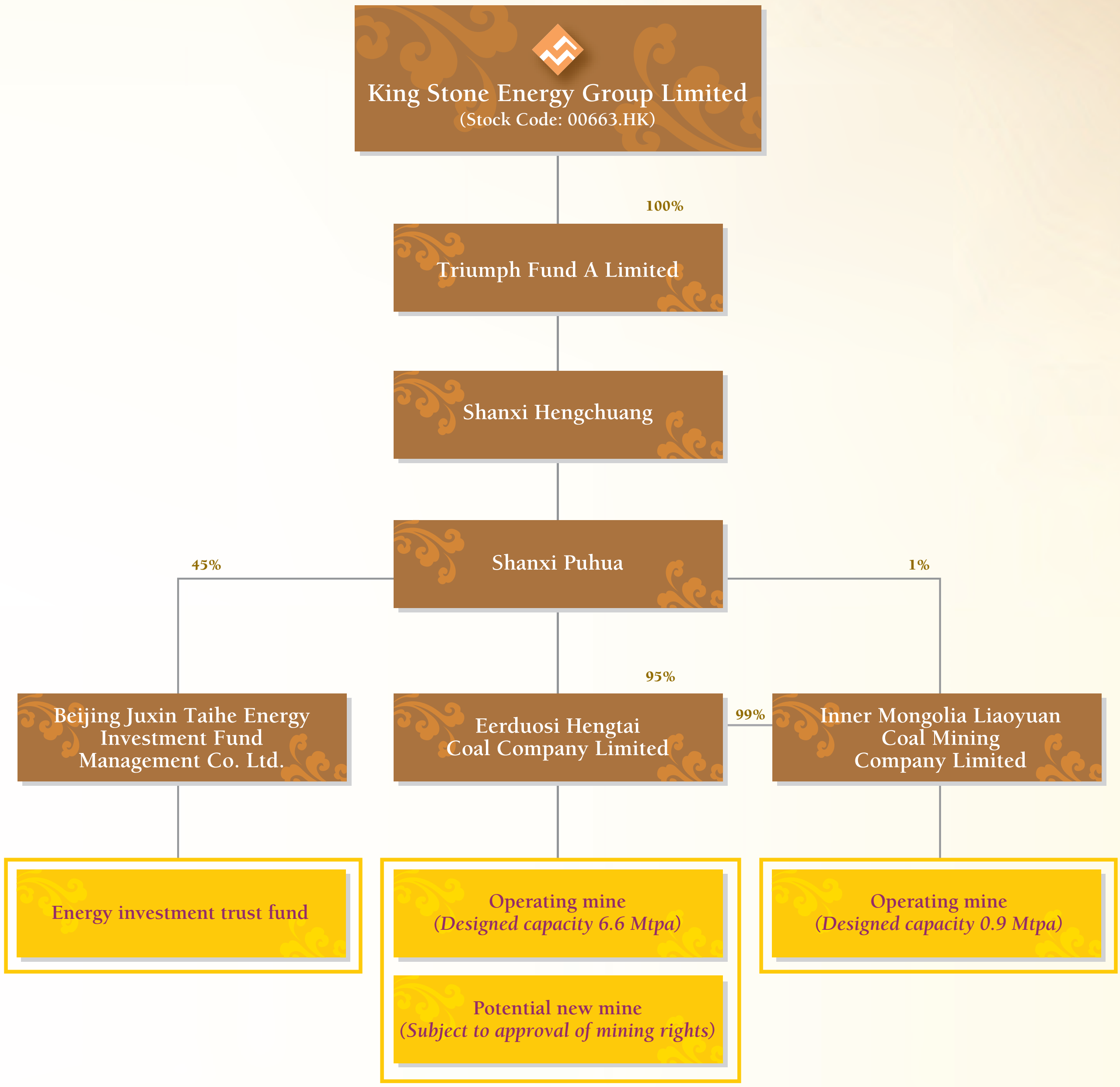
COMPANY WEBSITE

http://www.663hk.com

STOCK CODE

00663

GROUP STRUCTURE



CAPITAL EXPENDITURE

The capital expenditure for development and mining production activities was approximately HK$331 million (2011: HK815 million) during the year.

HENGTAI COAL MINE

Name	Eerduosi Hengtai Coal Company Limited ("Hengtai")
Location	Dongshen Coalfield of Inner Mongolia
Licensed area	~7 km^2
Mining rights validity	2007–2022
Mining Method	Underground
Coal type	Thermal
Designed capacity	6.6 million tons per annum
Status	Operating

	Resources (million tons)	Reserves (million tons)
Total resources/reserves (JORC compliant)	203.9	71.9
Actual output in 2010	(4.0)	(4.0)
Actual output in 2011	(3.6)	(3.6)
Actual output in 2012	(2.5)	(2.5)
Resources/reserves as at 31 December 2012	193.8	61.8

Note: The resources/reserves as at 31 December 2012 are derived from total resources/reserves extracted from technical report issued by John T. Boyd Company dated 18 November 2009 after deduction of actual output up to 31 December 2012 based on Hengtai's record.

LIAOYUAN COAL MINE

Name	Inner Mongolia Liaoyuan Coal Mining Company Limited ("Liaoyuan")
Location	YijinhuoLuoqi, Eerduosi, Inner Mongolia
Licensed area	8.396 km^2
Mining rights validity	2008–2013
Mining Method	Underground
Coal type	Thermal
Designed capacity	0.9 million tons per annum
Status	Operating

	Resources (million tons)
Resources as at 31 December 2011 (JORC equivalent)	15.8
Actual output in 2012	(0.5)
Resources as at 31 December 2012	15.3

Note: The resources as at 31 December 2012 are derived from the resources extracted from technical report issued by Roma Oil and Mining Associated Limited dated 30 March 2012 after deduction of actual output up to 31 December 2012 based on Liaoyuan's record.

CHAIRMAN STATEMENT

Dear Shareholders,

On behalf of the board of directors (the "Board") of King Stone Energy Group Limited (the "Company" or "King Stone Energy", together with its subsidiaries, the "Group"), I am delighted to present the annual results for the year ended 31 December 2012.

The year 2012 was a year full of challenges and opportunities for King Stone Energy.

With the coal market of China continuing to stagnate, it was hard for the Company as a large domestic coal producer to be completely insulated from such a difficult situation. In 2012, the coal output of Inner Mongolia-based Eerduosi Hengtai Coal Co. Ltd ("Hengtai") and Inner Mongolia Liaoyuan Coal Mining Co. Ltd ("Liaoyuan") of the Group was approximately 2.5 million tones and 0.5 million tones respectively, both representing a decrease as compared to the corresponding period in 2011. The selling price of coal and gross profit of the Group also decreased due to the influence of supply and demand factors, and therefore the Group made an impairment in respect of the mining assets of Hengtai and Liaoyuan of approximately HK$1,800 million in total during the year in order to truly reflect the fair value of the Group's assets and try our best to maintain the high transparency of our financial statements.

During the year, the Company grasped a golden opportunity to complete the restructuring of shareholding structure. On 17 October 2012, the Company entered into a share subscription agreement with a fund managed by Jade Bird Strategic Investment, pursuant to which the Company issued approximately 1,555 million new shares at the price of HK$0.45 per subscription share. The issuance completed on 31 January 2013, which generated capital of approximately HK$700 million for the Company for working capital and acquisition projects, and the fund acquired the controlling stake of the Company.

After completion of the share subscription, the Company also actively rebuilt its management team by introducing a number of experienced professionals in energy, mining, investment and other areas to join the Board of the Company. The new management team and I will continue to industriously explore for quality merger and acquisition projects for the Group, and when necessary, the Company will further strengthen its capital base by further raising equity funds and introducing quality long-term investors. I am fully confident that with the extensive business networks of the new controlling shareholder and the rich investment experience of our new management team which will bring additional resources and merger and acquisition opportunities to the Company, we will be able to improve our return of investment.

On behalf of the Board of King Stone Energy, I would like to convey our sincere gratitude to all staff, customers and business partners of the Group. I would also like to take this opportunity to thank the Shareholders who have been supporting and trusting the Group. We expect that the Company will seize investment opportunities in a new look in 2013 to create new value for our Shareholders.

Xu Zhendong
Chairman

28 March 2013

BUSINESS AND RESULTS REVIEW

The Group had encountered challenges in the year of 2012. Dampened coal market, tightened policies of the local government authorities and relocation of working faces of the coal mines have collectively resulted in significant drop in revenue and margins. The adverse situation even deepened in the second half of 2012.

Coal mining business

During the year under review, the operating mine of Eerduosi Hengtai Coal Co. Ltd. ("Hengtai") produced 2.5 million tons of coal, of which only 0.9 million tons were produced in the second half of the year. Inner Mongolia Liaoyuan Coal Mining Co. Ltd. ("Liaoyuan") produced 0.5 million tons of coal, of which only 0.2 million tons were produced in the second half of the year. Total coal output of the Group dropped by 26% on a year-to-year basis. Average selling prices of coal produced by Hengtai and Liaoyuan were also down by 31% and 19% respectively as compared to the year of 2011.

Fund management business

The Group started its fund management business through Beijing Juxin Taihe Energy Investment Fund Management Co. Ltd., (the "Fund Management Company") which was jointly set up with CITIC Trust Co. Ltd in 2011. The Fund Management Company managed energy trust funds which invested in quality coal mines and clean energy projects in China. While the business was nearly break even in 2011, the Group had shared a profit of HK$6.3 million in the year of 2012. It is believed that the continuous growth of the trust fund business will increasingly contribute a major part of income to the Group.

Revenue

The Group recorded total revenue of approximately HK$571.1 million (2011: HK$995.1 million) during the year, representing a decrease of 43% compared with last year. Hengtai and Liaoyuan (which was acquired by the Group in August 2011) contributed revenue of approximately HK$419 million (2011: HK$834.2 million) and approximately HK$152.1 million (five-month period from August 2011 to December 2011: HK$160.9 million) during the year, respectively.

The average selling prices ("ASPs") of raw coal produced by Hengtai and Liaoyuan during the year were approximately RMB135 (2011: RMB197) and RMB227 (2011: RMB279) per ton, respectively. Hengtai and Liaoyuan recorded sales volume of approximately 2.5 million tons (2011: 3.6 million tons) and 0.5 million tons (five-month period from August 2011 to December 2011: 0.5 million tons), respectively. Significant decreases in both ASPs and sales volume were mainly due to weak demand in coal market which was significantly affected by economic slowdown in China during the year.

Cost of inventories sold

Cost of inventories sold primarily consists of depreciation and amortisation, salaries and labour costs for the production, taxes, supplies, utilities and other incidental expenses in relation to production. Cost of inventories sold was approximately HK$662 million (2011: HK$612.2 million) during the year, representing an increase of 8% compared with last year. Notwithstanding a general decrease in production activities during the year, the Group recorded an increase in cost of inventories sold which was mainly attributable to (1) increase in depreciation charges by approximately HK$90 million; and (2) increase in cost of inventories sold for Liaoyuan due to consolidation of full year results of Liaoyuan in the Group's results during the year.

Gross profit/(loss) and gross profit/(loss) margin

The Group recorded a gross loss margin of 16% (2011: gross profit margin of 38%) during the year, which was mainly attributable to the decrease in ASPs and the increase in production costs as mentioned above during the year. Hengtai and Liaoyuan recorded gross loss margins of 20% (2011: gross profit margin of 39%) and 5% (2011: gross profit margin of 34.7%), respectively.

Gain on bargain purchase of a subsidiary

There was no acquisition of subsidiary during the year. In 2011, an one-off gain on acquisition of Liaoyuan of approximately HK$29.9 million was recognised.

Other income and gains

Other income and gains decreased from approximately HK$52.2 million to HK$3.3 million this year. The decrease was mainly due to the absence of a fair value gain on derivative component of convertible bonds of approximately HK$35.5 million and other income of HK$10 million arising from the termination of subscription agreements which were one-off items recorded in 2011.

Selling and distribution expenses

Selling and distribution expenses were HK$10.6 million during the year as compared with approximately HK$4.6 million for last year. The increase was mainly due to increase in transportation costs of coal to customers.

Administrative expenses

Administrative expenses mainly comprised staff costs for administrative and finance functions including equity-settled share option expenses, legal and professional fees incurred for operation and other incidental administrative expenses.

Administrative expenses were approximately HK$95.1 million (2011: HK$182.8 million) during the year. The significant decrease was mainly attributable to (1) decrease in equity-settled share option expenses from approximately HK$30.9 million in last year to approximately HK$8 million in current year; and (2) general decrease in administration costs which were in line with decrease in production activities.

Other expenses

Other expenses mainly comprised impairments of items of property, plant and equipment, mining rights, trade receivables and prepayments, deposits and other receivables of approximately HK$684.1 million, HK$1,127 million, HK$10.4 million and HK$126.9 million, respectively, during the year.

In view of the significant decreases of ASPs, sales volumes of coal during the year (especially in the second half this year) and other adverse changes mentioned below, which are indications of impairment, the management had estimated the recoverable amounts of the assets of the coal mining business of the Group. Based on the assessment of value in use of the assets (which the management considered as the recoverable amounts) for coal mining business by using discounted cash flow models which have been reviewed by an independent valuer, an impairment loss totaling HK$1,841 million was resulted and was allocated as to HK$684.1 million to property, plant and equipment (Hengtai: HK$634.4 million, Liaoyuan: HK$49.7 million), HK$1,127 million to mining rights (Hengtai: HK$903.1 million, Liaoyuan: HK$223.9 million) and HK$29.9 million to prepayments for property, plant and equipment (Hengtai: HK$29.9 million, Liaoyuan: nil) based on their relative carrying amounts.

As certain areas of the No.2 Coal Mine (one of the two coal mines owned by Hengtai) was included in the city development plan of the local government, the local government proposed to exchange another coal mine (the “New No.2 Coal Mine”) to Hengtai as compensation (the “Coal Mine Exchange”). As at 31 December 2012 and up to date of this report, the Coal Mine Exchange has not been formally approved by the local government and the mining license held by the Group for No.2 Coal Mine is still valid. Due to the possible Coal Mine Exchange, the production schedule of the No.2 Coal Mine has been delayed and is expected to commence in the forseeable future. The aforesaid delay in production schedule has been taken into account in such cash flow projections of the New No.2 Coal Mine.

An impairment loss of HK$33.5 million has been made to the indemnification asset (the “Indemnification Asset”) of RMB125.1 million (equivalent to approximately HK$155.6 million) during the year. As disclosed in the annual report of the Company for the year ended 31 December 2011 (the “2011 Annual Report”), the Indemnification Asset was recognised to represent an amount receivable from the vendor of Liaoyuan (the “Vendor”) as it had agreed under the sale and purchase agreement (the “Sale and Purchase Agreement”) to undertake the repayment of all liabilities of Liaoyuan existed prior to completion of acquisition of Liaoyuan. During 2011, the management negotiated with the Vendor to set off the Indemnification Asset against the unpaid consideration and other payable to the Vendor, which amounted to RMB128 million (approximately HK$157 million). Such set off arrangement has, however, not been agreed by the Vendor. The management assessed the recoverability of the Indemnification Asset based on the amount that could be recovered from the Vendor from time to time. As a result of the supplemental agreement entered in May 2012 (as detailed in sub-section headed “Supplemental Agreement of Acquisition” below), the Indemnification Asset would be recovered (and reduced) by the amount of net liabilities settled by a third party on behalf of Liaoyuan. Given that (1) the management assessed that HK$92.7 million would be recovered from the third party under the supplemental agreement; and (2) late payment charges of HK$29.4 million on outstanding consideration payable to the Vendor have been waived under the supplemental agreement, but the Indemnification Asset was aged over one year and remained unsettled as at the date of this report, an impairment loss of the Indemnification Asset of HK$33.5 million was made and was written off as uncollectible during the year.

Finance costs

Finance costs were approximately HK$136 million (2011: HK$171.8 million) during the year, which represented mainly interest expenses for bank and other loans in the People's Republic of China (the "PRC") amounting to approximately HK$115.2 million (2011: HK$106.2 million). Imputed interest expenses in respect of convertible notes amounting to approximately HK$20.8 million (2011: HK$26.9 million) were incurred during the year. No interest expenses in respect of the convertible bonds which were fully redeemed in September 2011 were incurred during the year (2011: HK$38.7 million).

Share of profit of a jointly-controlled entity

Share of profit of a jointly-controlled entity represented share of profit generated from the Fund Management Company. The investee was newly established and was operated at near break even in 2011.

Income tax

Income tax credit was approximately HK$521.9 million (2011: expenses of HK$40.4 million) during the year. It represented provision for taxation for operating profit generated from Liaoyuan of approximately HK$5.7 million (2011: HK$119.1 million) and write-back of deferred tax liabilities of approximately HK$527.6 million (2011: HK$78.7 million) which included (i) decrease in deferred tax liabilities of HK$192.5 million due to impairment, depreciation and amortisation of non-current assets during the year and (ii) decrease in deferred tax liabilities of HK$312.4 million related to deferred tax liabilities arising from fair value adjustments resulted from acquisition of subsidiaries in prior years. No provision for Hong Kong profits tax has been made during the year (2011: Nil).

Profit/(loss) for the year attributable to owners of the Company

Loss for the year attributable to owners of the Company was approximately HK$1,655.3 million (2011: profit of HK$55.3 million) during the year. The significant turnaround was mainly attributable to (1) significant decreases in revenue recorded; and (2) impairment losses of property, plant and equipment, mining rights, trade receivables, and prepayment, deposits and other receivables during the year.

LIQUIDITY AND FINANCIAL REVIEW

The Group mainly financed its day to day operations by internally generated cash flows and banking facilities during the year. As at 31 December 2012, the current ratio of the Group, measured as total current assets to total current liabilities, was 0.08:1 (2011: 0.37:1).

As at 31 December 2012, the cash and cash equivalents of the Group were approximately HK$15.9 million (2011: HK$51.9 million). During the year, the Group recorded a net cash inflows generated from its operating activities of approximately HK$246.9 million (2011: HK$784.6 million).

As at 31 December 2012, the Group had outstanding interest-bearing borrowings amounting to approximately HK$1,396 million (2011: HK$1,233.5 million). Of the Group's interest-bearing borrowings, 73%, 12% and 15% were repayable within one year, in the second year and in the third to the fifth year, inclusive, respectively (2011: 45%, 30%, 25%). All the interest-bearing loans of the Group were denominated in Renminbi. Interest-bearng loans of approximately HK$870.7 million (2011: HK$863.5 million) bear floating interest rates and interest-bearing loans of approximately HK$525.3 million (2011: HK$370 million) were charged at fixed rates of 6.15%–7.87% (2011: 6.31%) per annum.

As at 31 December 2012, the carrying amount of the liability component of the Group's zero coupon redeemable convertible notes was approximately HK$242.6 million (2011: HK$221.8 million). The zero coupon convertible notes, which have a 5-year term from 21 December 2009, are redeemable in whole or in part at face value by the Company at any time after 3 years from the issuance date (i.e. after 22 December 2012). No conversion or redemption of the convertible notes took place during the year. In March 2013, convertible notes of principal amount of HK$50 million have been early redeemed at par by the Company.

The Group conducted its continuing operational business transactions mainly in Renminbi and Hong Kong dollars. The Group did not arrange any forward currency contracts for hedging purposes.

GEARING RATIO

The gearing ratio of the Group, measured as net debt (which represents trade and bills payables, other payables and accruals and interest-bearing borrowings less cash and cash equivalents) to the total capital (which includes equity attributable to owners of the Company and convertible notes) was 2.18 as at 31 December 2012, as compared to 0.91 as at 31 December 2011.

SUBSCRIPTION FOR SHARES

On 12 October 2012, the Company entered into the subscription agreement with an investor pursuant to which the Company has conditionally agreed to issue and allot and the investor has conditionally agreed to subscribe in cash for 1,555,555,000 new shares at the subscription price of HK$0.45 per subscription share. The subscription was completed in January 2013, raising a gross proceed of HK$700 million. Details of the subscription were set out in the announcements dated 17 October 2012 and 31 January 2013 and the circular dated 15 November 2012.

SIGNIFICANT INVESTMENTS, MATERIAL ACQUISITIONS AND DISPOSALS

On 31 August 2011, the Company entered into a memorandum of understanding (the "MOU") to acquire not less than 51% equity interest of one of the coal mines in Shanxi, the PRC. The MOU lapsed on 31 January 2012 and the earnest money of HK$180 million has been refunded by the vendor accordingly.

Save as disclosed above, the Group had no other material acquisition or disposal during the year.

UPDATES OF ACQUISITION OF LIAOYUAN

1. Guaranteed Profit

As set out in the announcement of the Company dated 25 July 2011 in relation to acquisition of Liaoyuan (the "Acquisition"), the final consideration payable by the Group for the Acquisition of RMB100 million is subject to adjustment depending on whether the actual profit after tax of Liaoyuan for the period from the date of completion of Acquisition to 31 December 2011 (the "Actual Profit") reached RMB54 million or not (the "Guaranteed Profit"). Based on mutual understanding between the parties to the Sale and Purchase Agreement, the Actual Profit and Guaranteed Profit should be determined under the PRC accounting standards. Based on the financial statements of Liaoyuan prepared under the PRC accounting standards, the Actual Profit of Liaoyuan (which was generated from its ordinary and usual course of principal business and not from any extraordinary items) was approximately RMB54.8 million (approximately HK$65.9 million) which exceeded the Guaranteed Profit. As the Guaranteed Profit was met, no adjustment was required to be made to the consideration payable to the Vendor. The remaining consideration of RMB100 million was settled on 31 May 2012.

The reference to the profit of Liaoyuan of HK$62,971,000 in the 2011 Annual Report was determined and presented based on Hong Kong accounting standards which was so disclosed to be consistent with the accounting policies adopted by the Group in the 2011 Annual Report.

2. **Supplemental Agreement of Acquisition**

According to the supplemental agreement entered among the Vendor, the Group and 內蒙古華特能源有限公司, an independent third party (the "Third Party", who assisted the Vendor to operate Liaoyuan), in May 2012 (the "Supplemental Agreement"), (i) the Group agreed to release RMB100 million from the custody account to settle the remaining consideration of RMB100 million, (ii) there would be no claim by the Vendor against the Group for any delay in payment of the second instalment of RMB150 million in February and April 2012 which was obligated to be paid to the Vendor on 31 October 2011, (iii) the Third Party, who is specialised in mine operation and has extensive connection with local government authorities, would assist in smoothening the operation of Liaoyuan such as application for the mining licenses of approved production capacity to 0.9 million tons per annum; and (iv) certain assets and liabilities (i.e. net liabilities) of Liaoyuan existed prior to 1 June 2012 would be taken up by the Third Party and all the obligations of the Vendor under the Sale and Purchase Agreement should be considered duly fulfilled. Details of the Supplemental Agreement were set out in the announcement of the Company dated 5 October 2012.

CAPITAL COMMITMENTS, CHARGE ON GROUP ASSETS AND CONTINGENT LIABILITIES

As at 31 December 2012, the capital commitments of the Group were approximately HK$32.5 million (2011: HK$64.9 million). The capital commitments were mainly related to purchase of machineries for the operation of coal mines.

As at 31 December 2012, the bank loans of approximately HK$809 million were secured by certain of the Group's mining rights and guarantees given by a former shareholder of Triumph Fund A Limited (a subsidiary of the Company), a former director of Hengtai and certain independent third parties. In addition, an other loan from an independent third party of HK$382.5 million is secured by certain of the Group's construction in progress and prepayments, deposits and other receivables.

As at 31 December 2012, time deposits of approximately HK$3.5 million (2011: HK$2.9 million) were pledged for general bank facilities.

Save as disclosed above, the Group had no other pledge of assets as at 31 December 2012.

As at 31 December 2012 and 31 December 2011, the Group did not have any material contingent liability.

HUMAN RESOURCES AND SHARE OPTION SCHEME

As at 31 December 2012, the Group had 355 employees. The total staff costs for the year ended 31 December 2012 were approximately HK$69 million (2011: HK$88.6 million). The Group's remuneration policy is primarily based on the individual performance and experience of employees including directors, prevailing industry practice and market rates. In addition to the basic salaries, the Group provides staff benefits including medical insurance and contributions to the provident fund. Discretionary bonuses are also available to the Group's employees depending upon the overall performance of the Group. The Group also provides appropriate training programmes for employees' better personal development and growth.

Pursuant to the Company's new share option scheme adopted on 30 May 2012, the Company may offer to any eligible participants including employee of the Group options to subscribe for shares in the Company for a period of 10 years. As at 31 December 2012, a total of 24,616,000 share options were outstanding and were held by directors and employees. No share option was granted or exercised during the year.

FUTURE OUTLOOK

Stepping into the year of 2013, the Company is pleased to announce the completion of the share subscription with the introduction of a new controlling shareholder led by Beida Jade Bird Group. The subscription has provided the Company adequate funding to significantly improve its financial liquidity, as well as to grasp any potential investment opportunities when they arise. The new management team of the Company, who possesses profound industry knowledge of natural resources investments, is eager to bring the Company into a new prosperity.

In view of the performance of coal mining business, the Company will review its investment portfolios on a timely basis and on the other hand, the Company plans to further diversify its investments into other natural resources which include but not limited to precious metals, oil and gas on a worldwide basis. The new management team believes that by investing into commodities of which prices are highly transparent and are available for hedging, the revenue and cash flows of the Company will become relatively stable and foreseeable.

Leveraging on the solid experience of natural resources investments, the new management team will capably cope with the ever-changing market environment and react quickly to potential investment opportunities.

EXECUTIVE DIRECTORS

Mr. Xu Zhendong, aged 49, graduated from the Computer Science and Technology Department of Peking University in 1987. Currently, Mr. Xu is an executive director and chairman of board of directors of Beijing Beida Jade Bird Universal Sci-Tech Company Limited ("Jade Bird Universal") (a company listed on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (the "Stock Exchange") (stock code: 8095)). He is a director of each of Beida Jade Bird Universal Sci-Tech (Cayman) Development Company Limited and Beida Jade Bird Universal Investments (USA) Limited respectively, which are subsidiaries of Jade Bird Universal. Mr. Xu is also the chairman of each of boards of directors of Beijing Aptech Beida Jade Bird Information Technology Co., Ltd. and Beijing Beida Jade Bird Software System Co., Ltd. and a director of Shenzhen Beida Jade Bird Sci-Tech Co., Ltd. and Hang Zhou Beida Jade Bird Sci-Tech Co., Ltd.. He was appointed as the executive director and Chairman of the Company on 12 March 2013.

Mr. Zhang Wanzhong, aged 50, is an executive director and the president and compliance officer of Jade Bird Universal. Mr. Zhang is primarily responsible for overall business development, compliance and public relations of Jade Bird Universal. He graduated from Peking University with a Master's degree in science. He worked in several administrative departments of Peking University including the vice president of the Remote Sensing and Geographic Information System Department of Peking University, which was responsible for the State's focal science and technological project. Mr. Zhang is a director of Beida Jade Bird Universal Investments (USA) Limited, Beida Jade Bird Universal Fire Alarm Device Company Limited and Chuanqi Tourism Investment Co., Ltd., which are subsidiaries of Jade Bird Universal, a director of Beijing Beida Jade Bird International Education Investment Management Co., Ltd.. He was appointed as the executive director of the Company on 1 February 2013.

Mr. Zong Hao, aged 43, obtained a degree of the Master of Laws from Buffalo Law School, the State University of New York in 1997. Mr. Zong is currently an independent director of Suzhou Electrical Apparatus Science Academy Co., Ltd., a company listed on the Shenzhen Stock Exchange (stock code: 300215). Mr. Zong was the chief representative of Cherry Lane Music Publishing Company Inc. Beijing office from 2003 to 2010. He was also the executive vice president of Quintana China and Taggart China LLC from 2007 to January 2013. He was appointed as the executive director and chief executive officer of the Company on 1 February 2013.

Mr. Tian Wenwei, aged 42, holds an MBA at Business School of University of Alberta, Canada. He has over 15 years experience in finance, business and corporate merger and acquisition. He also has solid knowledge and experiences in coal industry. Mr. Tian is responsible for coal business development of the Group in China. Mr. Tian worked in the Bank of Communications, Xian Branch, from 1991 to 1997 and in China Digital Finance Times Company, a subsidiary of China Everbright Group from 2000 to 2001. He was an officer of Puda Coal, Inc., a public company in the United States of America from 2006 to 2009. He has been a director of Triumph Fund A Limited, a subsidiary of the Company since September 2009. He was appointed as the executive director of the Company on 18 January 2010.

Mr. Xu Zhuliang, aged 43, obtained a diploma from Taiyuan University of Technology in 1991. Mr. Xu holds the Safety Qualification Certificate issued by the State Administration of Work Safety. Since 2009, Mr. Xu has been the Assistant to President and Vice President of Beida Jade Bird Group, and is primarily responsible for the management of the company's coal mine and chemical projects. During the period from 2006 to 2008, Mr. Xu was the manager of Shanxi Tianchengdayang Energy Chemical Industry Co. Ltd., a company specialized in the development, production and processing of energy chemical products. Prior to that, Mr. Xu was the manager of Shanxi Glamour Science & Technology Co. Ltd. During the period from 2002 to 2006, he was responsible for the research and development, investment, construction and operation of the coal mine and chemical projects of that company. He was appointed as the executive director of the Company on 12 March 2013.

Mr. Benjamin Clark Danielson, aged 42, obtained Bachelor of Science degree from the United States Military Academy at West Point in 1992 and a Master of Business Administration degree from the University of Texas at Austin in 2000. Mr. Danielson has been managing and monitoring the activities of the fund portfolio companies as well as sourcing, evaluating and executing investments for private equity funds. During the period from 2006 to 2012, Mr. Danielson worked at Quintana Capital Group, a United States-based private equity fund focused in energy-related industries, most recently acting as Chief Investment Offer, China. He was appointed as the executive director and chief investment officer of the Company on 12 March 2013.

NON-EXECUTIVE DIRECTOR

Mr. Zhang Yongli, aged 48, graduated from the Geology Department of Peking University with a Bachelor's degree in science and subsequently obtained a doctor of philosophy in engineering from Geology and Mineralogy Department of China University of Geosciences. He has been appointed as deputy general manager and chief financial officer of Beijing Beida Jade Bird Limited since November 1998 and mainly responsible for administration and finance. Currently, Mr. Zhang is the chairman of the supervisory committee of Jade Bird Universal. Mr Zhang was a supervisor of Jade Bird Universal for the period before 8 January 2010 and was appointed as an executive director for the period from 8 January 2010 to 21 June 2012. Mr. Zhang is also the chairman of the supervisory committee of Weifang Beida Jade Bird Huaguang Technology Co., Ltd. (an A share listed company in the People's Republic of China). He is a director of Chuanqi Tourism Investment Co., Ltd. and the chairman of Beijing Beida High Technology Investment Co., Ltd. and Hang Zhou Beida Jade Bird Sci-Tech Co., Ltd. He was appointed as the non-executive director of the Company on 12 March 2013.

INDEPENDENT NON-EXECUTIVE DIRECTORS

Mr. Chiu Sui Keung, aged 45, has over 15 years experience in the strategic management in various listed companies, financial industry and accounting field. He has possessed extensive experience in corporate finance including initial public offerings, takeovers, mergers and acquisitions, fund raising and corporate advisory. Mr. Chiu graduated with a Bachelor's Degree in Commerce from the University of Melbourne, Australia and has obtained a Master's Degree in Applied Finance from Macquarie University in Sydney, Australia. He has also obtained a Diploma in Practices in Chinese Laws and Regulations Affecting Foreign Businesses jointly organized by Southwest University of Political Science and Law, the PRC and the Hong Kong Management Association. He is a member of the American Institute of Certified Public Accountants. He is currently the executive director and chief executive officer of Sino Resources Group Limited (stock code: 223) and was the non-executive director of China New Energy Power Group Limited (stock code: 1041) during the period from September 2008 to July 2009, both of the companies are listed on the Stock Exchange. He was appointed as the independent non-executive director of the Company on 18 January 2010.

Mr. Li Peiming, aged 61, has served in the People's Liberation Army for 15 years. After his service in the army, Mr. Li worked in National Audit Office of the People's Republic of China ("CNAO") and possesses over 20 years of experience in auditing. During his tenure in CNAO, he has been the director of Tourism and Overseas Chinese Affairs Audit Office and Economic Law Implementation Audit office, and the executive secretary to the Party Committee for CNAO. He is currently the independent director of Wuhan Kaidi Electric Power Co., Ltd, a listed company on the Shenzhen Stock Exchange (stock code 000939.sz). He was appointed as the independent non-executive director of the Company on 30 September 2011.

Mr. Lee Chi Hwa, Joshua, aged 40, is a fellow member of the Association of Chartered Certified Accountants and a member of the Hong Kong Institute of Certified Public Accountants. Mr. Lee has extensive experience in the fields of auditing, accounting and finance. Mr. Lee is an independent non-executive director of China Public Healthcare (Holdings) Limited (stock code: 8116) and CODE Agriculture (Holdings) Limited (stock code: 8153), which are listed on the Growth Enterprise Market board of the Stock Exchange. He was appointed as the independent non-executive director of the Company on 9 January 2012.

Mr. Lu Binghui, aged 37, graduated from Beijing University with a Bachelor Degree in Philosophy and a Master Degree in Economics. He has extensive experience of investment management in investment banks and private equity. From 2010 to 2012, he was the principal of Kohlberg Kravis Roberts & Co, a private equity, where he was mainly responsible for proprietary deal sourcing, transaction execution and post-investment management focusing on energy and natural resources sectors. Prior to that, he worked in Goldman Sachs Gaohua Securities Company Limited and Goldman Sachs China Business as executive director and A-share Sponsorship Representative from 2005 to 2010. From 2000 to 2005, he worked in investment banking department of Bank of China International. He was appointed as the independent non-executive director of the Company on 22 March 2013.

SENIOR MANAGEMENT

Mr. Lee Tao Wai, aged 34, is the company secretary of the Company. Mr. Lee is a member of the Hong Kong Institute of Certified Public Accountants and has over 10 years of experience in auditing, accounting and corporate field. Prior to joining the Company, Mr. Lee worked in an international accounting firm and a listed company in Hong Kong as senior executive. Mr. Lee holds a Bachelor Degree in Business Administration in Accounting from the Chinese University of Hong Kong and a Master Degree in Investment Management from The Hong Kong University of Science and Technology. He joined the Group in April 2010.

INTRODUCTION

The Company is committed to maintaining a high standard of corporate governance and has taken appropriate steps to adopt and comply with the provisions of its Code on Corporate Governance Practices (the "Code") which adopted practices that meet the requirements set out in Appendix 14 to the Rules Governing the Listing of Securities on the Stock Exchange (the "Listing Rules") during the year, except for certain deviations as explained on this report.

DIRECTORS' SECURITIES TRANSACTIONS

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") as set out in Appendix 10 to the Listing Rules as its own code for dealing in securities of the Company by the Directors of the Company (the "Directors"). Having made specific enquiry of all Directors, the Directors confirm that they have complied with the required standard as set out in the Model Code during the year ended 31 December 2012.

BOARD OF DIRECTORS

The Board of Directors (the "Board") is principally accountable to the shareholders and is responsible for the leadership and control of the Group including overseeing the Group's businesses, strategic directions, financial performance, setting objectives and business development plans, and monitoring the performance of the management.

The Board, with balance of skills and experience, meets regularly throughout the year to formulate overall strategy, monitor business development as well as the financial performance of the Group and has formal procedures on matters for consideration and decision. The Board has delegated certain authorities to the management for the day-to-day management of the Group's operation.

The Directors have no financial, business, family or other material/relevant relationship among themselves.

The Company has received the annual confirmation of independence from each of the independent non-executive Directors as required under Rule 3.13 of the Listing Rules. The Company considers all independent non-executive Directors to be independent.

DIRECTORS' ATTENDANCE RECORD AT MEETINGS

The attendance of each Director at the Board meetings, certain committee meetings and general meetings during the year is as follows:

		Attended/Eligible to attend				
		Board meeting	Audit Committee meeting	Remuneration Committee meeting	Nomination Committee meetings	General meetings
Executive Directors:						
Mr. Xu Zhendong *(Chairman)*	(appointed on 12 March 2013)	N/A	N/A	N/A	N/A	N/A
Mr. Tian Wenwei		13/14	N/A	N/A	N/A	1/2
Mr. Zong Hao	(appointed on 1 February 2013)	N/A	N/A	N/A	N/A	N/A
Mr. Zhang Wanzhong	(appointed on 1 February 2013)	N/A	N/A	N/A	N/A	N/A
Mr. Xu Zhuliang	(appointed on 12 March 2013)	N/A	N/A	N/A	N/A	N/A
Mr. Benjamin Clark Danielson	(appointed on 12 March 2013)	N/A	N/A	N/A	N/A	N/A
Mr. Wang Da Yong	(resigned on 1 February 2013)	14/14	N/A	1/1	N/A	2/2
Mr. Wang Tongtian	(resigned on 1 February 2013)	4/14	N/A	N/A	N/A	1/2
Mr. Chen Marlon Ray	(resigned on 12 March 2013)	4/14	N/A	N/A	N/A	2/2
Non-executive Directors:						
Mr. Seah Ang	(appointed on 25 June 2012 and resigned on 12 March 2013)	2/4	N/A	N/A	N/A	0/1
Mr. Wong Chun Hung	(appointed on 16 April 2012 and resigned on 12 March 2013)	4/7	N/A	N/A	N/A	2/2
Mr. Li Yi	(resigned on 1 June 2012)	0/8	N/A	N/A	N/A	0/1
Mr. Su Bin	(resigned on 1 June 2012)	1/8	N/A	N/A	N/A	0/1
Mr. Li Feng	(resigned on 27 February 2012)	0/2	N/A	N/A	N/A	0/0
Mr. Wang Daoyuan	(resigned on 27 February 2012)	0/2	N/A	N/A	N/A	0/0
Mr. Zhang Yongli	(appointed on 12 March 2013)	N/A	N/A	N/A	N/A	N/A
Independent non-executive Directors:						
Mr. Chiu Sui Keung		5/14	2/2	1/1	1/1	0/2
Mr. Li Peiming		4/14	2/2	1/1	1/1	1/2
Mr. Lee Chi Hwa, Joshua	(appointed on 9 January 2012)	2/13	N/A	N/A	1/1	0/2
Mr. Lam Ka Wai, Graham	(appointed on 23 April 2012 and resigned on 22 March 2013)	2/6	1/1	0/1	0/1	0/2
Mr. Cao Kuangyu	(resigned on 23 April 2012)	1/7	1/1	0/0	0/0	0/0
Mr. Lu Binghui	(appointed on 22 March 2013)	N/A	N/A	N/A	N/A	N/A

ROLES AND RESPONSIBILITIES OF CHAIRMAN AND CHIEF EXECUTIVE OFFICER

Under provision A.2.1 of the Code, the roles of chairman and chief executive officer should be separate and should not be performed by the same individual.

During the year, Mr. Wang Da Yong, was the chief executive officer and chairman of the Company. The Board considers that the structure did not impair the balance of power and authority between the Board and the management of the Group. The balance of power and authority was ensured by the operations of the board committees which comprise experienced and high calibre individuals and met frequently to discuss issues. The Board also considered that the structure enabled the effectiveness and efficiency of the Group's operations and was beneficial to the business prospects of the Group.

Following the resignation of Mr. Wang Da Yong as Director with effect from 1 February 2013, Mr. Xu Zhendong is now the chairman while Mr. Zong Hao is the chief executive officer. In this connection, the Company has complied with this provision.

TERM OF NON-EXECUTIVE DIRECTORS

Under provision A.4.1 of the Code, non-executive Directors should be appointed for a specific term, and subject to re-election in accordance with the articles of association of the Company (the "Articles of Association"). All of the existing non-executive Directors and independent non-executive Directors are not appointed for specific terms, however, all of them are subject to retirement by rotation in accordance with the Articles of Association.

According to the Articles of Association, one third of the Directors shall retire from office by rotation at the annual general meeting of the Company and every Director shall be subject to retirement by rotation at least once every three years. The Board considers that sufficient measures were taken to ensure the corporate governance practices of the Company are not less than those in the Code.

AUDIT COMMITTEE

The Company has established an audit committee ("Audit Committee") with written terms of reference which are in line with the code provisions set out in the Code. The Audit Committee meets at least twice a year for, among other matters, reviewing the reporting of annual and interim results and other information to the shareholders, the effectiveness and objectivity of the audit process and the Company's policy and practices on corporate governance. Additional meetings may be held by the Audit Committee from time to time to discuss special projects or other issues which the Audit Committee considers necessary. The external auditors of the Company may request a meeting if they consider that one is necessary. The Audit Committee also provides an important link between the Board and the Company's auditors in matters coming within the scope of its terms of reference and keeps under review the independence and objectivity of the auditors. The terms of reference of the Audit Committee are disclosed on the websites of the Company and the Stock Exchange. The Audit Committee currently consists of Mr. Chiu Sui Keung as chairman and Mr. Li Peiming and Mr. Lu Binghui as members. All of them are independent non-executive Directors.

The Audit Committee is also responsible for performing the functions set out in the provision D.3.1 of the Code. The Audit Committee reviewed the Company's corporate governance policies and practices, training and continuous professional development of Directors and senior management, the Company's policies and practices on compliance with legal and regulatory requirements, the code of conduct and compliance manual (if any) applicable to employees and Directors, the compliance of the Listing Rules, and the Company's compliance with the Code and disclosure in this Corporate Governance Report.

During the year, the Audit Committee held two meetings and reviewed with the management and the Company's auditors the accounting principles and practices adopted by the Group, discussed auditing, internal control and financial reporting matters including the annual results for the year ended 31 December 2011 and interim results for the six months ended 30 June 2012 and reviewed the Company's compliance with the Code.

REMUNERATION COMMITTEE

The remuneration committee ("Remuneration Committee") of the Group was established in September 2005 with written terms of reference in line with the Code. The responsibilities of the Remuneration Committee include, among other matters, considering and recommending to the Board the Group's remuneration policy and structure and reviewing and determining the remuneration packages of the individual executive Directors and senior management. The Directors were remunerated with reference to their respective duties and responsibility with the Company, the Company's performance and current market situation. The terms of reference of the Remuneration Committee are disclosed on the websites of the Company and the Stock Exchange. Details of remunerations of the Directors for the year are disclosed in note 9 to the financial statements.

The Remuneration Committee currently comprises two independent non-executive Directors, Mr. Chiu Sui Keung (Chairman) and Mr. Li Peiming, and one executive Director, Mr. Tian Wenwei. The Remuneration Committee held one meeting to review the existing remuneration policy and structure of the Company during the year.

NOMINATION COMMITTEE

According to the Articles of Association, the Board has the power to appoint any person as a Director either to fill a causal vacancy or as an addition to the Board. The nomination should take into consideration the nominee's qualification, ability and potential contributions to the Company. All Directors should be subject to re-election in accordance with the Articles of Association.

The nomination committee ("Nomination Committee") was established in March 2012 with written terms of reference to (i) review and recommend the structure, size, composition and skills mix of the Board at least annually; (ii) identify and nominate candidates to fill casual vacancies of Directors for the Board's approval; (iii) assess the independence of independent non-executive Directors; (iv) regularly review the time required from a Director to perform his responsibilities; (v) make recommendations to the Board on relevant matters relating to the appointment or re-appointment of Directors and succession planning for Directors in particular the chairman of the Board and the chief executive. The terms of reference of the Nomination Committee are disclosed on the websites of the Company and the Stock Exchange. The Nomination Committee currently comprises one executive Director, Mr. Zhang Wanzhong (Chairman), and three independent non-executive Directors, Mr. Chiu Sui Keung, Mr. Li Peiming and Mr. Lee Chi Hwa, Joshua.

The Nomination Committee held one meeting to review the board composition during the year.

ACCOUNTABILITY AND AUDIT

Directors' Responsibilities for the Financial Statements

The Directors are responsible for the preparation of the financial statements for each financial period which give a true and fair view of the state of affairs of the Group and the Company and of the results and cash flows of the Group for that period. In preparing the financial statements for the year ended 31 December 2012, the Directors have selected suitable accounting policies and applied them consistently, made judgments and estimates that are prudent, fair and reasonable and prepared the financial statements on a going concern basis. The Directors are also responsible for keeping proper accounting records with reasonable accuracy for safeguarding the assets of the Group and for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Save as disclosed in note 2 to the financial statements, there are no material uncertainties relating to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern.

The Board has not taken any different view from that of the Audit Committee regarding the selection, appointment, resignation or dismissal of external auditors.

Auditors' Responsibilities and Remuneration

An analysis of remuneration in respect of services provided by the auditors, (Ernst & Young) and advisors (Ernst & Young Advisory Services Limited), of the Group is as follows:

	HK$'000
Annual audit services	2,730
Agreed-upon procedures on interim financial reports	420
Internal control review services	210
	3,360

The statement of the auditors of the Company regarding their reporting responsibilities is set out in the Independent Auditors' Report on pages 34 to 35.

Internal Control

During the year, the Company has adopted and reviewed the effectiveness of the Group's internal control procedures which include the policies, procedures, monitoring and communication activities and standard of behavior established for safeguarding the interests of the shareholders of the Company. The system of internal control 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, the risks of failure when business objectives are being sought.

Based on its assessment which covers all material controls including financial, operational and compliance controls and risk management functions, the Board believes that for the year ended 31 December 2012, the Company's internal control is effective. The Board is satisfied that there are adequate resources of staff with appropriate qualifications and experience in its accounting and financial reporting team and that sufficient training and budget have been provided.

DIRECTORS' TRAINING

Each newly appointed Director has received comprehensive, formal and tailored induction on the first occasion of his appointment, so as to ensure that he has appropriate understanding of the business and operations of the Group and that he is fully aware of his responsibilities and obligations under the Listing Rules and relevant regulatory requirements. There are also arrangements in place for providing continuing briefing and professional development to Directors at the Company's expenses whenever necessary.

During the year, all Directors were provided with regular updates on the Group's business and operations. An in house briefing was organised for Directors during the year to update the Directors on the amendments on the Listing Rules and guidelines on disclosure of insider information. Mr. Li Peiming, Mr. Chiu Sui Keung and Mr. Lam Ka Wai, Graham also attended seminars and/or conferences and/or forums to refresh knowledge and skills.

SHAREHOLDERS' RIGHTS

The Board endeavours to maintain an on-going dialogue with shareholders. The Company encourages the shareholders to attend the general meetings and the Chairmen of the Board and the board committees should attend the annual general meeting to answer questions.

Shareholders should direct their enquiries about their shareholdings to the Company's branch share registrar, Tricor Secretaries Limited. For other enquiries, shareholders may send written enquiries to the Company, for the attention of company secretary, by email to king.stone@663hk.com, fax to (852) 2530 5663, mail to Unit 7603, 76/F, The Center, 99 Queen's Road Central, Hong Kong or by submitting enquiry form at www.663hk.com.

Under Section 113 of the Companies Ordinance (Chapter 32 of the Laws of Hong Kong), the shareholders can convene an extraordinary general meeting. Requisition to convene an extraordinary general meeting can be deposited by the members of the Company holding at the date of the deposit of the requisition not less than one-twentieth of such of the paid-up capital of the Company as at the date of the deposit carries the right of voting at general meetings of the Company. The requisitionists must submit their requisition in writing, in which it must state the objects of the meeting, and be duly signed by the requisitionists, mailed and deposited at Unit 7603, 76/F, The Center, 99 Queen's Road Central, Hong Kong (attention of company secretary); and may consist of several documents in like form, each signed by one or more requisitionists. The requisition will be verified with the Company's share registrar and upon its confirmation that the requisition is proper and in order, the company secretary will arrange the Board to convene an extraordinary general meeting by serving sufficient notice in accordance with the statutory requirements to all registered shareholders, provided that the requisitionists have deposited a sum of money reasonably sufficient to meet the Company's expenses involved in convening an extraordinary general meeting . On the contrary, if the requisition has been verified as not in order, the requisitionists will be advised of this outcome and accordingly, an extraordinary general meeting will not be convened as requested.

If within 21 days from the date of the deposit of the requisition proceed duly the Directors do not convene a meeting for a day not more than 28 days after the date on which the notice convening the meeting is given, the requisitionists, or any of them representing more than one-half of the total voting rights of all of them, may themselves convene a meeting, but any meeting so convened shall not be held after the expiration of 3 months from the said date. A meeting convened under this section by the requisitionists shall be convened in the same manner, as nearly as possible, as that in which meetings are to be convened by Directors in accordance to the Articles of Association of the Company and the Listing Rules. Any reasonable expenses incurred by the requisitionists by reason of the failure of the Directors duly to convene a meeting shall be refunded to the requisitionists by the Company.

In accordance with Section 115A of the Companies Ordinance (Chapter 32 of the Laws of Hong Kong), the following shareholders namely: (a) any number of members representing not less than 2.5% of the total voting rights of the Company on the date of the requisition; or (b) not less than 50 members holding shares in the Company on which there has been paid up on average sum, per member, of not less than HK$2,000; are entitled to submit a requisition in writing requesting the Company: (a) to give to members of the Company entitled to receive notice of the next annual general meeting notice of any resolution which may properly be moved and is intended to be moved at that meeting; and/or (b) to circulate to members entitled to have notice of any general meeting sent to them any statement of not more than 1,000 words with respect to the matter referred to in any proposed resolution or the business to be dealt with at that meeting. A requisition signed by the shareholders concerned (or 2 or more copies which between them containing signatures of all the shareholders concerned) must be deposited at the registered office of the Company at Unit 7603, 76th Floor, The Center, 99 Queen's Road Central, Hong Kong for the attention of the Company Secretary not less than 6 weeks before an annual general meeting in the case of a requisition requiring notice of a resolution and not less than 1 week before an annual general meeting in case of any other requisition. In addition, the concerned shareholders must deposit with the requisition a sum reasonably sufficient to meet the expenses in giving effect the above. However, if, after a requisition requiring notice of a resolution has been deposited at the registered office of the Company, an annual general meeting is called for a date 6 weeks or less after the requisition has been deposited, the requisition though not deposited within the time required as referred to above shall be deemed to have been properly deposited.

The procedures for proposing a person for election as a Director are made available at the Company's website (www.663hk.com).

INVESTOR RELATIONS

The Company believes in regular and timely communication with shareholders as part of its efforts to help shareholders understand its business better and the way the Company operates. To promote effective communication with the public, the Company maintains a website (www.663hk.com) on which comprehensive information about the Company's major businesses, press releases, notices, financial information, announcements, annual and interim reports and shareholders circulars are being made available.

There was no change in the Company's constitutional documents during the year ended 31 December 2012.

REPORT OF THE DIRECTORS

The Directors (the "Directors") of King Stone Energy Group Limited (the "Company") present their report and the audited financial statements of the Company and its subsidiaries (together, the "Group") for the year ended 31 December 2012.

PRINCIPAL ACTIVITIES

The principal activity of the Company is investment holding. Details of the principal activities of the subsidiaries are set out in note 17 to the financial statements. There were no significant changes in the nature of the Group's principal activities during the year.

RESULTS

The Group's loss for the year ended 31 December 2012 and the state of affairs of the Company and the Group at that date are set out in the financial statements on pages 36 to 105.

SUMMARY FINANCIAL INFORMATION

A summary of the published results and assets, liabilities and non-controlling interests of the Group for the last five financial years, as extracted from the audited financial statements, is set out on page 106. This summary does not form part of the audited financial statements.

PROPERTY, PLANT AND EQUIPMENT

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

SHARE CAPITAL, SHARE OPTIONS AND CONVERTIBLE NOTES

Details of movements in the Company's share capital, share options and convertible notes during the year are set out in notes 29, 30 and 27 to the financial statements, respectively.

PURCHASE, REDEMPTION OR SALE OF LISTED SECURITIES OF THE COMPANY

Neither the Company, nor any of its subsidiaries purchased, redeemed or sold any of the Company's listed securities during the year ended 31 December 2012.

RESERVES

Details of movements in the reserves of the Company and the Group during the year are set out in note 31(b) to the financial statements and in the consolidated statement of changes in equity, respectively.

DISTRIBUTABLE RESERVES

At 31 December 2012, the Company had no retained profits calculated in accordance with the provisions of Section 79B of the Hong Kong Companies Ordinance, available for distribution. However, the Company's share premium account, in the amount of HK$1,166,813,000, may be distributed in the form of fully paid bonus shares.

MAJOR CUSTOMERS AND SUPPLIERS

In the year under review, sales to the Group's five largest customers accounted for 64% of the total sales for the year and sales to the largest customer included therein amounted to 31% of the total sales. Purchases from the Group's five largest suppliers accounted for 49% of the total purchases for the year and purchase from the largest supplier included therein amounted to 24% of the total purchases.

None of the Directors or any of their associates or any shareholders (which, to the best knowledge of the Directors, own more than 5% of the Company's issued share capital) had any beneficial interest in the Group's five largest customers and suppliers.

DIRECTORS

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

Executive Directors:

Mr. Xu Zhendong *(Chairman)*	(appointed on 12 March 2013)
Mr. Tian Wenwei	
Mr. Zong Hao	(appointed on 1 February 2013)
Mr. Zhang Wanzhong	(appointed on 1 February 2013)
Mr. Xu Zhuliang	(appointed on 12 March 2013)
Mr. Benjamin Clark Danielson	(appointed on 12 March 2013)
Mr. Chen Marlon Ray	(resigned on 12 March 2013)
Mr. Wang Da Yong	(resigned on 1 February 2013)
Mr. Wang Tongtian	(resigned on 1 February 2013)

Non-executive Directors:

Mr. Zhang Yongli	(appointed on 12 March 2013)
Mr. Seah Ang	(appointed on 25 June 2012 and resigned on 12 March 2013)
Mr. Wong Chun Hung	(appointed on 16 April 2012 and resigned on 12 March 2013)
Mr. Li Yi	(resigned on 1 June 2012)
Mr. Su Bin	(resigned on 1 June 2012)
Mr. Li Feng	(resigned on 27 February 2012)
Mr. Wang Daoyuan	(resigned on 27 February 2012)

Independent non-executive Directors:

Mr. Chiu Sui Keung	
Mr. Li Peiming	
Mr. Lu Binghui	(appointed on 22 March 2013)
Mr. Lee Chi Hwa, Joshua	(appointed on 9 January 2012)
Mr. Lam Ka Wai, Graham	(appointed on 23 April 2012 and resigned on 22 March 2013)
Mr. Cao Kuangyu	(resigned on 23 April 2012)

In accordance with the Company's articles of association, (i) Directors appointed during the year shall hold office until the forthcoming annual general meeting and eligible for re-election and (ii) at each annual general meeting, one-third of the Directors shall retire from office by rotation. Mr. Xu Zhengdong, Mr. Zhang Wanzhong, Mr. Zong Hao, Mr. Tian Wenwei, Mr. Xu Zhuliang, Mr. Benjamin Clark Danielson, Mr. Zhang Yongli and Mr. Lu Binghui will retire and, being eligible, will offer themselves for re-election at the forthcoming annual general meeting.

DIRECTORS' AND SENIOR MANAGEMENT BIOGRAPHIES

Biographical details of the Directors and senior management of the Group are set out on pages 14 to 16 of the annual report.

DIRECTORS' SERVICE CONTRACTS

No Director proposed for re-election at the forthcoming annual general meeting has a service contract with the Company which is not determinable by the Company within one year without payment of compensation, other than statutory compensation.

DIRECTORS' REMUNERATION

The remuneration of the Directors are determined by the remuneration committee of the Company with reference to the Directors' duties, responsibilities and performance and the results of the Group. Further details of the Company's remuneration committee are set out in the corporate governance report on pages 17 to 23 of the annual report.

DIRECTORS' INTERESTS IN CONTRACTS

No Director had a material interest, either directly or indirectly, in any contract of significance to the business of the Group to which the Company or any of its subsidiaries was a party during the year.

DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS AND SHORT POSITIONS IN SHARES AND UNDERLYING SHARES

As at 31 December 2012, the following Directors or the chief executive of the Company and their respective associates had or were deemed to have interests in the long or short positions in the shares or underlying shares of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO"), Chapter 571 of the Laws of Hong Kong) which (i) were required to be notified to the Company and The Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests in the long or short positions which they were taken or deemed to have under such provision of the SFO); or (ii) were required, pursuant to section 352 of the SFO, to be entered in the register referred to therein; or (iii) were required to be notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies (the "Model Code") contained in The Rules Governing the Listing of Securities on the Stock Exchange (the "Listing Rules").

Name of Director	Capacity	Interest in shares	Interest in underlying shares	Total interest in shares	Approximate percentage of the Company's issued share capital
Mr. Wang Da Yong (note 1)	Through controlled corporation/ spouse/ beneficial owner	278,784,500	5,000,000	283,784,500	19.86%
Mr. Tian Wenwei (note 2)	Beneficial owner	—	3,750,000	3,750,000	0.26%
Mr. Wang Tongtian (note 3)	Beneficial owner	—	1,500,000	1,500,000	0.10%
Mr. Chiu Sui Keung (note 4)	Beneficial owner	—	500,000	500,000	0.03%

Notes:

1. These shares and underlying shares are held by Mr. Wang Da Yong under the below capacities:

   (a) 160,082,000 shares are held by Join Ascent Limited, which is held as to 80% and 20% by Mr. Wang Da Yong and Mr. Tian Wenwei, respectively.

   (b) 27,838,500 shares are held by China Coal and Coke Investment Holding Company Limited, which is wholly owned by Sino Bridge Investments Limited, a company wholly owned by Mr. Wang Da Yong.

   (c) 81,885,000 shares are held by Sky Circle International Limited, which is wholly owned by Mr. Wang Da Yong.

   (d) 2,671,000 shares are held by Ms. Yuan Hong, the spouse of Mr. Wang Da Yong.

   (e) 6,308,000 shares are held personally by Mr. Wang Da Yong.

   (f) 5,000,000 underlying shares represent share options granted to Mr. Wang Da Yong under the share option scheme of the Company which are exercisable at the subscription price of HK$4.96 per share (subject to adjustments) at any time during a period of two years commencing from and including 10 November 2011 to 9 November 2013.

2. These represent share options granted to Mr. Tian Wenwei under the share option scheme of the Company which are exercisable at the subscription price of HK$4.96 per share (subject to adjustments) at any time during a period of two years commencing from and including 12 May 2011 to 11 May 2013.

3. These represent 1,000,000 share options and 500,000 share options granted to Mr. Wang Tongtian under the share option scheme of the Company which are exercisable at the subscription price of HK$4.96 per share (subject to adjustments) at any time during a period of two years commencing from and including 12 May 2011 to 11 May 2013 and a period of two years commencing from and including 26 August 2011 to 25 August 2013, respectively.

4. These represent share options granted to Mr. Chiu Sui Keung under the share option scheme of the Company which are exercisable at the subscription price of HK$4.96 per share (subject to adjustments) at any time during a period of two years commencing from and including 26 August 2011 to 25 August 2013.

Save as disclosed above, as at 31 December 2012, none of the Directors and the chief executive of the Company and their respective associates had or was deemed to have any interests in the long or short positions in the shares or underlying shares of the Company or its associated corporations (within the meaning of Part XV of the SFO) which (i) were required to be notified to the Company and the Stock Exchange pursuant to Division 7 and 8 of Part XV of the SFO (including interests in the long or short positions which they were taken or deemed to have under such provisions of the SFO); or (ii) were required, pursuant to section 352 of the SFO, to be entered in the register referred to therein; or (iii) were required to be notified to the Company and the Stock Exchange pursuant to the Model Code adopted by the Company.

SHARE OPTION SCHEME

The Company operated a share option scheme which was expired on 28 May 2012 (the "Expired Scheme") and a new share option scheme (the "Scheme") was approved by the shareholders of the Company and was effective from 30 May 2012. The Scheme is operated for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations. Upon the expiry of the Expired Scheme, no further share option can be granted under the Expired Scheme but the Share options already granted under the Expired Scheme shall remain in full force and effect until the options expired. Further details of the Scheme are disclosed in the circular of the Company dated 27 April 2012 and note 30 to the financial statements.

The following table discloses movements in the Company's share options outstanding during the year:

		Number of share options		
Name or category of participant	Notes	At 1 January 2012	Reclassification during the year	At 31 December 2012
Executive Directors:				
Mr. Wang Da Yong	(d)	5,000,000	—	5,000,000
Mr. Tian Wenwei	(b)	3,750,000	—	3,750,000
Mr. Wang Tongtian	(b)	1,000,000	—	1,000,000
	(c)	500,000	—	500,000
		10,250,000	—	10,250,000
Non-executive Directors:				
Mr. Li Yi (resigned on 1 June 2012)	(b)	1,000,000	(1,000,000)	—
Mr. Su Bin (resigned on 1 June 2012)	(c)	1,000,000	(1,000,000)	—
		2,000,000	(2,000,000)	—
Independent non-executive Directors:				
Mr. Chiu Sui Keung	(c)	500,000	—	500,000
Mr. Cao Kuangyu (resigned on 23 April 2012)	(c)	500,000	(500,000)	—
		1,000,000	(500,000)	500,000
Others:				
In aggregate	(a)	616,000	—	616,000
	(b)	10,250,000	1,000,000	11,250,000
	(c)	500,000	1,500,000	2,000,000
		11,366,000	2,500,000	13,866,000
Total		24,616,000	—	24,616,000

There were no outstanding share options for other directors as at 31 December 2012.

Notes:

(a) These share options were granted on 29 September 2008 at an exercise price of HK$2.5@ per ordinary share of the Company. The closing price of the Company's ordinary shares on the Stock Exchange on the trading day immediately prior to the date of grant of the share options was HK$2.5† per share. The share options may be exercised at any time commenced on 29 September 2008 and, if not otherwise exercised, all of the share options will lapse on 29 September 2013. The vesting period is from the date of grant to the commencement date of the exercise period.

(b) These share options were granted on 12 May 2010 at an exercise price of HK$4.96@ per ordinary share of the Company. The closing price of the Company's ordinary shares on the Stock Exchange on the trading day immediately prior to the date of grant of the share options was HK$4.62† per share. The share options may be exercised in two equal portions. The first 50% portion is exercisable for a period of two years commenced on 12 May 2011 and the other 50% portion is exercisable for a period of one year commenced on 12 May 2012 and, if not otherwise exercised, all of the share options will lapse on 12 May 2013. The vesting periods of each of the portion is from the date of grant to the respective commencement dates of the exercise periods.

(c) These share options were granted on 26 August 2010 at an exercise price of HK$4.96@ per ordinary share of the Company. The closing price of the Company's ordinary shares on the Stock Exchange on the trading day immediately prior to the date of grant of the share options was HK$3.08† per share. The share options may be exercised in two equal portions. The first 50% portion is exercisable for a period of two years commenced on 26 August 2011 and the other 50% portion is exercisable for a period of one year commenced on 26 August 2012 and, if not otherwise exercised, all of the share options will lapse on 26 August 2013. The vesting periods of each of the portion is from the date of grant to the respective commencement dates of the exercise periods.

(d) These share options were granted on 10 November 2010 at an exercise price of HK$4.96@ per share of the Company. The closing price of the Company's ordinary shares on the Stock Exchange on the trading day immediately prior to the date of grant of the share options was HK$4.54† per share. The share options may be exercised in two equal portions. The first 50% portion is exercisable for a period of two years commenced on 10 November 2011 and the other 50% portion is exercisable for a period of one year commenced on 10 November 2012 and, if not otherwise exercised, all of the share options will lapse on 10 November 2013. The vesting periods of each of the portion is from the date of grant to the respective commencement dates of the exercise periods.

@ The exercise price of these share options is subject to adjustment in the case of rights or bonus issues, or other similar changes in the Company's share capital.

† The closing price of the Company's ordinary shares as disclosed above had been adjusted for the twenty-to-one share consolidation taken place on 24 June 2011.

Save as disclosed above, at no time during the year were rights to acquire benefits by means of the acquisition of shares in or debentures of the Company granted to any of the Directors or their respective spouses or minor children, or were any such rights exercised by them; or was the Company or any of its subsidiaries a party to any arrangement to enable the Directors to acquire such rights in any other body corporate.

CONTRACT OF SIGNIFICANCE

No contracts of significance in relation to the Group's business in which the Company or any of its subsidiaries was a party and in which a Director had a material interest, whether directly or indirectly, subsisted during or at the end of the year.

SUBSTANTIAL SHAREHOLDERS AND OTHER PERSON'S INTERESTS IN SHARES AND UNDERLYING SHARES

So far as was known to the Directors and the chief executive of the Company, as at 31 December 2012, the following persons (not being Directors or chief executive of the Company of which interests were disclosed above) had, or were deemed to have, interests or short positions in the shares or underlying shares of the Company which would fall to be disclosed to the Company and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO, or as recorded in the register required to be kept under Section 336 of the SFO, or who was, directly or indirectly, interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at a general meeting of the Company or any member of the Group:

Name	Capacity	Total interests in shares/ underlying shares	Approximate percentage of the Company's issued share capital
Jade Bird Strategic Investment (note 1)	Beneficial owner	1,555,555,000	108.88%
Simsen International Corporation Limited (note 2)	Beneficial owner and through controlled corporation	231,364,000	16.19%
Join Ascent Limited (note 3)	Beneficial owner	160,082,000	11.20%
Simsen Asset Management (Asia) Limited (note 2)	Beneficial owner	119,364,000	8.35%
Chrism Investments Limited (note 4)	Beneficial owner	93,250,000	6.53%
Sky Circle International Limited (note 5)	Beneficial owner	81,885,000	5.73%

Notes:

1. The shares represented the number of shares subscribed by Jade Bird Strategic Investment pursuant to the subscription agreement entered into with the Company dated 12 October 2012.

2. Simsen International Corporation Limited, a listed company in Hong Kong with stock code 993, together with its subsidiary, Simsen Asset Management (Asia) Limited, held convertible notes which entitle the holder thereof to convert into an aggregate of 231,364,000 shares at the conversion price of HK$1.25 per share (subject to adjustment).

3. Join Ascent Limited is held as to 80% and 20% by Mr. Wang Da Yong and Mr. Tian Wenwei, respectively, both of which were Directors of the Company.

4. The number of shares held by Chrism Investments Limited was 1,865,000,000 pursuant to disclosure of interests notice dated 20 May 2011. The number of shares disclosed in the above table has been adjusted for the twenty-to-one share consolidation effective from 27 June 2011.

5. Sky Circle International Limited is a company wholly owned by Mr. Wang Da Yong.

Save as disclosed above, as at 31 December 2012, the Directors and the chief executive of the Company were not aware of any other person (other than the Directors and the chief executive of the Company) who had, or was deemed to have, interests and/or short positions in the shares or underlying shares of the Company or any associated corporations (within the meaning of Part XV of the SFO) which would fall to be disclosed to the Company and the Stock Exchange under the provisions of Division 2 and 3 of Part XV of the SFO or as recorded in the register required to be kept under Section 336 of the SFO, or who was, directly or indirectly, interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of the Company or any other member of the Group.

SUFFICIENCY OF PUBLIC FLOAT

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

EVENTS AFTER THE REPORTING PERIOD

Details of the significant events of the Group after the reporting period are set out in note 40 to the financial statements.

AUDITORS

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

ON BEHALF OF THE BOARD

Xu Zhendong
Chairman

Hong Kong
28 March 2013

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To the shareholders of King Stone Energy Group Limited
(Incorporated in Hong Kong with limited liability)

We have audited the consolidated financial statements of King Stone Energy Group Limited (the "Company") and its subsidiaries (together, the "Group") set out on pages 36 to 105, which comprise the consolidated and company statements of financial position as at 31 December 2012, and the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory 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 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.

AUDITORS' RESPONSIBILITY

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. Our report is made solely to you, as a body, in accordance with Section 141 of the Hong Kong Companies Ordinance, 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.

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

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

OPINION

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2012, and of the Group's loss and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the Hong Kong Companies Ordinance.

EMPHASIS OF MATTER ON GOING CONCERN

Without qualifying our opinion, we draw attention to note 2 in the financial statements which indicates that as at 31 December 2012, the Group has current liabilities exceeded its current assets by HK$1,860 million. Such condition, along with other matters as set forth in note 2, indicates the existence of a material uncertainty that may cast significant doubt about the Group's ability to continue as a going concern. Should the Group be unable to continue as a going concern, adjustments relating to the carrying amounts and reclassification of assets and liabilities of the Group and the Company would have to be made to the financial statements.

Ernst & Young
Certified Public Accountants
Hong Kong
28 March 2013

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

Year ended 31 December 2012

	Notes	2012 HK$'000	2011 HK$'000
REVENUE	6	571,129	995,100
Cost of inventories sold		(661,970)	(612,248)
Gross profit/(loss)		(90,841)	382,852
Gain on bargain purchase of a subsidiary	32	–	29,948
Other income and gains	6	3,257	52,195
Selling and distribution expenses		(10,640)	(4,632)
Administrative expenses		(95,116)	(182,754)
Other expenses		(1,953,845)	–
Finance costs	7	(136,014)	(171,751)
Share of profit/(loss) of a jointly-controlled entity	18	6,279	(28)
PROFIT/(LOSS) BEFORE TAX	8	(2,276,920)	105,830
Income tax credit/(expense)	11	521,878	(40,396)
PROFIT/(LOSS) FOR THE YEAR		(1,755,042)	65,434
OTHER COMPREHENSIVE INCOME			
Exchange differences on translation of foreign operations		24,466	108,432
OTHER COMPREHENSIVE INCOME FOR THE YEAR, NET OF TAX		24,466	108,432
TOTAL COMPREHENSIVE INCOME/(LOSS) FOR THE YEAR		(1,730,576)	173,866

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (Continued)

Year ended 31 December 2012

	Notes	2012 HK$'000	2011 HK$'000
Profit/(loss) for the year attributable to:			
Owners of the Company	12	(1,655,263)	55,339
Non-controlling interests		(99,779)	10,095
		(1,755,042)	65,434
Total comprehensive income/(loss) for the year attributable to:			
Owners of the Company	12	(1,632,094)	157,139
Non-controlling interests		(98,482)	16,727
		(1,730,576)	173,866
EARNINGS/(LOSS) PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE COMPANY	13		
Basic and diluted		HK$ (1.16)	HK$0.04

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

31 December 2012

	Notes	2012 HK$'000	2011 HK$'000
NON-CURRENT ASSETS			
Property, plant and equipment	14	1,547,178	2,151,176
Prepaid land premiums	15	14,856	15,080
Mining rights	16	1,739,255	2,964,936
Investment in a jointly-controlled entity	18	23,117	16,623
Prepayments and deposits	21	60,734	155,964
Total non-current assets		3,385,140	5,303,779
CURRENT ASSETS			
Inventories	19	15,479	17,216
Trade and bills receivables	20	46,026	117,100
Prepayments, deposits and other receivables	21	90,686	566,144
Pledged deposits	22	3,517	2,936
Cash and cash equivalents	22	15,913	51,928
Total current assets		171,621	755,324
CURRENT LIABILITIES			
Trade and bills payables	23	93,016	5,048
Other payables and accruals	24	696,437	1,181,973
Interest-bearing borrowings	25	1,013,511	555,075
Income tax payable		228,721	272,526
Total current liabilities		2,031,685	2,014,622
NET CURRENT LIABILITIES		(1,860,064)	(1,259,298)
TOTAL ASSETS LESS CURRENT LIABILITIES		1,525,076	4,044,481
NON-CURRENT LIABILITIES			
Interest-bearing borrowings	25	382,513	678,425
Convertible notes	27	242,556	221,782
Deferred tax liabilities	28	125,028	646,748
Total non-current liabilities		750,097	1,546,955
Net assets		774,979	2,497,526

CONSOLIDATED STATEMENT OF FINANCIAL POSITION (Continued)

31 December 2012

	Notes	2012 HK$'000	2011 HK$'000
EQUITY			
Equity attributable to owners of the Company			
Issued capital	29	142,873	142,873
Reserves	31	610,060	2,234,125
		752,933	2,376,998
Non-controlling interests		22,046	120,528
Total equity		774,979	2,497,526

Director
Xu Zhendong

Director
Zong Hao

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

Year ended 31 December 2012

		Attributable to owners of the Company									
	Notes	Issued capital HK$'000 (Note 29)	Share premium account HK$'000 (Note 31(b)(i))	Capital redemption reserve HK$'000 (Note 31(b)(ii))	Equity component of convertible notes HK$'000 (Note 27)	Share option reserve HK$'000 (Note 31(b)(iii))	Exchange fluctuation reserve HK$'000 (Note 31(a))	Retained earnings/ (accumulated losses) HK$'000	Total HK$'000	Non-controlling interests HK$'000	Total equity HK$'000
At 1 January 2011		226,298	3,065,615	–	1,239,114	24,626	70,100	(2,700,820)	1,924,933	103,801	2,028,734
Profit for the year		–	–	–	–	–	–	55,339	55,339	10,095	65,434
Other comprehensive income for exchange differences on translation of foreign operations during the year		–	–	–	–	–	101,800	–	101,800	6,632	108,432
Total comprehensive income for the year		–	–	–	–	–	101,800	55,339	157,139	16,727	173,866
Conversion of convertible notes	29(a)	49,027	922,611	–	(700,230)	–	–	–	271,408	–	271,408
Share issue expenses		–	(99)	–	–	–	–	–	(99)	–	(99)
Repurchase of shares	29(b)	(523)	–	523	–	–	–	–	–	–	–
Share repurchase expense	29(b)	–	–	–	–	–	–	(7,322)	(7,322)	–	(7,322)
Capital reduction	29(c)(ii)	(131,929)	131,929	–	–	–	–	–	–	–	–
Share premium reduction	29(c)(iii)	–	(2,953,243)	–	–	–	–	2,953,243	–	–	–
Equity-settled share option arrangement	30	–	–	–	–	30,939	–	–	30,939	–	30,939
At 31 December 2011 and 1 January 2012		142,873	1,166,813*	523*	538,884*	55,565*	171,900*	300,440*	2,376,998	120,528	2,497,526
Loss for the year		–	–	–	–	–	–	(1,655,263)	(1,655,263)	(99,779)	(1,755,042)
Other comprehensive income for exchange differences on translation of foreign operations during the year		–	–	–	–	–	23,169	–	23,169	1,297	24,466
Total comprehensive loss for the year		–	–	–	–	–	23,169	(1,655,263)	(1,632,094)	(98,482)	(1,730,576)
Equity-settled share option arrangement	30	–	–	–	–	8,029	–	–	8,029	–	8,029
At 31 December 2012		142,873	1,166,813*	523*	538,884*	63,594*	195,069*	(1,354,823)*	752,933	22,046	774,979

* These reserve accounts comprise the consolidated reserves of HK$610,060,000 (2011: HK$2,234,125,000) in the consolidated statement of financial position.

CONSOLIDATED STATEMENT OF CASH FLOWS

Year ended 31 December 2012

	Notes	2012 HK$'000	2011 HK$'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Profit/(loss) before tax		(2,276,920)	105,830
Adjustments for:			
Finance costs	7	136,014	171,751
Gain on bargain purchase of a subsidiary	32	—	(29,948)
Bank interest income	6	(286)	(262)
Other interest income	6	(1,500)	(6,270)
Gain on disposal of items of property, plant and equipment	6	(1,049)	—
Fair value gain on derivative component of convertible bonds	6, 26	—	(35,452)
Depreciation	8, 14	248,778	157,880
Amortisation of prepaid land premiums	8, 15	346	357
Amortisation of mining rights	8, 16	128,842	162,831
Write-off of items of property, plant and equipment	8	—	22,789
Impairment of items of property, plant and equipment	8, 14(a)	684,145	—
Impairment of mining rights	8, 14(a)	1,126,973	—
Impairment of trade receivables	8, 20(b)	10,424	144
Impairment of prepayment of property, plant and equipment	8, 14(a)	29,854	—
Impairment of the Indemnification Asset	8, 32(a)	33,500	—
Impairment of other prepayments, deposits and other receivables	8, 21	63,541	1,086
Equity-settled share option expenses	8, 30	8,029	30,939
Share of loss/(profit) of a jointly-controlled entity	18	(6,279)	28
		184,412	581,703
Decrease/(increase) in inventories		1,737	(7,157)
Decrease in trade and bills receivables		60,650	146,102
Decrease in prepayments, deposits and other receivables		126,504	30,539
Increase/(decrease) in trade and bills payables		87,968	(3,521)
Increase/(decrease) in other payables and accruals		(49,574)	159,572
Cash generated from operations		411,697	907,238
Interest paid		(115,240)	(107,745)
Income tax paid		(49,564)	(14,927)
Net cash flows from operating activities		246,893	784,566

CONSOLIDATED STATEMENT OF CASH FLOWS (Continued)

Year ended 31 December 2012

	Notes	2012 HK$'000	2011 HK$'000
CASH FLOWS FROM INVESTING ACTIVITIES			
Interest received		1,786	6,532
Purchases of items of property, plant and equipment		(334,253)	(823,160)
Proceeds from disposal of items of property, plant and equipment		25,236	625
Acquisition of subsidiaries	32	(307,350)	(292,887)
Investment in a jointly-controlled entity		–	(16,651)
Decrease in prepayments for non-current assets		287,900	30,069
Increase in pledged time deposits		(581)	(2,519)
Net cash flows used in investing activities		(327,262)	(1,097,991)
CASH FLOWS FROM FINANCING ACTIVITIES			
Share issue expenses	29	–	(99)
Repurchase of shares	29(b)	–	(7,322)
Redemption of convertible bonds	26	–	(159,000)
New bank and other loans		606,094	431,725
Repayment of bank and other loans		(451,576)	(555,075)
Increase/(decrease) in other borrowings included in other payables		(99,223)	37,318
Net cash flows from/(used in) financing activities		55,295	(252,453)
NET DECREASE IN CASH AND CASH EQUIVALENTS		(25,074)	(565,878)
Cash and cash equivalents at beginning of year		51,928	625,216
Effect of foreign exchange rate changes, net		(10,941)	(7,410)
CASH AND CASH EQUIVALENTS AT END OF YEAR		15,913	51,928
ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS			
Cash and bank balances other than time deposits	22	15,913	41,928
Non-pledged time deposits	22	–	10,000
Cash and cash equivalents as stated in the consolidated statement of financial position and the consolidated statement of cash flows	22	15,913	51,928

STATEMENT OF FINANCIAL POSITION

31 December 2012

	Notes	2012 HK$'000	2011 HK$'000
NON-CURRENT ASSETS			
Property, plant and equipment	14	343	1,077
Investments in subsidiaries	17(a)	802,302	1,810,195
Total non-current assets		802,645	1,811,272
CURRENT ASSETS			
Due from subsidiaries	17(c)	—	237
Prepayments, deposits and other receivables	21	17,808	211,140
Cash and cash equivalents	22	7,642	19,676
Total current assets		25,450	231,053
CURRENT LIABILITIES			
Due to a subsidiary	17(c)	420	—
Other payables and accruals	24	12,740	3,683
Total current liabilities		13,160	3,683
NET CURRENT ASSETS		12,290	227,370
TOTAL ASSETS LESS CURRENT LIABILITIES		814,935	2,038,642
NON-CURRENT LIABILITY			
Convertible notes	27	242,556	221,782
Net assets		572,379	1,816,860
EQUITY			
Issued capital	29	142,873	142,873
Reserves	31(b)	429,506	1,673,987
Total equity		572,379	1,816,860

Director
Xu Zhendong

Director
Zong Hao

1. CORPORATE INFORMATION

King Stone Energy Group Limited (the "Company") is a limited liability company incorporated in Hong Kong and the shares of which are listed on the Main Board of The Stock Exchange of Hong Kong Limited (the "Stock Exchange"). The registered address of the Company is located at Unit 7603, 76/F, The Center, 99 Queen's Road Central, Hong Kong.

During the year, the Company and its subsidiaries (collectively referred to as the "Group") were involved in the mining and selling of coal.

2. BASIS OF PREPARATION, PRESENTATION AND CONSOLIDATION

Basis of preparation

As at 31 December 2012, the current liabilities of the Group exceeded its current assets by approximately HK$1,860 million, which indicates the existence of a material uncertainty that may cast significant doubt about the Group's ability to operate as a going concern. The consolidated financial statements of the Group have been prepared on a going concern basis, the validity of which depends upon the outcome of various measures adopted by the directors of the Company as mentioned below and the future performance of the Group.

Subsequent to the end of the reporting period, (i) on 31 January 2013, 1,555,555,000 ordinary shares of the Company with par value of HK$0.1 per share were issued and allotted to a new investor at HK$0.45 each, resulting in a net proceeds of approximately HK$663 million being received by the Company; and (ii) part of these proceeds of HK$50 million has been used to early redeem part of the Company's convertible notes with a principal amount of HK$50 million issued by the Company with a redemption date of not later than 20 December 2014.

As at the date of approval of these financial statements, the Group is in process of negotiating with a financial institution to obtain new loans for the purpose of meeting the Group's liabilities as and when they fall due. Based on the communications with the relevant financial institution and after taking into account the Group's availability of mining rights (free of charges and encumbrances) and a coal washing factory (free of charges and encumbrances) with an aggregate carrying value of HK$718 million as at 31 December 2012 for pledging purposes, operating performance and other factors, the directors of the Company are confident that these new loans will be obtained.

In addition, a substantial shareholder of the Company, Jade Bird Energy Fund II, LP, has confirmed its ability and agreement to provide continual financial support and adequate funds to the Group to meet with the Group's liabilities as and when they fall due in the foreseeable future.

The directors of the Company are also considering/taking other alternatives to monitor and improve the cash flows of the Group, which included extension of repayment dates of existing bank loans and other liabilities, and other financing arrangements. The directors of the Company expect that payments of certain liabilities of the Group can be extended to twelve months after 31 December 2012.

2. BASIS OF PREPARATION, PRESENTATION AND CONSOLIDATION (Continued)

Basis of preparation (Continued)

In light of the measures described above, and after taking into account the performance of the Group and the cash flow projection prepared by the directors of the Company, the directors of the Company are confident that the Group will have sufficient working capital to meet with its financial obligations in the foreseeable future. Accordingly the directors of the Company are of the opinion that it is appropriate to prepare these financial statements on a going concern basis. These financial statements do not include any adjustments that might be necessary should the Group not be able to continue as a going concern.

Basis of presentation

These financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") (which include all Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards ("HKASs") and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), accounting principles generally accepted in Hong Kong and the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention, except for the derivative component of convertible bonds for the year ended 31 December 2011, which has been measured at fair value. These financial statements are presented in Hong Kong dollars and all values are rounded to the nearest thousand (HK$'000) except when otherwise indicated.

Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries for the year ended 31 December 2012. The financial statements of the subsidiaries are prepared for the same reporting period as the Company. The results of subsidiaries are consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases. All intra-group balances, transactions, unrealised gains and losses resulting from intra-group transactions and dividends are eliminated on consolidation in full. Adjustments are made to bring into line any dissimilar accounting policies that may exist.

Total comprehensive income within a subsidiary is attributed to the non-controlling interest even if that results in a deficit balance.

A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction.

If the Group loses control over a subsidiary, it derecognises (i) the assets (including goodwill) and liabilities of the subsidiary, (ii) the carrying amount of any non-controlling interest and (iii) the cumulative translation differences recorded in equity; and recognises (i) the fair value of the consideration received, (ii) the fair value of any investment retained and (iii) any resulting surplus or deficit in profit or loss. The Group's share of components previously recognised in other comprehensive income is reclassified to profit or loss or retained profits, as appropriate.

3.1 CHANGES IN ACCOUNTING POLICY AND DISCLOSURES

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

HKFRS 1 Amendments	Amendments to HKFRS 1 *First-time Adoption of Hong Kong Financial Reporting Standards — Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters*
HKFRS 7 Amendments	Amendments to HKFRS 7 *Financial Instruments: Disclosures — Transfers of Financial Assets*
HKAS 12 Amendments	Amendments to HKAS 12 *Income Taxes — Deferred Tax: Recovery of Underlying Asset*

The adoption of the revised HKFRSs has had no significant financial effect on these financial statements.

3.2 ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS

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

HKFRS 1 Amendments	Amendments to HKFRS 1 *First-time Adoption of Hong Kong Financial Reporting Standards — Government Loans*[2]
HKFRS 7 Amendments	Amendments to HKFRS 7 *Financial Instruments: Disclosures — Offsetting Financial Assets and Financial Liabilities*[2]
HKFRS 9	*Financial Instruments*[4]
HKFRS 10	*Consolidated Financial Statements*[2]
HKFRS 11	*Joint Arrangements*[2]
HKFRS 12	*Disclosure of Interests in Other Entities*[2]
HKFRS 10, HKFRS 11 and HKFRS 12 Amendments	Amendments to HKFRS 10, HKFRS 11 and HKFRS 12 — *Transition Guidance*[2]
HKFRS 10, HKFRS 12 and HKAS 27 (2011) Amendments	Amendments to HKFRS 10, HKFRS 12 and HKAS 27 (2011) — *Investment Entities*[3]
HKFRS 13	*Fair Value Measurement*[2]
HKAS 1 Amendments	Amendments to HKAS 1 *Presentation of Financial Statements — Presentation of Items of Other Comprehensive Income*[1]
HKAS 19 (2011)	*Employee Benefits*[2]
HKAS 27 (2011)	*Separate Financial Statements*[2]
HKAS 28 (2011)	*Investments in Associates and Joint Ventures*[2]
HKAS 32 Amendments	Amendments to HKAS 32 *Financial Instruments: Presentation — Offsetting Financial Assets and Financial Liabilities*[3]
HK(IFRIC)-Int 20	Stripping Costs in the Production Phase of a Surface Mine[2]
Annual Improvements 2009-2011 Cycle	Amendments to a number of HKFRSs issued in June 2012[2]

1 Effective for annual periods beginning on or after 1 July 2012
2 Effective for annual periods beginning on or after 1 January 2013
3 Effective for annual periods beginning on or after 1 January 2014
4 Effective for annual periods beginning on or after 1 January 2015

3.2 ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS (Continued)

Further information about those new and revised HKFRSs that are expected to be applicable to the Group is as follows:

(a) The HKFRS 7 Amendments require an entity to disclose information about rights to set-off and related arrangements (e.g., collateral agreements). The disclosures would provide users with information that is useful in evaluating the effect of netting arrangements on an entity's financial position. The new disclosures are required for all recognised financial instruments that are set off in accordance with HKAS 32 *Financial Instruments: Presentation*. The disclosures also apply to recognised financial instruments that are subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are set off in accordance with HKAS 32. The Group expects to adopt the amendments from 1 January 2013.

(b) HKFRS 9 issued in November 2009 is the first part of phase 1 of a comprehensive project to entirely replace HKAS 39 *Financial Instruments: Recognition and Measurement*. This phase focuses on the classification and measurement of financial assets. Instead of classifying financial assets into four categories, an entity shall classify financial assets as subsequently measured at either amortised cost or fair value, on the basis of both the entity's business model for managing the financial assets and the contractual cash flow characteristics of the financial assets. This aims to improve and simplify the approach for the classification and measurement of financial assets compared with the requirements of HKAS 39.

In November 2010, the HKICPA issued additions to HKFRS 9 to address financial liabilities (the "Additions") and incorporated in HKFRS 9 the current derecognition principles of financial instruments of HKAS 39. Most of the Additions were carried forward unchanged from HKAS 39, while changes were made to the measurement of financial liabilities designated at fair value through profit or loss using the fair value option ("FVO"). For these FVO liabilities, the amount of change in the fair value of a liability that is attributable to changes in credit risk must be presented in other comprehensive income ("OCI"). The remainder of the change in fair value is presented in profit or loss, unless presentation of the fair value change in respect of the liability's credit risk in OCI would create or enlarge an accounting mismatch in profit or loss. However, loan commitments and financial guarantee contracts which have been designated under the FVO are scoped out of the Additions.

HKAS 39 is aimed to be replaced by HKFRS 9 in its entirety. Before this entire replacement, the guidance in HKAS 39 on hedge accounting and impairment of financial assets continues to apply. The Group expects to adopt HKFRS 9 from 1 January 2015. The Group will quantify the effect in conjunction with other phases, when the final standard including all phases is issued.

3.2 ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS (Continued)

(c) HKFRS 10 establishes a single control model that applies to all entities including special purpose entities or structured entities. It includes a new definition of control which is used to determine which entities are consolidated. The changes introduced by HKFRS 10 require management of the Group to exercise significant judgement to determine which entities are controlled, compared with the requirements in HKAS 27 and HK(SIC)-Int 12 *Consolidation — Special Purpose Entities*. HKFRS 10 replaces the portion of HKAS 27 *Consolidated and Separate Financial Statements* that addresses the accounting for consolidated financial statements. It also addresses the issues raised in HK(SIC)-Int 12. Based on the preliminary analysis performed, HKFRS 10 is not expected to have any impact on the currently held investments of the Group.

HKFRS 11 replaces HKAS 31 *Interests in Joint Ventures* and HK(SIC)-Int 13 *Jointly Controlled Entities — Non-Monetary Contributions by Venturers*. It describes the accounting for joint arrangements with joint control. It addresses only two forms of joint arrangements, i.e., joint operations and joint ventures, and removes the option to account for joint ventures using proportionate consolidation.

HKFRS 12 includes the disclosure requirements for subsidiaries, joint arrangements, associates and structured entities previously included in HKAS 27 *Consolidated and Separate Financial Statements*, HKAS 31 *Interests in Joint Ventures* and HKAS 28 *Investments in Associates*. It also introduces a number of new disclosure requirements for these entities.

In July 2012, the HKICPA issued amendments to HKFRS 10, HKFRS 11 and HKFRS 12 which clarify the transition guidance in HKFRS 10 and provide further relief from full retrospective application of these standards, limiting the requirement to provide adjusted comparative information to only the preceding comparative period. The amendments clarify that retrospective adjustments are only required if the consolidation conclusion as to which entities are controlled by the Group is different between HKFRS 10 and HKAS 27 or HK(SIC)-Int 12 at the beginning of the annual period in which HKFRS 10 is applied for the first time. Furthermore, for disclosures related to unconsolidated structured entities, the amendments will remove the requirement to present comparative information for periods before HKFRS 12 is first applied.

The amendments to HKFRS 10 issued in December 2012 include a definition of an investment entity and provide an exception to the consolidation requirement for entities that meet the definition of an investment entity. Investment entities are required to account for subsidiaries at fair value through profit or loss in accordance with HKFRS 9 rather than consolidate them. Consequential amendments were made to HKFRS 12 and HKAS 27 (2011). The amendments to HKFRS 12 also set out the disclosure requirements for investment entities. The Group expects that these amendments will not have any impact on the Group as the Company is not an investment entity as defined in HKFRS 10.

Consequential amendments were made to HKAS 27 and HKAS 28 as a result of the issuance of HKFRS 10, HKFRS 11 and HKFRS 12. The Group expects to adopt HKFRS 10, HKFRS 11, HKFRS 12, HKAS 27 (2011), HKAS 28 (2011), and consequential amendments to these standards issued in July and December 2012 from 1 January 2013.

3.2 ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS (Continued)

(d) HKFRS 13 provides a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across HKFRSs. The standard does not change the circumstances in which the Group is required to use fair value, but provides guidance on how fair value should be applied where its use is already required or permitted under other HKFRSs. The Group expects to adopt HKFRS 13 prospectively from 1 January 2013.

(e) The HKAS 1 Amendments change the grouping of items presented in OCI. Items that could be reclassified (or recycled) to profit or loss at a future point in time (for example, exchange differences on transaction of foreign operations) would be presented separately from items which will never be reclassified. The amendments will affect presentation only and have no impact on the financial position or performance. The Group expects to adopt the amendments from 1 January 2013.

(f) The HKAS 32 Amendments clarify the meaning of "currently has a legally enforceable right to setoff" for offsetting financial assets and financial liabilities. The amendments also clarify the application of the offsetting criteria in HKAS 32 to settlement systems (such as central clearing house systems) which apply gross settlement mechanisms that are not simultaneous. The amendments are not expected to have any impact on the financial position or performance of the Group upon adoption on 1 January 2014.

(g) The Annual Improvements to *HKFRSs 2009-2011 Cycle* issued in June 2012 sets out amendments to a number of HKFRSs. The Group expects to adopt the amendments from 1 January 2013. There are separate transitional provisions for each standard. While the adoption of some of the amendments may result in changes in accounting policies, none of these amendments are expected to have a significant financial impact on the Group. The amendment that is expected to have a significant impact on the Group's policies is HKAS 1 *Presentation of Financial Statements*.

The improvement to HKAS 1 clarifies the difference between voluntary additional comparative information and the minimum required comparative information. Generally, the minimum required comparative period is the previous period. An entity must include comparative information in the related notes to the financial statements when it voluntarily provides comparative information beyond the previous period. The additional comparative information does not need to contain a complete set of financial statements. In addition, the amendment clarifies that the opening statement of financial position as at the beginning of the preceding period must be presented when an entity changes its accounting policies; makes retrospective restatements or makes reclassifications, and that change has a material effect on the statement of financial position. However, the related notes to the opening statement of financial position as at the beginning of the preceding period are not required to be presented.

3.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Subsidiaries

A subsidiary is an entity in which the Company, directly or indirectly, controls more than half of its voting power or issued share capital or controls the composition of its board of directors; or over which the Company has a contractual right to exercise a dominant influence with respect to that entity's financial and operating policies.

The results of subsidiaries are included in the Company's profit or loss to the extent of dividends received and receivable. The Company's investments in subsidiaries are stated at cost less any accumulated impairment losses.

Joint ventures

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

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

A joint venture is treated as a jointly-controlled entity, if the Group does not have unilateral control, but has joint control, directly or indirectly, over the joint venture.

Jointly-controlled entities

A jointly-controlled entity is a joint venture that is subject to joint control, resulting in none of the participating parties having unilateral control over the economic activity of the jointly-controlled entity.

The Group's investment in a jointly-controlled entity is stated in the consolidated statement of financial position at the Group's share of net assets under the equity method of accounting. Adjustments are made to bring into line any dissimilar accounting policies that may exist. The Group's share of the results and reserves of the jointly-controlled entity is included in profit or loss and consolidated reserves, respectively.

Business combinations

Business combination is accounted for using the acquisition method. The consideration transferred is measured at the acquisition date fair value which is the sum of the acquisition date fair values of assets transferred by the Group and liabilities assumed by the Group to the former owners of the acquiree. For each business combination, the Group elects whether to measures the non-controlling interests in the acquiree that are present ownership interests and entitle their holders to a proportionate share of net assets in the event of liquidation at fair value or at the proportionate share of the acquiree's identifiable net assets. All other components of non-controlling interests are measured at fair value. Acquisition-related costs are expensed as incurred.

3.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Business combinations (Continued)

When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

If the business combination is achieved in stages, the previously held equity interest is remeasured at its acquisition date fair value and any resulting gain or loss is recognised in profit or loss.

Any contingent consideration to be transferred by the acquirer is recognised at fair value at the acquisition date. Contingent consideration classified as an asset or liability that is financial instrument and within the scope of HKAS 39 is measured at fair value with changes in fair value either recognised in profit or loss or as a change to other comprehensive income. If the contingent consideration is not within the scope of HKAS 39, it is measured in accordance with the appropriate HKFRS. Contingent consideration that is classified as equity is not remeasured and subsequent settlement is accounted for within equity.

Impairment of non-financial assets

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

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

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

3.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Related parties

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

(a) the party is a person or a close member if that person's family and that person (i) has control or joint control over the Group; (ii) has significant influence over the Group; or (iii) is a member of the key management personnel of the Group or of a parent of the Group; or

(b) the party is an entity where any of the following conditions applies:

(i) the entity and the Group are members of the same group;

(ii) one entity is an associate or joint venture of the other entity (or of a parent, subsidiary or fellow subsidiary of the other entity);

(iii) the entity and the Group are joint ventures of the same third party;

(iv) one entity is a joint venture of a third entity and the other entity is an associate of the third entity;

(v) the entity is a post-employment benefit plan for the benefit of the employees of either the Group or an entity related to the Group;

(vi) the entity is controlled or jointly controlled by a person identified in (a); and

(vii) a person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or a parent of the entity).

Property, plant and equipment and depreciation

Property, plant and equipment, other than construction in progress, are stated at cost less accumulated depreciation and any accumulated impairment losses. The cost of an item of property, plant and equipment comprises its purchases price and any directly attributable costs of bringing the asset to its working condition and location for its intended use.

Expenditure incurred after items of property, plant and equipment have been put into operation, such as repairs and maintenance, is normally charged to profit or loss in the period in which it is incurred. In situations where the recognition criteria are satisfied, the expenditure for a major inspection is capitalised in the carrying amount of the asset as a replacement. Where significant parts of property, plant and equipment are required to be replaced at intervals, the Group recognises such parts as individual assets with specific useful lives and depreciates them accordingly.

3.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Property, plant and equipment and depreciation (Continued)

Depreciation is calculated on the straight-line basis to write off the cost of each item of property, plant and equipment to its residual value over its estimated useful life. The principal annual rates used for this purpose are as follows:

Buildings	Over the lease term
Leasehold improvements	Over the shorter of the lease terms and five years
Plant and machinery	6.7% to 12.5%
Furniture, fixtures and equipment	10% to 20%
Motor vehicles	20%

In addition, certain plant and machinery used in the coal mines is depreciated on the unit of production method based on the actual production volume and over the total estimated proven and probable reserves of the coal mine.

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

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

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

Construction in progress represents a building or mining structure and other assets under construction, which is stated at cost less any accumulated impairment losses, and is not depreciated. Cost comprises the direct costs of construction and capitalised borrowing costs on related borrowed funds during the period of construction. Construction in progress is reclassified to the appropriate category of property, plant and equipment when completed and ready for use.

Operating leases

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

Prepaid land premiums under operating leases are stated at cost less accumulated amortisation and any impairment losses, and amortisation is calculated on the straight-line basis over the lease term of 50 years.

Mining rights

Mining rights are stated at cost less accumulated amortisation and any impairment losses, and are amortised on the units of production method based on the actual production volume and over the total estimated proven and probable reserves of the coal mine.

3.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Mining rights (Continued)

The cost of mining rights acquired in a business combination is the fair value as at the date of acquisition. The mining rights are subsequently assessed for impairment whenever there is an indication that the mining rights may be impaired. The amortisation period and the amortisation method for the mining rights are reviewed at least at each financial year end.

Investments and other financial assets

Initial recognition and measurement

The Group determines the classification of its financial assets at initial recognition. The Group's financial assets are classified as loans and receivables under HKAS 39. When financial assets are recognised initially, they are measured at fair value plus transaction costs.

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

Subsequent measurement

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

Derecognition of financial assets

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

- the rights to receive cash flows from the asset have expired; or

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

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

3.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Derecognition of financial assets (Continued)

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

Impairment of financial assets

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

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

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

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

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

3.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial liabilities

Initial recognition and measurement

Financial liabilities within the scope of HKAS 39 are classified as loans and borrowings at initial recognition. All financial liabilities are recognised initially at fair value and net of directly attributable transaction costs.

The Group's financial liabilities include trade and bills payables, other payables, accruals, interest-bearing loans, and the liability component of convertible bonds and convertible notes.

Subsequent measurement

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

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

Convertible bonds/notes

Convertible bonds which entitle the holder to convert the bonds into equity instruments, other than into a fixed number of equity instruments at a fixed conversion price, are regarded as combined instruments consisting of a liability component and a derivative component.

On initial recognition, the derivative component of the convertible bonds is measured at fair value and presented as part of the derivative liability. Any excess of net proceeds over the amount initially recognised as the derivative component is recognised as the liability component. Subsequently, changes in the fair value of the derivative component of the convertible bonds are recognised in profit or loss in the year in which they arise and the liability component of the convertible bonds is stated at amortised cost using the effective interest rate method.

Convertible notes which entitle the holder to convert the notes into a fixed number of equity instruments at a fixed conversion price are regarded as combined instruments consisting of a liability component and an equity component.

On initial recognition, the component of convertible notes that exhibits characteristics of a liability is recognised as a liability in the statement of financial position, net of transaction costs. The fair value of the liability component is determined using a market rate for an equivalent non-convertible note; and this amount is carried as a liability on the amortised cost basis using the effective interest rate method until extinguished on conversion or redemption. In addition, the fair value of the conversion option is assessed and is recognised and included in shareholders' equity as "Equity component of convertible notes". The carrying amount of the conversion option recognised in shareholders' equity is not remeasured in subsequent years.

3.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial liabilities (Continued)

Convertible bonds/notes (Continued)

Upon the exercise of the conversion option of the convertible bonds/notes, the resulting ordinary shares issued are recorded by the Company as additional share capital at the nominal value of the ordinary shares issued, and the excess of the total carrying amounts of the derivative, liability and equity components of the convertible bonds/notes over the nominal value of the ordinary shares issued is recorded in the share premium account. No gain or loss is recognised in profit or loss upon conversion of the convertible bonds/notes.

When the convertible bonds/notes are redeemed, the carrying amount of the equity component of the convertible bonds/notes, if any, is transferred to retained profit or accumulated losses as a movement in reserves and any difference between the amount paid and the carrying amounts of the derivative and liability components is recognised in profit or loss. No gain or loss is recognised in profit or loss upon expiration of the conversion option.

Derecognition of financial liabilities

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

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

Fair value of financial instruments

For financial instruments where there is no active market, the fair value is determined using appropriate valuation techniques. These techniques include using recent arm's length market transactions; reference to the current market value of another instrument which is substantially the same; a discounted cash flow analysis; and other valuation models.

Offsetting of financial instruments

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

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined on the weighted average basis and, in the case of work in progress and finished goods, comprises direct materials, direct labour and an appropriate proportion of overheads. Net realisable value is based on estimated selling prices less any estimated costs to be incurred to completion and disposal.

3.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Cash and cash equivalents

For the purpose of the consolidated statement of cash flows, cash and cash equivalents comprise cash on hand and demand deposits that have a short maturity of generally within three months when acquired.

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

Provisions

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

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

Income tax

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

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

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

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

- when the deferred tax liability arises from the initial recognition of goodwill or an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of taxable temporary differences associated with investments in subsidiaries and a jointly-controlled entity, when the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

3.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Income tax (Continued)

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

- when the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of deductible temporary differences associated with investments in subsidiaries and a jointly-controlled entity, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

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

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

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

Revenue recognition

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

(a) from the sale of goods, when the significant risks and rewards of ownership have been transferred to the buyer, provided that the Group maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold; and

(b) interest income, on an accrual basis using the effective interest rate method by applying the rate that exactly discounts the estimated future cash receipts over the expected life of the financial instrument or a shorter period, when appropriate, to the net carrying amount of the financial asset.

3.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Share-based payments

The Company operates a share option scheme for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations. Employees (including directors) of the Group receive remuneration in the form of share-based payments, whereby employees render services as consideration for equity instruments ("equity-settled transactions").

The cost of equity-settled transactions with employees for grants after 7 November 2002 is measured by reference to the fair value at the date at which they are granted. The fair value is determined by an external valuer using a binomial model, further details of which are given in note 30 to the financial statements.

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled. The cumulative expense recognised for equity-settled transactions at the end of each reporting period until the vesting date reflects the extent to which the vesting period has expired and the Group's best estimate of the number of equity instruments that will ultimately vest. The charge or credit to profit or loss for a period represents the movement in the cumulative expense recognised as at the beginning and end of that period.

No expense is recognised for awards that do not ultimately vest, except for equity-settled transactions where vesting is conditional upon a market or non-vesting condition, which are treated as vesting irrespective of whether or not the market or non-vesting condition is satisfied, provided that all other performance and/or service conditions are satisfied.

Where the terms of an equity-settled award are modified, as a minimum an expense is recognised as if the terms had not been modified, if the original terms of the award are met. In addition, an expense is recognised for any modification that increases the total fair value of the share-based payments, or is otherwise beneficial to the employee as measured at the date of modification.

Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. This includes any award where non-vesting conditions within the control of either the Group or the employee are not met. However, if a new award is substituted for the cancelled award, and is designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award, as described in the previous paragraph.

The dilutive effect of outstanding options, if any, is reflected as additional share dilution in the computation of earnings per share.

3.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Other employee benefits — Pension schemes

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

Subsidiaries of the Group in the People's Republic of China (the "PRC") contribute on a monthly basis to defined contribution retirement schemes organised by relevant municipal and provincial governments in the PRC. The municipal and provincial governments undertake to assume the retirement benefits payable to all existing and future retired employees under these plans and the Group has no further obligations for respective post-retirement benefits beyond the contributions made. The contributions to the schemes are charged to profit or loss as and when incurred.

Borrowing costs

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

Foreign currencies

These financial statements are presented in Hong Kong dollars, which is the Company's functional and presentation currency. Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency. Foreign currency transactions recorded by the entities in the Group are initially recorded using their respective functional currency rates prevailing at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency rates of exchange ruling at the end of the reporting period. Differences arising on settlement or translation of monetary items are recognised in profit or loss.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined. The gain or loss arising on translation of a non-monetary item measured at fair value is treated in line with the recognition of the gain or loss on change in fair value of the item (i.e., translation difference on the item whose fair value gain or loss is recognised in other comprehensive income or profit or loss is also recognised in other comprehensive income or profit or loss, respectively).

3.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Foreign currencies (Continued)

The functional currency of certain subsidiaries and a jointly-controlled entity in the PRC is currency other than the Hong Kong dollar. As at the end of the reporting period, the assets and liabilities of these entities are translated into the presentation currency of the Company at the exchange rate prevailing at the end of the reporting period and their profits or losses are translated into Hong Kong dollars at the weighted average exchange rates for the year. The resulting exchange differences are recognised in other comprehensive income and accumulated in the exchange fluctuation reserve. On disposal of a foreign operation, the component of other comprehensive income relating to that particular foreign operation is recognised in profit or loss.

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

4. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES

The preparation of the Group's financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts of revenue, expenses, assets and liabilities, and their accompanying disclosures. Uncertainty about these assumptions and estimates could result in outcomes that could require a material adjustment to the carrying amounts of the assets or liabilities affected in the future.

Judgements

In the process of applying the Group's accounting policies, management has made the following judgements, apart from those involving estimations, which have the most significant effect on the amounts recognised in the financial statements:

Impairment of assets

The Group has to exercise judgement in determining whether an asset is impaired or the event previously causing the asset impairment no longer exists, particularly in assessing: (1) whether an event has occurred that may affect the asset value or such event affecting the asset value has not been in existence; (2) whether the carrying value of an asset can be supported by the net present value of future cash flows which are estimated based upon the continued use of the asset or disposal; and (3) the appropriate key assumptions to be applied in preparing cash flow projections including whether these cash flow projections are discounted using an appropriate rate. Changing the assumptions selected by management to determine the level of impairment, including the discount rates or the growth rate assumptions in the cash flow projections, could materially affect the net present value used in the impairment test.

4. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES (Continued)

Estimation uncertainties

The key assumptions concerning the future and other key sources of estimation uncertainty at the end of each 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, are described below.

Useful lives and residual values of property, plant and equipment

In determining the useful lives and residual values of items of property, plant and equipment, the Group has to consider various factors, such as technical or commercial obsolescence arising from changes or improvements in production, or from a change in the market demand for the product or service output of the asset, the expected usage of the asset, the expected physical wear and tear, the care and maintenance of the asset, and legal or similar limits in the use of the asset. The estimation of the useful life of the asset is based on the experience of the Group with similar assets that are used in a similar way. Additional depreciation is made if the estimated useful lives and/or the residues values of items of property, plant and equipment are different from the previous estimation. Useful lives and residual values are reviewed, at each financial year end date based on changes in circumstances. The net carrying amounts of property, plant and equipment in the consolidated statement of financial position of the Group at 31 December 2012 was HK$1,547,178,000 (2011: HK$2,151,176,000) (note 14).

Impairment of property, plant and equipment and mining rights

The Group assesses each cash-generating unit annually to determine whether any indication of impairment exists. Where an indicator of impairment exists, a formal estimate of the recoverable amount is made, which is considered to be the higher of the fair value less costs to sell and value in use. The carrying value of property, plant and equipment, including mining structures and mining rights, is reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable in accordance with the accounting policy as disclosed in the financial statements. Estimating the value in use requires the Group to estimate future cash flows from the cash generating unit and to choose a suitable discount rate in order to calculate the present value of those cash flows. The net carrying amounts of property, plant and equipment and mining rights carried as assets in the consolidated statement of financial position of the Group at 31 December 2012 were HK$1,547,178,000 (2011: HK$2,151,176,000) (note 14) and HK$1,739,255,000 (2011: HK$2,964,936,000) (note 16), respectively.

Mine reserves

Engineering estimates of the Group's mine reserves are inherently imprecise and represent only approximate amounts because of the significant judgements involved in developing this information. There are authoritative guidelines regarding the engineering criteria that have to be met before estimated mine reserves can be designated as "proved" and "probable". Proved and probable mine reserve estimates are updated on regular intervals taking into account recent production and technical information about each mine. In addition, as prices and cost levels change from year to year, the estimate of proved and probable mine reserves also changes. This change is considered a change in estimate for accounting purposes and is reflected on a prospective basis in both depreciation and amortisation rates calculated on a unit of production basis. Changes in the estimate of mine reserves are also taking into account in the impairment assessment of mining rights. The net carrying amount of mining rights in the consolidated statement of financial position of the Group at 31 December 2012 was HK$1,739,255,000 (2011: HK$2,964,936,000) (note 16).

4. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES (Continued)

Estimation uncertainties (Continued)

Write-down of inventories to net realisable value

Write-down of inventories to net realisable value is made based on the ageing and estimated net realisable value of inventories. The assessment of the write-down amount requires management's estimates and judgement. Where the actual outcome or expectation in the future is different from the original estimate, the differences will impact the carrying value of inventories and write-down/write-back of inventories in the period in which the estimate has been changed. The net carrying amount of inventories in the consolidated statement of financial position of the Group at 31 December 2012 was HK$15,479,000 (2011: HK$17,216,000) (note 19).

Impairment of trade and bills receivables, prepayments, deposits and other receivables

Impairment of receivables is made based on an assessment of the recoverability of receivables. The identification of impairment requires management's judgements and estimates. Where the actual outcome is different from the original estimate, the differences will impact the carrying values of the receivables and impairment loss in the period in which the estimate has been changed. The net carrying amounts of trade and bills receivables, prepayments, deposits and other receivables in the consolidated statement of financial position of the Group at 31 December 2012 were HK$46,026,000 and HK$151,420,000, respectively (2011: HK$117,100,000 and HK$722,108,000, respectively) (notes 20 and 21).

Provision for rehabilitation

Provision for rehabilitation is based on estimates of future expenditures incurred by management to undertake rehabilitation and restoration work a to a coal mine which are discounted at a rate reflecting the term and nature of the obligation. Significant estimates and assumptions are made in determining the provision for rehabilitation as there are numerous factors that will affect the ultimate liability payable. These factors include estimates of the extent and costs of rehabilitation activities, technological changes, regulatory changes, cost increases and changes in the discount rate. Those uncertainties may result in future actual expenditure differing from the amounts currently provided. The provision at the end of the reporting period represents management's best estimate of the present value of the future rehabilitation costs required. Changes to estimated future costs are recognised in the consolidated statements of financial position of the Group by adjusting the rehabilitation liability. At 31 December 2012, the directors of the Company estimated that no provision for rehabilitation is required (2011: Nil).

Current tax

The Group is subject to income taxes in Hong Kong and Mainland China. The Group carefully evaluates tax implications of its transactions in accordance with prevailing tax regulations and makes tax provision accordingly. However, judgement is required in determining the Group's provision for income taxes as there are many transactions and calculations of which the ultimate tax determination is uncertain during the ordinary course of business. Where the final tax outcome of these matters is different from the amounts that were initially recorded, the differences will impact on the income tax and deferred tax provision in the periods in which the determination is made.

The carrying amount of current tax payable carried as liabilities in the consolidated statement of financial position as at 31 December 2012 was HK$228,721,000 (2011: HK$272,526,000).

5. OPERATING SEGMENT INFORMATION

Over 90% of the Group's revenue, expenses and assets are generated from the business of mining and selling coal in Mainland China. The management of the Group makes decisions about resources allocation and assesses performance of the Group based on the operating results from these business activities. Accordingly, the directors of the Company are of the opinion that mining and selling coal in Mainland China is a single reportable segment of the Group.

The Group's revenue from external customers is derived solely from its operations in the PRC, and over 90% of the non-current assets of the Group are located in the PRC.

During the year, the Group had transactions with three (2011: three) external customers which individually contributed to over 10% of the Group's total revenue. The revenue generated from sales to each of these customers is set out below:

	2012 HK$'000	2011 HK$'000
Customer A	174,646	83,469
Customer B	63,550	102,949
Customer C	57,851	*
Customer D	*	288,878
	296,047	475,296

* Less than 10% of the Group's total revenue

6. REVENUE, OTHER INCOME AND GAINS

Revenue, which is also the Group's turnover, represents the invoiced value of coal sold to customers, net of sales tax, value added tax and allowances for returns and trade discounts.

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

	2012 HK$'000	2011 HK$'000
Other income		
Bank interest income	286	262
Other interest income	1,500	6,270
Other income from termination of subscription agreements	—	10,000
Others	20	—
	1,806	16,532

6. REVENUE, OTHER INCOME AND GAINS (Continued)

An analysis of the Group's other income and gains is as follows: (continued)

	2012 HK$'000	2011 HK$'000
Gains		
Gain on disposal of items of property, plant and equipment	1,049	—
Fair value gain on derivative component of convertible bonds (note 26)	—	35,452
Others	402	211
	1,451	35,663
Other income and gains	3,257	52,195

7. FINANCE COSTS

An analysis of the Group's finance costs is as follows:

	2012 HK$'000	2011 HK$'000
Interest on bank and other loans wholly repayable within five years	115,240	106,155
Imputed interest on convertible bonds (note 26)	—	37,104
Imputed interest on convertible notes (note 27)	20,774	26,902
Interest on convertible bonds	—	1,590
	136,014	171,751

8. PROFIT/(LOSS) BEFORE TAX

The Group's profit/(loss) before tax is arrived at after charging:

	Notes	2012 HK$'000	2011 HK$'000
Depreciation	14	248,778	157,880
Amortisation of prepaid land premiums	15	346	357
Amortisation of mining rights	16	128,842	162,831
Employee benefit expense (including directors' remuneration):			
Wages, salaries and other benefits		49,254	48,247
Equity-settled share option expense	30	8,029	30,939
		57,283	79,186
Pension scheme contributions (defined contribution scheme)		11,707	9,453
		68,990	88,639
Auditors' remuneration		2,730	2,480
Write-off of items of property, plant and equipment		—	22,789
Impairment of items of property, plant and equipment#	14(a)	684,145	—
Impairment of mining rights#	14(a), 16	1,126,973	—
Impairment of trade receivables#	20(b)	10,424	144
Impairment of prepayment of property, plant and equipment#	14(a), 21	29,854	—
Impairment of the Indemnification Asset#	21, 32(a)	33,500	—
Impairment of other prepayments, deposits and other receivables#	21	63,541	1,086
Operating lease rentals in respect of buildings		2,410	2,376

These items are included in "Other expenses" in the consolidated statement of comprehensive income during the current year.

9. DIRECTORS' REMUNERATION

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

	Group	
	2012	2011
	HK$'000	HK$'000
Fees	**1,138**	1,080
Other emoluments:		
Salaries, allowances and benefits in kind	**4,610**	5,170
Pension scheme contributions	**28**	25
Equity-settled share option expenses	**5,124**	18,220
	9,762	23,415
	10,900	24,495

During the year ended 31 December 2010, certain directors were granted share options, in respect of their services to the Group, under the share option scheme of the Company, further details of which are set out in note 30 to the financial statements. The fair value of these options, which has been recognised in profit or loss over the vesting period, was determined as at the date of grant and the amount included in the financial statements for the current and prior years is included in the above directors' remuneration disclosures.

During the years ended 31 December 2012 and 2011, no share options have been granted to the directors of the Company.

9. DIRECTORS' REMUNERATION (Continued)

An analysis of director's remuneration, on a named basis, for directors who are holding office during the year is as follows:

Group

	Fees HK$'000	Salaries, allowances and benefits in kind HK$'000	Pension scheme contributions HK$'000	Equity-settled share options expense HK$'000	Total remuneration HK$'000
Year ended 31 December 2012					
Executive directors:					
Wang Da Yong	—	3,128	14	2,906	6,048
Tian Wenwei	—	1,302	14	1,015	2,331
Wang Tongtian	—	180	—	403	583
Chen Marlon Ray	—	—	—	—	—
	—	4,610	28	4,324	8,962
Non-executive directors:					
Wong Chun Hung (appointed on 16 April 2012)	128	—	—	—	128
Seah Ang (appointed on 25 June 2012)	62	—	—	—	62
Li Feng (resigned on 27 February 2012)	—	—	—	—	—
Wang Daoyuan (resigned on 27 February 2012)	—	—	—	—	—
Li Yi (resigned on 1 June 2012)	275	—	—	271	546
Su Bin (resigned on 1 June 2012)	75	—	—	265	340
	540	—	—	536	1,076
Independent non-executive directors:					
Chiu Sui Keung	180	—	—	132	312
Li Peiming	180	—	—	—	180
Lee Chi Hwa, Joshua (appointed on 9 January 2012)	98	—	—	—	98
Cao Kuangyu (resigned on 23 April 2012)	57	—	—	132	189
Lam Ka Wai, Graham (appointed on 23 April 2012)	83	—	—	—	83
	598	—	—	264	862
Total	1,138	4,610	28	5,124	10,900

9. DIRECTORS' REMUNERATION (Continued)

Group (Continued)

	Fees HK$'000	Salaries, allowances and benefits in kind HK$'000	Pension scheme contributions HK$'000	Equity-settled share options expense HK$'000	Total remuneration HK$'000
Year ended 31 December 2011					
Executive directors:					
Wang Da Yong	—	3,406	13	8,499	11,918
Tian Wenwei	—	1,404	12	4,653	6,069
Wang Tongtian	—	360	—	1,672	2,032
Chen Marlon Ray (appointed on 21 December 2011)	—	—	—	—	—
	—	5,170	25	14,824	20,019
Non-executive directors:					
Li Yi	360	—	—	1,241	1,601
Su Bin	180	—	—	862	1,042
Li Feng	—	—	—	—	—
Wang Daoyuan	—	—	—	—	—
	540	—	—	2,103	2,643
Independent non-executive directors:					
Cao Kuangyu	180	—	—	431	611
Chiu Sui Keung	180	—	—	431	611
Li Peiming (appointed on 30 September 2011)	45	—	—	—	45
Jacobsen William Keith (resigned on 30 September 2011)	135	—	—	431	566
	540	—	—	1,293	1,833
Total	1,080	5,170	25	18,220	24,495

There was no arrangement under which a director waived or agreed to waive any remuneration during the year (2011: Nil).

10. FIVE HIGHEST PAID EMPLOYEES

The five highest paid employees during the year included two (2011: three) directors, details of whose remuneration are set out in note 9 above. Details of the remuneration of the remaining three (2011: two) non-director, highest paid employees for the year are as follows:

	2012 HK$'000	2011 HK$'000
Salaries, allowances and benefits in kind	2,760	2,096
Pension scheme contributions	28	24
Equity-settled share option expenses	947	4,344
	3,735	6,464

The number of non-director, highest paid employees whose remuneration fell within the following bands is as follows:

	Number of employees	
	2012	2011
Nil to HK$1,000,000	1	—
HK$1,000,001 to HK$1,500,000	1	—
HK$1,500,001 to HK$2,000,000	1	—
HK$2,500,001 to HK$3,000,000	—	1
HK$3,000,001 to HK$3,500,000	—	1
	3	2

During the year ended 31 December 2010, the non-director, highest paid employees were granted share options of the Company, in respect of their services to the Group, under the share option scheme of the Company, further details of which are set out in note 30 to the financial statements. The fair value of these options, which has been recognised in profit or loss over the vesting period, was determined as at the date of grant and the amount included in the financial statements for the current and prior years is included in the above non-director, highest paid employees' remuneration disclosures.

During the years ended 31 December 2012 and 2011, no share options have been granted to the above non-director, highest paid employees.

11. INCOME TAX

No provision for Hong Kong profits tax has been made as the Group did not generate any assessable profits arising in Hong Kong during the year (2011: Nil). Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the jurisdictions in which the Group operates.

	2012 HK$'000	2011 HK$'000
Current — Mainland China	5,759	119,108
Deferred (note 28)	(527,637)	(78,712)
Total tax charge/(credit) for the year	(521,878)	40,396

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

Group
Year ended 31 December 2012

	Hong Kong		Mainland China		Total	
	HK$'000	%	HK$'000	%	HK$'000	%
Loss before tax	(63,944)		(2,212,976)		(2,276,920)	
Tax at the statutory tax rates	(10,550)	16.5	(553,244)	25.0	(563,794)	24.8
Profit attributable to a jointly-controlled entity	—	—	(1,570)	0.1	(1,570)	0.1
Income not subject to tax	—	—	(1,473)	0.1	(1,473)	0.1
Expenses not deductible for tax	10,550	(16.5)	34,170	(1.5)	44,720	(2.0)
Tax losses not recognised	—	—	239	—	239	—
Tax credit at the Group's effective rate	—	—	(521,878)	23.7	(521,878)	23.0

11. INCOME TAX (Continued)

Group (Continued)
Year ended 31 December 2011

	Hong Kong HK$'000	%	Mainland China HK$'000	%	Total HK$'000	%
Profit/(loss) before tax	(80,632)		186,462		105,830	
Tax at the statutory tax rates	(13,304)	16.5	46,616	25.0	33,312	31.5
Income not subject to tax	(7,547)	9.4	(7,487)	(4.0)	(15,034)	(14.2)
Expenses not deductible for tax	18,197	(22.6)	916	0.4	19,113	18.1
Tax losses not recognised	2,654	(3.3)	351	0.2	3,005	2.8
Tax charge at the Group's effective rate	—	—	40,396	21.6	40,396	38.2

The share of tax attributable to the jointly-controlled entity amounting to HK$2,161,000 (2011: Nil) (note 18) is included in "Share of profit/(loss) of a jointly-controlled entity" in the consolidated statement of comprehensive income.

12. PROFIT/(LOSS) ATTRIBUTABLE TO OWNERS OF THE COMPANY

The consolidated profit/(loss) attributable to owners of the Company for the year ended 31 December 2012 includes a loss of HK$63,807,000 (2011: HK$80,476,000) which has been dealt with in the financial statements of the Company.

A reconciliation of the above amount to the Company's loss for the year is as follows:

	Notes	2012 HK$'000	2011 HK$'000
Amount of consolidated loss for the year attributable to owners of the Company dealt with in the financial statements of the Company		63,807	80,476
Impairment of interests in subsidiaries recognised during the year in profit or loss:			
Investment costs in subsidiaries	17(b)	1,007,893	—
Amounts due from subsidiaries	17(b)	180,810	—
The Company's loss for the year	31(b)	1,252,510	80,476

13. EARNINGS/(LOSS) PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE COMPANY

The calculation of the basic loss (2011: earnings) per share amounts is based on the loss (2011: profit) for the year attributable to ordinary equity holders of the Company, and the weighted average number of ordinary shares of 1,428,729,168 (2011: 1,313,416,291) in issue during the year.

No adjustment has been made to the basic earnings/loss per share amounts presented for the years ended 31 December 2012 and 2011 in respect of a dilution, as the share options of the Company outstanding during these years and the deemed conversion of the convertible bonds/notes issued by the Company have either no dilutive effect or an anti-dilutive effect on the basic earnings/loss per share amounts for these years.

14. PROPERTY, PLANT AND EQUIPMENT

Group

	Notes	Buildings HK$'000	Leasehold improvements HK$'000	Plant and machinery HK$'000	Furniture, fixtures and equipment HK$'000	Motor vehicles HK$'000	Construction in progress HK$'000 (Note (b))	Total HK$'000
Year ended 31 December 2012								
At 31 December 2011 and 1 January 2012:								
Cost		52,417	878	1,979,255	14,843	13,102	387,380	2,447,875
Accumulated depreciation		(5,314)	(308)	(282,487)	(4,969)	(3,621)	—	(296,699)
Net carrying amount		47,103	570	1,696,768	9,874	9,481	387,380	2,151,176
At 1 January 2012, net of accumulated depreciation		47,103	570	1,696,768	9,874	9,481	387,380	2,151,176
Additions		900	—	44,524	1,957	959	285,913	334,253
Disposals		—	(394)	(23,211)	(7)	(575)	—	(24,187)
Impairment	(a)	(17,523)	—	(643,756)	(3,275)	(2,357)	(17,234)	(684,145)
Depreciation provided during the year		(2,855)	(176)	(240,528)	(2,777)	(2,442)	—	(248,778)
Transfers		3,441	—	281,560	—	—	(285,001)	—
Exchange realignment		415	—	15,038	74	54	3,278	18,859
At 31 December 2012, net of accumulated depreciation and impairment		31,481	—	1,130,395	5,846	5,120	374,336	1,547,178
At 31 December 2012:								
Cost		57,251	—	2,289,023	16,932	12,224	391,570	2,767,000
Accumulated depreciation and impairment		(25,770)	—	(1,158,628)	(11,086)	(7,104)	(17,234)	(1,219,822)
Net carrying amount		31,481	—	1,130,395	5,846	5,120	374,336	1,547,178
Year ended 31 December 2011								
At 1 January 2011:								
Cost		36,941	878	1,256,281	8,221	7,434	107,625	1,417,380
Accumulated depreciation		(2,220)	(132)	(107,659)	(1,330)	(451)	—	(111,792)
Net carrying amount		34,721	746	1,148,622	6,891	6,983	107,625	1,305,588
At 1 January 2011, net of accumulated depreciation		34,721	746	1,148,622	6,891	6,983	107,625	1,305,588
Additions		621	—	524,150	4,618	3,398	290,373	823,160
Disposals and written-off		—	—	—	—	(463)	(22,951)	(23,414)
Acquisition of a subsidiary	32	8,772	—	106,446	496	1,295	5,544	122,553
Depreciation provided during the year		(2,316)	(176)	(150,758)	(2,525)	(2,105)	—	(157,880)
Transfers		3,355	—	1,940	—	—	(5,295)	—
Exchange realignment		1,950	—	66,368	394	373	12,084	81,169
At 31 December 2011, net of accumulated depreciation		47,103	570	1,696,768	9,874	9,481	387,380	2,151,176

14. PROPERTY, PLANT AND EQUIPMENT (Continued)

Company

	Furniture, fixtures and equipment HK$'000	Leasehold improvements HK$'000	Motor vehicles HK$'000	Total HK$'000
Year ended 31 December 2012				
At 31 December 2011 and and 1 January 2012:				
Cost	183	878	596	1,657
Accumulated depreciation	(65)	(307)	(208)	(580)
Net carrying amount	118	571	388	1,077
At 1 January 2012, net of accumulated depreciation	118	571	388	1,077
Depreciation provided during the year	(37)	(175)	(119)	(331)
Disposal	(7)	(396)	—	(403)
At 31 December 2012, net of accumulated depreciation	74	—	269	343
At 31 December 2012:				
Cost	168	—	596	764
Accumulated depreciation	(94)	—	(327)	(421)
Net carrying amount	74	—	269	343
Year ended 31 December 2011				
At 1 January 2011:				
Cost	183	878	596	1,657
Accumulated depreciation	(28)	(132)	(89)	(249)
Net carrying amount	155	746	507	1,408
At 1 January 2011, net of accumulated depreciation	155	746	507	1,408
Depreciation provided during the year	(37)	(175)	(119)	(331)
At 31 December 2011, net of accumulated depreciation	118	571	388	1,077

14. PROPERTY, PLANT AND EQUIPMENT (Continued)

Notes:

(a) In view of the adverse conditions, inter alia, significant decline of coal prices and sales volumes, since the second quarter of 2012, which are indicators of impairment, the directors of the Company had estimated the recoverable amounts (considered to be the same as the value-in-use by the directors of the Company) of the assets of the coal mining businesses (i.e. cash-generating units) of the Group (the "Mining Assets") which included property, plant and equipment, mining rights and prepayments for property, plant and equipment.

The Company had engaged Savills Valuation and Professional Services Limited, an independent professional valuer, to assess the value-in-use of the cash-generating units and the directors of the Company had derived the value-in-use of the Mining Assets from the value-in-use of the cash-generating units. In assessing the value-in-use of the cash-generating units, the future cash flows of the coal mining businesses, which cover the periods to utilise the remaining reserves of the coal mines, are discounted to the related present values using a pre-tax discount rate that reflects current assessments of the time value of money and the risks specific to such businesses. Parameters used in the projected cash flows included but were not limited to selling prices and sales volumes of coal, production cost and other expenses, capital expenditure, production plan and discount rate, which reflected the current conditions of the market and the Group and estimated trend in the future. Key assumptions used in assessing the value-in-use of the cash-generating units included discount rate of 14% and perpetual growth rate of 3% after the fifth year.

Based on the assessment, the directors of the Company are of the opinion that an impairment loss of the Mining Assets totaling HK$1,841 million was resulted and allocated to property, plant and equipment, mining rights and prepayments for property, plant and equipment based on their relative carrying amounts amongst the Mining Assets. Accordingly, impairment provision of items of property, plant and equipment of HK$684,145,000, impairment provision of mining rights of HK$1,126,973,000 (note 16) and impairment provision of prepayments for property, plant and equipment of HK$29,854,000 (note 21) were recognised as "Other expenses" in the consolidated statement of comprehensive income during the year.

(b) The Group's construction in progress with a net carrying amount of approximately HK$30,680,000 as at 31 December 2012 (2011: Nil) were pledged to secure an interest-bearing other borrowing of the Group (note 25).

15. PREPAID LAND PREMIUMS

		Group	
	Note	2012 HK$'000	2011 HK$'000
Carrying amount at 1 January		15,080	12,299
Acquisition of a subsidiary	32	—	2,523
Amortisation provided during the year		(346)	(357)
Exchange realignment		122	615
Carrying amount at 31 December		14,856	15,080

The leasehold land is situated in Mainland China and is held under a medium term lease.

16. MINING RIGHTS

	Notes	Group 2012 HK$'000	2011 HK$'000
At 1 January:			
Cost		3,263,190	2,470,650
Accumulated amortisation		(298,254)	(127,506)
Net carrying amount		2,964,936	2,343,144
Cost at 1 January, net of accumulated amortisation		2,964,936	2,343,144
Acquisition of a subsidiary	32	—	670,646
Amortisation provided during the year	8	(128,842)	(162,831)
Impairment provided during the year	14(a)	(1,126,973)	—
Exchange realignment		30,134	113,977
At 31 December		1,739,255	2,964,936
At 31 December:			
Cost		3,295,748	3,263,190
Accumulated amortisation and impairment		(1,556,493)	(298,254)
Net carrying amount		1,739,255	2,964,936

The Group's mining rights with a net carrying amount of approximately HK$1,364,856,000 as at 31 December 2012 (2011: HK$2,327,383,000) were pledged to secure certain interest-bearing bank borrowings of the Group (note 25).

The net carrying value of mining rights at 31 December 2012 included cost less accumulated amortisation and impairment of the mining right of Nianpanliang No.2 Coal Mine (the "Old No.2 Coal Mine") amounted to HK$726 million. The area of the Old No.2 Coal Mine had been included in the scope of city development plan of the local government, hence the local government proposed to exchange another coal mine (the "New No.2 Coal Mine") located adjacent to an existing coal mine of the Group as compensation (the "Coal Mine Exchange"). As at 31 December 2012, the Group already incurred net prepayment of HK$32 million for the purchase of property, plant and equipment to be used in the New No.2 Coal Mine. However, as at the date of approval of these financial statements, the Coal Mine Exchange has not been formally approved by the relevant government authorities and therefore the Coal Mine Exchange is not yet commenced.

16. MINING RIGHTS (Continued)

Notwithstanding the above delay, the Group is currently continuing with its application for the completion of Coal Mine Exchange and obtaining the mining right certificate of the New No. 2 Coal Mine. After due and careful enquiry and taking into account legal and other advices, the directors of the Company are of the opinion that (i) the Group has valid mining right certificate on the Old No. 2 Coal Mine which entitled the Group to exchange for the mining right certificate of the New No.2 Coal Mine as compensation from local government; (ii) the application for the exchange is conducted in accordance with relevant PRC regulations and local government's coal resource integration policies; and (iii) there are no legal or other impediments to complete the Coal Mine Exchange.

The directors of the Company estimate that the mining right certificate of the New No. 2 Coal Mine will be obtained in the foreseeable future such that the New No. 2 Coal Mine is expected to commence production in due course after construction and development. During the impairment assessment of related mining rights and prepayment for property, plant and equipment as further detailed in note 14(a) to the financial statements, the directors of the Company have considered the impact of the delay in completion of the Coal Mine Exchange.

17. INTERESTS IN SUBSIDIARIES

		Company	
	Notes	2012 HK$'000	2011 HK$'000
Investment in subsidiaries, included in non-current assets:			
Unlisted shares, at cost	(a)	1,810,195	1,810,195
Impairment of unlisted shares	(b)	(1,007,893)	—
		802,302	1,810,195
Due from subsidiaries, included in current assets	(c)	180,810	237
Impairment	(b)	(180,810)	—
		—	237
Due to a subsidiary, included in current liabilities	(c)	(420)	—
Total interests in subsidiaries		801,882	1,810,432

17. INTERESTS IN SUBSIDIARIES (Continued)

Notes:

(a) Particulars of the principal subsidiaries, which were all indirectly held by the Company, are as follows:

Name	Place of incorporation/ registration and place of operations	Nominal value of issued ordinary/ registered share capital	Percentage of indirect equity attributable to the Company	Principal activities
Triumph Fund A Limited	Cayman Islands	US$50,000	100	Investment holding
Shanxi Puhua Deqin Metallurgy Technology Co., Ltd. ("Shanxi Puhua Deqin")#	The PRC/Mainland China	RMB150,000,000	99	Investment holding
Eerduosi Hengtai Coal Co., Ltd. ("Hengtai") #	The PRC/Mainland China	RMB180,000,000	94	Mining and selling of coal
Inner Mongolia Liaoyuan Mining Co., Ltd. ("Liaoyuan") #	The PRC/Mainland China	RMB5,000,000	94	Mining and selling of coal

Registered as limited liability companies under PRC law

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

(b) In view of the HK$1,841 million impairment of the Mining Assets (note 14(a)) held by the subsidiaries during the year, which is an indicator of impairment of the Company's investment in the subsidiaries, the directors of the Company have assessed and made an impairment provision of HK$1,007,893,000 (note 12) against the Company's investments in subsidiaries.

In addition, during the year, impairment provision of HK$180,810,000 (note 12) was made against amounts due from subsidiaries which had been loss-making for some time.

(c) All balances with subsidiaries as at 31 December 2012 and 2011 are unsecured, interest-free and have no fixed terms of repayment.

18. INVESTMENT IN A JOINTLY-CONTROLLED ENTITY

	Group 2012 HK$'000	2011 HK$'000
Share of net assets	23,117	16,623

Notes:

(a) Particulars of the jointly-controlled entity, which is indirectly held by the Company, registered and operated in the PRC, are as follows:

Name	Registered and paid-up capital	Percentage of Ownership interest	Percentage of Voting power	Percentage of Profit sharing	Principal activities
聚信泰和能源投資基金管理有限責任公司	RMB30,000,000	45	45	45	Fund management

(b) The following table illustrates the summarised financial information of the Group's jointly-controlled entity:

	2012 HK$'000	2011 HK$'000
Share of the jointly-controlled entity's assets and liabilities:		
Current assets	19,932	15,235
Non-current assets	6,073	2,303
Current liabilities	(2,888)	(915)
Net assets	23,117	16,623
Share of the jointly-controlled entity's results:		
Revenue	13,753	2,336
Total expenses	(5,313)	(2,364)
Income tax	(2,161)	—
Profit/(loss) for the year	6,279	(28)

19. INVENTORIES

	Group 2012 HK$'000	2011 HK$'000
Raw materials	8,925	10,362
Finished goods	6,352	6,672
Sub-materials and parts	202	182
	15,479	17,216

20. TRADE AND BILLS RECEIVABLES

	Notes	Group 2012 HK$'000	2011 HK$'000
Trade and bills receivables	(a)	56,450	117,100
Impairment of trade receivables	(b)	(10,424)	—
	(c)	46,026	117,100

Notes:

(a) The Group's trading terms with its customers are mainly on credit, except for new customers, where payment in advance is normally required. The credit period is generally one month, extending up to six months for major customers. Each customer has a maximum credit limit. The Group seeks to maintain strict control over its outstanding receivables and overdue balances are reviewed regularly by the management. Trade and bills receivables are non-interest-bearing and the Group does not hold any collateral or other credit enhancements over its trade receivable balances.

(b) The movements in the provision for impairment of trade receivables are as follows:

	Group 2012 HK$'000	2011 HK$'000
At 1 January	–	7,014
Impairment losses recognised (note 8)	10,424	144
Amount written off as uncollectible	–	(7,158)
At 31 December	10,424	–

20. TRADE AND BILLS RECEIVABLES (Continued)

Notes: (continued)

(b) (continued)

At 1 January 2011, the provision for impairment of trade receivables were full provision for individually impaired trade receivables of HK$7,014,000. The individually impaired trade receivables related to customers that were in financial difficulties and the receivables were not expected to be recovered. The amount, together with impairment loss of HK$144,000 recognised during the year ended 31 December 2011, had been fully written off as uncollectible during the year ended 31 December 2011.

At 31 December 2012, the provision for impairment of trade receivables is a provision for individually impaired trade receivables of HK$10,424,000 with a carrying amount before provision of HK$20,783,000. The individually impaired trade receivables were related to customers that were in financial difficulties and the receivables may not be fully recovered.

(c) An aged analysis of the trade and bills receivables as at the end of the reporting period, based on the invoice date and net of provisions, is as follows:

	Group	
	2012 HK$'000	2011 HK$'000
Less than six months	30,409	116,427
Six months to one year	4,674	—
Over one year	21,367	673
	56,450	117,100
Provision for impairment (note (b))	(10,424)	—
	46,026	117,100

An aged analysis of the trade and bills receivables that are not individually nor collectively considered to be impaired is as follows:

	Group	
	2012 HK$'000	2011 HK$'000
Neither past due nor impaired	20,769	116,427
Past due for less than six months	9,640	—
Past due for over six months	5,258	673
	35,667	117,100

Receivables that were neither past due nor impaired to various customers for whom there was no recent history of default.

Receivables that were past due but not impaired relate to a number of independent customers that have a good track record with the Group. Based on past experience, the directors of the Company are of the opinion that no provision for impairment is necessary in respect of these balances as there has not been a significant change in credit quality and the balances are still considered fully recoverable.

21. PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

		Group		Company	
	Notes	2012 HK$'000	2011 HK$'000	2012 HK$'000	2011 HK$'000
Prepayments, deposits and other receivables	(a)	244,815	722,108	32,808	211,140
Impairment	(b)	(93,395)	—	(15,000)	—
		151,420	722,108	17,808	211,140
Portion classified as current assets		(90,686)	(566,144)	(17,808)	(211,140)
Non-current portion		60,734	155,964	—	—

Notes:

(a) The Group's prepayments, deposits and other receivables with a net carrying amount of approximately HK$31,617,000 as at 31 December 2012 (2011: Nil) were pledged to secure an interest-bearing other borrowing of the Group (note 25).

(b) The movement in the provision for impairment of prepayments, deposits and other receivables is as follows:

	Group	
	2012 HK$'000	2011 HK$'000
At 1 January	—	15,526
Impairment loss recognised	126,895	1,086
Amount written off as uncollectible (note 32(a))	(33,500)	(16,612)
At 31 December	93,395	—

During the year ended 31 December 2012, the impairment loss recognised in profit or loss included impairment of prepayments for property, plant and equipment of HK$29,854,000 (notes 8 and 14(a)); impairment of the Indemnification Asset (as defined in note 32(a)) of HK$33,500,000 (notes 8 and 32(a)), and impairment of other individually impaired receivable balances which had past due and the directors of the Company expect the receivables will be either unrecoverable or only partially recoverable aggregating to HK$63,541,000 (note 8).

22. PLEDGED DEPOSITS AND CASH AND CASH EQUIVALENTS

	Group		Company	
	2012 HK$'000	2011 HK$'000	**2012 HK$'000**	2011 HK$'000
Cash and bank balances other than time deposits	**15,913**	41,928	**7,642**	9,676
Time deposits	**3,517**	12,936	**—**	10,000
	19,430	54,864	**7,642**	19,676
Less: Time deposits pledged for general bank facilities	**(3,517)**	(2,936)	**—**	—
Cash and cash equivalents	**15,913**	51,928	**7,642**	19,676

Notes:

(a) At 31 December 2012, the cash and bank balances of the Group denominated in Renminbi ("RMB") amounted to HK$8,273,000 (2011: HK$32,252,000). The RMB is not freely convertible into other currencies. However, under Mainland China's Foreign Exchange Control Regulations and Administration of Settlement, Sale and Payment of Foreign Exchange Regulations, the Group is permitted to exchange RMB for other currencies through banks authorised to conduct foreign exchange business.

(b) Cash at banks earns interest at floating rates based on daily bank deposit rates. Time deposits are made for varying periods of between one day and three months depending on the immediate cash requirements of the Group, and earn interest at the respective time deposit rates. The bank balances are deposited with creditworthy banks with no recent history of default.

23. TRADE AND BILLS PAYABLES

The trade payables are non-interest-bearing and are normally settled on 60-day terms and bills payables are settled on 180-day terms. An aged analysis of the trade and bills payables as at the end of the reporting period, based on the invoice date, is as follows:

	Group	
	2012 HK$'000	2011 HK$'000
Less than six months	**92,336**	3,202
Six months to one year	**645**	1,805
Over one year	**35**	41
	93,016	5,048

24. OTHER PAYABLES AND ACCRUALS

		Group		Company	
		2012	2011	**2012**	2011
	Notes	**HK$'000**	HK$'000	**HK$'000**	HK$'000
Accruals		**295,913**	288,854	**2,740**	2,480
Receipts in advance		**31,808**	29,048	**—**	—
Interest payable		**16,537**	16,399	**—**	—
Value-added tax and other tax payables		**305,069**	288,845	**—**	—
Loans from third parties	(a)	**35,126**	218,347	**—**	—
Consideration payable for the acquisition of a subsidiary	(b)	**—**	324,007	**—**	—
Other payables	(c)	**11,984**	16,473	**10,000**	1,203
		696,437	1,181,973	**12,740**	3,683

Notes:

(a) Except for a loan from an independent third party with an outstanding amount of RMB35,776,000 (equivalent to HK$44,005,000, at the then exchange rate) as at 31 December 2011, which bore interest at an annual interest rate of 7.4% and was repayable by quarterly instalments up to November 2012, the remaining balances of loans from independent third parties as at 31 December 2012 and 2011 are unsecured, interest-free and have no fixed terms of repayment.

(b) The balance as at 31 December 2011 represents the unpaid consideration for the acquisition of a subsidiary in 2011, further details of which are included in note 32 to the financial statements. The amount was fully settled during the year.

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

25. INTEREST-BEARING BORROWINGS

Group

		2012			2011		
	Notes	Effective interest rate (%)	Maturity	HK$'000	Effective interest rate (%)	Maturity	HK$'000
Current							
Bank loans — unsecured	(c)	6.31–9.47	2013	472,682	6.31–8.58	2012	555,075
Bank loans — secured	(b), (c)	8.65–8.84	2013	497,560	—	—	—
Current portion of an other loan — secured	(d)	6.15	2013	43,269	—	—	—
				1,013,511			555,075
Non-current							
Bank loans — secured	(b), (c)	8.65	2014–2015	310,975	8.39–8.58	2013–2015	678,425
Other loan — secured	(d)	6.15	2014–2015	71,538	—	—	—
				382,513			678,425
				1,396,024			1,233,500
Bank loans:							
Repayable:							
Within one year				970,242			555,075
In the second year				124,390			370,000
In the third to fifth years, inclusive				186,585			308,425
				1,281,217			1,233,500
Other loan:							
Repayable:							
Within one year				43,269			—
In the second year				46,886			—
In the third to fifth years, inclusive				24,652			—
				114,807			—
				1,396,024			1,233,500

25. INTEREST-BEARING BORROWINGS (Continued)

Notes:

(a) All the interest-bearing loans are denominated in RMB.

(b) Certain of the Group's bank loans are secured by certain of the Group's mining rights (note 16).

(c) Certain of the Group's bank loans are guaranteed by a subsidiary of the Group, Shanxi Puhua Deqin, and certain independent third parties, including 內蒙古恒東能源集團有限責任公司 (formerly known as 內蒙古伊東集團恒東能源有限責任公司), 內蒙古東達蒙古王有限公司, 內蒙古蒙發煤炭有限責任公司, 山西普大煤業集團有限公司, Mr. Zhao Ming (a former shareholder and convertible notes holder of the Company) and Mr. Hao Shenhai (a former director of Hengtai).

(d) At 31 December 2012, the Group's other loan from an independent third party is secured by certain of the Group's construction in progress (note 14(b)) and prepayments, deposits and other receivables (note 21(a)), bears interest at a fixed annual rate of 6.15% and is repayable by 12 quarterly instalments commenced on 18 April 2012.

26. CONVERTIBLE BONDS

On 24 September 2010, the Company issued one-year convertible bonds with a principal amount of HK$195,000,000 which bear interest at a rate of 2% per annum payable semi-annually in advance. The convertible bonds were convertible into ordinary shares at an initial conversion price of HK$4.0 per share (adjusted for the twenty-to-one share consolidation which took place on 24 June 2011 (note 29 (c)(i))).

The conversion option of the convertible bonds exhibited characteristics of an embedded derivative and was separated from its liability component. On initial recognition, the derivative component of the convertible bonds was measured at fair value as determined by reference to a valuation performed by independent professionally qualified valuers, and presented as part of the derivative liability. The excess of the net proceeds received by the Company over the amount initially recognised as the derivative component was recognised as the liability component. Subsequently, changes in the fair value of the derivative component of the convertible bonds were recognised in profit or loss within the year in which they arise and the liability component of the convertible bonds was stated at amortised cost.

On 24 September 2011, the convertible bonds matured and the outstanding principal amount has been fully redeemed on 26 September 2011. The movements of the derivative component of the convertible bonds during the year ended 31 December 2011 are as follows:

	Note	HK$'000
At 1 January 2011		35,452
Fair value change, net	6	(35,452)
At 31 December 2011		—

26. CONVERTIBLE BONDS (Continued)

The movements of the liability component of convertible bonds during the year ended 31 December 2011 are as follows:

	Note	HK$'000
At 1 January 2011		121,896
Imputed interest expense	7	37,104
Redeem on maturity		(159,000)
At 31 December 2011		—

27. CONVERTIBLE NOTES

On 21 December 2009, the Company issued zero coupon redeemable convertible notes in an aggregate principal amount of HK$1,805,000,000, for the acquisition of Triumph Fund A Limited and its subsidiaries. These convertible notes have a maturity term of five years, however, the Company has the right at any time after three years of the issuance date (i.e., 21 December 2012) to redeem in whole or in part of the convertible notes at par value. The convertible notes can be converted into ordinary shares at the initial conversion price of HK$1.25 per share (adjusted for the twenty-to-one share consolidation which took place on 24 June 2011 (note 29 (c)(i))).

During the year ended 31 December 2011, convertible notes with an aggregate principal amount of HK$375,795,000 were converted into 3,903,720,000 ordinary shares of the Company (note 29(a)).

The movements in the carrying and the principal amounts of the convertible notes are as follows:

Group and Company

		2012		2011	
	Notes	**Carrying amount HK$'000**	**Principal amount HK$'000**	Carrying amount HK$'000	Principal amount HK$'000
At 1 January		**221,782**	**289,205**	466,288	665,000
Converted into ordinary shares of the Company	29(a)	**—**	**—**	(271,408)	(375,795)
Imputed interest expense	7	**20,774**	**—**	26,902	—
At 31 December		**242,556**	**289,205**	221,782	289,205

28. DEFERRED TAX LIABILITIES

The movements in deferred tax liabilities during the year are as follows:

Group

	Loss available for offsetting future taxable profit HK$'000	Accruals of salary and welfare HK$'000	Impairment, depreciation and amortisation of non-current assets HK$'000	Fair value adjustments arising from acquisition of subsidiaries HK$'000	Total HK$'000
At 1 January 2011	—	(23,244)	6,012	556,018	538,786
Acquisition of a subsidiary (note 32)	—	(3,080)	—	165,009	161,929
Deferred tax charged/(credited) to profit or loss during the year (note 11)	—	(40,341)	756	(39,127)	(78,712)
Exchange realignment	—	(2,205)	311	26,639	24,745
At 31 December 2011 and 1 January 2012	—	(68,870)	7,079	708,539	646,748
Deferred tax charged/(credited) to profit or loss during the year (note 11)	(28,004)	5,219	(192,467)	(312,385)	(527,637)
Exchange realignment	(330)	(368)	(264)	6,879	5,917
At 31 December 2012	(28,334)	(64,019)	(185,652)	403,033	125,028

Notes:

(a) At 31 December 2012, deferred tax assets have not been recognised in respect of unused tax losses of approximately HK$255,372,000 (2011: HK$223,230,000) as they have arisen in the Company and certain subsidiaries that have been loss-making for some time and it is not considered probable that taxable profits will be available against which these tax losses can be utilised.

(b) Pursuant to the PRC Corporate Income Tax Law, a 10% withholding tax is levied on dividends declared to foreign investors from the foreign investment enterprises established in Mainland China. The requirement is effective from 1 January 2008 and applies to earnings after 31 December 2007. A lower withholding tax rate may be applied if there is tax treaty between Mainland China and the jurisdiction of the foreign investors. For the Group, the applicable rate is 10%. The Group is therefore liable for withholding taxes on dividends distributed by those subsidiaries established in Mainland China in respect of earnings generated from 1 January 2008.

At 31 December 2012, no deferred tax has been recognised for withholding taxes that would be payable on the unremitted earnings that are subject to withholding taxes of the Group's subsidiaries established in Mainland China (2011: Nil). In the opinion of the directors, it is not probable that these subsidiaries will distribute such earnings in the foreseeable future. There were no other temporary differences associated with investments in subsidiaries in Mainland China for which deferred tax liabilities have not been recognised as at 31 December 2012 (2011: Nil).

29. SHARE CAPITAL

Shares

	2012 HK$'000	2011 HK$'000
Authorised: 15,000,000,000 ordinary shares of HK$0.1 each	1,500,000	1,500,000
Issued and fully paid: 1,428,729,168 ordinary shares of HK$0.1 each	142,873	142,873

A summary of the transactions during the year ended 31 December 2011 with reference to the movements in the Company's issued share capital is as follows:

	Notes	Number of shares in issue	Issued capital HK$'000	Share premium account HK$'000	Total HK$'000
At 1 January 2011		22,629,743,370	226,298	3,065,615	3,291,913
Conversion of convertible notes	(a)	3,903,720,000	49,027	922,611	971,638
Share issue expenses		—	—	(99)	(99)
Repurchase of shares	(b)	(38,278,000)	(523)	—	(523)
Share consolidation	(c)(i)	(25,066,456,202)	—	—	—
Capital reduction	(c)(ii)	—	(131,929)	131,929	—
Share premium reduction	(c)(iii)	—	—	(2,953,243)	(2,953,243)
At 31 December 2011, 1 January 2012 and 31 December 2012		1,428,729,168	142,873	1,166,813	1,309,686

Notes:

(a) During the year ended 31 December 2011, 3,792,720,000 ordinary shares of a par value of HK$0.01 each and 111,000,000 ordinary shares of a par value of HK$0.1 each were issued upon partial conversion of the convertible notes with an aggregate principal amount of HK$375,795,000. The aggregate carrying amount of these convertible notes (including liability component of HK$271,408,000 and equity component of HK$700,230,000) was HK$971,638,000, and the excess of the carrying amount of the convertible notes over the aggregate par value of HK$49,027,000 for the ordinary shares issued, which amounted to HK$922,611,000, was credited to the share premium account of the Company.

29. SHARE CAPITAL (Continued)

Shares (Continued)

Notes: (Continued)

(b) During the year 31 December 2011, 36,720,000 ordinary shares of the Company of a par value of HK$0.01 each and 1,558,000 shares of par value of HK$0.1 each were repurchased by the Company on the Stock Exchange at a total consideration, before expenses, of HK$7,278,000.

Details of the shares repurchased were as follows:

Month/year	Number of shares repurchased	Highest price paid per share HK$	Lowest price paid per share HK$	Aggregate price paid HK$
June 2011	36,720,000	0.12	0.11	4,293,000
July 2011	1,558,000	1.99	1.78	2,985,000
	38,278,000			7,278,000

The repurchased shares were cancelled and accordingly the issued share capital of the Company was reduced by the nominal value of these shares. Pursuant to Section 49H of the Hong Kong Companies Ordinance, an amount equivalent to the par value of the shares cancelled of HK$523,000 was transferred to the capital redemption reserve. The premium paid for the repurchase of the shares, including expenses incurred for repurchase, of approximately HK$7,322,000 was charged to the accumulated losses.

(c) On 24 June 2011, the shareholders of the Company approved a proposed capital reorganisation (the "Capital Reorganisation") which comprised:

(i) the share consolidation, i.e., consolidation of 20 existing shares of par value of HK$0.01 each into one consolidated share of par value of HK$0.20;

(ii) the capital reduction, i.e., reduction of the par value of the consolidated shares of HK$0.20 each to HK$0.10 each by cancelling HK$0.10 of the par value in each consolidated share. The paid-up capital so cancelled is transferred to the share premium account of the Company; and

(iii) reduction of share premium account, i.e., reduction of the share premium account by HK$2,953,243,000, being a sum representing the accumulated losses of the Company as at 31 December 2010 and the application of the credit arising from the reduction to eliminate the accumulated losses.

Details of the Capital Reorganisation were set out in the Company's announcement dated 12 May 2011 and the circular dated 25 May 2011. The share consolidation and capital reduction were effective on 27 June 2011 when the authorised and issued capital consisted of 300,000,000,000 and 26,385,743,370 ordinary shares of HK$0.01 each, respectively, were reduced by 285,000,000,000 and 25,066,456,202 ordinary shares, respectively. Furthermore, upon completion of the capital reduction, an aggregate of paid-up capital of HK$131,929,000 was cancelled and transferred to the share premium account of the Company. The share consolidation and capital reduction were duly registered in the Companies Registry of Hong Kong on 7 July 2011. The reduction of share premium account was approved by the court on 23 December 2011 and the sealed copy of the court order has been duly registered in the Company Registry of Hong Kong on 29 December 2011. Accordingly, the reduction of share premium account was effective on 29 December 2011.

(d) On 12 October 2012, the Company entered into a subscription agreement with an independent third party, pursuant to which, the Company conditionally agreed to issue and allot and the subscriber conditionally agreed to subscribe in cash for 1,555,555,000 new shares of the Company at the subscription price of HK$0.45 per subscription share. The transaction was approved by the shareholders of the Company on 5 December 2012 and was subsequently completed on 31 January 2013.

29. SHARE CAPITAL (Continued)

Share option

Details of the Company's share option scheme (the "Scheme") and the share options issued under the Scheme are included in note 30 to the financial statements.

30. SHARE OPTION SCHEME

The Company operated a share option scheme which expired on 28 May 2012 (the "Expired Scheme") and a new share option scheme (the "Scheme") was approved by the shareholders of the Company which was effective from 30 May 2012, for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations. Upon the expiry of the Expired Scheme, no further share options can be granted under the Expired Scheme but the share options already granted under the Expired Scheme shall remain in full force and effect until the options expired. Further details of the Scheme were disclosed in the circular of the Company dated 27 April 2012.

The maximum number of unexercised share options currently permitted to be granted under the Scheme is an amount equivalent, upon their exercise, up to 10% of the shares of the Company in issue at any time. The maximum number of shares issuable under share options to each eligible participant in the Scheme within any 12-month period is limited to 1% of the shares of the Company in issue at any time. Any further grant of share options in excess of this limit is subject to shareholders' approval in a general meeting.

Share options granted to a director, chief executive or substantial shareholder of the Company, or to any of their associates, are subject to approval in advance by the independent non-executive directors. In addition, any share options granted to a substantial shareholder or an independent non-executive director of the Company, or to any of their associates, in excess of 0.1% of the shares of the Company in issue at any time or with an aggregate value (based on the price of the Company's shares at the date of the grant) in excess of HK$5 million, within any 12-month period, are subject to shareholders' approval in advance in a general meeting.

The offer of a grant of share options may be accepted within 21 days from the date of the offer, upon payment of a nominal consideration of HK$1 in total by the grantee. The share option may be exercised under the Scheme at any time during a period not exceeding five years after the date when the option is granted and expiring on the last date of this period.

The exercise price (which has been adjusted for the twenty-to-one share consolidation which took place on 24 June 2011 (note 29(c)(i)) is determined by the directors, but shall not be less than the higher of (i) the Stock Exchange closing price of the Company's shares on the date of offer of the share options; (ii) the average Stock Exchange closing price of the Company's shares for the five trading days immediately preceding the date of the offer; and (iii) the nominal value of an ordinary share. Share options do not confer rights on the holders to dividends or to vote at shareholders' meetings.

30. SHARE OPTION SCHEME (Continued)

No share options were granted or exercised during the year. The exercise prices and exercise periods of the share options outstanding as at 31 December 2012 and 2011 are as follows:

Number of options*	Exercise price* HK$ per share	Exercise period From	To
616,000	2.50	29 September 2008	28 September 2013
8,000,000	4.96	12 May 2011	11 May 2013
8,000,000	4.96	12 May 2012	11 May 2013
1,500,000	4.96	26 August 2011	25 August 2013
1,500,000	4.96	26 August 2012	25 August 2013
2,500,000	4.96	10 November 2011	9 November 2013
2,500,000	4.96	10 November 2012	9 November 2013
24,616,000			

* The number of the share options and the exercise price are subject to adjustment in case of rights or bonus issues, or other similar changes in the Company's share capital. As at 31 December 2012 and 2011, the exercise price and the number of the share options has been adjusted for the twenty-to-one share consolidation which took place on 24 June 2011 (note 29(c)(i)).

The fair value of the share options granted under the Scheme was determined as at the date of grant and has been recognised in profit or loss over the vesting period. During the year, equity-settled share option expense of HK$8,029,000 (2011: HK$30,939,000) was recognised in profit or loss in respect of the share options granted under the Scheme.

At the end of the reporting period, the Company had 24,616,000 (2011: 24,616,000) share options outstanding under the Scheme. There were no additional grant of share options during the years ended 31 December 2012 and 2011. The exercise in full of the outstanding share options would, under the present capital structure of the Company, result in the issue of 24,616,000 additional ordinary shares of the Company and additional share capital of HK$2,461,600 and share premium of HK$118,118,400 (before issue expenses and without taking into account of any transfer of share option reserve to the share premium account).

At the date of approval of these financial statements, the Company had 24,616,000 share options outstanding under the Scheme, which represented approximately 0.82% of the Company's shares in issue as at that date.

31. RESERVES

(a) Group

The amounts of the Group's reserves and the movements therein for the current and prior years are presented in the consolidated statement of changes in equity.

The Group's exchange fluctuation reserve comprises all foreign exchange differences arising from the translation of the financial statements of operations with presentation currency different from that of the Company.

(b) Company

	Notes	Share premium account HK$'000 (note (i))	Capital redemption reserve HK$'000 (note (ii))	Equity component of convertible notes HK$'000 (note 27)	Share option reserve HK$'000 (note(iii))	Accumulated losses HK$'000	Total HK$'000
At 1 January 2011		3,065,615	—	1,239,114	24,626	(2,953,243)	1,376,112
Loss for the year and total comprehensive loss for the year	12	—	—	—	—	(80,476)	(80,476)
Conversion of convertible notes	29(a)	922,611	—	(700,230)	—	—	222,381
Share issue expenses		(99)	—	—	—	—	(99)
Repurchase of shares	29(b)	—	523	—	—	—	523
Share repurchase expenses	29(b)	—	—	—	—	(7,322)	(7,322)
Capital reduction	29(c)(ii)	131,929	—	—	—	—	131,929
Share premium reduction	29(c)(iii)	(2,953,243)	—	—	—	2,953,243	—
Equity-settled share option arrangement	30	—	—	—	30,939	—	30,939
At 31 December 2011 and 1 January 2012		1,166,813	523	538,884	55,565	(87,798)	1,673,987
Loss for the year and total comprehensive loss for the year	12	—	—	—	—	(1,252,510)	(1,252,510)
Equity-settled share option arrangement	30	—	—	—	8,029	—	8,029
At 31 December 2012		1,166,813	523	538,884	63,594	(1,340,308)	429,506

31. RESERVES (Continued)

(b) Company (Continued)

Notes:

(i) The share premium account represents the excess of the issued price net of any share issue expenses over the par value of the shares issued.

(ii) The capital redemption reserve represents an amount equivalent to the par value of the shares repurchased by the Company which were cancelled and transferred from the issued capital account pursuant to Section 49H of the Hong Kong Companies Ordinance.

(iii) The share option reserve comprises the fair value of share options vested which are yet to be exercised, as further explained in the accounting policy of share-based payments in note 3.3 to the financial statements. The amount will either be transferred to the share premium account when the related share options are exercised, or transferred to accumulated losses should the related share options expire or be forfeited.

32. BUSINESS COMBINATION

On 11 August 2011, the Group acquired a 100% equity interest in an entity in the PRC, Liaoyuan, which owns and operates a thermal coal mine in Eerduosi City, Inner Mongolia, at a consideration of RMB512,673,000 (equivalent to HK$625,668,000, at the then exchange rate), inclusive of contingent consideration of RMB112,673,000 (equivalent to HK$137,507,000, at the then exchange rate) which was determined with reference to the net profit of Liaoyuan for the post-acquisition period up to 31 December 2011 as calculated by accounting principles generally accepted in the PRC. In the opinion of the directors, the post-acquisition net profit of Liaoyuan met the prescribed threshold and no adjustment was made to the contingent consideration during the year ended 31 December 2011.

The acquisition aimed to boost the Group's annual coal production capacity.

32. BUSINESS COMBINATION (Continued)

The fair values of the identifiable assets and liabilities of Liaoyuan as at the date of the acquisition were as follows:

	Notes	2011 HK$'000
Property, plant and equipment	14	122,553
Prepaid land premiums	15	2,523
Mining rights	16	670,646
Prepayments for non-current assets		1,348
Inventories		5,776
Prepayments, deposits and other receivables		2,487
Cash and bank balances		12,214
Trade and bills payables		(7,666)
Other payables and accruals		(122,346)
Other non-current liabilities		(13,410)
Income tax payable		(9,309)
Deferred tax liabilities	28	(161,929)
		502,887
An indemnification asset	(a)	152,729
Gain on bargain purchase		(29,948)
		625,668
Satisfied by:		
Cash		305,101
Other payable		320,567
		625,668

32. BUSINESS COMBINATION (Continued)

An analysis of the net outflow of cash and cash equivalents in respect of the above acquisition for the years ended 31 December 2012 and 2011 are as follows:

	2012 HK$'000	2011 HK$'000
Cash consideration paid	307,350	305,101
Cash and bank balances acquired	—	(12,214)
Net outflow of cash and cash equivalents included in cash flows used in investing activities	307,350	292,887

Notes:

(a) The balance represented receivable from the vendor (the "Vendor") in relation to the acquisition of Liaoyuan during the year ended 31 December 2011. Pursuant to the relevant sale and purchase agreement (the "Sale and Purchase Agreement"), the Vendor had agreed to undertake the repayment of all liabilities of Liaoyuan which existed prior to the completion of the acquisition. Therefore, the Group has recognised the amount of such liabilities undertaken by the Vendor amounting to RMB125.1 million (equivalent to HK$155.6 million) (2011: HK$152.7 million at the then exchange rate) upon the completion of the acquisition as an indemnification asset due from the Vendor (the "Indemnification Asset") which is included in prepayment, deposits and other receivables in the consolidated statement of financial position as at 31 December 2011.

In settlement of the Indemnification Asset by the Vendor and the unpaid consideration by the Group, in May 2012, a supplemental agreement (the "Supplemental Agreement") was entered into between the Vendor, the Group and an independent third party (the "Third Party"). Pursuant to the terms of Supplemental Agreement, *inter alia*, (i) the Group agreed to release the final payment in respect of the purchase consideration to the Vendor upon the execution of the Supplemental Agreement; (ii) all receivables and liabilities of Liaoyuan which existed prior to 1 June 2012 and any disputes arose in respect thereof would be taken up by the Third Party; and (iii) except for matters agreed in the Supplemental Agreement, upon the execution of the Supplemental Agreement, all the obligations of the Vendor, the Group and the Third Party under the Sale and Purchase Agreement are immediately fulfilled.

After due and careful review, the directors of the Company consider that Liaoyuan's net liabilities as at 31 May 2012 (after net-off of receivables of RMB5.0 million, equivalent to HK$6.1 million, entitled by the Third Party) of at least RMB74.7 million (equivalent to HK$92.7 million) shall be undertaken by the Third Party. The directors of the Company also noted that such net liabilities mainly included payables to the Third Party and its affiliated entities, and payables and charges already settled by the Third Party after 31 May 2012. Also, the Group has not encountered any claims or demand for settlement of such liabilities up to the date of approval of these financial statements. In addition, the Supplemental Agreement has not required the Group to pay for any late payment charges on the outstanding purchase consideration of Liaoyuan under the Sale and Purchase Agreement, but stipulated that upon its execution, all the previous contractual obligations of the Group under the Sale and Purchase Agreement are fulfilled immediately, and hence such late payment charges of RMB23.9 million (equivalent to HK$29.4 million) on the outstanding purchase consideration of Liaoyuan under the Sale and Purchase Agreement shall no longer be payable by the Group.

Accordingly, net liabilities of the Group aggregating to HK$122.1 million has been derecognised from the Group's financial statements as at 31 December 2012, and the Group's Indemnification Asset has been reduced to the extent of the aggregate net liabilities undertaken by the Third Party and the Vendor, which amounted to HK$122.1 million. The remaining balance of the Indemnification Asset of HK$33.5 million, which shall no longer be recoverable from the Vendor or the Third Party, is considered impaired and written off in the Group's financial statements for the year ended 31 December 2012 (note 21).

32. BUSINESS COMBINATION (Continued)

Notes: (Continued)

(b) Since the acquisition, Liaoyuan contributed HK$160,871,000 to the Group's revenue and HK$62,971,000 to the consolidated profit for the year ended 31 December 2011.

Had the combination taken place in the beginning of the year ended 31 December 2011, the revenue of the Group for the year ended 31 December 2011 would have been HK$1,218,333,000. Due to the fact that profit or loss attributed by the combination involves assessments of fair values of consideration and the identifiable assets and liabilities of Liaoyuan as at the date of acquisition, the directors of the Company were of the opinion that it was impractical to disclose the profit or loss of the Group had the combination taken place at the beginning of the year ended 31 December 2011.

33. CONTINGENT LIABILITIES

At the end of the reporting period, neither the Group nor the Company had any significant contingent liabilities (2011: Nil).

34. OPERATING LEASE ARRANGEMENTS

The Group leases certain of its office premises and staff quarters under operating lease arrangements. Leases are negotiated for terms ranging from one to three years.

At 31 December 2012, the Group and the Company had total future minimum lease payments under non-cancellable operating leases falling due as follows:

	Group and Company	
	2012	2011
	HK$'000	HK$'000
Within one year	**593**	2,765
In the second to fifth years, inclusive	**105**	2,953
	698	5,718

35. CAPITAL COMMITMENTS

In addition to the operating lease commitments detailed in note 34 above, the Group had the following capital commitments in respect of the acquisition of items of property, plant and equipment at the end of the reporting period:

	Group	
	2012 HK$'000	2011 HK$'000
Contracted, but not provided for	**32,520**	64,854

At the end of the reporting period, the Company had no material capital commitments (2011: Nil).

36. RELATED PARTY DISCLOSURES

(a) Except for those transactions detailed elsewhere in these financial statements, the Group had no transactions with related parties during the year (2011: Nil).

(b) Compensation of key management personnel of the Group:

Remuneration for key management personnel of the Group, including amounts paid to the Company's directors as disclosed in note 9 and certain of the highest paid employees as disclosed in note 10, is as follows:

	2012 HK$'000	2011 HK$'000
Short-term employee benefits	**8,508**	8,346
Post-employment benefits	**56**	49
Equity-settled share option expense	**6,071**	22,564
Total compensation paid to key management personnel	**14,635**	30,959

37. FINANCIAL INSTRUMENTS BY CATEGORY

All financial assets and liabilities of the Group and the Company as at 31 December 2012 and 2011 were loans and receivables and financial liabilities stated at amortised cost, respectively.

38. FAIR VALUE OF FINANCIAL INSTRUMENTS

The fair values of the financial assets and liabilities are included at the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. The following methods and assumptions were used to estimate the fair values:

(a) The fair values of financial assets and liabilities which are due to be received or settled within one year approximate to their carrying amounts largely due to the short term maturities of these instruments.

(b) The fair values of the interest-bearing borrowings due over one year have been calculated by discounting the expected future cash flows using rates currently available for instruments on similar terms, credit risk and remaining maturities. The fair values of the liabilities component of the convertible notes are estimated using an equivalent market interest rate for a similar convertible notes. The fair value of these financial liabilities approximate to their carrying amounts as they are charged at floating rate or carried at amortised cost using an effective interest rate approximate to the market rate.

Since the carrying amounts of the Group's financial instruments approximate their fair values, no separate disclosure of the fair values of the Group's financial instruments is made in the financial statements.

39. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's principal financial instruments comprise other receivables and payables, interest-bearing borrowings and convertible notes. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various other financial assets and liabilities such as trade and bills receivables and trade and bills payables, which arise directly from its operations.

It is the Group's policy that no trading in financial instruments shall be undertaken.

The main risks arising from the Group's financial instruments are (a) interest rate risk, (b) foreign currency risk, (c) credit risk and (d) liquidity risk. The board of directors reviews and agrees policies for managing each of these risks and they are summarised below.

(a) Interest rate risk

The Group's and Company's exposure to the risk of changes in market interest rates relates primarily to the Group's and Company's cash at banks and the Group's interest-bearing borrowings with floating interest rates. Nevertheless, as there is no significant fluctuation in the market interest rate, in the opinion of the directors, the Group had no significant interest rate risk for the year ended 31 December 2012.

39. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

(b) Foreign currency risk

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

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

(c) Credit risk

It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures and receivable balances are monitored on an ongoing basis.

At 31 December 2012 and 2011, trade and bills receivables from external customers which individually contributed to over 10% of the Group's total revenue for the years ended 31 December 2012 and 2011 were:

	2012 HK$'000	2011 HK$'000
Number of individual external customers which contributed to over 10% of the Group's total revenue for the year	3	3
Trade and bills receivables (before impairment) from the above customers	10,890	39,419
Percentage of total trade and bills receivables (before impairment) as at the end of the reporting period	19%	34%

Save as aforesaid, at the end of each of the reporting period, in the opinion of the directors, there was no significant concentration of credit risk of trade and bills receivables.

The credit risk of the Group's other financial assets, which comprise cash and cash equivalents, and prepayments, deposits and other receivables, arises from default of the counterparty, with a maximum exposure equal to the carrying amounts of these instruments.

39. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

(d) Liquidity risk

At 31 December 2012, the Group had a net current liability of HK$1,860,064,000. However, the directors of the Company considered that the liquidity risk of the Group is minimal as (i) there was capital injection from a new investor subsequently in January 2013; (ii) the management expects that new borrowings will be obtained; and (iii) a substantial shareholder has confirmed its ability and agreement to provide continual financial support and adequate funds to the Group to enable it to meet its liabilities as and when they fall due in the foreseeable future. Accordingly, the Group expects to have adequate sources of funding to finance the Group and manage its liquidity position. Further details of these matters are set out in note 2 to the financial statements.

The maturity profile of the Group's financial liabilities, as at the end of the reporting period, based on the contractual undiscounted payments, is as follows:

Group

	Within one year or on demand HK$'000	One to five years HK$'000	Total HK$'000
At 31 December 2012			
Trade and bills payables	93,016	—	93,016
Other payables and accruals	696,437	—	696,437
Interest-bearing borrowings	1,099,420	424,535	1,523,955
Convertible notes	—	289,205	289,205
	1,888,873	713,740	2,602,613
At 31 December 2011			
Trade and bills payables	5,048	—	5,048
Other payables and accruals	1,152,925	—	1,152,925
Interest-bearing borrowings	631,934	769,904	1,401,838
Convertible notes	—	289,205	289,205
	1,789,907	1,059,109	2,849,016

39. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

(d) Liquidity risk (continued)

Company

	Within one year or on demand HK$'000	One to five years HK$'000	Total HK$'000
At 31 December 2012			
Amount due to a subsidiary	420	—	420
Other payables and accruals	12,740	—	12,740
Convertible notes	—	289,205	289,205
	13,160	289,205	302,365
At 31 December 2011			
Other payables and accruals	3,683	—	3,683
Convertible notes	—	289,205	289,205
	3,683	289,205	292,888

(e) Capital management

The primary objectives of the Group's capital management are to safeguard the Group's ability to continue as a going concern and to maintain healthy capital ratios in order to support its business and maximise shareholders' value.

The Group manages its capital structure and makes adjustments to it in light of changes in economic conditions. In order to maintain or adjust the capital structure, the Group may issue new shares to increase capital. The Group is not subject to any externally imposed capital requirements. No changes were made in the objectives, policies or processes for managing capital during the years ended 31 December 2012 and 31 December 2011.

39. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

(e) Capital management (continued)

The Group monitors capital using the gearing ratio, which is net debt divided by the capital. Net debt includes trade and bills payables, other payables and accruals, interest-bearing borrowings, less cash and cash equivalents. Capital includes liability component of convertible notes and equity attributable to owners of the Company. The gearing ratio as at the end of the reporting periods were as follows:

	Group	
	2012 HK$'000	2011 HK$'000
Trade and bills payables	93,016	5,048
Other payables and accruals	696,437	1,181,973
Interest-bearing borrowings	1,396,024	1,233,500
Less: Cash and cash equivalents	(15,913)	(51,928)
Net debt	2,169,564	2,368,593
Convertible notes	242,556	221,782
Equity attributable to owners of the Company	752,933	2,376,998
Capital	995,489	2,598,780
Gearing ratio	2.18	0.91

40. EVENTS AFTER THE REPORTING PERIOD

Subsequent to the end of the reporting period, the Group carried out the following significant transactions:

a) On 31 January 2013, the Company issued and allotted 1,555,555,000 new ordinary shares with par value of HK$0.1 each to a new investor at a cash consideration of HK$0.45 per share. Net proceeds of the issuance amounted to approximately HK$663,000,000. Upon completion, total issued shares of the Company increased from 1,428,729,168 shares to 2,984,284,168 shares.

b) On 11 March 2013, the Group exercised its rights under the terms of the convertible notes to partially redeem the outstanding convertible notes in the principal amount of HK$50,000,000 at par value. After the redemption, the principal amount of the outstanding convertible notes amounted to HK$239,205,000. The management estimated that a loss on early redemption of convertible notes amounting to HK$7,341,000 will be recognised for the year ending 31 December 2013.

41. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on 28 March 2013.

FIVE-YEAR FINANCIAL SUMMARY

A summary of the results and of the assets, liabilities and non-controlling interests of the Group for the last five financial years, as extracted from the published audited financial statements, is set out below:

RESULTS

	Year ended 31 December				
	2012 HK$'000	2011 HK$'000	2010 HK$'000	2009 HK$'000	2008 HK$'000
CONTINUING OPERATIONS					
REVENUE	571,129	995,100	1,007,740	88,710	627,056
PROFIT/(LOSS) BEFORE TAX	(2,276,920)	105,830	(785,589)	(1,078,819)	(20,457)
Tax credit/(charge)	521,878	(40,396)	(100,405)	159	—
PROFIT/(LOSS) FOR THE YEAR FROM CONTINUING OPERATIONS	(1,755,042)	65,434	(885,994)	(1,078,660)	(20,457)
DISCONTINUED OPERATIONS					
Loss for the year from discontinued operations	—	—	—	—	(57,574)
PROFIT/(LOSS) FOR THE YEAR	(1,755,042)	65,434	(885,994)	(1,078,660)	(78,031)
Attributable to:					
Owners of the Company	(1,655,263)	55,339	(905,164)	(1,078,519)	(78,031)
Non-controlling interests	(99,779)	10,095	19,170	(141)	—
	(1,755,042)	65,434	(885,994)	(1,078,660)	(78,031)

ASSETS, LIABILITIES AND NON-CONTROLLING INTERESTS

	As at 31 December				
	2012 HK$'000	2011 HK$'000	2010 HK$'000	2009 HK$'000	2008 HK$'000
TOTAL ASSETS	3,556,761	6,059,103	5,160,468	3,751,078	191,063
TOTAL LIABILITIES	(2,781,782)	(3,561,577)	(3,131,734)	(4,248,245)	(139,008)
NON-CONTROLLING INTERESTS	(22,046)	(120,528)	(103,801)	(80,384)	—
	752,933	2,376,998	1,924,933	(577,551)	52,055

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