**THIS CIRCULAR IS IMPORTANT AND REQUIRES YOUR IMMEDIATE ATTENTION**

**If you are in any doubt** as to any aspect of this circular or as to the action to be taken, you should consult your stockbroker, or other licensed securities dealer, bank manager, solicitors, professional accountant or other professional adviser.

**If you have sold or transferred** all your shares in KanHan Technologies Group Limited (the "**Company**"), you should at once hand this circular and accompanying form of proxy to the purchaser or transferee, or to the bank, stockbroker or other agent through whom the sale or transfer was effected for transmission to the purchaser or the transferee.

The Stock Exchange of Hong Kong Limited takes no responsibility for the contents of this circular, makes no representation as to its accuracy or completeness and expressly disclaims any liability whatsoever for any losses howsoever arising from or in reliance upon the whole or any part of the contents of this circular.

This circular appears for information purposes only and does not constitute an invitation or offer to acquire, purchase or subscribe for the securities.

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# KANHAN TECHNOLOGIES GROUP LIMITED
# 看漢科技集團有限公司*

*(Proposed to be renamed as Shen Nong China (Group) Limited 神農中國(集團)有限公司)*
*(incorporated in the Cayman Islands with limited liability)*
(Stock Code: 8175)

## MAJOR TRANSACTION:
## THE ACQUISITION OF THE ENTIRE EQUITY INTEREST IN PROUD DRAGON LIMITED

**Financial adviser to the Company**

**INCU Corporate Finance Limited**

A notice convening an extraordinary general meeting (the "**EGM**") of the Company to be held on Monday, 4 February 2008 at 11:00 a.m. at 15th Floor, Sun House, 181 Des Voeux Road Central, Hong Kong is set out on pages 155 to 156 of this circular. A form of proxy for the EGM is enclosed with this circular. Whether or not you are able to attend the EGM, you are encouraged to complete and return the enclosed form of proxy in accordance with the instructions printed thereon and return the same to the branch share registrar of the Company in Hong Kong, Tricor Standard Limited at 26th Floor, Tesbury Centre, 28 Queen's Road East, Wanchai, Hong Kong as soon as possible and in any event no later than 48 hours before the time appointed for the holding of the EGM. Completion and return of the enclosed form of proxy will not preclude you from attending and voting in person at such meeting or any adjournment meeting should you so wish.

*This circular will remain on the GEM website at http://www.hkgem.com on the "Latest Company Announcements" page for seven days from the date of its publication.*

18 January 2008

* *for identification purpose only*

**GEM has been established as a market designed to accommodate companies to which a high investment risk may be attached. In particular, companies may list on GEM with neither a track record of profitability nor any obligation to forecast future profitability. Furthermore, there may be risks arising out of the emerging nature of companies listed on GEM and the business sectors or countries in which the companies operate. Prospective investors should be aware of the potential risks of investing in such companies and should make the decision to invest only after due and careful consideration. The greater risk profile and other characteristics of GEM mean that it is a market more suited to professional and other sophisticated investors.**

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

**The principal means of information dissemination on GEM is publication on the Internet website operated by the Stock Exchange. Listed companies are not generally required to issue paid announcements in gazetted newspapers. Accordingly, prospective investors should note that they need to have access to the GEM website in order to obtain up-to-date information on GEM-listed issuers.**

# CONTENTS

*In this circular, unless the context otherwise requires, the following expressions shall have the following meanings when used herein:*

| | |
|---|---|
| "Agreement" | the conditional agreement dated 29 October 2007 as supplemented by the Supplemental Agreement and entered into among the Vendor, the Purchaser and Proud Dragon in respect of the acquisition of the Sale Shares and the subscription of the Subscription Shares by the Purchaser |
| "associates" | has the meaning ascribed thereto in the GEM Listing Rules |
| "Board" | the board of Directors |
| "Bond Certificate" | the certificate to be issued by the Company on Completion evidencing the entitlement of the holders thereof to the Convertible Bond |
| "Bondholder" | the holder of the Convertible Bond |
| "business day" | any day (other than a Saturday or Sunday or public holiday) on which licensed banks in Hong Kong are generally open for business throughout their normal business hours |
| "Company" | KanHan Technologies Group Limited, a company incorporated in the Cayman Islands with limited liability, the issued Shares of which are listed on GEM |
| "Completion" | completion of the Agreement |
| "Conversion Price" | the initial conversion price of HK$0.25 per Conversion Share, subject to adjustments, pursuant to the terms of the Convertible Bond |
| "Conversion Shares" | 40,000,000 Shares to be issued upon the exercise of the conversion rights attaching to the Convertible Bond |
| "Convertible Bond" | the convertible bond in the principal amount of HK$10,000,000, to be issued by the Company to the Vendor |
| "Deposit" | collectively (i) HK$3,000,000 paid by the Purchaser to the Vendor within three business days from the date of the MOU; (ii) HK$3,200,000 paid by the Purchaser to the Vendor on the date of the Agreement, together being part of the Sale Consideration; and (iii) HK$15,800,000 payable by the Purchaser to Proud Dragon within three business days from the date on which conditions (c) and (h) under the sub-section headed "Condition precedents" under the section headed "The Agreement" have been fulfilled, being the Subscription Consideration |

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| "Directors" | directors of the Company |
| "EGM" | the extraordinary general meeting of the Company to be convened to consider and, if thought fit, approve the Proposed Acquisition |
| "Enlarged Group" | the Group as enlarged by the Proposed Acquisition |
| "GEM" | the Growth Enterprise Market of the Stock Exchange |
| "GEM Listing Rules" | the Rules Governing the Listing of Securities on GEM |
| "Group" | the Company and its subsidiaries |
| "Guarantee Certificate" | the certificate to be given by the auditors for the time being of Proud Dragon certifying the amount of the Actual Profit 2008 or, as the case may be, the Average Actual Profit |
| "HK Subsidiary" | Jetrise Development Limited, a company incorporated in Hong Kong with limited liability and is wholly and beneficially owned by Proud Dragon |
| "Hong Kong" | the Hong Kong Special Administrative Region of the PRC |
| "Latest Practicable Date" | 15 January 2008, being the latest practicable date prior to the printing of this circular for ascertaining certain information contained herein |
| "Manciple" | Manciple Enterprises Ltd., a company incorporated in the British Virgin Islands and is wholly and beneficially owned by Mr. Lau |
| "MOU" | the memorandum of understanding dated 4 October 2007 and entered into among the Company, the Vendor and Proud Dragon in respect of the proposed acquisition of the whole or part of equity interest held by the Vendor in Proud Dragon |
| "Mr. Lau" | Mr. Lau Kim Hung Jack |
| "Mr. Ma" | Mr. Ma She Shing Albert, a non-executive Director |
| "Mr. Mo" | Mr. Mo Wai Ming Lawrence, an executive Director |

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|---|---|
| "Mr. Pang" | Mr. Pang Hong Tao, an executive Director and chairman of the Company |
| "Mr. Yang" | Mr. Yang Pei Gen, an executive Director and chief executive officer of the Company |
| "Ms. Au" | Ms. Au Shui Ming Anna, an executive Director |
| "Open Offer" | the completed offer for subscription by the qualified Shareholders for a total of 443,458,360 offer shares, the details of which set out in the announcement of the Company dated 2 November 2007 and 17 December 2007 and the prospectus of the Company dated 26 November 2007 |
| "PRC" | the People's Republic of China, which for the purpose of this circular excludes Hong Kong, the Macau Special Administrative Region of the PRC and Taiwan |
| "Promissory Note" | the promissory note to be executed by the Company in favour of the Vendor for the purpose of settling partially the Sale Consideration |
| "Proposed Acquisition" | the proposed acquisition of the Proud Dragon Group through the purchase of the Sale Shares and the Subscription Shares by the Purchaser as contemplated under the Agreement |
| "Proud Dragon" | Proud Dragon Limited, a company incorporated in the British Virgin Islands with limited liability and is wholly owned by the Vendor as at the date of the Agreement |
| "Proud Dragon Group" | Proud Dragon and its subsidiaries, including the HK Subsidiary and after completion of the Reorganisation, Zhong Tian Water Supply |
| "Proud Dragon Shares" | the ordinary shares of US$1.00 each in the share capital of Proud Dragon |
| "Purchaser" or "Rise Assets" | Rise Assets Limited, a company incorporated in the British Virgin Islands and is wholly and beneficially owned by the Company |
| "Reorganisation" | the reorganisation of the Proud Dragon Group upon completion, of which Proud Dragon, through the HK Subsidiary, will own as to 70% equity interest in Zhong Tian Water Supply, which will be transformed into a Chinese foreign equity joint venture |

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| "Sale Consideration" | the consideration for the sale and purchase of the Sale Shares, being HK$31,800,000 |
| "Sale Shares" | 318 Proud Dragon Shares, being the entire issued share capital of Proud Dragon as at the date of the Agreement, representing the entire issued share capital of Proud Dragon as at the date of this circular |
| "SFO" | Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong) |
| "Share(s)" | existing ordinary share(s) of HK$0.05 each in the share capital of the Company |
| "Shareholder(s)" | holder(s) of Shares |
| "Silky Sky" | Silky Sky Investments Limited, an indirect wholly owned subsidiary of the Group |
| "Stock Exchange" | The Stock Exchange of Hong Kong Limited |
| "Subscription" | the subscription of the Subscription Shares in accordance with the terms of the Agreement |
| "Subscription Consideration" | the consideration for the subscription and allotment and issue, of the Subscription Shares, being HK$15,800,000 |
| "Subscription Shares" | 158 Proud Dragon Shares to be allotted and issued by Proud Dragon to the Purchaser in accordance with the terms of the Agreement |
| "Supplemental Agreement" | the supplemental agreement dated 14 January 2008 and entered into among the Vendor, the Purchaser and Proud Dragon relating to extension of the long-stop date of the Agreement |
| "Takeovers Code" | The Hong Kong Code on Takeovers and Mergers |
| "Vendor" | Mr. Yip Yuk Tong, the ultimate beneficial owner of 100% interest in Proud Dragon, and to the best of the Directors' knowledge, information and belief and having made all reasonable enquiries, is a third party independent of the Company and its connected persons under the GEM Listing Rules |

| | |
|---|---|
| "Zhong Tian Water Supply" | Dang Tu Xian Zhong Tian Water Supply Limited (當涂縣中天供水有限公司), a company established in the PRC with limited liability which immediately upon completion of the Reorganisation, will be transformed into a Chinese foreign equity joint venture and will be owned as to 70% of its equity interest indirectly by Proud Dragon through the HK Subsidiary |
| "HK$" | Hong Kong dollars, the lawful currency of Hong Kong |
| "RMB" | Renminbi, the lawful currency of the PRC |
| "US$" | United States dollar(s), the lawful currency of the United States of America |
| "%" | per cent |

# KANHAN TECHNOLOGIES GROUP LIMITED
# 看漢科技集團有限公司*

*(Proposed to be renamed as Shen Nong China (Group) Limited 神農中國(集團)有限公司)*
*(incorporated in the Cayman Islands with limited liability)*
(Stock Code: 8175)

*Executive Directors:*
Mr. Pang Hong Tao, Peter
Mr. Yang Pei Gen
Mr. Mo Wai Ming, Lawrence
Ms. Au Shui Ming, Anna

*Non-executive Director:*
Mr. Ma She Shing, Albert

*Independent non-executive Directors:*
Mr. Hsu William Shiu Foo
Mr. Lee Kun Hung
Mr. Kwok Chi Sun, Vincent

*Registered office:*
Caledonian Bank & Trust Limited
Caledonian House
P.O. Box 1043
George Town
Grand Cayman
Cayman Islands

*Head office and principal place of business in Hong Kong:*
15th Floor, Sun House
181 Des Voeux Road Central
Hong Kong

18 January 2008

*To the Shareholders*

Dear Sir or Madam,

## MAJOR TRANSACTION: THE ACQUISITION OF THE ENTIRE EQUITY INTEREST IN PROUD DRAGON LIMITED

## INTRODUCTION

Reference is made to the announcement of the Company dated 2 November 2007 in which the Board announced that the Agreement in respect of the Proposed Acquisition was entered into among the Purchaser, a wholly-owned subsidiary of the Company, the Vendor and Proud Dragon on 29 October 2007.

* *for identification purpose only*

The entering into of the Agreement constitutes a major transaction on the part of the Company under Chapter 19 of the GEM Listing Rules.

The purpose of this circular is to provide you with further details regarding the Proposed Acquisition in accordance with the GEM Listing Rules.

**THE AGREEMENT**

**Date**: 29 October 2007

**Parties:**

**Purchaser:** the Purchaser, a wholly owned subsidiary of the Company

**Vendor:** Mr. Yip Yuk Tong

To the best of the Directors' knowledge, information and belief, having made all reasonable enquiries, the Vendor is a third party independent of the Company and its connected persons (as defined in the GEM Listing Rules). The Vendor is a merchant and a private investor and has extensive experience in the management, operation and strategic planning in various corporations engaging in a variety of business activities in Hong Kong and the PRC.

**Target:** Proud Dragon

**Assets to be acquired**

The Sale Shares and the Subscription Shares together will represent the entire issued share capital of Proud Dragon upon the allotment and issue of the Subscription Shares.

The Subscription Shares, when allotted, fully paid and issued, will rank pari passu in all respects with the other shares of Proud Dragon in issue on the date of allotment and issue of the Subscription Shares.

**Consideration**

The total consideration of HK$47,600,000 comprises the Sale Consideration and the Subscription Consideration:

*Sale Consideration*

The Sale Consideration of HK$31,800,000 shall be settled in the following manner:

(i) HK$3,000,000 was paid by the Purchaser to the Vendor within three business days from the date of the MOU;

(ii) HK$3,200,000 was paid by the Purchaser to the Vendor on the date of the Agreement;

(iii) HK$10,000,000 will be settled by the Purchaser procuring the Company to issue to the Vendor on Completion the Convertible Bond, which shall then be delivered to the Purchaser for it to hold in escrow until the fulfillment of the Guaranteed Profit, the details of which can be found in the section headed "Profit Guarantee"; and

(iv) HK$15,600,000 will be settled by the Purchaser procuring the Company to issue to the Vendor on Completion the Promissory Note.

*Subscription Consideration*

The Subscription Consideration of HK$15,800,000 shall be settled by the Purchaser in cash and will be paid by the Purchaser as deposit within three business days from the date on which conditions (c) and (h) under the sub-section headed "Conditions precedent" under the section headed "The Agreement" have been fulfilled.

The total consideration of HK$47,600,000 for the Proposed Acquisition represents a price earning ratio of approximately 6.8 times of the Guaranteed Profit of HK$7,000,000 for the year ending 31 December 2008. The Sale Consideration and the Subscription Consideration were agreed between the Vendor and the Purchaser after arm's length negotiations and having considering: (i) the Guaranteed Profit given by the Vendor; (ii) the future prospect and business plan of the Proud Dragon Group as stated in the section "Profit Guarantee" below; (iii) the issuance of the Convertible Bond to the Vendor only after the fulfillment of the Guaranteed Profit; (iv) the Proposed Acquisition will be able to synergize with the Group's current business of the development, production and distribution of organic fertilizer in the PRC and provide additional channel to the Group's development in the agricultural industry in the PRC in long term; (v) the current price earning ratios of companies listed on the Stock Exchange engaging in business similar to Zhong Tian Water Supply ranging from about 19 to 84 times; and (vi) the Proposed Acquisition will serve to provide a stable income source to the Group. The Directors consider the terms and conditions of the Proposed Acquisition to be fair and reasonable and are in the interest of the Company and the Shareholders as a whole.

The Directors are of the view that Zhong Tian Water Supply is currently at its early stage of development and hence, its current net asset value is not able to reflect the profitability of Zhong Tian Water Supply in the future upon Completion. Accordingly, instead of basing on its current net asset value, the Consideration was based on, among others, the price earning ratios of companies listed on the Stock Exchange engaging in business similar to Zhong Tian Water Supply ranging from about 19 to 84 times.

**Conditions precedent**

Completion is subject to the following conditions having been fulfilled or waived (as the case may be):

(a) the Purchaser being satisfied with the results of the due diligence review to be conducted on the assets, liabilities, operations and affairs of the Proud Dragon Group;

(b) all necessary consents and approvals required to be obtained on the part of the Vendor and Proud Dragon in respect of the sale of the Sale Shares and the subscription of the Subscription Shares having been obtained;

(c) the passing by the Shareholders at the EGM and an ordinary resolution to approve the Agreement and the transactions contemplated thereunder, including but not limited to the issue of the Convertible Bond and Promissory Note to the Vendor;

(d) the obtaining of a PRC legal opinion (in a form and substance satisfactory to the Purchaser) from a PRC legal adviser appointed by the Purchaser in relation to the Agreement and the transactions contemplated thereunder;

(e) the warranties provided by the Vendor under the Agreement remaining true and accurate in all respects;

(f) the GEM Listing Committee of the Stock Exchange granting listing of and permission to deal in the Conversion Shares;

(g) all necessary consents and approvals required to be obtained on the part of the Purchaser in respect of the purchase of the Sale Shares and the subscription of the Subscription Shares having been obtained; and

(h) completion of the Reorganisation.

Conditions (a) and (e) above are waivable by the Purchaser under the Agreement. The Purchaser has no current intention to waive such conditions. Other than conditions (a) and (e), the other conditions are incapable of being waived.

On 29 December 2007, Zhong Tian Water Supply has obtained the Certificate of Approval for Establishment of Enterprise with foreign investment in the PRC. Save as disclosed, as at the Latest Practicable Date, none of the conditions precedent as stated above has been fulfilled.

**Completion**

Completion shall take place at 4:00 p.m. within three Business Days after all the conditions of the Agreement have been fulfilled or waived or such later date as may be agreed between the Vendor, Proud Dragon and the Purchaser.

Upon Completion, the Company will hold 100% interest in Proud Dragon and Proud Dragon will become an wholly-owned subsidiary of the Company with Proud Dragon Group accounts consolidated into that of the Group. The Company will also through its interest in Proud Dragon, hold 70% indirect interest in Zhong Tian Water Supply. The Directors confirm that the Group will nominate not less than two directors to the board of Proud Dragon which consists of solely the Vendor in an effort to obtain majority control of the Proud Dragon Group upon Completion.

The Proposed Acquisition will not result in a change of control of the Company.

**Long-stop date**

If all of the conditions are not fulfilled (or as the case may be, waived by the Purchaser) on or before 29 February 2008 (or such later date as the Vendor and the Purchaser may agree), the Agreement shall cease and terminate and together, neither party shall have any obligations towards each other.

**Profit Guarantee**

The Vendor has warranted and guaranteed to the Purchaser that the audited consolidated net profit after tax and extraordinary or exceptional items of the Proud Dragon Group for the financial year ending 31 December 2008 (the "Actual Profit 2008") will not be less than HK$7,000,000 (the "Guaranteed Profit"). The Bond Certificate will be released to the Vendor after the fulfillment of the Guaranteed Profit.

If the Actual Profit 2008 is less than the Guaranteed Profit but more than HK$5,000,000, (a) the Vendor shall warrant to the Purchaser that the average of the audited consolidated net profit after tax and extraordinary or exceptional items of the Proud Dragon Group for the financial years ending 31 December 2008 and 31 December 2009 (the "Average Actual Profit") shall not be less than the Guaranteed Profit and (b) the Purchaser shall continue to hold the Bond Certificate until the Average Actual Profit meets the Guaranteed Profit.

If the Actual Profit 2008 is less than HK$5,000,000 or the Average Actual Profit is less than the Guaranteed Profit, the Vendor shall set off such shortfall against the payment obligations of the Company under the Convertible Bond on a dollar to dollar basis.

If the Proud Dragon Group records a loss for the year ending 31 December 2008, or where appropriate, for the Average Actual Profit, the compensation amount will be the aggregation of the amount of such loss (expressed in positive figure) and the amount of the Guaranteed Profit. The Vendor shall set off such shortfall against the payment obligations of the Company under the Convertible Bond on a dollar to dollar basis and any shortfall remaining after such set off shall be paid by the Vendor to the Purchaser in cash.

Having considered (i) the continuing development of economy in the PRC which will lead to demand of higher living standard by people including those staying in the rural areas; (ii) the long term national policy of agricultural development and improvement of living standard of farmers staying in the rural areas; and (iii) the exclusive rights granted by the PRC Government to Zhong Tian Water Supply to carry out the provision of water supply service in Dangtu County (當涂縣), Maanshan City (馬鞍山市), the Directors (including the independent non-executive Directors) are of the view that the business of Zhong Tian Water Supply will grow substantially in the years ending 31 December 2008 and 2009 as a result of the increase in demand of water for both the industrial and domestic usage. The Directors are of the view that the mechanism of the Guaranteed Profit (the two thresholds of Actual Profit 2008 and the Average Actual Profit) serves to capitalize the aforesaid substantial growth of Zhong Tian Water Supply in the years ending 31 December 2008 and 2009. Further announcement will be made by the Company in the event that the Vendor is not able to achieve the Guaranteed Profit.

## TERMS OF PROMISSORY NOTE

The terms of the Promissory Note have been negotiated on an arm's length basis and the principal terms of which are summarised below:

**Issuer**

The Company

**Principal amount**

HK$15,600,000

**Interest**

The Promissory Note carries interest at a rate of 1% per annum, payable quarterly.

**Maturity**

A fixed term of three years from the date of issue of the Promissory Note.

**Early repayment**

The Company could, at its option, repay the Promissory Note in whole or in part in multiples of HK$500,000 by giving a prior written notice to the Vendor, commencing on the date of the Promissory Note up to the date immediately prior to the maturity date. There will not be any premium or discount to the payment obligations under the Promissory Note for any early repayment.

**Assignment**

The Promissory Note may be transferred or assigned by the holder of the Promissory Note to any party other than a connected person of the Company in multiples of HK$500,000.

## TERMS OF CONVERTIBLE BOND

The terms of the Convertible Bond have been negotiated on an arm's length basis and the principal terms of which are summarised below:

**Issuer**

The Company

**Principal amount**

HK$10,000,000

**Interest**

The Convertible Bond will carry interest at a rate of 1% per annum, payable quarterly.

**Maturity**

A fixed term of three years from the date of issue of the Convertible Bond. Unless previously redeemed, converted or cancelled as provided in the agreement pursuant to which the Convertible Bond were issued, the Company shall redeem the outstanding principal amount of the Convertible Bond on the maturity date.

**Conversion**

The Bondholder may convert the whole or part (in multiples of HK$500,000) of the principal amount of the Convertible Bond into the Conversion Shares at the Conversion Price for the period commencing after the fulfillment of the Guaranteed Profit and the issue of the Guarantee Certificate up to the maturity date.

**Conversion Price**

The Conversion Price is HK$0.25 per Conversion Share subject to adjustments.

The adjustments for Conversion Price include the following:

(i) an alteration of the nominal amount of each Share by reason of any consolidation or subdivision;

(ii) an issue (other than in lieu of a cash dividend) by the Company of Shares credited as fully paid by way of capitalization of profits or reserves (including any share premium account or capital redemption reserve fund);

(iii) a capital distribution being made by the Company, whether on a reduction of capital or otherwise, to Shareholders (in their capacity as such) or a grant by the Company to Shareholders (in their capacity as such) of rights to acquire for cash assets of the Company or any of its subsidiaries;

(iv) an offer of new Shares for subscription by way of rights, or a grant of options or warrants to subscribe new Shares being made by the Company to Shareholders (in their capacity as such);

(v) an issue wholly for cash being made by the Company of securities convertible into or exchangeable for or carrying rights of subscription for new Shares and the total effective consideration per Share receivable for such securities is less than 70% of the market price on the date of announcement of the terms of the issue of such securities; and

(vi) an issue of Shares wholly for cash at a price per Share which is less than 70% of the market price on the date of announcement of the terms of such issue.

The Company will issue an announcement when there is any adjustment to the Conversion Price and the adjustment will be certified by the Company's auditor or by merchant bank.

The Conversion Price represents

(i) a premium of approximately 6.38% over the closing price of HK$0.235 per Share as quoted on the Stock Exchange on 29 October 2007, being the last trading day of the Shares on the Stock Exchange prior to the publication of the announcement in relation to the Proposed Acquisition;

(ii) a premium of approximately 5.93% over the average of the closing prices of approximately HK$0.236 per Share for the last five trading days up to and including 29 October 2007;

(iii) a premium of approximately 558% over the net asset value per Share of HK$0.038 based on the audited consolidated financial statements of the Group as of 31 December 2006; and

(iv) a premium of approximately 58.23% over the closing price of HK$0.158 per Share as quoted on the Stock Exchange on the Latest Practicable Date.

The Conversion Price was determined by the Purchaser and the Vendor on an arm's length basis with reference to the current market price of the Shares and the duration of the Convertible Bond.

**Conversion Shares**

Assuming there is an immediate exercise in full of the conversion rights attaching to the Convertible Bond in the aggregate principal amount of HK$10,000,000 at the Conversion Price by the Bondholder, the Company will issue an aggregate of 40,000,000 new Shares, representing (i) approximately 3.01% of the existing issued share capital of the Company; and (ii) approximately 2.92% of the issued share capital of the Company as enlarged by the allotment and issue of the Conversion Share. The Conversion Shares will be issued pursuant to the specific mandate to be sought at the EGM.

**Early redemption**

The Company could, at its option, redeem the Convertible Bond in whole or in part in multiples of HK$500,000 by giving a prior written notice to the Bondholder, at any time prior to the maturity date.

**Ranking**

The Conversion Shares, when allotted and issued, will rank pari passu in all respects with all existing Shares in issue at the date of the conversion notice.

**Status of the Convertible Bond**

The Convertible Bond constitutes a direct, general, unconditional and unsecured obligation of the Company and ranks pari passu and rateably without preference (with the exception of obligations in respect of taxes) equally with all other present and/or future unsecured and unsubordinated obligations of the Company.

**Transferability**

The Convertible Bond may be transferred or assigned by the Bondholder to any party other than a connected person of the Company provided that no transfer or assignment of the Convertible Bond can be made by the Bondholder prior to the issue of the Guarantee Certificate.

**Voting rights**

The Convertible Bond does not confer any voting rights at any meetings of the Company.

**Application for listing**

No application will be made by the Company for the listing of the Convertible Bond. Application will be made by the Company to the GEM Listing Committee for the listing of, and permission to deal in, the Conversion Shares.

## CHANGES IN THE SHAREHOLDING STRUCTURE OF THE COMPANY ARISING FROM THE PROPOSED ACQUISITION

| | **As at the Latest Practicable Date before the allotment and issue of the Conversion Shares** | | **Immediately after the allotment and issue of the Conversion Shares** | |
|---|---|---|---|---|
| | *Number of Shares* | % | *Number of Shares* | % |
| Manciple *(Note 1)* | 299,478,238 | 22.51% | 299,478,238 | 21.85% |
| The Vendor | – | – | 40,000,000 | 2.92% |
| Directors: *(Note 2)* | | | | |
| Mr. Yang | 177,125,000 | 13.31% | 177,125,000 | 12.93% |
| Mr. Pang | 10,500,000 | 0.79% | 10,500,000 | 0.77% |
| Mr. Ma | 870,000 | 0.07% | 870,000 | 0.06% |
| Mr. Mo | 21,385,920 | 1.61% | 21,385,920 | 1.56% |
| Ms. Au | 22,500,000 | 1.69% | 22,500,000 | 1.64% |
| *sub-total* | *232,380,920* | *17.47%* | *232,380,920* | *16.96%* |
| **Public Shareholders** | 798,515,922 | 60.02% | 798,515,922 | 58.27% |
| | 1,330,375,080 | 100.00% | 1,370,375,080 | 100.00% |

*Notes:*

1. Manciple, a company incorporated in the British Virgin Islands and is wholly and beneficially owned by Mr. Lau.

2. Mr. Yang, Mr. Pang, Mr. Mo and Ms. Au are executive Directors. Mr. Ma is a non-executive Director.

## INFORMATION ON THE PROUD DRAGON GROUP

Upon completion of the Reorganization, the Proud Dragon Group will principally be engaged in the management of water plants and the provision of water supply service in the rural areas of the agricultural province, Anhui Province (安徽省) in the PRC.

The Reorganisation involves the acquisition by HK Subsidiary of 70% of the equity interest in Zhong Tian Water Supply and transformation of Zhong Tian Water Supply from a domestic company to a Chinese foreign equity joint venture. Zhong Tian Water Supply has obtained the Certificate of Approval for Establishment of Enterprises with foreign investment in the PRC on 29 December 2007. The Reorganisation is expected to be completed by January 2008 and before Completion.

According to the audited consolidated financial statements of Proud Dragon for the period commencing from 30 August 2007, being the date of incorporation, to 30 September 2007, there was no turnover and the net loss after taxation and extraordinary items was approximately HK$22,000. As at 30 September 2007, the net liabilities value of the Proud Dragon Group was approximately HK$22,000.

Zhong Tian Water Supply currently is a private enterprise established in the PRC and is owned by four PRC individuals, who are third parties independent of the Company and its connected persons (as defined in the GEM Listing Rules). It is principally engaged in the management of water plants and the provision of water supply in the rural areas of the PRC. Through the entering into of the exclusive operation agreements with the local government of Dangtu County (當涂縣), Anhui Province (安徽省), it provides water supply service to certain towns and villages in Dangtu County (當涂縣) on a BOT (Build, Operate, Transfer) and exclusive basis. It currently owns and operates three water plants in Dangtu County (當涂縣), Maanshan City (馬鞍山市), a rapidly developing major industrial region in the agricultural province, Anhui Province (安徽省).

The Directors, after consultation with its PRC legal advisers, named Fujian Minjiang Law Firm, confirm that the Drinking Water Hygiene Approval License (生活飲用水衛生許可證) is required to be obtained in an effort to legally engage in the provision of water supply service in the PRC. The Directors also confirm that Zhong Tian Water Supply has obtained the Drinking Water Hygiene Approval License and all the necessary licenses and approvals to operate legally in the PRC and the transformation of Zhong Tian Water Supply into a Chinese foreign equity joint venture upon the completion of the Reorganization will not impose any impact on its eligibility of operation in the PRC.

The three water plants are located in Shi Qiao Town (石橋鎮), Nian Dou Town (年陡鎮) and Hu Yang Village (湖陽鄉) of Dangtu County (當涂縣) and supply water to approximately 280,000 inhabitants. The provision of such water supply services by Zhong Tian Water Supply is supported by the PRC Government and the construction of such three water supply plants were partially subsidised by the PRC Government. Of the three water plants, one is in full operation as at the Latest Practicable Date. It is expected that all the three water supply plants will be in full operation by the first half of the year 2008. The funding for the two water plants under construction will be financed by the existing internal resources and working capital of Zhong Tian Water Supply. It will be settled by Zhong Tian Water Supply upon completion of the Reorganisation. Hence, no outstanding capital commitments will be borne by the Group upon Completion.

Upon completion of the Reorganisation, the registered capital of Zhong Tian Water Supply will be RMB21.43 million, of which the equity interest of Zhong Tian Water Supply will be owned as to 70% by the HK Subsidiary and the balance of 30% by five PRC individuals, who are third parties independent of the Company and its connected persons (as defined in the GEM Listing Rules).

Of the five PRC individuals, four of them are involved in the management and supervision of the operation of Zhong Tian Water Supply. The Directors confirm that such four PRC individuals will be retained in Zhong Tian Water Supply upon the Completion to ensure management continuity.

According to the audited financial statements of Zhong Tian Water Supply for the period from 22 August 2005 to 31 December 2005, there was no turnover and the net loss after taxation and extraordinary items was approximately RMB302,000.

According to the audited financial statements of Zhong Tian Water Supply for the year ended 31 December 2006, the turnover was approximately RMB1,395,000 and the net loss after taxation and extraordinary items was approximately RMB1,838,000.

According to the audited financial statements of Zhong Tian Water Supply for the period commencing from 1 January 2007 to 30 September 2007, the turnover was approximately RMB150,000 and the net loss after taxation and extraordinary items was approximately RMB902,000.

As at 30 September 2007, the principal assets of Zhong Tian Water Supply are the three water plants (two of which are still under construction) of approximately RMB47,000,000 and net assets of Zhong Tian Water Supply was approximately RMB3,958,000.

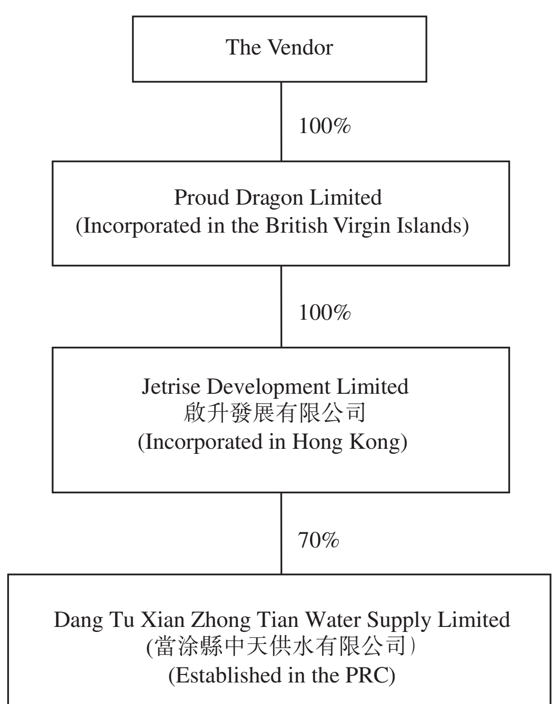
As at 30 September 2007, the net book value of the buildings in Zhong Tian Water Supply were approximately RMB393,000. The Company engaged Greater China Appraisal Limited, an independent valuer, to value the buildings held by Zhong Tain Water Supply and that the valuation of the buildings as at 31 October 2007 shows no commercial value as Zhong Tian Water Supply's buildings were erected on a leasehold land under BOT basis with the local Government of Dangtu County which Zhong Tian Water Supply has the right to use solely for the purpose of carrying water supply services and does not have the right to sub-lease, mortgage or transfer. Owing to the restriction on the usage of the leasehold land, thus, the buildings have no commercial value.

Disclosure of the reconciliation of the property interests of Zhong Tian Water Supply and the valuation of such property interests as required under Rule 8.30 of the GEM Listing Rules is set out below:

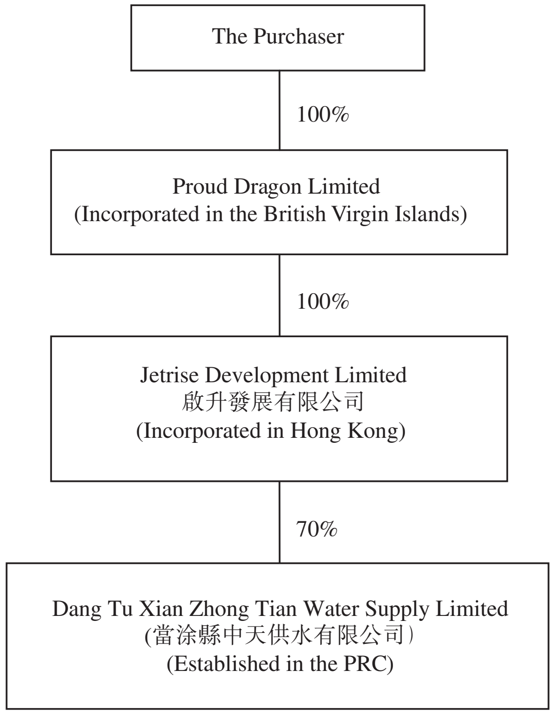
| | *RMB* *('000)* | *RMB* *('000)* |
|---|---|---|
| Valuation of properties as at 31 October 2007 as set out in the Valuation Report included in Appendix VII | | – |
| Net book value of the following properties as at 30 September 2007 as set out in the Accountants' Report of Zhong Tian Water Supply included in Appendix II | | |
| – Buildings | 393 | |
| Less: Depreciation of properties during the period from 1 October 2007 to 31 October 2007 (unaudited) | (3) | |
| Net book value of properties as at 31 October 2007 subject to valuation as set out in the Valuation Report included in Appendix VII | | 390 |
| Value-in-use not recognised in commercial aspect | | 390 |

The following charts show the group structure of the Proud Dragon Group (i) immediately after the completion of the Reorganisation and before the Completion and (ii) immediately after the Completion:

**Immediately after completion of the Reorganisation and before Completion**



**Immediately after Completion**




In an effort to fulfill its fiduciary duties and care to the Company pursuant to Rule 5.01 of the GEM Listing Rules, the Board has conducted, among others, the following key due diligence works in relation to the Proposed Acquisition:

**(i) Legal due diligence**

(a) engagement of a PRC legal adviser to provide preliminary advice in relation to the Proposed Acquisition;

(b) review the legal and statutory documents of Zhong Tian Water Supply; and

(c) discuss with local government of Dangtu County (當涂縣) in relation to the Proposed Acquisition and the exclusive operation agreement.

**(ii) Operation due diligence**

(a) physically visit the three water plants of Zhong Tian Water Supply; and

(b) interview with the customers of Zhong Tian Water Supply.

**(iii) Financial due diligence**

(a) engagement of auditors to prepare an audited financial statement; and

(b) review financial statements of Zhong Tian Water Supply.

The Directors confirmed that they had performed sufficient due diligence on Proud Dragon and Zhong Tian Water Supply and ensure that:

(a) up to 31 December 2007, there has been no material adverse changes in the financial position of Proud Dragon and Zhong Tian Water Supply since 30 September 2007; and

(b) there is no event since 30 September 2007 which would materially affect the financial information of Proud Dragon and Zhong Tian Water Supply.

## REASONS FOR THE PROPOSED ACQUISITION

The Group is engaged in the development and marketing of patented server based technology and the provision of software related services. The Group recorded net loss of approximately HK$6.27 million and approximately HK$0.99 million for the year ended 31 December 2006 and the six months ended 30 June 2007 and had cash of HK$12.66 million as at 30 June 2007 respectively.

Since May 2007, the Company has commenced its business of the development, production and distribution of organic fertilizer in the PRC with a vision to actively participate and develop the Group business in the agricultural industry in the PRC in the long term.

Both the organic fertilizer business and the provision of water supply business are agricultural related and target the same group of customers, i.e. farmers staying in the rural areas. Accordingly, with the substantial growth of provision of water supply business as stated in the sub-section "Profit Guarantee" above, the customer base of the organic fertilizer business will also be enhanced. Hence, the Directors are of the view that the provision of water supply business in the rural areas in the PRC synergize with the Group's organic fertilizer business in the PRC and most importantly, serves as a channel to further develop and consolidate the business development of the Group in the agricultural industry in the PRC. Therefore, the Company has decided to enter into the Agreement in an effort to maximize return to the Group through its development in the agricultural industry in the PRC.

Although the Company has no prior experience in the water supply business in the PRC, the Company will retain the existing management team of Zhong Tian Water Supply, which has over ten years experience in management of water supply business in the PRC, to manage the water supply business of the Group in the PRC.

Based on the above-mentioned reasons, the Directors believe that the Proposed Acquisition would further enhance the future growth and profitability of the Group.

Taking into account the benefits of the Proposed Acquisition, the Board is of the view that the terms of the Proposed Acquisition are fair and reasonable and the Proposed Acquisition is in the interests of the Company and the Shareholders as a whole.

**Management discussion and analysis of the results of Proud Dragon and HK Subsidiary**

*(i) Financial and business performance*

Proud Dragon and HK Subsidiary are incorporated on 30 August 2007 and 4 July 2007 respectively, both companies have not commenced any operation from the date of incorporation to 30 September 2007, so there were no turnover. The principal business of the both companies are investment holdings and the establishment of both companies were for the acquisition of Zhong Tian Water Supply.

*(ii) Capital Structure*

Proud Dragon's capital structure as at 30 September 2007 consisted of approximately HK$8 as registered capital and deficit of approximately HK$7,500.

HK Subsidiary's capital structure as at 30 September 2007 consisted of approximately HK$1 as registered capital and deficit of approximately HK$15,000.

*(iii) Liquidity and financial resources*

As at 30 September 2007, Proud Dragon and HK Subsidiary did not have any cash and bank balances and long-term liabilities.

*(iv) Significant investments*

On 28 September 2007, HK Subsidiary entered into a share transfer agreement to acquire a 70% equity interest in Zhong Tian Water Supply. Save for that, Proud Dragon and HK Subsidiary did not have any significant investment as at 30 September 2007.

*(v) Material acquisitions or disposal of subsidiaries and affiliated companies*

Save for acquiring 70% equity interest in Zhong Tian Water Supply, Proud Dragon and HK Subsidiary did not have any material acquisitions or disposal of subsidiaries and affiliated companies as at 30 September 2007.

*(vi) Segment information*

Since Proud Dragon and HK Subsidiary did not have any turnover, no analysis by either business or geographical segment was noted.

*(vii) Number of employees and remuneration policies*

As at 30 September 2007, each of Proud Dragon and HK Subsidiary had 1 director only and there were no salary and allowances for the nine months ended 30 September 2007.

*(viii) Charges on assets of Proud Dragon and HK Subsidiary*

There was no charge on the assets of both Proud Dragon and HK Subsidiary as at 30 September 2007.

*(ix) Future plans for material investments*

As at the Latest Practicable Date, there are no proposed material investments of Proud Dragon and HK Subsidiary.

*(x) Exposure to exchange rates*

Most of the transactions of Proud Dragon and HK Subsidiary were denominated in United States dollars and Hong Kong dollars. As the exchange of United States dollars to Hong Kong Dollars were fairly stable, hence, no hedging or other arrangements to reduce the currency risk were implemented.

*(xi) Contingent liabilities*

There were no contingent liabilities of Proud Dragon and HK Subsidiary as at 30 September 2007.

*(xii) Gearing*

There were no bank borrowings of Proud Dragon and HK Subsidiary as at 30 September 2007.

**Management discussion and analysis of the results of Zhong Tian Water Supply**

Set out below is a summary of the key financial data of Zhong Tian Water Supply, of which 70% of the shareholding interest will held by the Purchaser upon Completion and are extracted from the accountant's report of Zhong Tian Water Supply as contained in Appendix II to this circular prepared based on the generally accepted accounting principles in Hong Kong.

| | Nine months ended 30 September 2007 (audited) *RMB'000* | Year ended 31 December 2006 (audited) *RMB'000* | Period from 22 August 2005 (date of incorporation) to 31 December 2005 (audited) *RMB'000* |
|---|---|---|---|
| Result | | | |
| Turnover | 150 | 1,395 | – |
| Loss before tax | (902) | (1,838) | (302) |
| Loss after tax | (902) | (1,838) | (302) |
| | **As at 30 September 2007 (audited)** *RMB'000* | **As at 31 December 2006 (audited)** *RMB'000* | **As at 31 December 2005 (audited)** *RMB'000* |
| Assets and liabilities | | | |
| Total assets | 49,793 | 30,917 | 8,908 |
| Net assets value | 3,958 | 4,861 | 4,698 |

*(i) Financial and business performance*

Zhong Tian Water Supply was incorporated on 22 August 2005. There was no turnover for the period ended 31 December 2005 as the operation was not commenced until August 2006. For the year ended 31 December 2006, turnover was approximately RMB1,395,000, of which approximately RMB1,274,000 was derived from water supply related installation income and approximately RMB121,000 was derived from the provision of water supply. For the nine months ended 30 September 2007, turnover was approximately RMB150,000 which solely represented the sub-contracting income derived from the subcontracting agreement entered into by Zhong Tian Water Supply with an independent third party not connected with Zhong Tian Water Supply dated 25 December 2006, pursuant to which such independent third party would manage the water plant on behalf of Zhong Tian Water Supply for a period of one year from 1 January 2007 to 31 December 2007. Such independent third party would be required to bear and be eligible to receive the expenses and income in connection with the management of the water plant for the period. In return, a subcontracting income of RMB200,000 would be received by Zhong Tian Water Supply.

On an annualized basis, the turnover for the nine months ended 30 September 2007 represents a decrease of approximately 85.66% as compared to the same of the financial year ended 31 December 2006, which was mainly due to the fact that the water supply related installation income, which was an one-off payment of the customers upon opening of the water supply accounts, was paid by the customers in 2006. For the year ended 31 December 2006, there was approximately RMB1,274,000 water supply related installation income, while there was no such income for the nine months ended 30 September 2007.

As at 31 December 2005, 31 December 2006 and 30 September 2007, there were total assets of approximately RMB8,908,000, RMB30,917,000 and RMB49,793,000 respectively. The increase in total assets was mainly due to the increase in property, plant and equipment. The property, plant and equipment increased of approximately RMB20,000,000 from 31 December 2005 to 31 December 2006 and increase of approximately RMB19,000,000 from 31 December 2006 to 30 September 2007.

*(ii) Capital Structure*

Zhong Tian Water Supply's capital structure as at 31 December 2005 consisted of approximately RMB5,000,000 as registered capital and deficit of approximately RMB302,000.

Zhong Tian Water Supply's capital structure as at 31 December 2006 consisted of approximately RMB5,000,000 as registered capital and deficit of approximately RMB2,139,000.

Zhong Tian Water Supply's capital structure as at 30 September 2007 consisted of approximately RMB7,000,000 as registered capital and deficit of approximately RMB3,042,000.

*(iii) Liquidity and financial resources*

As at 31 December 2005, there were cash and bank balances of approximately RMB1,102,000 and long-term liabilities of deferred government grants of approximately RMB2,400,000.

As at 31 December 2006, there were cash and bank balances of approximately RMB1,143,000 and long-term liabilities of approximately RMB12,232,000. The increase in long term liabilities was mainly due to the increase in deferred government grants.

As at 30 September 2007, there were cash and bank balances of approximately RMB1,054,000 and long-term liabilities of approximately RMB21,826,000. The increase in long term liabilities was mainly attributable to the increase in deferred government grants.

The deferred government grants are obtained according to the Exclusive Operation Agreement that Government will provide subsidy for Zhong Tian Water Supply to establish water supply plants. Zhong Tian has used such grants to build the water supply plants.

*(iv) Significant investments*

Zhong Tian Water Supply did not have any significant investments as at 31 December 2005, 31 December 2006 and 30 September 2007.

*(v) Material acquisitions or disposal of subsidiaries and affiliated companies*

There were no material acquisitions or disposal of subsidiaries and affiliated companies as at 31 December 2005, 31 December 2006 and 30 September 2007.

*(vi) Exiting business of the Proud Dragon Group*

Upon completion of the Reorganization, the Proud Dragon Group will principally be engaged in the management of water plants and the provision of water supply service in the rural areas of the agricultural province, Anhui Province (安徽省) in the PRC. As a result of the Acquisition, the Directors expect to expand the customer base, operation scale and variety of services provided by Zhong Tian Water Supply to meet the market demand.

*(vii) Segment information*

Zhong Tian Water Supply's turnover and operating assets were attributable to the provision of water supply services in Anhui Province, the PRC. Accordingly, no analysis by either business or geographical segment was noted.

*(viii) Number of employees and remuneration policies*

As at 30 September 2007, the Zhong Tian Water Supply had about 70 employees. Total salary and allowances amounted to about HK$684,000 for the nine months ended 30 September 2007. Zhong Tian Water Supply's remuneration policy includes a pension scheme.

*(ix) Charges on the Zhong Tian Water Supply's assets*

There was no charge on the Zhong Tian Water Supply's assets as at 31 December 2005, 31 December 2006 and 30 September 2007.

*(x) Future plans for material investments*

As at the Latest Practicable Date, there are no proposed material investments of Zhong Tian Water Supply.

*(xi) Exposure to exchange rates*

Most of the transactions of Zhong Tian Water Supply were denominated in Renminbi. The exchange of Renminbi to Hong Kong Dollars were fairly stable, and hence, no hedging or other arrangements to reduce the currency risk were implemented.

*(xii) Contingent liabilities*

There were no contingent liabilities of Zhong Tian Water Supply as at 31 December 2005, 31 December 2006 and 30 September 2007.

*(xiii) Gearing*

There were no bank borrowings as at 31 December 2005, 31 December 2006 and 30 September 2007.

The Company has applied a waiver from strict compliance of Rule 7.05(1) of the GEM Listing Rules in respect of inclusion of the accountants' reports' of Proud Dragon and Zhong Tian Water Supply comprising three financial years up to 31 December 2007.

**FINANCIAL EFFECT OF THE PROPOSED ACQUISITION**

**(1) Assets**

After the Completion, the unaudited pro forma net assets value of the Enlarged Group is about HK$54,189,000. The increase in unaudited net assets value of the Enlarged Group is mainly attributable to the goodwill and net assets of Zhong Tian Water Supply arising from acquisition of the Proud Dragon Group.

Upon Completion, a Convertible Bond in the principal amount of HK$10,000,000 will be issued, entitling the Bondholders the conversion right of 40,000,000 Convertible Shares at the Conversion Price. As a result of the conversion of the Convertible Bond, the issued share capital will be enlarged and net asset value of the Company will be increased.

**(2) Earnings**

The Group recorded an audited consolidated loss attributable to Shareholders of approximately HK$6.27 million for the year ended 31 December 2006. Zhong Tian Water Supply recorded an audited loss after tax of approximately RMB902,000 for the nine months ended 30 September 2007. The Proposed Acquisition is expected to enhance the revenue and earning base of the Group and the Enlarged Group looks forward to the business opportunities to be arised from the water supply service industry in the PRC.

**(3) Liabilities**

The liabilities of the Enlarged Group upon Completion will be increased by approximately HK$72,901,000, which mainly represents the Convertible Bond and the Promissory Note due to the Vendor and the liabilities of Zhong Tian Water Supply.

**FINANCIAL AND TRADING PROSPECTS OF THE ENLARGED GROUP**

The Group is engaged in the development and marketing of patented server based technology and the provision of software related services. The Group recorded net loss of approximately HK$6.27 million and approximately HK$0.99 million for the year ended 31 December 2006 and the six months ended 30 June 2007 and had cash of HK$12.66 million as at 30 June 2007 respectively.

Since May 2007, the Company has commenced its business of the development, production and distribution of organic fertilizer in the PRC with a vision to actively participate and develop the Group business in the agricultural industry in the PRC in the long term.

Through the Proposed Acquisition, the Group will also be engaging in the provision of water supply service to the agricultural population in the rural areas of the PRC, another agricultural business.

**Organic fertilizer**

In May 2007, Rise Assets acquired from Mr. Yang the entire issued share capital of Silky Sky for a total consideration of HK$61,000,000, payable by way of cash, promissory note and the issue and allotment of 135,750,000 Shares. The effect of such acquisition is reflected in the consolidated financial statements of the Group for the six months ended 30 June 2007.

Sky Rich Investments Limited, a wholly-owned subsidiary of Silky Sky, was owned as to 51% of interests in Jinan Shiji Jiangshan Resource Recycling Technology Limited ("Shiji Jiangshan") (formerly known as Beijing Shiji Jianshan Resource Recycling Technology Limited). Shiji Jiangshan, an equity joint venture company established in the PRC, is principally engaged in the production and distribution of organic fertilizer through a technology which converts organic wastes into organic fertilizer.

The Directors are of the opinion that the fertilizer production industry is in a growing trend with immense potential. According to the China Statistical Year Book 2006, to meet the increasing market demand, the fertilizer production in the PRC increase from approximately 33 million metric tones in 1999 to approximately to 52 million metric tones in 2005. The Directors consider that the organic fertilizer production business is a fast growing industry in the PRC in view of the ongoing development of the agricultural industry in the PRC and the increasing emphasis of environmental protection by the PRC Government. The Directors consider that the entering into the organic fertilizer business represents a good opportunity for the Group to enter into the agricultural industry in the PRC.

The Directors confirm that there is no variation to the remuneration or benefits in kind payable to the director of Silky Sky as a result of the acquisition of Silky Sky.

Details of which were disclosed in the announcements of the Company dated 9 February 2007, 21 March 2007 and 22 May 2007, and the circular of the Company dated 20 April 2007.

**Water supply service**

On 29 October 2007, the Purchaser entered into the Agreement with Proud Dragon and the Vendor for the acquisition and subscription of the entire interest in Proud Dragon at a consideration of HK$47,600,000 payable by way of cash, convertible bonds and promissory note. The Proposed Acquisition is subject to Shareholder's approval.

Upon Completion, the Group will have 70% indirect interest in Zhong Tian Water Supply.

Zhong Tian Water Supply is a private enterprise established in the PRC and is principally engaged in the management of water plants and the provision of water supply in the rural areas of the PRC. It currently owns and operates three water plants in Dangtu County (當涂縣), Maanshan City (馬鞍山市), a rapidly developing major industrial region in the agricultural province, Anhui Province (安徽省). It has the exclusive right to provide water supply service to eight villages with around 280,000 inhabits.

The Directors confirm that there is no variation to the remuneration or benefits in kind payable to the director of Proud Dragon as a result of the Proposed Acquisition.

Having considered (i) the continuing development of economy in the PRC which will lead to demand of higher living standard by people including those staying in the rural areas ; (ii) the long term national policy of agricultural development and improvement of living standard of farmers staying in the rural areas; and (iii) the exclusive rights granted by the PRC Government to Zhong Tian Water Supply to carry out the provision of water supply service in Dangtu County (當涂縣), Maanshan City (馬鞍山市), the Directors are of the view that the business of Zhong Tian Water Supply will grow substantially and hence, generate profitability to the Company and the Shareholders as a whole.

In view of the substantial growth of provision of water supply business, the customer base of the organic fertilizer business will also be enhanced. The Directors are of the view that the provision of water supply business in the rural areas in the PRC synergize with the Group's organic fertilizer business in the PRC and most importantly, serves as a channel to further develop and consolidate the business development of the Group in the agricultural industry in the PRC.

Both the organic fertilizer business and the provision of water supply business are agricultural related and target the same group of customers, i.e. agricultural population staying in the rural areas.

In view of the development of the organic fertilizer business and the water supply business in the PRC and the synergy effect generated from these agricultural projects, the Directors are of the view that the Group is well positioned to become a market leader in the agricultural industry in the PRC and hence, generate profitability to the Group.

**GEM LISTING RULES IMPLICATION**

The Proposed Acquisition constitutes a major transaction on the part of the Company under the GEM Listing Rules and is subject to the approval of the Shareholders at the EGM. To the best belief, information and knowledge of the Directors, after having made reasonable enquiries, no Shareholders have material interest in the Proposed Acquisition and are required to abstain from voting at the EGM.

## PROCEDURE FOR DEMANDING A POLL AT GENERAL MEETING

In accordance with the Articles of Association of the Company, a resolution put to the vote of the meeting shall be decided on a show of hands unless a poll is (before or on the declaration of the result of the show of hands or on the withdrawal of any other demand for a poll) demanded:

(a) by the Chairman of the meeting; or

(b) by at least 2 Shareholders present in person (or, in the case of a Shareholder being a corporation, by its duly authorized representative) or by proxy for the time being entitled to vote at the meeting; or

(c) by any Shareholder or Shareholders present in person (or, in the case of a Shareholder being a corporation, by its duly authorized representative) or by proxy and representing not less than one-tenth of the total voting rights of all the Shareholders having the right to vote at the meeting; or

(d) by any Shareholder or Shareholders present in person (or, in the case of a Shareholder being a corporation, by its duly authorized representative) or by proxy and holding Shares in the Company conferring a right to vote at the meeting being Shares on which an aggregate sum has been paid up equal to not less than one-tenth of the total sum paid up on all the Shares conferring that right.

## RECOMMENDATION

The Board considers that the terms of the Proposed Acquisition are fair and reasonable and are in the interests of the Company and the Shareholders as a whole. Accordingly, the Board recommends the Shareholders to vote in favour of the resolution as set out in the notice of the EGM.

## ADDITIONAL INFORMATION

Your attention is drawn to the additional information set out in the appendices to this circular.

By order of the Board
**KANHAN TECHNOLOGIES GROUP LIMITED**
**Pang Hong Tao**
*Chairman*

*The following is the text of a report, prepared for the sole purpose of inclusion in this circular, received from the reporting accountants, Vision A. S. Limited.*

***Vision A. S. Limited* Certified Public Accountants**
泓信會計師行有限公司

18 January 2008

The Board of Directors
KanHan Technologies Group Limited
15/F., Sun House
181 Des Voeux Road Central
Hong Kong

Dear Sirs,

We set out below our report on the financial information (the "Financial Information") regarding Proud Dragon Limited ("Proud Dragon") and its subsidiary, Jetrise Development Limited ("Jetrise") (hereafter collectively referred to as the "Proud Dragon Group") for the period from 20 August 2007 (date of incorporation of Proud Dragon) to 30 September 2007 (the "Period") for inclusion in the circular of KanHan Technologies Group Limited (the "Company") dated 18 January 2008 (the "Circular") in connection with the proposed acquisition of the entire issued share capital of Proud Dragon by Rise Assets Limited ("Rise Assets"), a wholly-owned subsidiary of the Company (the "Acquisition").

Proud Dragon was incorporated in the British Virgin Islands on 20 August 2007 with limited liability under the BVI Business Companies Act, 2004 of the British Virgin Islands and acts as an investment holding company. The registered office of Proud Dragon is located at P.O. Box 957, Offshore Incorporations Centre, Road Town, Tortola, British Virgin Islands. Jetrise was incorporated in Hong Kong on 4 July 2007 with limited liability and with an authorized share capital of HK$10,000 divided into 10,000 shares of HK$1 each. Proud Dragon has become the holding company of Jetrise since Proud Dragon acquired one share, representing the entire issued share capital, of Jetrise on 24 September 2007. Jetrise remained dormant up to the date of this report.

All companies of Proud Dragon Group have adopted 31 December as their financial year end date.

Up to the date of this report, no audited financial statements have been prepared for the companies comprising the Proud Dragon Group as they were either incorporated shortly before 30 September 2007 or are not subject to statutory audit requirements under the relevant rules and regulations in their jurisdictions of incorporation.

For the purpose of this report, the sole director of Proud Dragon has prepared the consolidated financial statements of the Proud Dragon Group for the Period (the "Underlying Financial Statements") in accordance with Hong Kong Financial Reporting Standards ("HKFRSs"), which also include all Hong Kong Accounting Standards ("HKASs") and Interpretations issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA"). For the purpose of this report, we have performed independent audit procedures on the Underlying Financial Statements in accordance with Hong Kong Standards on Auditing issued by the HKICPA.

The Financial Information set out in Sections A to B below has been prepared by the sole director of Proud Dragon based on the Underlying Financial Statements. We have examined the Financial Information and have carried out such additional procedures as are necessary in accordance with the Auditing Guideline 3.340 "Prospectuses and the Reporting Accountant" as recommended by the HKICPA.

The preparation of the Underlying Financial Statements and the Financial Information which give a true and fair view is the responsibility of the sole director of Proud Dragon. In preparing the Underlying Financial Statements and the Financial Information, it is fundamental that appropriate accounting policies are selected and applied consistently. The directors of the Company are responsible for the contents of the Circular in which this report is included. It is our responsibility to form an independent opinion, based on our examination, on the Financial Information and to report our opinion to you.

In our opinion, the Financial Information gives, for the purpose of this report, a true and fair view of the state of affairs of the Proud Dragon Group and Proud Dragon as at 30 September 2007 and of the consolidated results and cash flows of Proud Dragon Group for the Period.

## A. FINANCIAL INFORMATION

### CONSOLIDATED INCOME STATEMENT

*Period from 20 August 2007 (date of incorporation) to 30 September 2007*

| | *Notes* | *HK$* |
|---|---|---|
| TURNOVER | | – |
| Administrative expenses | | (22,500) |
| LOSS BEFORE TAX | | (22,500) |
| Tax | *6* | – |
| LOSS FOR THE PERIOD | | (22,500) |

**CONSOLIDATED BALANCE SHEET**
*30 September 2007*

| | *Notes* | *HK$* |
|---|---|---|
| CURRENT ASSETS | | |
| Cash and bank balances | | 8 |
| Total current assets | | 8 |
| CURRENT LIABILITIES | | |
| Accruals | *8* | 22,500 |
| Total current liabilities | | 22,500 |
| Net liabilities | | (22,492) |
| EQUITY | | |
| Issued capital | *10* | 8 |
| Accumulated loss | | (22,500) |
| Total equity | | (22,492) |

**BALANCE SHEET**
*30 September 2007*

| | *Notes* | *HK$* |
|---|---|---|
| NON-CURRENT ASSETS | | |
| Investment in a subsidiary | *7* | 1 |
| Total non-current assets | | 1 |
| CURRENT ASSETS | | |
| Cash and bank balances | | 8 |
| Total current assets | | 8 |
| CURRENT LIABILITIES | | |
| Accruals | *8* | 7,500 |
| Due to a subsidiary | *9* | 1 |
| Total current liabilities | | 7,501 |
| NET CURRENT LIABILITIES | | (7,493) |
| Net liabilities | | (7,492) |
| EQUITY | | |
| Issued capital | *10* | 8 |
| Accumulated loss | | (7,500) |
| Total equity | | (7,492) |

**CONSOLIDATED STATEMENT OF CHANGES IN EQUITY**

*Period from 20 August 2007 (date of incorporation) to 30 September 2007*

| | Issued capital | Accumulated loss | Total |
|---|---|---|---|
| | *HK$* | *HK$* | *HK$* |
| Issued of shares – *note 10* | 8 | – | 8 |
| Net loss for the period | – | (22,500) | (22,500) |
| At 30 September 2007 | 8 | (22,500) | (22,492) |

**CONSOLIDATED CASH FLOW STATEMENT**

*Period from 20 August 2007 (date of incorporation) to 30 September 2007*

| | HK$ |
|---|---|
| OPERATING ACTIVITIES | |
| Loss before tax | (22,500) |
| Operating cash flows before working capital changes | (22,500) |
| Increase in accruals | 22,500 |
| NET CASH FROM OPERATING ACTIVITIES | – |
| FINANCING ACTIVITIES | |
| Proceeds from issue of shares | 8 |
| NET CASH FROM FINANCING ACTIVITIES | 8 |
| NET INCREASE IN CASH AND CASH EQUIVALENTS | 8 |
| Cash and cash equivalents at the beginning of period | – |
| CASH AND CASH EQUIVALENTS AT END OF PERIOD | 8 |
| ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS | |
| Cash and bank balances | 8 |

## B. NOTES TO THE FINANCIAL INFORMATION

### 1. GENERAL INFORMATION

Proud Dragon is a limited liability company incorporated in the British Virgin Islands. The registered office of Proud Dragon is located at P.O. Box 957, Offshore Incorporations Centre, Road Town, Tortola, British Virgin Islands.

Proud Dragon acts as an investment holding company during the Period. Its subsidiary remained dormant during the Period.

### 2. ADOPTION OF NEW OR REVISED STANDARDS

The Financial Information has been prepared in accordance with HKFRSs issued by the HKICPA, accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. The Financial Information has been prepared under the historical cost convention.

New HKFRSs issued but not yet effective are not early adopted. The sole director of Proud Dragon anticipates that the application of these new HKFRSs will have no material impact on the Financial Information.

### 3. PRINCIPAL ACCOUNTING POLICIES

#### (a) Basis of preparation

The Financial Information have been prepared in accordance with accounting principles generally accepted in Hong Kong including all applicable HKFRSs and HKASs issued by the HKICPA. They have been prepared on the historical cost convention. The measurement bases are fully described in the accounting policies below.

The Financial Information have been prepared on a going concern basis notwithstanding that Proud Dragon and the Proud Dragon Group have net liabilities as at 30 September 2007 as the sole shareholder has undertaken to provide continuous financial support to Proud Dragon, and to maintain it as a going concern.

#### (b) Basis of consolidation

The consolidated financial statements incorporate the financial statements of Proud Dragon and its subsidiary for the Period. The result of the subsidiary is consolidated from the date of acquisition, being the date on which Proud Dragon Group obtains control, and continues to be consolidated until the date that such control ceases.

The acquisition of subsidiary during the Period has been accounted for using purchase method of accounting. This method involves allocating the cost of the business combinations to the fair value of the assets acquired, and liabilities and contingent liabilities assumed at the date of acquisition. The cost of the acquisition is measured at the aggregate of the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition.

#### (c) Subsidiary

A subsidiary is an entity in which Proud Dragon controls, directly or indirectly, its financial and operating policies so as to obtain benefits from its activities.

The result of subsidiary is included in Proud Dragon's income statement to the extent of dividends received and receivable. Proud Dragon's investment in a subsidiary is stated at cost less any impairment losses.

**(d) Impairment of assets**

Where an indication of impairment exists, or when annual impairment testing for an asset is required (other than inventories, construction contract assets, financial assets, investment properties, goodwill and non-current assets/disposal group classified as held for sale), the asset's recoverable amount is estimated. An asset's recoverable amount is calculated as 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 group of assets, in which case, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

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

An assessment is made at each balance sheet date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If any such indication exists, the asset's recoverable amount is estimated. A previously recognised impairment loss of an asset other than goodwill is reversed only if there has been a change in the estimates used to determine the recoverable amount of that asset, however not to an amount higher than the carrying amount that would have been determined (net of any depreciation), had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is credited to the income statement in the period in which it arises, unless the asset is carried at a revalued amount, in which case the reversal of the impairment loss is accounted for in accordance with the relevant accounting policy for that revalued asset.

**(e) Related parties**

A party is considered to be related to Proud Dragon if:

a) directly, or indirectly through one or more intermediaries, the party (i) controls, is controlled by, or is under common control with Proud Dragon; (ii) has an interest in Proud Dragon that gives it significant influence over Proud Dragon; or (iii) has joint control over Proud Dragon;

b) the party is an associate;

c) the party is a jointly-controlled entity;

d) the party is a member of the key management personnel of Proud Dragon;

e) the party is a close member of the family of any individual referred to in (a) or (d);

f) the party is an entity that is controlled, jointly controlled or significantly influenced by or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (d) or (e); or

g) the party is a post employment benefit plan for the benefit of employees of Proud Dragon, or of any entity that is related party of Proud Dragon.

**(f) Cash and cash equivalents**

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

**(g) Income tax**

Income tax comprises current and deferred tax. Income tax is recognised in the income statement or in equity if it relates to items that are recognised in the same or a different period, 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.

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

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

- where the deferred tax liability 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 taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

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

- where the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability 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, associates and interests in joint ventures, 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 each balance sheet date 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. Conversely, previously unrecognised deferred tax assets are reassessed at each balance sheet date and are recognised to the extent that it is probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised.

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 at the balance sheet date.

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.

**(h) Foreign currencies**

These financial statements are presented in Hong Kong dollars, which is Proud Dragon's functional and presentation currency. Foreign currency transactions are initially recorded using the functional currency rates ruling at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rates of exchange ruling at the balance sheet date. All differences are taken to 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 date 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.

## 4. SIGNIFICANT ACCOUNTING JUDGEMENTS

**Judgements**

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

**Impairment of assets**

In determining whether an asset is impaired or whether the event previously causing the impairment no longer exists, Proud Dragon has to exercise judgement in the area of asset impairment, particularly in assessing: (1) whether an event has occurred that may affect the asset value, or such an 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 derecognition; 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 have a material effect on the net present value used in the impairment test.

## 5. DIRECTORS' REMUNERATION

The sole director of Proud Dragon did not receive or will not receive any fees or emoluments in respect of his services to Proud Dragon during the Period.

## 6. TAX

No provision for Hong Kong profits tax has been made as Proud Dragon did not generate any assessable profits arising in Hong Kong during the Period.

There are no material unprovided deferred tax assets and liabilities at the balance sheet date.

A reconciliation of the tax expense applicable to loss before tax using the statutory rate to the tax expense at the effective tax rate is as follows:

| | *HK$* |
|---|---|
| Loss before tax | (22,500) |
| Tax at the statutory tax rate | 3,937 |
| Expenses not deductible for tax | (3,937) |
| Tax charge at effective rate | – |

## 7. INVESTMENT IN A SUBSIDIARY

| | HK$ |
|---|---|
| Unlisted shares, at cost | 1 |

Particulars of the subsidiary are as follows:

| Name | Place of incorporation | Nominal value of issued ordinary share capital | Percentage of equity attributable to Proud Dragon | Principal activity |
|---|---|---|---|---|
| Jetrise Development Limited | Hong Kong | HK$1 | 100% | Dormant |

## 8. ACCRUALS

| | The Group HK$ | The Company HK$ |
|---|---|---|
| Accruals | 22,500 | 7,500 |

## 9. DUE TO A SUBSIDIARY

The amount due to a subsidiary is unsecured, interest-free and has no fixed terms of repayment.

## 10. SHARE CAPITAL

| | HK$ |
|---|---|
| *Authorised:* | |
| 50,000 ordinary shares of US$1 each | 390,000 |
| *Issued and fully paid:* | |
| 1 ordinary share of US$1 each | 8 |

Upon incorporation, the authorised share capital of Proud Dragon was US$50,000 divided into 50,000 shares of US$1 each. One subscriber share was issued for cash at par for the initial capital of Proud Dragon.

## 11. CAPITAL COMMITMENTS

On 28 September 2007, Jetrise, the subsidiary of Proud Dragon, entered into a capital contribution agreement (the "Capital Contribution Agreement") to acquire 70% equity interest in 當涂縣中天供水有限公司 (Dang Tu Xian Zhong Tian Water Supply Limited*) ("Zhong Tian Water Supply"), a company registered in the People's Republic of China ("PRC") on 22 August 2005. The capital contributions payable to Zhong Tian Water Supply is RMB15,000,000.

* *Englich translation of company name is for identification purpose only.*

**12. CONTINGENT LIABILITIES**

At 30 September 2007, Proud Dragon and the Proud Dragon Group have no significant contingent liabilities.

**13. FINANCIAL RISKS AND MANAGEMENT**

Proud Dragon's overall risk management programme seeks to minimise potential adverse effects on the financial performance of Proud Dragon.

**(i) Foreign currency risk**

Proud Dragon does not have any significant financial instrument or transaction denominated in foreign currency.

**(ii) Liquidity risk**

Proud Dragon aims to manage its operating cash flows and the availability of funding so as to ensure that all repayment and funding needs. As part of its overall liquidity management, Proud Dragon maintains sufficient levels of cash to meet its working capital requirements.

**(iii) Fair values**

The carrying amounts of the financial assets and liabilities in the Financial Information approximately their fair values.

## C. SUBSEQUENT EVENT

On 29 October 2007, 317 new shares of US$1 each were issued for cash at par for additional working capital of Proud Dragon.

There is no other material subsequent event subsequent to 30 September 2007.

## D. SUBSEQUENT FINANCIAL STATEMENTS

No audited financial statements have been prepared for the Proud Dragon Group in respect of any period subsequent to 30 September 2007.

Yours faithfully,
**Vision A. S. Limited**
*Certified Public Accountants*
Hong Kong

**Cheung Man Yau, Timothy**
Practising Certificate No.: P01417

*The following is the text of a report, prepared for the sole purpose of inclusion in this circular, received from the reporting accountants, Vision A. S. Limited.*

***Vision A. S. Limited*** **Certified Public Accountants**
**泓信會計師行有限公司**

18 January 2008

The Board of Directors
KanHan Technologies Group Limited
15/F., Sun House
181 Des Voeux Road Central
Hong Kong

Dear Sirs,

We set out below our report on the financial information (the "Financial Information") regarding 當涂縣中天供水有限公司 (Dang Tu Xian Zhong Tian Water Supply Limited*) ("Zhong Tian Water Supply") for the period from 22 August 2005 (date of incorporation of Zhong Tian Water Supply) to 31 December 2005, year ended 31 December 2006 and the nine months ended 30 September 2007 (the "Relevant Periods") for inclusion in the circular of KanHan Technologies Group Limited (the "Company") dated 18 January 2008 (the "Circular") in connection with the proposed acquisition of the entire issued share capital of Proud Dragon Limited ("Proud Dragon") by Rise Assets Limited ("Rise Assets"), a wholly-owned subsidiary of the Company (the "Acquisition").

Proud Dragon is the immediate holding company of Jetrise Development Limited ("Jetrise") since Proud Dragon acquired 1 share, representing the entire issued capital of Jetrise on 24 September 2007. Jetrise will become the immediate holding company of Zhong Tian Water Supply upon completion of the Reorganization in relation to the acquisition of 70% equity interest of Zhong Tian Water Supply, which is described more fully in the section headed "Letter from the Board" in this circular.

Zhong Tian Water Supply was incorporated in the People's Republic of China ("PRC") on 22 August 2005 with limited liability. The principal activities of Zhong Tian Water Supply are management of water plants and the provision of water supply in the rural areas of the PRC. The registered office and principal place of business of Zhong Tian Water Supply are located at 中國安徽省馬鞍山市當涂縣石橋鎮 and 中國安徽省馬鞍山市當涂縣, respectively.

The statutory financial statements of Zhong Tian Water Supply for the year ended 31 December 2006 was prepared in accordance with the applicable accounting principles and financial regulations in the People's Republic of China (the "PRC GAAP") and was audited by 安徽新中天會計師事務所, certified public accountants registered in the PRC. No audit has been performed on the financial statements of Zhong Tian Water Supply prepared under PRC GAAP for the period from 22 August 2005 (date of incorporation) to 31 December 2005. No audited financial statements have been prepared for Zhong Tian Water Supply for the nine months ended 30 September 2007.

* *English translation of company name is for identification purpose only*

For the purpose of this report, the directors of Zhong Tian Water Supply have prepared financial statements of Zhong Tian Water Supply for the Relevant Periods (the "Underlying Financial Statements") in accordance with Hong Kong Financial Reporting Standards ("HKFRSs"), which also include all Hong Kong Accounting Standards ("HKASs") and Interpretations issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA"). For the purpose of this report, we have performed independent audit procedures on the Underlying Financial Statements in accordance with Hong Kong Standards on Auditing issued by the HKICPA.

The Financial Information set out in Sections A to B below has been prepared by the directors of Zhong Tian Water Supply based on the Underlying Financial Statements. We have examined the Financial Information and have carried out such additional procedures as are necessary in accordance with the Auditing Guideline 3.340 "Prospectuses and the Reporting Accountant" as recommended by the HKICPA.

The preparation of the Underlying Financial Statements and the Financial Information which give a true and fair view is the responsibility of the directors of Zhong Tian Water Supply. In preparing the Underlying Financial Statements and the Financial Information, it is fundamental that appropriate accounting policies are selected and applied consistently. The directors of the Company are responsible for the contents of the Circular in which this report is included. It is our responsibility to form an independent opinion, based on our examination, on the Financial Information and to report our opinion to you.

In our opinion, the Financial Information gives, for the purpose of this report, a true and fair view of the state of affairs of Zhong Tian Water Supply as at 31 December 2005, 31 December 2006 and 30 September 2007 and of the results and cash flows of Zhong Tian Water Supply for each of the Relevant Periods.

The comparative income statement, statement of changes in equity and cash flow statement of Zhong Tian Water Supply for the nine months ended 30 September 2006 together with notes thereon (the "2006 Comparative Financial Information") have been extracted from Zhong Tian Water Supply's financial information for the same period which was prepared by the directors of Zhong Tian Water Supply solely for the purpose of this report. We have reviewed the financial information for the nine months ended 30 September 2006, in accordance with Statements of Auditing Standards 700 "Engagements to Review Interim Financial Reports" issued by the HKICPA. A review consists principally of making enquiries of the management and applying analytical procedures to the financial information and based thereon, assessing whether the accounting policies and presentation have been consistently applied unless otherwise disclosed. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit and therefore provides a lower level of assurance than an audit. Accordingly, we do not express an audit opinion on the 2006 Comparative Financial Information. On the basis of our review, which does not constitute an audit, we are not aware of any material modifications that should be made to the 2006 Comparative Financial Information.

## A. FINANCIAL INFORMATION

### Income statements

| | Notes | Period from 22 August 2005 (date of incorporation) to 31 December 2005 RMB (audited) | Year ended 31 December 2006 RMB (audited) | Nine months ended 30 September 2007 RMB (audited) | Nine months ended 30 September 2006 RMB (unaudited) |
|---|---|---|---|---|---|
| TURNOVER | 5 | – | 1,394,828 | 150,000 | 1,153,875 |
| Cost of services rendered | | – | (309,748) | (7,500) | (278,522) |
| Gross profit | | – | 1,085,080 | 142,500 | 875,353 |
| Other revenue | 5 | 557 | 70,364 | 1,306,565 | 47,861 |
| Administrative expenses | | (295,926) | (2,882,492) | (2,271,931) | (2,528,484) |
| Finance costs | 6 | (6,479) | (110,484) | (79,590) | (106,217) |
| LOSS BEFORE TAX | 7 | (301,848) | (1,837,532) | (902,456) | (1,711,487) |
| Tax | 9 | – | – | – | – |
| LOSS FOR THE YEAR/PERIOD | | (301,848) | (1,837,532) | (902,456) | (1,711,487) |

**Balance sheets**

| | Notes | As at 31 December 2005 RMB (audited) | As at 31 December 2006 RMB (audited) | As at 30 September 2007 RMB (audited) |
|---|---|---|---|---|
| NON-CURRENT ASSETS | | | | |
| Property, plant and equipment | *10* | 6,799,471 | 27,396,571 | 46,908,859 |
| Prepaid land lease payments | *11* | 101,436 | 679,284 | 661,185 |
| Total non-current assets | | 6,900,907 | 28,075,855 | 47,570,044 |
| CURRENT ASSETS | | | | |
| Prepaid land lease payments | *11* | 3,540 | 24,132 | 24,132 |
| Accounts receivable | *12* | – | – | 150,000 |
| Prepayments, deposits and other receivables | *13* | 851,747 | 1,674,906 | 994,266 |
| Due from a director | *14* | 42,900 | – | – |
| Due from shareholders | *15* | 6,427 | – | – |
| Cash and bank balances | | 1,102,043 | 1,142,514 | 1,054,445 |
| Total current assets | | 2,006,657 | 2,841,552 | 2,222,843 |
| CURRENT LIABILITIES | | | | |
| Accounts payable | *16* | 490,186 | 7,915,660 | 16,474,132 |
| Deposits received, accruals and other payables | *17* | 1,319,226 | 3,769,182 | 4,891,595 |
| Due to a director | *18* | – | 900,000 | 1,098,373 |
| Due to shareholders | *18* | – | 700,000 | 1,004,235 |
| Government loan | *18* | – | 540,000 | 540,000 |
| Total current liabilities | | 1,809,412 | 13,824,842 | 24,008,335 |
| NET CURRENT ASSETS/(LIABILITIES) | | 197,245 | (10,983,290) | (21,785,492) |
| TOTAL ASSETS LESS CURRENT LIABILITIES | | 7,098,152 | 17,092,565 | 25,784,552 |
| NON-CURRENT LIABILITIES | | | | |
| Deferred government grants | *19* | 2,400,000 | 12,231,945 | 21,826,388 |
| Net assets | | 4,698,152 | 4,860,620 | 3,958,164 |
| EQUITY | | | | |
| Share capital | *20* | 5,000,000 | 7,000,000 | 7,000,000 |
| Accumulated losses | | (301,848) | (2,139,380) | (3,041,836) |
| Total equity | | 4,698,152 | 4,860,620 | 3,958,164 |

**Statements of changes in equity**

| | Notes | Share capital RMB | Accumulated losses RMB | Total RMB |
|---|---|---|---|---|
| Increase in paid-up capital | *20* | 5,000,000 | – | 5,000,000 |
| Loss for the period | | – | (301,848) | (301,848) |
| At 31 December 2005 and 1 January 2006 | | 5,000,000 | (301,848) | 4,698,152 |
| Increase in paid-up capital | *20* | 2,000,000 | – | 2,000,000 |
| Loss for the year | | – | (1,837,532) | (1,837,532) |
| At 31 December 2006 and 1 January 2007 | | 7,000,000 | (2,139,380) | 4,860,620 |
| Loss for the period | | – | (902,456) | (902,456) |
| At 30 September 2007 | | 7,000,000 | (3,041,836) | 3,958,164 |

**Cash flow statements**

| | Period from 22 August 2005 (date of incorporation) to 31 December 2005 | Year ended 31 December 2006 | Nine months ended 30 September 2007 | 2006 |
|---|---|---|---|---|
| | *RMB* | *RMB* | *RMB* | *RMB* |
| | (audited) | (audited) | (audited) | (unaudited) |
| OPERATING ACTIVITIES | | | | |
| Loss from operating activities before tax | (301,848) | (1,837,532) | (902,456) | (1,711,487) |
| Adjustments for: | | | | |
| Depreciation | 720 | 616,725 | 559,394 | 372,703 |
| Amortisation of prepaid land lease payments | 1,024 | 19,370 | 18,099 | 13,736 |
| Release of government grants | – | (68,055) | (105,557) | (46,667) |
| Interest income | (557) | (2,309) | (1,008) | (1,194) |
| Finance costs | 6,479 | 110,484 | 79,590 | 106,217 |
| Operating loss before working capital changes | (294,182) | (1,161,317) | (351,938) | (1,266,692) |
| Increase in accounts receivable | – | – | (150,000) | – |
| Decrease/(increase) in prepayments, deposits and other receivables | (851,747) | (823,159) | 680,640 | (469,635) |
| Decrease/(increase) in amount due from a director | (42,900) | 42,900 | – | 42,900 |
| Decrease/(increase) in amount due from shareholders | (6,427) | 6,427 | – | 6,427 |
| Increase in accounts payable | 490,186 | 7,425,474 | 8,558,472 | (81,315) |
| Increase in deposits received and accruals and other payables | 1,319,226 | 2,449,956 | 1,122,413 | 2,285,004 |
| Increase in amount due to a director | – | 900,000 | 198,373 | – |
| Increase in amount due to shareholders | – | 700,000 | 304,235 | – |
| NET CASH FROM OPERATING ACTIVITIES | 614,156 | 9,540,281 | 10,362,195 | 516,689 |
| INVESTING ACTIVITIES | | | | |
| Interest received | 557 | 2,309 | 1,008 | 1,194 |
| Purchases of property, plant and equipment | (6,800,191) | (21,213,825) | (20,071,682) | (3,672,293) |
| Prepaid land lease payments | (106,000) | (617,810) | – | (570,000) |
| NET CASH USED IN INVESTING ACTIVITIES | (6,905,634) | (21,829,326) | (20,070,674) | (4,241,099) |
| FINANCING ACTIVITIES | | | | |
| Interest paid | (6,479) | (110,484) | (79,590) | (106,217) |
| Capital contributions received | 5,000,000 | 2,000,000 | – | – |
| Government grants received | 2,400,000 | 9,900,000 | 9,700,000 | 3,400,000 |
| Government loan raised | – | 540,000 | – | 540,000 |
| NET CASH FROM FINANCING ACTIVITIES | 7,393,521 | 12,329,516 | 9,620,410 | 3,833,783 |
| NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS | 1,102,043 | 40,471 | (88,069) | 109,373 |
| Cash and cash equivalents at beginning of year/period | – | 1,102,043 | 1,142,514 | 1,102,043 |
| CASH AND CASH EQUIVALENTS AT END OF YEAR/PERIOD | 1,102,043 | 1,142,514 | 1,054,445 | 1,211,416 |
| ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS | | | | |
| Cash and bank balances | 1,102,043 | 1,142,514 | 1,054,445 | 1,211,416 |

## B. NOTES TO THE FINANCIAL INFORMATION

### 1. GENERAL INFORMATION

Zhong Tian Water Supply is a limited liability company incorporated in the PRC. The registered office of Zhong Tian Water Supply is located at 中國安徽省馬鞍山市當涂縣石橋鎮.

Zhong Tian Water Supply is principally engaged in the management of water plants and provision of water supply during the Relevant Periods.

### 2. ADOPTION OF NEW OR REVISED STANDARDS

The Financial Information has been prepared in accordance with HKFRSs issued by the HKICPA, accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. The Financial Information has been prepared under the historical cost convention.

New HKFRSs issued but not yet effective are not early adopted. The directors of Zhong Tian Water Supply anticipate that the application of these new HKFRSs will have no material impact on the Financial Information.

### 3. PRINCIPAL ACCOUNTING POLICIES

#### (a) Basis of preparation

The Financial Information and 2006 Comparative Financial Information have been prepared in accordance with accounting principles generally accepted in Hong Kong including all applicable HKFRSs and HKASs issued by the HKICPA. They have been prepared on the historical cost convention. The measurement bases are fully described in the accounting policies below.

The Financial Information and 2006 Comparative Financial Information have been prepared on a going concern basis notwithstanding that Zhong Tian Water Supply has net current liabilities as at 30 September 2007 as the shareholders have undertaken to provide continuous financial support to Zhong Tian Water Supply, and to maintain it as a going concern.

#### (b) Property, plant and equipment and depreciation

Property, plant and equipment, other than construction in progress, are stated at cost less accumulated depreciation and any impairment losses, except that when an item of property, plant and equipment is classified as held for sale, it is not depreciated and is measured at the lower of carrying amount and fair value less costs to sell. The cost of an item of property, plant and equipment comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Cost may also include transfers from equity of any gains/losses on qualifying cash flow hedges of foreign currency purchases of property, plant and equipment.

Expenditure incurred after items of property, plant and equipment have been put into operation, such as repairs and maintenance, is normally charged to the income statement in the period in which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of an item of property, plant and equipment and the cost of the item can be measured reliably, the expenditure is capitalised as an additional cost of that asset or as a replacement.

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 30 years |
| Plant and machineries | Over 10 years |
| Water pipelines | Over 10 years |
| Furniture, fixtures and equipment | Over 5 years |
| Motor vehicles | Over 5 years |

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

Residual values, useful lives and depreciation method are reviewed, and adjusted if appropriate, at each balance sheet date.

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

Construction in progress represents buildings, water pipelines, plant and machineries under construction, which is stated at cost less any 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.

**(c) Prepaid land lease payments**

Prepaid land lease payments under operating leases are initially stated at cost and subsequently recognised on the straight-line basis over the lease terms, except where an alternative basis is more representative of the pattern of benefits to be derived from the land leased.

**(d) Impairment of assets**

Where an indication of impairment exists, or when annual impairment testing for an asset is required (other than inventories, construction contract assets, financial assets, investment properties, goodwill and non-current assets/disposal group classified as held for sale), the asset's recoverable amount is estimated. An asset's recoverable amount is calculated as 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 group of assets, in which case, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

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

An assessment is made at each balance sheet date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If any such indication exists, the asset's recoverable amount is estimated. A previously recognised impairment loss of an asset other than goodwill is reversed only if there has been a change in the estimates used to determine the recoverable amount of that asset, however not to an amount higher than the carrying amount that would have been determined (net of any depreciation), had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is credited to the income statement in the period in which it arises, unless the asset is carried at a revalued amount, in which case the reversal of the impairment loss is accounted for in accordance with the relevant accounting policy for that revalued asset.

**(e) Related parties**

A party is considered to be related to Zhong Tian Water Supply if:

a) directly, or indirectly through one or more intermediaries, the party (i) controls, is controlled by, or is under common control with Zhong Tian Water Supply; (ii) has an interest in Zhong Tian Water Supply that gives it significant influence over Zhong Tian Water Supply; or (iii) has joint control over Zhong Tian Water Supply;

b) the party is an associate;

c) the party is a jointly-controlled entity;

d) the party is a member of the key management personnel of Zhong Tian Water Supply;

e) the party is a close member of the family of any individual referred to in (a) or (d);

f) the party is an entity that is controlled, jointly controlled or significantly influenced by or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (d) or (e); or

g) the party is a post employment benefit plan for the benefit of employees of Zhong Tian Water Supply, or of any entity that is related party of Zhong Tian Water Supply.

**(f) Leases**

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. Rentals payable under the operating leases are charged to the income statement on the straight-line basis over the lease terms.

**(h) Income tax**

Income tax comprises current and deferred tax. Income tax is recognised in the income statement or in equity if it relates to items that are recognised in the same or a different period, 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.

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

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

- where the deferred tax liability arises from the initial recognition of 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, associates and interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

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

- where the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability 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, associates and interests in joint ventures, 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 each balance sheet date 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. Conversely, previously unrecognised deferred tax assets are reassessed at each balance sheet date and are recognised to the extent that it is probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised.

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 at the balance sheet date.

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.

**(i) Government grants**

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

**(j) Revenue recognition**

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

(i) water supply related installation and construction income is recognized when services are rendered and income can be measured reliably;

(ii) revenue arising from water supply is recognized based on water supplied as recorded by meters read during the year; and

(iii) interest income, on time proportion basis taking into account the principal outstanding and the effective interest rate applicable.

**(k) Employee benefits**

*Pension scheme*

The employees of Zhong Tian Water Supply, which operates in Mainland China, are required to participate in a central pension scheme operated by the local municipal government. Zhong Tian Water Supply is required to contribute certain percentage of its payroll costs to the central pension scheme. The contributions are charged to the income statements as they become payable in accordance with the rules of the central pension scheme.

**(l) Borrowing costs**

Borrowing costs are charged to the income statement in the period in which they are incurred.

**(m) Foreign currencies**

These financial statements are presented in Renminbi ("RMB"), which is Zhong Tian Water Supply's functional and presentation currency. Foreign currency transactions are initially recorded using the functional currency rates ruling at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rates of exchange ruling at the balance sheet date. All differences are taken to 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 date 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.

**4. SIGNIFICANT ACCOUNTING JUDGEMENTS**

**Judgements**

In the process of applying Zhong Tian Water Supply's accounting policies, management has made the following judgements, apart from those involving estimations, which have the most significant effect on the amounts recognized in the financial statements.

*Impairment of assets*

In determining whether an asset is impaired or whether the event previously causing the impairment no longer exists, Zhong Tian Water Supply has to exercise judgement in the area of asset impairment, particularly in assessing: (1) whether an event has occurred that may affect the asset value, or such an 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 derecognition; 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 have a material effect on the net present value used in the impairment test.

## 5. TURNOVER AND OTHER REVENUE

Turnover represents the net value of meters charged for water supplies, installation fee and sub-contracting income therefrom for the Relevant Periods.

An analysis of Zhong Tian Water Supply's turnover and other revenue for the Relevant Periods is as follows:

| | Period from 22 August 2005 (date of incorporation) to 31 December | Year ended 31 December | Nine months ended 30 September | |
|---|---|---|---|---|
| | **2005** | **2006** | **2007** | **2006** |
| | *RMB* | *RMB* | *RMB* | *RMB* |
| | (audited) | (audited) | (audited) | (unaudited) |
| **TURNOVER** | | | | |
| Water supply related installation income | – | 1,273,500 | – | 1,062,879 |
| Water supply | – | 121,328 | – | 90,996 |
| Sub-contracting income | – | – | 150,000 | – |
| | – | 1,394,828 | 150,000 | 1,153,875 |
| **OTHER REVENUE** | | | | |
| Government grants premium* | – | – | 1,200,000 | – |
| Release of deferred government grants | – | 68,055 | 105,557 | 46,667 |
| Bank interest income | 557 | 2,309 | 1,008 | 1,194 |
| | 557 | 70,364 | 1,306,565 | 47,861 |
| | 557 | 1,465,192 | 1,456,565 | 1,201,736 |

* *Government grants premium represents monetary award from relevant authority in the PRC in respect of the construction progress of water supply plants expedited by the Company.*

## 6. FINANCE COSTS

| | Period from 22 August 2005 (date of incorporation) to 31 December 2005 | Year ended 31 December 2006 | Nine months ended 30 September 2007 | Nine months ended 30 September 2006 |
|---|---|---|---|---|
| | *RMB* | *RMB* | *RMB* | *RMB* |
| | (audited) | (audited) | (audited) | (unaudited) |
| Interest on other loans | 6,479 | 110,484 | 79,590 | 106,217 |

## 7. LOSS BEFORE TAX

Loss before tax is arrived at after charging:

| | Period from 22 August 2005 (date of incorporation) to 31 December 2005 | Year ended 31 December 2006 | Nine months ended 30 September 2007 | Nine months ended 30 September 2006 |
|---|---|---|---|---|
| | *RMB* | *RMB* | *RMB* | *RMB* |
| | (audited) | (audited) | (audited) | (unaudited) |
| Cost of services rendered | – | 309,748 | 7,500 | 278,522 |
| Depreciation of property, plant and equipment | 720 | 616,725 | 559,394 | 372,703 |
| Amortisation of prepaid land lease payments | 1,024 | 19,370 | 18,099 | 13,736 |
| Minimum lease payments under operating leases on land and buildings | 10,650 | 32,671 | 12,211 | 15,990 |
| Staff cost (excluding directors' remuneration – *note 8*) | | | | |
| Salaries and allowances | 98,622 | 823,439 | 521,650 | 670,628 |
| Pension scheme contributions | 19,724 | 164,688 | 104,330 | 134,126 |
| | 118,346 | 988,127 | 625,980 | 804,754 |

## 8. DIRECTORS' REMUNERATION AND FIVE HIGHEST PAID EMPLOYEES

Remuneration paid or payable to the directors were as follows:

| | Period from 22 August 2005 (date of incorporation) to 31 December | Year ended 31 December | Nine months ended 30 September | |
|---|---|---|---|---|
| | **2005** | **2006** | **2007** | **2006** |
| | *RMB* | *RMB* | *RMB* | *RMB* |
| | (audited) | (audited) | (audited) | (unaudited) |
| Fees | – | – | – | – |
| Other emoluments: | | | | |
| Salaries and benefits in kind | 14,800 | 19,200 | 12,800 | 14,400 |
| Pension scheme contributions | 3,960 | 3,840 | 2,560 | 2,880 |
| | 18,760 | 23,040 | 15,360 | 17,280 |

Of the five individuals with highest emoluments, one (year ended 31 December 2006 and period ended 31 December 2005: one) of them is director whose emoluments are disclosed as above. Details of the remuneration of the remaining four (year ended 31 December 2006 and period ended 31 December 2005: four) non-directors, highest paid employees are as follows:

| | Period from 22 August 2005 (date of incorporation) to 31 December | Year ended 31 December | Nine months ended 30 September | |
|---|---|---|---|---|
| | **2005** | **2006** | **2007** | **2006** |
| | *RMB* | *RMB* | *RMB* | *RMB* |
| | (audited) | (audited) | (audited) | (unaudited) |
| Salaries and benefits in kind | 59,200 | 76,800 | 35,200 | 57,600 |
| Pension scheme contributions | 11,840 | 15,360 | 7,040 | 11,520 |
| | 71,040 | 92,160 | 42,240 | 69,120 |

During the Relevant Periods, no emoluments were paid by Zhong Tian Water Supply to the directors or any of the five highest paid individuals as an inducement to join or upon joining Zhong Tian Water Supply or as compensation for loss of office. No director waived any emoluments during the Relevant Periods.

## 9. TAX

Zhong Tian Water Supply is subject to PRC Enterprise Income Tax at a rate of 33% on its assessable profits for the Relevant Periods. No PRC Enterprise Income Tax was provided as Zhong Tian Water Supply had no assessable profits for the Relevant Periods.

No provision for Hong Kong profits tax has been made as Zhong Tian Water Supply did not generate any assessable profits arising in Hong Kong during the Relevant Periods.

There are no material unprovided deferred tax assets and liabilities at the respective balance sheet dates.

A reconciliation of the tax expense applicable to loss before tax using the statutory rate to the tax expense at the effective tax rate is as follows:

| | **Period from 22 August 2005 (date of incorporation) to 31 December** | **Year ended 31 December** | **Nine months ended 30 September** | |
|---|---|---|---|---|
| | **2005** | **2006** | **2007** | **2006** |
| | *RMB* | *RMB* | *RMB* | *RMB* |
| | (audited) | (audited) | (audited) | (unaudited) |
| Loss before tax | (301,848) | (1,837,532) | (902,456) | (1,711,487) |
| Tax at the statutory tax rate | (99,610) | (606,386) | (297,810) | (564,791) |
| Tax loss not recognised | 99,610 | 606,386 | 297,810 | 564,791 |
| Tax charge at effective rate | – | – | – | – |

## 10. PROPERTY, PLANT AND EQUIPMENT

| | Buildings | Plant and machinery | Water pipeline | Furniture, fixtures and equipment | Motor vehicles | Construction in progress | Total |
|---|---|---|---|---|---|---|---|
| | *RMB* | *RMB* | *RMB* | *RMB* | *RMB* | *RMB* | *RMB* |
| **Cost:** | | | | | | | |
| Additions | – | – | – | 14,386 | – | 6,785,805 | 6,800,191 |
| At 31 December 2005 and 1 January 2006 | – | – | – | 14,386 | – | 6,785,805 | 6,800,191 |
| Additions | – | – | – | 32,850 | 8,650 | 21,172,325 | 21,213,825 |
| Transfers | 415,358 | 1,842,612 | 5,360,987 | – | – | (7,618,957) | – |
| At 31 December 2006 and 1 January 2007 | 415,358 | 1,842,612 | 5,360,987 | 47,236 | 8,650 | 20,339,173 | 28,014,016 |
| Additions | – | – | – | 31,840 | – | 20,039,842 | 20,071,682 |
| Transfers | – | – | 1,166 | – | – | (1,166) | – |
| At 30 September 2007 | 415,358 | 1,842,612 | 5,362,153 | 79,076 | 8,650 | 40,377,849 | 48,085,698 |
| **Accumulated depreciation:** | | | | | | | |
| Charge for the period | – | – | – | 720 | – | – | 720 |
| At 31 December 2005 and 1 January 2006 | – | – | – | 720 | – | – | 720 |
| Charge for the year | 11,538 | 153,551 | 446,749 | 4,311 | 576 | – | 616,725 |
| At 31 December 2006 and 1 January 2007 | 11,538 | 153,551 | 446,749 | 5,031 | 576 | – | 617,445 |
| Charge for the period | 10,384 | 138,196 | 402,161 | 6,923 | 1,730 | – | 559,394 |
| At 30 September 2007 | 21,922 | 291,747 | 848,910 | 11,954 | 2,306 | – | 1,176,839 |
| **Net book value:** | | | | | | | |
| At 30 September 2007 | 393,436 | 1,550,865 | 4,513,243 | 67,122 | 6,344 | 40,377,849 | 46,908,859 |
| At 31 December 2006 | 403,820 | 1,689,061 | 4,914,238 | 42,205 | 8,074 | 20,339,173 | 27,396,571 |
| At 31 December 2005 | – | – | – | 13,666 | – | 6,785,805 | 6,799,471 |

The buildings are situated in PRC and are held under medium term lease.

Zhong Tian Water Supply has restriction to sub-lease, mortgage or transfer the property, plant and equipment as follows:

| | At 31 December 2005 | At 31 December 2006 | At 30 September 2007 |
|---|---|---|---|
| | *RMB* | *RMB* | *RMB* |
| Buildings | – | 403,820 | 393,436 |
| Plant and machinery | – | 1,689,061 | 1,550,865 |
| Construction in progress | 6,785,805 | 20,339,173 | 40,377,849 |

## 11. PREPAID LAND LEASE PAYMENTS

| | As at 31 December | | As at 30 September |
|---|---|---|---|
| | 2005 | 2006 | 2007 |
| | *RMB* | *RMB* | *RMB* |
| | (audited) | (audited) | (audited) |
| Carrying amount at the beginning of the year/period | – | 104,976 | 703,416 |
| Additions during the year/period | 106,000 | 617,810 | – |
| Amortised during the year/period | (1,024) | (19,370) | (18,099) |
| Carrying amount at the end of the year/period | 104,976 | 703,416 | 685,317 |
| Current portion | (3,540) | (24,132) | (24,132) |
| Non-current portion | 101,436 | 679,284 | 661,185 |

The leasehold lands are situated in PRC and are held under medium term leases.

## 12. ACCOUNTS RECEIVABLE

The ageing analysis of accounts receivable was as follows:

| | As at 31 December | | As at 30 September |
|---|---|---|---|
| | 2005 | 2006 | 2007 |
| | *RMB* | *RMB* | *RMB* |
| | (audited) | (audited) | (audited) |
| 0 – 30 days | – | – | 150,000 |

## 13. PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

| | As at 31 December | | As at 30 September |
|---|---|---|---|
| | 2005 | 2006 | 2007 |
| | *RMB* | *RMB* | *RMB* |
| | (audited) | (audited) | (audited) |
| Prepayments | 769,246 | 1,458,747 | 782,515 |
| Deposits | 1,000 | – | – |
| Other receivables | 81,502 | 216,159 | 211,751 |
| Total | 851,748 | 1,674,906 | 994,266 |

## 14. DUE FROM A DIRECTOR

Particulars of the amount due from a director disclosed pursuant to Section 161B of the Hong Kong Companies Ordinance are as follows:

| | **As at 31 December** | | **As at 30 September** |
|---|---|---|---|
| | **2005** | **2006** | **2007** |
| | *RMB* | *RMB* | *RMB* |
| | (audited) | (audited) | (audited) |
| Zhong Ming Xian | 42,900 | – | – |

The amount due from a director is unsecured, interest-free and has no fixed terms of repayment.

Maximum amount outstanding during the Relevant Periods are as follows:

| | **Period from 22 August 2005 (date of incorporation) to 31 December 2005** | **Year ended 31 December 2006** | **Nine months ended 30 September 2007** |
|---|---|---|---|
| | *RMB* | *RMB* | *RMB* |
| | (audited) | (audited) | (audited) |
| Zhong Ming Xian | 42,900 | 42,900 | – |

## 15. DUE FROM SHAREHOLDERS

The amount due from shareholders is unsecured, interest-free and has no fixed terms of repayment.

## 16. ACCOUNTS PAYABLE

The ageing analysis of accounts payable was as follows:

| | **As at 31 December** | | **As at 30 September** |
|---|---|---|---|
| | **2005** | **2006** | **2007** |
| | *RMB* | *RMB* | *RMB* |
| | (audited) | (audited) | (audited) |
| 0 – 30 days | 469,686 | 7,236,797 | 6,529,098 |
| 31 – 60 days | 20,500 | 103,046 | 8,419,755 |
| 61 – 90 days | – | – | 15,000 |
| 91 – 120 days | – | – | – |
| Over 120 days | – | 575,817 | 1,510,279 |
| Total | 490,186 | 7,915,660 | 16,474,132 |

## 17. DEPOSITS RECEIVED, ACCRUALS AND OTHER PAYABLES

| | As at 31 December | | As at 30 September |
|---|---|---|---|
| | **2005** | **2006** | **2007** |
| | *RMB* | *RMB* | *RMB* |
| | (audited) | (audited) | (audited) |
| Deposits received and accruals | 269,226 | 301,372 | 417,651 |
| Other loans – interest-bearing of 5% – 6% per annum | 1,000,000 | 2,800,000 | 3,369,077 |
| Other loans – non-interest bearing | 50,000 | 667,810 | 1,104,867 |
| Total | 1,319,226 | 3,769,182 | 4,891,595 |

The other loans are unsecured and have no fixed terms of repayment.

## 18. DUE TO A DIRECTOR/SHAREHOLDERS/GOVERNMENT LOAN

The amounts due to a director/shareholders and government loan are unsecured, interest-free and have no fixed terms of repayment.

## 19. DEFERRED GOVERNMENT GRANTS

| | *RMB* |
|---|---|
| Grants received during the period | 2,400,000 |
| At 31 December 2005 and 1 January 2006 | 2,400,000 |
| Grants received during the year | 9,900,000 |
| Released during the year | (68,055) |
| At 31 December 2006 and 1 January 2007 | 12,231,945 |
| Grants received during the period | 9,700,000 |
| Released during the period | (105,557) |
| At 30 September 2007 | 21,826,388 |

## 20. SHARE CAPITAL

| | *Notes* | As at 31 December 2005 *RMB* (audited) | As at 31 December 2006 *RMB* (audited) | As at 30 September 2007 *RMB* (audited) |
|---|---|---|---|---|
| Registered: | | | | |
| Registered capital at the beginning of year/period | *(i)* | 500,000 | 5,000,000 | 10,000,000 |
| Increase in registered capital | *(ii), (iii)* | 4,500,000 | 5,000,000 | – |
| Registered capital at the end of year/period | | 5,000,000 | 10,000,000 | 10,000,000 |
| Paid-up: | | | | |
| Paid-up capital at the beginning of year/period | *(i)* | 500,000 | 5,000,000 | 7,000,000 |
| Increase in paid-up capital | *(ii), (iii)* | 4,500,000 | 2,000,000 | – |
| Paid-up capital at the end of year/period | | 5,000,000 | 7,000,000 | 7,000,000 |

*Notes:*

(i) Upon incorporation, the registered capital of Zhong Tian Water Supply was RMB500,000 and was fully paid-up as at the date of incorporation.

(ii) On 4 December 2005, Zhong Tian Water Supply increased its registered capital from RMB500,000 to RMB5,000,000 and was fulfilled by the cash contribution from its shareholders according to their respective share of equity interest in Zhong Tian Water Supply.

(iii) On 5 December 2006, Zhong Tian Water Supply increased its registered capital from RMB5,000,000 to RMB10,000,000. RMB2,000,000 was fulfilled by the cash contribution from its shareholders according to their respective share of equity interest in Zhong Tian Water Supply.

## 21. COMMITMENTS

At each of balance sheet dates, Zhong Tian Water Supply had the following capital commitments at the balance sheet date:

| | As at 31 December | | As at 30 September |
|---|---|---|---|
| | **2005** | **2006** | **2007** |
| | *RMB* | *RMB* | *RMB* |
| Contracted, but not provided for in respect of | | | |
| construction of property, plant and equipment | 8,487,532 | 14,202,328 | 12,902,806 |
| security and consultancy services | – | 10,000 | 10,667 |
| | 8,487,532 | 14,212,328 | 12,913,473 |

## 22. CONTINGENT LIABILITIES

At each of balance sheet dates, Zhong Tian Water Supply has no significant contingent liabilities.

## 23. FINANCIAL RISKS AND MANAGEMENT

Zhong Tian Water Supply's overall risk management programme seeks to minimise potential adverse effects on the financial performance of Zhong Tian Water Supply.

### (i) Interest rate risk

Zhong Tian Water Supply had interest-bearing borrowing at fixed interest rates. Interest income derived from interest-bearing assets was insignificant. Zhong Tian Water Supply's income and cash flows are substantially independent of changes in market interest rates.

### (ii) Foreign currency risk

Zhong Tian Water Supply does not have any significant financial instrument or transaction denominated in foreign currency.

### (iii) Credit risk

Credit risk refers to the risk that debtors will default on their obligations to repay the amounts owing to the Zhong Tian Water Supply, resulting in a loss. The exposure to these are actively monitored by the management to avoid significant concentration of credit risk.

### (iv) Liquidity risk

Zhong Tian Water Supply aims to manage its operating cash flows and the availability of funding so as to ensure that all repayment and funding needs. As part of its overall liquidity management, Zhong Tian Water Supply maintains sufficient levels of cash to meet its working capital requirements.

### (v) Fair values

The carrying amounts of the financial assets and liabilities in the Financial Information approximately their fair values.

## C. SUBSEQUENT EVENT

In November 2007, Zhong Tian Water Supply made an application for reconstitution from a PRC joint stock limited liability company to a sino-foreign joint venture company, with its registered capital increased from RMB10,000,000 to RMB21,430,000 as part of the reconstitution scheme. Completion of the reconstitution was approved by the PRC government department on 29 December 2007.

## D. SUBSEQUENT FINANCIAL STATEMENTS

No audited financial statements have been prepared for Zhong Tian Water Supply in respect of any period subsequent to 30 September 2007.

Yours faithfully,
**Vision A. S. Limited**
*Certified Public Accountants*
Hong Kong

**Cheung Man Yau, Timothy**
Practising Certificate No.: P01417

## 1. SUMMARY OF FINANCIAL INFORMATION

*The following table summaries the results, assets and liabilities for each of the three years ended 31 December 2006 as extracted from the relevant published financial statements of the Group:*

**CONSOLIDATED INCOME STATEMENT**
*For the year ended 31 December*

| | 2004 | 2005 | 2006 |
|---|---|---|---|
| | *HK$'000* | *HK$'000* | *HK$'000* |
| Turnover | 4,320 | 4,472 | 6,622 |
| Cost of sales | (1,645) | (1,888) | (3,489) |
| Gross profit | 2,675 | 2,584 | 3,133 |
| Other income | – | 204 | 656 |
| Research and development expenses | (2,460) | (1,250) | (1,166) |
| Selling and distribution expenses | (2,348) | (1,062) | (1,189) |
| Administrative expenses | (6,817) | (5,389) | (7,707) |
| Loss before taxation | (8,950) | (4,913) | (6,273) |
| Taxation | – | – | – |
| Loss for the year | (8,950) | (4,913) | (6,273) |
| Attributable to: | | | |
| Equity holders of the Company | (8,950) | (4,913) | (6,273) |
| | (Restated) | (Restated) | |
| Loss per share – Basic | (2.54 cents) | (1.13 cents) | (1.11 cents) |

**CONSOLIDATED BALANCE SHEET**
*At 31 December*

| | **2004** | **2005** | **2006** |
|---|---|---|---|
| | *HK$'000* | *HK$'000* | *HK$'000* |
| NON-CURRENT ASSETS | | | |
| Property, plant and equipment | 467 | 334 | 158 |
| CURRENT ASSETS | | | |
| Inventories, at cost | 200 | – | 62 |
| Trade and other receivables | 1,296 | 1,807 | 4,638 |
| Bank balances and cash | 4,216 | 2,253 | 22,707 |
| | 5,712 | 4,060 | 27,407 |
| CURRENT LIABILITIES | | | |
| Trade and other payables | 2,211 | 2,305 | 3,989 |
| Financial assistance from government | 223 | 166 | 236 |
| | 2,434 | 2,471 | 4,225 |
| NET CURRENT ASSETS | 3,278 | 1,589 | 23,182 |
| TOTAL ASSETS LESS CURRENT LIABILITIES | 3,745 | 1,923 | 23,340 |
| NON-CURRENT LIABILITIES | | | |
| Financial assistance from government | 1,196 | 1,172 | 1,059 |
| NET ASSETS | 2,549 | 751 | 22,281 |
| CAPITAL AND RESERVES | | | |
| Share capital | 5,837 | 7,004 | 29,498 |
| Reserves | (3,288) | (6,253) | (7,217) |
| TOTAL EQUITY | 2,549 | 751 | 22,281 |

## 2. AUDITED FINANCIAL STATEMENTS

*Set out below is the audited financial information of the Group for the two years ended 31 December 2006 as extracted from the annual report 2006 of the Company.*

### CONSOLIDATED INCOME STATEMENT

*For the year ended 31 December 2006*

| | Note | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|---|
| Turnover | 3 | 6,622 | 4,472 |
| Cost of sales | | (3,489) | (1,888) |
| Gross profit | | 3,133 | 2,584 |
| Other income | 5 | 656 | 204 |
| Research and development expenses | | (1,166) | (1,250) |
| Selling and distribution expenses | | (1,189) | (1,062) |
| Administrative expenses | | (7,707) | (5,389) |
| Loss before taxation | 6 | (6,273) | (4,913) |
| Taxation | 8 | – | – |
| Loss for the year | | (6,273) | (4,913) |
| Attributable to: | | | |
| Equity holders of the Company | 10 | (6,273) | (4,913) |
| | | | (Restated) |
| Loss per share – Basic | 11 | (1.11 cents) | (1.13 cents) |

## CONSOLIDATED BALANCE SHEET

*At 31 December 2006*

| | Note | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|---|
| **NON-CURRENT ASSETS** | | | |
| Property, plant and equipment | 12 | 158 | 334 |
| **CURRENT ASSETS** | | | |
| Inventories, at cost | | 62 | – |
| Trade and other receivables | 14 | 4,638 | 1,807 |
| Bank balances and cash | | 22,707 | 2,253 |
| | | 27,407 | 4,060 |
| **CURRENT LIABILITIES** | | | |
| Trade and other payables | 15 | 3,989 | 2,305 |
| Financial assistance from government | 16 | 236 | 166 |
| | | 4,225 | 2,471 |
| **NET CURRENT ASSETS** | | 23,182 | 1,589 |
| **TOTAL ASSETS LESS CURRENT LIABILITIES** | | 23,340 | 1,923 |
| **NON-CURRENT LIABILITIES** | | | |
| Financial assistance from government | 16 | 1,059 | 1,172 |
| **NET ASSETS** | | 22,281 | 751 |
| **CAPITAL AND RESERVES** | | | |
| Share capital | 17 | 29,498 | 7,004 |
| Reserves | 18 | (7,217) | (6,253) |
| **TOTAL EQUITY** | | 22,281 | 751 |

**BALANCE SHEET**
*At 31 December 2006*

| | Note | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|---|
| NON-CURRENT ASSETS | | | |
| Interests in subsidiaries | 13 | 132 | 2,041 |
| CURRENT ASSETS | | | |
| Other receivables | | 2,804 | 181 |
| Bank balances | | 22,150 | 30 |
| | | 24,954 | 211 |
| CURRENT LIABILITIES | | | |
| Other payables | | 532 | 369 |
| NET CURRENT ASSETS (LIABILITIES) | | 24,422 | (158) |
| NET ASSETS | | 24,554 | 1,883 |
| CAPITAL AND RESERVES | | | |
| Share capital | 17 | 29,498 | 7,004 |
| Reserves | 18 | (4,944) | (5,121) |
| TOTAL EQUITY | | 24,554 | 1,883 |

## CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

*For the year ended 31 December 2006*

| | Share capital HK$'000 | Share premium HK$'000 | Special reserve HK$'000 (note a) | Warrant subscription reserve HK$'000 | Exchange reserve HK$'000 | Employee share-based compensation reserve HK$'000 | Accumulated losses HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|---|---|---|
| At 1 January 2004 | 4,864 | 11,836 | 10,084 | – | – | – | (23,745) | 3,039 |
| Issue of shares under the placing | 973 | 8,027 | – | – | – | – | – | 9,000 |
| Share issue expenses | – | (540) | – | – | – | – | – | (540) |
| Loss for the year | – | – | – | – | – | – | (8,950) | (8,950) |
| At 1 January 2005 | 5,837 | 19,323 | 10,084 | – | – | – | (32,695) | 2,549 |
| Issue of shares under the placing | 1,167 | 1,518 | – | – | – | – | – | 2,685 |
| Share issue expenses | – | (137) | – | – | – | – | – | (137) |
| Employee share-based compensation | – | – | – | – | – | 567 | – | 567 |
| Loss for the year | – | – | – | – | – | – | (4,913) | (4,913) |
| At 31 December 2005 | 7,004 | 20,704 | 10,084 | – | – | 567 | (37,608) | 751 |
| Issue of rights shares | 22,124 | 3,097 | – | – | – | – | – | 25,221 |
| Issue of warrants under the placing | – | – | – | 1,767 | – | – | – | 1,767 |
| Share/warrants issue expenses | – | (2,250) | – | (298) | – | – | – | (2,548) |
| Shares issued upon exercise of share options | 370 | 1,270 | – | – | – | (567) | – | 1,073 |
| Employee share-based compensation | – | – | – | – | – | 2,314 | – | 2,314 |
| Exchange differences arising from consolidation | – | – | – | – | (24) | – | – | (24) |
| Loss for the year | – | – | – | – | – | – | (6,273) | (6,273) |
| At 31 December 2006 | 29,498 | 22,821 | 10,084 | 1,469 | (24) | 2,314 | (43,881) | 22,281 |

*Note:*

(a) The special reserve represents the difference between the nominal amount of shares and share premium of KanHan Technologies Inc. ("KanHan (BVI)") at the date on which it was acquired by the Company and the nominal amount of the Company's shares issued as consideration pursuant to the Group reorganisation taken place in 2003.

**CONSOLIDATED CASH FLOW STATEMENT**

*For the year ended 31 December 2006*

| | Note | 2006<br>HK$'000 | 2005<br>HK$'000 | 2004<br>HK$'000 |
|---|---|---|---|---|
| NET CASH USED IN OPERATING ACTIVITIES | 19 | (5,553) | (4,384) | (8,804) |
| INVESTING ACTIVITIES | | | | |
| Purchase of property, plant and equipment | | (49) | (73) | (375) |
| Interest received | | 585 | 27 | 4 |
| NET CASH USED IN INVESTING ACTIVITIES | | 536 | (46) | (371) |
| FINANCING ACTIVITIES | | | | |
| Proceeds from issue of shares | | – | 2,685 | 9,000 |
| Proceeds from issue of rights shares | | 25,221 | – | – |
| Proceeds from exercise of share options | | 1,073 | – | – |
| Proceeds from issue of warrants | | 1,767 | – | – |
| Share/warrants issue expenses | | (2,548) | (137) | (540) |
| Decrease in amounts due from shareholders | | – | – | 3,971 |
| Repayment of financial assistance from government | | (43) | (81) | (40) |
| NET CASH FROM FINANCING ACTIVITIES | | 25,470 | 2,467 | 12,391 |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | | 20,453 | (1,963) | 3,216 |
| CASH AND CASH EQUIVALENTS AT BEGINNING OF THE YEAR | | 2,253 | 4,216 | 1,000 |
| CHANGES IN FOREIGN EXCHANGE RATE | | 1 | – | – |
| CASH AND CASH EQUIVALENTS AT END OF THE YEAR, REPRESENTED BY BANK BALANCES AND CASH | | 22,707 | 2,253 | 4,216 |

## NOTES TO THE FINANCIAL STATEMENTS

*For the year ended 31 December 2006*

### 1. CORPORATE INFORMATION

The Company was incorporated in the Cayman Islands on 10 October 2002 as an exempted company with limited liability under the Companies Law (Revised) of the Cayman Islands.

The shares of the Company were listed on the Growth Enterprise Market ("GEM") of The Stock Exchange of Hong Kong Limited on 25 February 2003.

The principal activity of the Company is investment holding. Details of the principal activities of its subsidiaries are set out in note 13.

### 2. PRINCIPAL ACCOUNTING POLICIES

A summary of the principal accounting policies adopted by the Group is set out below.

#### (a) Basis of preparation

These financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRS"), which collective term includes all applicable individual HKFRS, Hong Kong Accounting Standards ("HKAS") and Interpretations issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance.

These financial statements have been prepared on a basis consistent with the accounting policies adopted in the 2005 financial statements. A summary of the principal accounting policies adopted by the Group is set out below.

The measurement basis used in the preparation of these financial statements is historical cost.

#### (b) Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries made up to 31 December each year.

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

All inter-company transactions and balances within the Group have been eliminated on consolidation.

#### (c) Subsidiaries

A subsidiary is an entity, in which the Company, directly or indirectly, has the power to govern the financial and operating policies so as to obtain benefits from its activities.

In the Company's balance sheet, investments in subsidiaries are stated at cost less accumulated impairment losses. The carrying amount of the investment is reduced to its recoverable amount on an individual basis. The results of subsidiaries are accounted for by the Company on the basis of dividends received and receivable.

**(d) Property, plant and equipment**

Property, plant and equipment are recorded at cost less accumulated depreciation and accumulated impairment losses.

The cost of an item of property, plant and equipment comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Repairs and maintenance are charged to the income statement during the year in which they are incurred.

Depreciation is provided to write off the cost less accumulated impairment losses of property, plant and equipment over their estimated useful lives as set out below from the date on which they are available for use and after taking into account of their estimated residual values, using the straight-line method, at the following rates per annum:

| | |
|---|---|
| Leasehold improvements | $33^1/_3$% |
| Furniture, fixtures and office equipment | 20% |
| Computer equipment | $33^1/_3$% |

**(e) Trade receivables and payables**

Trade receivables and payables are recognised at cost which approximates to their fair values, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all the amounts due according to the original terms of receivables. The amount of the provision is the difference between the assets' carrying amount and the present value of estimated future cash flow, discounted at the effective interest rate. The amount of provision is recognised in the income statement.

**(f) Revenue recognition**

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

Sales of licensed software is recognised on the transfer of risks and rewards of ownership, which generally coincides with the time when the goods are delivered to customers and titles have been passed.

Software maintenance service income, which is received or receivable from customers when the maintenance service contracts are entered into, is amortised and credited to the income statement on a straight-line basis over the respective term of the maintenance service contract.

Software rental and subscription income from software application, website development and Putonghua learning platform are derived from providing software application to customers. The income is recognised when services are provided.

**(g) Foreign currency translation**

*(i) Functional and presentation currency*

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The consolidated financial statements are presented in Hong Kong dollars, which is the Group's functional and presentation currency.

*(ii) Transactions and balances*

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

*(iii) Overseas subsidiaries*

On consolidation, the results and financial position of all overseas subsidiaries that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

(a) assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;

(b) income and expenses for each income statement are translated at average exchange rates; and

(c) all resulting exchange differences are recognised as a separate component of equity.

**(h) Inventories**

Inventories, which represent the licensed softwares for sale, are stated at lower of cost and net realisable value. Cost, which comprises all costs of purchase and, where applicable, other costs that have been incurred in bringing the inventories to their present location and condition, is calculated using the first in, first out method. Net realisable value represents the estimated selling price in the ordinary course of business less the estimated costs necessary to make the sale.

**(i) Impairment of non-financial assets**

At each balance sheet date, the Group reviews internal and external sources of information to determine whether its property, plant and equipment have suffered an impairment loss or impairment loss previously recognised no longer exists or may be reduced. If any such indication exists, the recoverable amount of the asset is estimated, based on the higher of its fair value less costs to sell and value in use. Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the smallest group of assets that generates cash flows independently (i.e. cash-generating unit).

If the recoverable amount of an asset or a cash-generating unit is estimated to be less than its carrying amount, the carrying amount of the asset or cash-generating unit is reduced to its recoverable amount. Impairment losses are recognised as an expense immediately.

A reversal of impairment loss is limited to the carrying amount of the asset or cash-generating unit that would have been determined had no impairment loss been recognised in prior years. Reversal of impairment loss is recognised as income immediately.

**(j) Leases**

Leases which do not transfer substantially all the risks and rewards of ownership to the Group are classified as operating leases. Rentals payable under operating leases are charged to the income statement on a straight-line basis over the term of the relevant lease.

**(k) Employee benefits**

*(i) Defined contribution plan*

The obligations for contributions to defined contribution retirement scheme are recognised as an expense in the income statement as incurred. The assets of the scheme are held separately from those of the Group in an independently administered fund.

*(ii) Share-based compensation transactions*

The Group operates an employee share option plan for the purpose of providing incentives and/or rewards, to eligible employees of the Group.

Employees of the Group (including Directors) receives remuneration in the form of share-based payment transactions, whereby the employees render services in exchange for shares or rights over shares. The cost of such transactions with employees is measured by reference to the fair value at the transaction date. The fair value of share options granted to employees is recognised as an employee cost with a corresponding increase in a reserve within equity. The fair value is determined using Black-Scholes option pricing model, taking into account the terms and conditions of the transactions, other than conditions linked to the price of the shares of the Company ("market conditions").

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the year in which the performance conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award ("vesting date"). During the vesting period, the number of share options that is expected to vest ultimately is reviewed. Any adjustment to the cumulative fair value recognised in prior years is charged/credited to the income statement for the year of the review, with a corresponding adjustment to the reserve within equity. When the option is exercised, the amount will be transferred to the share premium account.

**(l) Taxation**

The charge for current income tax is based on the results for the year as adjusted for items that are non-assessable or disallowed. It is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, if the deferred tax arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither the accounting profit nor taxable profit or loss, it is not accounted for.

The deferred tax liabilities and assets are measured at the tax rates that are expected to apply to the period when the asset is recovered or the liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted at the balance sheet date. Deferred tax assets are recognised to the extent that it is probable that future taxable profits will be available against which the deductible temporary differences, tax losses and credits can be utilised.

**(m) Related parties**

A party is related to the Group if (a) directly, or indirectly through one or more intermediaries, the party controls, is controlled by or is under common control with the Group; or has an interest in the Group that gives it significant influence over the Group; or has joint control over the Group; (b) the party is an associate of the Group; (c) the party is a joint venture in which the Group is a venturer; (d) the party is a member of the key management personnel of the Group or its parent; (e) the party is a close member of the family of any individual referred to in (a) or (d); (f) the party is an entity that is controlled, jointly controlled or significantly influenced by or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (d) or (e); or (g) the party is a post-employment benefit plan for the benefit of employees of the Group, or of any entity that is a related party of the Group.

**(n) Critical accounting estimates and judgements**

Estimates and judgements are currently evaluated and are based on historical experience and other factors including expectations of future events that are believed to be reasonable under the circumstances.

*Allowance for bad and doubtful debts*

The provisioning policy for bad and doubtful debts of the Group is based on the evaluation of collectability and ageing analysis of the trade receivables and on management judgements. A considerable amount of judgement is required in assessing the ultimate realisation of these receivables, including assessing the current creditworthiness and the past collection history of each customer. If the financial conditions of these customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowance will be required.

**(o) Future changes in HKFRS**

At the date of authorisation of these financial statements, the Group has not early adopted the new/revised standards and interpretations issued by HKICPA that are not effective for the current year. The directors anticipate that the adoption of these new HKFRS in the future periods will have no material impact on the results of the Group.

**3. TURNOVER AND REVENUE**

The Group is principally engaged in provision of server-based language technology. Turnover and revenue recognised during the year are as follows:

| | **2006** | **2005** |
|---|---|---|
| | *HK$'000* | *HK$'000* |
| | | (Restated) |
| Sales of licensed software | 4,979 | 2,624 |
| Software maintenance service | 741 | 780 |
| Software rental and subscription income | 306 | 294 |
| Website development | 308 | 384 |
| Putonghua learning platform | 288 | 390 |
| | 6,622 | 4,472 |

## 4. SEGMENT INFORMATION

For the years ended 31 December 2005 and 2006, more than 90% of the Group's turnover and operating assets were attributable to the development of server-based language technologies in the Special Administrative Region of Hong Kong. Accordingly, no analysis by either business or geographical segment is included in these financial statements.

## 5. OTHER INCOME

| | **2006** | **2005** |
|---|---|---|
| | *HK$'000* | *HK$'000* |
| Bank interest income | 585 | 27 |
| Commission income | 41 | 177 |
| Gain on exchange | 30 | – |
| | 656 | 204 |

## 6. LOSS BEFORE TAXATION

| | **2006** | **2005** |
|---|---|---|
| | *HK$'000* | *HK$'000* |
| This is stated after charging: | | |
| Employee salaries and other benefits | 3,402 | 3,194 |
| Employee retirement benefit scheme contributions | 152 | 140 |
| Employee share-based payment | 1,264 | 353 |
| Total staff costs (excluding directors' emoluments) | 4,818 | 3,687 |
| Auditors' remuneration | | |
| – Underprovision in prior year | 20 | – |
| – Current year | 260 | 220 |
| Cost of services and inventories | 3,489 | 1,888 |
| Depreciation | 173 | 206 |
| Operating lease payments | | |
| – director's quarter | – | 240 |
| – office premises | 395 | 355 |

## 7. EMOLUMENTS OF THE DIRECTORS AND THE HIGHEST PAID INDIVIDUALS

### (a) Directors' Emoluments

| | Directors' fees | Salaries and other allowances | Retirement benefit | Employee share-based compensation | 2006 Total |
|---|---|---|---|---|---|
| | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* |
| *Executive directors* | | | | | |
| Mo Wai Ming, Lawrence | 120 | 1,200 | 12 | 525 | 1,857 |
| Ma She Shing, Albert | 120 | – | 6 | 525 | 651 |
| *Independent non-executive directors* | | | | | |
| Hsu Shiu Foo, William | 60 | – | – | – | 60 |
| Lee Kun Hung | 60 | – | – | – | 60 |
| Kwok Chi Sun, Vincent | 60 | – | – | – | 60 |
| | 420 | 1,200 | 18 | 1,050 | 2,688 |

| | Directors' fees | Salaries and other allowances | Retirement benefit | Employee share-based compensation | 2006 Total |
|---|---|---|---|---|---|
| | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* |
| *Executive directors* | | | | | |
| Mo Wai Ming, Lawrence | 60 | 1,300 | 12 | 107 | 1,479 |
| Ma She Shing, Albert (appointed on 1 June 2005) | 70 | – | 4 | 107 | 181 |
| Wai Lai Yung (resigned on 1 June 2005) | 21 | – | – | – | 21 |
| Lee Chi Ming (resigned on 1 January 2005) | – | – | – | – | – |
| *Non-executive director* | | | | | |
| Yuen Ka Lok, Ernest (resigned on 1 May 2005) | 17 | – | – | – | 17 |
| *Independent non-executive directors* | | | | | |
| Hsu Shiu Foo, William (appointed on 10 June 2005) | 34 | – | – | – | 34 |
| Lee Kun Hung (appointed on 1 June 2005) | 34 | – | – | – | 34 |
| Kwok Chi Sun, Vincent | 55 | – | – | – | 55 |
| Li Mo Ching, Joyce (resigned on 10 June 2005) | 22 | – | – | – | 22 |
| Tam Cheuk Ling, Jacqueline (resigned on 1 June 2005) | 21 | – | – | – | 21 |
| | 334 | 1,300 | 16 | 214 | 1,864 |

**(b) Five Highest Paid Individuals' Emoluments**

The five highest paid individuals included one (2005: one) director of the Company, details of whose emoluments are set out above. The emoluments of the remaining four (2005: four) individuals, which fall within the band of nil to HK$1,000,000 for each of the two years ended 31 December 2006 and 2005, are as follows:

| | **2006** | **2005** |
|---|---|---|
| | *HK$'000* | *HK$'000* |
| Salaries and other benefits | 1,268 | 1,320 |
| Retirement benefit scheme contributions | 47 | 41 |
| | 1,315 | 1,361 |

During the year, no emoluments were paid by the Group to any of the directors or the five highest paid individuals (including directors and employees) as an inducement to join or upon joining the Group or as compensation for loss of office. In addition, none of the directors has waived any emoluments during each of the years ended 31 December 2006 and 2005.

## 8. TAXATION

No provision for Hong Kong Profits Tax has been made in the financial statements as the Company and its subsidiaries incurred tax loss during both years.

The tax charge for the year can be reconciled to the loss before taxation as follows:

| | **2006** | | **2005** | |
|---|---|---|---|---|
| | *HK$'000* | *%* | *HK$'000* | *%* |
| Loss before taxation | (6,273) | | (4,913) | |
| Income tax at applicable tax rate of 17.5% (2005: 17.5%) | (1,098) | (17.5) | (860) | (17.5) |
| Non-deductible expenses | 705 | 11.3 | 362 | 7.3 |
| Tax exempt revenue | (23) | (0.4) | (32) | (0.7) |
| Unrecognised temporary difference | 21 | 0.3 | – | – |
| Unrecognised tax losses | 395 | 6.3 | 530 | 10.9 |
| Taxation for the year | – | – | – | – |

## 9. DIVIDEND

No dividend has been paid or declared by the Company during the years ended 31 December 2006 and 2005.

## 10. LOSS ATTRIBUTABLE TO EQUITY HOLDERS OF THE COMPANY

The net loss attributable to equity holders of the Company included a loss of HK$5,156,000 (2005: HK$9,063,000) which has been dealt with in the financial statements of the Company.

## 11. LOSS PER SHARE

The computation of the basic loss per share is based on the net loss attributable to shareholders for the year of HK$6,273,000 (2005: HK$4,913,000) and the weighted average number of 565,096,432 (2005: Restated 432,915,369) shares in issue during the year.

The weighted average number of shares for the purpose of calculating the basic loss per share for the year 2006 and 2005 have been adjusted for the effect of the share consolidation and the rights issue as described in note 17 to these financial statements.

No diluted loss per share was presented as the share options and the conversion of the outstanding warrants of the Company are anti-dilutive.

## 12. PROPERTY, PLANT AND EQUIPMENT

| | **Leasehold improvements** | **Furniture, fixtures and office equipment** | **Computer equipment** | **Total** |
|---|---|---|---|---|
| | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* |
| **THE GROUP** | | | | |
| COST | | | | |
| At 1 January 2006 | 165 | 354 | 846 | 1,365 |
| Additions | 11 | 13 | 25 | 49 |
| Disposal | – | (53) | – | (53) |
| Exchange difference | – | 1 | – | 1 |
| At 31 December 2006 | 176 | 315 | 871 | 1,362 |
| ACCUMULATED DEPRECIATION | | | | |
| At 1 January 2006 | 67 | 241 | 723 | 1,031 |
| Charge for the year | 57 | 23 | 93 | 173 |
| At 31 December 2006 | 124 | 264 | 816 | 1,204 |
| NET BOOK VALUES | | | | |
| At 31 December 2006 | 52 | 51 | 55 | 158 |

| | Leasehold improvements *HK$'000* | Furniture, fixtures and office equipment *HK$'000* | Computer equipment *HK$'000* | Total *HK$'000* |
|---|---|---|---|---|
| **THE GROUP** | | | | |
| COST | | | | |
| At 1 January 2005 | 157 | 339 | 796 | 1,292 |
| Additions | 8 | 15 | 50 | 73 |
| At 31 December 2005 | 165 | 354 | 846 | 1,365 |
| ACCUMULATED DEPRECIATION | | | | |
| At 1 January 2005 | 13 | 201 | 611 | 825 |
| Charge for the year | 54 | 40 | 112 | 206 |
| At 31 December 2005 | 67 | 241 | 723 | 1,031 |
| NET BOOK VALUES | | | | |
| At 31 December 2005 | 98 | 113 | 123 | 334 |

**13. INTERESTS IN SUBSIDIARIES**

| | THE COMPANY | |
|---|---|---|
| | **2006** *HK$'000* | **2005** *HK$'000* |
| Unlisted shares, at cost | 3,162 | 3,162 |
| Impairment loss | (3,162) | (3,162) |
| | – | – |
| Due from subsidiaries | 22,012 | 22,236 |
| Provision for doubtful debts | (21,880) | (20,195) |
| | 132 | 2,041 |
| | 132 | 2,041 |

Details of the subsidiaries at 31 December 2006 are as follows:

| Name of subsidiary | Place of incorporation | Issued and fully paid up ordinary share capital | Proportion of ownership interest and voting power held Directly % | Indirectly % | Principal activity | Place of operation |
|---|---|---|---|---|---|---|
| KanHan Technologies Inc. | British Virgin Islands | US$116,225 | 100 | – | Investment holding | Hong Kong |
| KanHan Technologies Limited | Hong Kong | HK$200,000 | – | 100 | Provision of communication software platforms | Hong Kong |
| China Rise Investment Limited | Hong Kong | HK$1 | – | 100 | Investment holding | Hong Kong |
| KanHan Technologies (China) Limited | The People's Republic of China | HK$1,000,000 | – | 100 | Provision of communication software platforms | The People's Republic of China |
| Rise Assets Limited | British Virgin Islands | US$1 | 100 | – | Investment holding | Hong Kong |
| Pharmanet Asia Limited | Hong Kong | HK$1 | – | 100 | Sourcing agent | Hong Kong |

The amounts due from subsidiaries are unsecured, interest-free and have no fixed term of repayment. In the opinion of the directors, the amounts are not expected to be realised in the next twelve months from the balance sheet date.

None of the subsidiaries had any debt capital outstanding at the end of the year or at any time during the year.

## 14. TRADE AND OTHER RECEIVABLES

| | THE GROUP 2006 *HK$'000* | 2005 *HK$'000* |
|---|---|---|
| Trade receivables | 775 | 1,019 |
| Deposits, prepayments and other receivables | 1,363 | 788 |
| Deposits paid under a non-legally binding memorandum of understanding *(note (a))* | 2,500 | – |
| | 4,638 | 1,807 |

The Group has a policy of allowing a credit period from 30 to 120 days to its trade customers. The following is an ageing analysis of the trade receivables at the balance sheet date:

| | THE GROUP | |
|---|---|---|
| | **2006** | **2005** |
| | *HK$'000* | *HK$'000* |
| 0 – 30 days | 175 | 177 |
| 31 – 60 days | 559 | 494 |
| 61 – 90 days | 10 | – |
| Over 90 days | 31 | 348 |
| | 775 | 1,019 |

*Note:*

(a) On 15 May 2006, the Company entered into a non-legally binding memorandum of understanding ("MOU") with Excel State Group Limited ("Excel State") and Mr. Yang Shuxin in relation to the proposed acquisition of the whole or part of equity interests held by Mr. Yang Shuxin in Excel State, which holds 51% indirect interests in Shantou Jinshui Technology Limited ("Jinshui").

Jinshui is a company established in the People's Republic of China ("PRC") and is principally engaged in the design, provision and distribution of software and hardware for tax control purpose and the provision of other related services in the PRC.

A refundable amount of HK$2,500,000 was paid by the Company to Mr. Yang Shuxin as earnest money. As additional time is required for the negotiation process on the terms of the proposed acquisition, the long-stop date of the MOU has been extended from 31 August 2006 to 31 March 2007. If no legally-binding formal agreement has been entered into on or before 31 March 2007, the sum will be refunded to the Company in full.

**15. TRADE AND OTHER PAYABLES**

| | THE GROUP | |
|---|---|---|
| | **2006** | **2005** |
| | *HK$'000* | *HK$'000* |
| Trade payables | 269 | 499 |
| Accrued charges and other creditors | 3,720 | 1,806 |
| | 3,989 | 2,305 |

The following is an ageing analysis of the trade payables at the balance sheet date:

| | THE GROUP | |
|---|---|---|
| | **2006** | **2005** |
| | *HK$'000* | *HK$'000* |
| 0 – 30 days | 126 | 499 |
| 31 – 60 days | 31 | – |
| 61 – 90 days | 112 | – |
| | 269 | 499 |

## 16. FINANCIAL ASSISTANCE FROM GOVERNMENT

The Innovation and Technology Fund ("ITF") of the Hong Kong Special Administrative Region government has provided financial assistance to the Group to assist in a specific product development. The funding is unsecured, non-interest bearing and repayable to ITF when revenue is generated from the specific product. The amount repaid, if any, will be in stages and calculated with reference to the revenue generated and received.

In the opinion of the directors, HK$236,000 (2005: HK$166,000) will be repayable to the ITF within the next twelve months from 31 December 2006 by reference to the forecast revenue generated to be from the specific product. Accordingly, HK$236,000 (2005: HK$166,000) has been classified as current liabilities and the remaining balance of HK$1,059,000 (2005: HK$1,172,000) is classified as non-current liabilities.

## 17. SHARE CAPITAL

| | **Number of shares** | **Amount** |
|---|---|---|
| | | *HK$'000* |
| *Authorised:* | | |
| At 1 January 2005 and 31 December 2005, at HK$0.01 each | 2,000,000,000 | 20,000 |
| Share consolidation on 28 February 2006 *(note (a))* | (1,600,000,000) | – |
| Increase in authorised share capital *(note (a))*: 1,600,000,000 ordinary shares of HK$0.05 each | 1,600,000,000 | 80,000 |
| At 31 December 2006, at HK$0.05 each | 2,000,000,000 | 100,000 |
| Issued and fully paid: | | |
| At 1 January 2005, at HK$0.01 each | 583,718,400 | 5,837 |
| Issue of shares under the placement on 27 June 2005 116,740,000 ordinary shares of HK$0.01 each | 116,740,000 | 1,167 |
| At 31 December 2005, at HK$0.01 each | 700,458,400 | 7,004 |
| Shares issued upon exercise of share options on 2 February 2006 (*note 20*): 37,000,000 ordinary shares of HK$0.01 each | 37,000,000 | 370 |
| | 737,458,400 | 7,374 |
| Share consolidation on 28 February 2006 (*note (a)*) | (589,966,720) | – |
| At 28 February 2006, at HK$0.05 each | 147,491,680 | 7,374 |
| Issue of shares under the rights issue on 30 March 2006 (*note b*): 442,475,040 ordinary shares of HK$0.05 each | 442,475,040 | 22,124 |
| At 31 December 2006, at HK$0.05 each | 589,966,720 | 29,498 |

*Notes:*

(a) Pursuant to an ordinary resolution passed by the shareholders in the extraordinary general meeting ("EGM") held on 28 February 2006, every five shares of HK$0.01 each in the issued and unissued ordinary share capital of the Company are consolidated into one consolidated share HK$0.05 each (the "Share Consolidation"). Subsequently, the authorised share capital of the Company has been increased from HK$20,000,000 divided into 400,000,000 shares of HK$0.05 each to HK$100,000,000 divided into 2,000,000,000 shares of HK$0.05 each by the creation of an additional 1,600,000,000 unissued shares of HK$0.05 each.

(b) Pursuant to an ordinary resolution passed by the shareholders in the EGM held on 28 February 2006, 442,475,040 ordinary shares are issued by way of rights issue on the basis of three rights shares for every one consolidated share of HK$0.05 each at a subscription price of HK$0.057 each. The shares were allotted by the Company on 30 March 2006.

All shares issued during the year rank pari passu with the existing shares in all respects.

## 18. RESERVES

### THE GROUP

| | Share premium | Special reserve | Warrant subscription reserve | Exchange reserve | Employee share-based compensation reserve | Accumulated losses | Total |
|---|---|---|---|---|---|---|---|
| | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* |
| | | | *(note d)* | | *(note c)* | | |
| At 1 January 2005 | 19,323 | 10,084 | – | – | – | (32,695) | (3,288) |
| Issue of share under the placing | 1,518 | – | – | – | – | – | 1,518 |
| Share issue expenses | (137) | – | – | – | – | – | (137) |
| Employee share-based compensation | – | – | – | – | 567 | – | 567 |
| Loss for the year | – | – | – | – | – | (4,913) | (4,913) |
| At 31 December 2005 | 20,704 | 10,084 | – | – | 567 | (37,608) | (6,253) |
| Issue of rights shares | 3,097 | – | – | – | – | – | 3,097 |
| Issue of warrants under the placing | – | – | 1,767 | – | – | – | 1,767 |
| Share/warrants issue expenses | (2,250) | – | (298) | – | – | – | (2,548) |
| Shares issued upon exercise of share options | 1,270 | – | – | – | (567) | – | 703 |
| Employee share-based compensation | – | – | – | – | 2,314 | – | 2,314 |
| Exchange differences arising from consolidation | – | – | – | (24) | – | – | (24) |
| Loss for the year | – | – | – | – | – | (6,273) | (6,273) |
| At 31 December 2006 | 22,821 | 10,084 | 1,469 | (24) | 2,314 | (43,881) | (7,217) |

**THE COMPANY**

| | Share premium *HK$'000* | Contributed surplus *HK$'000* *(note a)* | Warrant subscription reserve *HK$'000* *(note d)* | Employee share-based compensation reserve *HK$'000* *(note c)* | Accumulated losses *HK$'000* | Total *HK$'000* |
|---|---|---|---|---|---|---|
| At 1 January 2005 | 19,323 | 3,047 | – | – | (20,376) | 1,994 |
| Issue of shares under the placing | 1,518 | – | – | – | – | 1,518 |
| Share issue expenses | (137) | – | – | – | – | (137) |
| Employee share-based compensation | – | – | – | 567 | – | 567 |
| Loss for the year | – | – | – | – | (9,063) | (9,063) |
| At 31 December 2005 | 20,704 | 3,047 | – | 567 | (29,439) | (5,121) |
| Issue of rights shares | 3,097 | – | – | – | – | 3,097 |
| Issue of warrants under the placing | – | – | 1,767 | – | – | 1,767 |
| Share/warrants issue expenses | (2,250) | – | (298) | – | – | (2,548) |
| Share issued upon exercise of share options | 1,270 | – | – | (567) | – | 703 |
| Employee share-based compensation | – | – | – | 2,314 | – | 2,314 |
| Loss for the year | – | – | – | – | (5,156) | (5,156) |
| At 31 December 2006 | 22,821 | 3,047 | 1,469 | 2,314 | (34,595) | (4,944) |

(a) The contributed surplus of the Company arose from the Group Reorganisation took place on 15 January 2003. The balance represents the difference between the nominal amount of the Company's shares issued and the consolidated shareholders' fund of KanHan (BVI).

(b) The Company did not have reserves available for distribution to shareholders as at 31 December 2006 (2005: Nil).

(c) Employee share-based compensation reserve represents the fair value of the actual or estimated number of unexercised share options granted to employees recognised in accordance with the accounting policy adopted for share-based compensation as described in note 2(k)(ii) to the financial statements.

(d) On 28 August 2006, the Company entered into a conditional placing agreement in relation to a private placing of 117,800,000 warrants granted to a subscriber at an issued price of HK$0.015 per warrant. The warrants entitle the subscriber to subscribe for new 117,800,000 ordinary shares of par value HK$0.05 at an initial price of HK$0.155 per new share for a period of 18 months commencing from the issue date of the warrants. Each warrant carries the right to subscribe for one new share.

## 19. NET CASH USED IN OPERATING ACTIVITIES

| | 2006 | 2005 |
|---|---|---|
| | *HK$'000* | *HK$'000* |
| OPERATING ACTIVITIES | | |
| Loss before taxation | (6,273) | (4,913) |
| Adjustments for: | | |
| Depreciation | 173 | 206 |
| Exchange difference | (25) | – |
| Loss on disposal of property, plant and equipment | 53 | – |
| Employee share-based compensation | 2,314 | 567 |
| Interest income | (585) | (27) |
| Changes in working capital: | | |
| Increase in trade and other receivables | (2,829) | (511) |
| (Increase) Decrease in inventories | (62) | 200 |
| Increase in trade and other payables | 1,681 | 94 |
| NET CASH USED IN OPERATING ACTIVITIES | (5,553) | (4,384) |

## 20. EMPLOYEE SHARE OPTION SCHEME

On 24 January 2003, a share option scheme was adopted by the Company pursuant to a written resolution of the Company (the "Scheme").

The purpose of the Scheme is to provide eligible employees with performance incentives for continuous and improved service with the Group and to enhance their contributions to increase profits by encouraging capital accumulation and share ownership. The Board of Directors may, at its discretion, invite any full-time employee of the Company, including any executive and non-executive directors of the Company, or any subsidiaries of the Company to take up options to subscribe for shares of the Company. The total number of shares in respect of which options may be granted under the Scheme shall not exceed 10% of the issued share capital of the Company from time to time. The total number of shares of the Company issued and to be issued upon exercise of the options granted to a participant under the Scheme and any other share option scheme adopted by the Company (including both exercised and outstanding options) in any 12-month period must not exceed 1% of the shares of the Company in issue from time to time.

An option may be exercised at any time during a period to be determined and notified by the Board of Directors to each participant. Options might be granted at a consideration of HK$1. Options granted to substantial shareholders or independent non-executive directors in excess of 0.1% of the Company's share capital or with a value in excess of HK$5 million must be approved in advance by the Company's shareholders.

The subscription price for the shares of the Company will be a price determined by the Board of Directors and will be the highest of (i) the closing price of the shares on the GEM as stated in the Stock Exchange's daily quotation on the date of the offer grant; (ii) the average closing price of the shares on the GEM as stated in the Stock Exchange's daily quotations for the five trading days immediately preceding the date of the offer grant; and (iii) the nominal value of the shares.

On 2 February 2006, all 37,000,000 share options granted on 8 July 2005 were exercised by the option holders at an exercise price of HK$0.029 each.

On 5 June 2006, the Company granted share options to certain of its directors and employees at a nominal consideration of HK$1 for each lot of share option to subscribe for an aggregate of 19,400,000 shares under the Scheme at an exercise price of HK$0.21 per share.

**(a)** Movement in the number of share options outstanding during the year is as follows:

| | Number of options 2006 | 2005 |
|---|---|---|
| At 1 January | 37,000,000 | – |
| Exercised on 2 February 2006 | (37,000,000) | – |
| Granted on 5 June 2006 (8 July 2005) | 19,400,000 | 37,000,000 |
| At 31 December | 19,400,000 | 37,000,000 |

**(b)** **Details of share options granted**

| Categories of grantees | Date of grant | Exercise period | Exercise price per share *HK$* | 2006 Number of options | 2005 Number of options |
|---|---|---|---|---|---|
| **Directors** | 8/7/2005 | 8/7/2005-7/7/2015 | 0.029 | – | 14,000,000 |
| | 5/6/2006 | 5/6/2006-4/6/2016 | 0.210 | 8,800,000 | – |
| **Employees** | 8/7/2005 | 8/7/2005-7/7/2015 | 0.029 | – | 23,000,000 |
| | 5/6/2006 | 5/6/2006-4/6/2016 | 0.210 | 10,600,000 | – |
| | | | | 19,400,000 | 37,000,000 |

**(c)** The fair value of services received in return for share options granted are measured by reference to the fair value of share options granted. The estimate of the fair value of the services received is measured based on the Black-Scholes option pricing model. The expected life of the option is used as an input into this model.

| **Fair value of share options and assumptions** | **2006** | **2005** |
|---|---|---|
| Fair value at measurement date | HK$0.1193 | HK$0.0153 |
| Share price at grant date | HK$0.210 | HK$0.027 |
| Exercise price | HK$0.210 | HK$0.029 |
| Expected option life | 3 years | 5 years |
| Expected volatility | 84.66% | 41.76% |
| Expected dividends | – | – |
| Risk-free interest rate (based on Exchange Fund Notes) | 4.6% | 3.78% |

The expected volatility is based on the historic volatility (calculated based on the weighted average remaining life of the share options), adjusted for any expected changes to future volatility due to publicly available information. Expected dividends are based on historical dividends. Changes in the subjective input assumptions could materially affect the fair value estimate.

## 21. RETIREMENT BENEFITS SCHEME

The Group operates a Mandatory Provident Fund Scheme ("Scheme") for all its qualifying employees. The assets of the Scheme are held separately from those of the Group in funds under the control of trustees. Both the Group and each eligible employee contribute the lower of 5% or HK$1,000 of the relevant payroll costs to the Scheme.

## 22. DEFERRED TAX

Recognised deferred tax (assets) liabilities

| | Depreciation allowances | Tax losses | Total |
|---|---|---|---|
| | *HK$'000* | *HK$'000* | *HK$'000* |
| At 1 January 2005 | 33 | (33) | – |
| (Credit) Charge to income | (21) | 21 | – |
| At 31 December 2005 | 12 | (12) | – |
| Charge (Credit) to income | (12) | 12 | – |
| At 31 December 2006 | – | – | – |

Unrecognised deferred tax assets arising from

| | 2006 | 2005 |
|---|---|---|
| | *HK$'000* | *HK$'000* |
| Deductible temporary differences | 47 | – |
| Tax losses | 32,267 | 29,887 |
| At the balance sheet date | 32,314 | 29,887 |

Both the tax losses and the deductible temporary differences do not expire under current tax legislation. Deferred tax assets have not been recognised in respect of these items because it is not probable that future taxable profit will be available against which the Group can utilise the benefits therefrom.

## 23. OPERATING LEASE COMMITMENTS

**The Group as lessee**

At the balance sheet date, the Group had total future minimum lease payments in respect of office premises under non-cancellable operating lease which are payable as follows:

| | THE GROUP | |
|---|---|---|
| | 2006 | 2005 |
| | *HK$'000* | *HK$'000* |
| Within one year | 543 | 281 |
| In the second to fifth years inclusive | 430 | – |
| | 973 | 281 |

## 24. FINANCIAL RISK MANAGEMENT OBJECTIVE AND POLICIES

The Group's principal financial instruments comprise bank balances and cash, trade receivables and trade payables, which arise directly from its business activities.

The Group does not have any written risk management policies and guidelines. However, the board of directors generally adopts conservative strategies on its risk management and limit the Group's exposure to these risks to a minimum.

The main risks arising from the Group's financial instruments are credit risks. The credit risks are managed via the following policies so as to minimise their exposure:

(a) The Group trades only with creditworthy third parties; and

(b) Receivables balances are monitored closely for objective evidence of any potential/existence of loss event.

## 25. POST BALANCE SHEET EVENTS

(a) On 13 February 2007, the Company granted further share options to certain of its directors and employees to subscribe for an aggregate 4,000,000 shares at a nominal consideration of HK$1 for each lot of share option under the Scheme at the exercise price of HK$0.19 per share.

(b) On 2 February 2007, Rise Assets Limited ("Rise Assets", a wholly-owned subsidiary of the Company) entered into a conditional legally binding memorandum of understanding ("MOU") with Mr. Yang Pei Gen ("Mr. Yang"), in which Rise Assets has agreed to acquire and Mr. Yang has agreed to sell: (i) the Sale Share, representing the entire issued share capital of Silky Sky Investments Limited ("Silky Sky"); and (ii) the Sale Loan, representing all obligation, indebtedness and liabilities due by Silky Sky to Mr. Yang, for a total consideration of HK$61,000,000. On 21 March 2007, a formal agreement ("Formal Agreement") was entered into between Rise Assets and Mr. Yang. Details of the MOU and the Formal Agreement were disclosed in the announcements of the Company dated 9 February 2007 and 21 March 2007 respectively.

Sky Rich Investments Limited, a wholly-owned subsidiary of Silky Sky, will be owned as to 51% of interests in Beijing Shiji Jiangshan Resource Recycling Technology Limited ("Shiji Jiangshan"). Shiji Jiangshan, an equity joint venture company established in the PRC, is principally engaged in the production and distribution of organic fertilizer through a technology which converts organic wastes into organic fertilizer.

Deposits HK$20,000,000 were paid by the Company to Mr. Yang as of the date of these financial statements.

## 26. COMPARATIVE FIGURES

Classification of certain revenue has been changed in order to better reflect their significance and nature in the financial statements as follows:

- Revenue from website development of HK$384,000 that was included in revenue from sales of licensed software in the 2005 financial statements has been separately disclosed to conform with the current year's presentation.

- Subscription income of HK$45,000 that was included in revenue from sales of licensed software in the 2005 financial statements has been reclassified to software rental and subscription income to conform with the current year's presentation.

## 3. INTERIM RESULTS

*Set out below is the unaudited financial information of the Group for the three months and six months ended 30 June 2007, together with comparative amounts, as extracted from the interim report 2007 of the Company respectively.*

### UNAUDITED CONDENSED CONSOLIDATED INCOME STATEMENT

*For the three months and six months ended 30 June 2007*

| | | Three months ended 30 June | | Six months ended 30 June | |
|---|---|---|---|---|---|
| | | **2007** | **2006** | **2007** | **2006** |
| | *Notes* | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* |
| Turnover | *3* | 2,385 | 1,651 | 3,777 | 3,066 |
| Cost of sales | | (1,204) | (768) | (1,841) | (1,539) |
| Gross profit | | 1,181 | 883 | 1,936 | 1,527 |
| Other income/(expenses) | | (70) | 250 | 338 | 342 |
| Research and development expenses | | (269) | (287) | (625) | (567) |
| Selling and distribution expenses | | (322) | (290) | (626) | (569) |
| Administrative expenses | | (1,625) | (1,281) | (3,131) | (2,376) |
| Loss before taxation | *5* | (1,105) | (725) | (2,108) | (1,643) |
| Taxation | *6* | – | – | – | – |
| Loss for the period | | (1,105) | (725) | (2,108) | (1,643) |
| Attributable to: | | | | | |
| Equity holders of the Company | | (990) | (725) | (1,993) | (1,643) |
| Minority interests | | (115) | – | (115) | – |
| Loss per share – Basic | *8* | (0.15 cents) | (0.12 cents) | (0.32 cents) | (0.30 cents) |

## UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEET

*As at 30 June 2007*

| | Notes | 30 June 2007 HK$'000 | (Audited) 31 December 2006 HK$'000 |
|---|---|---|---|
| NON-CURRENT ASSETS | | | |
| Fixed assets | | 762 | 158 |
| Intangible assets | 9 | 53,572 | – |
| | | 54,334 | 158 |
| CURRENT ASSETS | | | |
| Inventories | 10 | 153 | 62 |
| Trade and other receivables | 11 | 12,395 | 4,638 |
| Bank balances, deposits and cash | | 12,659 | 22,707 |
| | | 25,207 | 27,407 |
| CURRENT LIABILITIES | | | |
| Trade and other payables | 12 | 7,401 | 3,989 |
| Financial assistance from government | | 336 | 236 |
| | | 7,737 | 4,225 |
| NET CURRENT ASSETS | | 17,470 | 23,182 |
| TOTAL ASSETS LESS CURRENT LIABILITIES | | 71,804 | 23,340 |
| NON-CURRENT LIABILITIES | | | |
| Promissory note | 13 | 24,031 | – |
| Financial assistance from government | | 959 | 1,059 |
| | | 24,990 | 1,059 |
| NET ASSETS | | 46,814 | 22,281 |
| EQUITY AND RESERVES | | | |
| Share capital | | 37,436 | 29,498 |
| Reserves | | 2,815 | (7,217) |
| | | 40,251 | 22,281 |
| MINORITY INTERESTS | | 6,563 | – |
| | | 46,814 | 22,281 |

## UNAUDITED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

*For the six months ended 30 June 2007*

| | Share capital | Share premium | Special reserve | Warrant subscription reserve | Exchange reserve | Employee share-based compensation reserve | Accumulated losses | Total | Minority interests | Total |
|---|---|---|---|---|---|---|---|---|---|---|
| | *HK$'000* | *HK$'000* | *HK$'000* (Note a) | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* |
| **2006** | | | | | | | | | | |
| At 1 January 2006 | 7,004 | 20,704 | 10,084 | – | – | 567 | (37,608) | 751 | – | 751 |
| Exercise of share options | 370 | 1,270 | – | – | – | (567) | – | 1,073 | – | 1,073 |
| Issue of rights shares | 22,124 | 3,097 | – | – | – | – | – | 25,221 | – | 25,221 |
| Share issue expenses | – | (2,250) | – | – | – | – | – | (2,250) | – | (2,250) |
| Loss for the period | – | – | – | – | – | – | (1,643) | (1,643) | – | (1,643) |
| At 30 June 2006 | 29,498 | 22,821 | 10,084 | – | – | – | (39,251) | 23,152 | – | 23,152 |

| | Share capital | Share premium | Special reserve | Warrant subscription reserve | Exchange reserve | Employee share-based compensation reserve | Accumulated losses | Total | Minority interests | Total |
|---|---|---|---|---|---|---|---|---|---|---|
| | *HK$'000* | *HK$'000* | *HK$'000* (Note a) | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* |
| **2007** | | | | | | | | | | |
| At 1 January 2007 | 29,498 | 22,821 | 10,084 | 1,469 | (24) | 2,314 | (43,881) | 22,281 | – | 22,281 |
| Exercise of share options | 150 | 837 | – | – | – | (357) | – | 630 | – | 630 |
| Exercise of warrants | 1,000 | 2,349 | – | (249) | – | – | – | 3,100 | – | 3,100 |
| Issue of consideration shares (Note b) | 6,788 | 10,181 | – | – | – | – | – | 16,969 | – | 16,969 |
| Share issue expenses | – | (744) | – | – | – | – | – | (744) | – | (744) |
| Exchange differences arising from consolidation | – | – | – | – | 8 | – | – | 8 | – | 8 |
| Acquisition of subsidiary | – | – | – | – | – | – | – | – | 6,678 | 6,678 |
| Loss for the period | – | – | – | – | – | – | (1,993) | (1,993) | (115) | (2,108) |
| At 30 June 2007 | 37,436 | 35,444 | 10,084 | 1,220 | (16) | 1,957 | (45,874) | 40,251 | 6,563 | 46,814 |

*Notes:*

(a) The special reserve represents the difference between the nominal amount of shares and share premium of KanHan Technologies Inc. at the date on which it was acquired by the Company and the nominal amount of the Company's shares issued as consideration pursuant to the Group reorganisation taken place in 2003.

(b) The Company issued 135,750,000 shares of HK$0.125 each and credited as fully paid in consideration for acquisition of the entire equity interest in Silky Sky Investments Limited.

**UNAUDITED CONDENSED CONSOLIDATED CASH FLOW STATEMENT**
*For the six months ended 30 June 2007*

| | **Six months ended 30 June 2007** | **Six months ended 30 June 2006** |
|---|---|---|
| | *HK$'000* | *HK$'000* |
| Net cash used in operating activities | (6,472) | (3,595) |
| Net cash used in investing activities | (6,562) | (24) |
| Net cash outflow before financing activities | (13,034) | (3,619) |
| Net cash inflow from financing activities | 2,986 | 24,029 |
| Net increase/(decrease) in cash and cash equivalents | (10,048) | 20,410 |
| Cash and cash equivalents at beginning of the period | 22,707 | 2,253 |
| Cash and cash equivalents at end of the period | 12,659 | 22,663 |

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

### 1. GENERAL

The Company was incorporated in the Cayman Islands on 10 October 2002 as an exempted company with limited liability under the Companies Law (Revised) of the Cayman Islands. The shares of the Company were listed on the GEM of the Stock Exchange on 25 February 2003.

The Company and its subsidiaries are principally engaged in developing and marketing patented server based technology for its real time on-line communication software platform for the Chinese language. The Company is also engaged in the provision of software related services. In addition, the Group is engaged in the production and distribution of organic fertilizer through a technology which converts organic waste into organic fertilizer.

### 2. BASIS OF PREPARATION

The unaudited consolidated results have been prepared in accordance with Hong Kong Financial Reporting Standards and Hong Kong Accounting Standards issued by the Hong Kong Institute of Certified Public Accountants, accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. The measurement basis used in the preparation of these unaudited consolidated results is historical cost.

The accounting policies adopted in preparing the unaudited consolidated results are consistent with those followed in the preparation of the annual financial statements for the year ended 31 December 2006.

### 3. TURNOVER

Turnover comprises revenue from the following activities in the Group's server-based language technology business:

| | Three months ended 30 June | | Six months ended 30 June | |
|---|---|---|---|---|
| | **2007** | **2006** | **2007** | **2006** |
| | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* |
| Sales of licensed software | 1,617 | 1,280 | 2,604 | 2,263 |
| Software maintenance | 181 | 191 | 367 | 375 |
| Software rental and subscription income | 112 | 60 | 160 | 124 |
| Website development | 329 | – | 329 | 148 |
| Putonghua learning platform | 146 | 120 | 317 | 156 |
| | 2,385 | 1,651 | 3,777 | 3,066 |

## 4. SEGMENT INFORMATION

### (a) Business segments

The following tables present revenue, results and certain assets, liabilities and expenditure information for the Group's business segments.

| | Six months ended 30 June, | | | | | |
|---|---|---|---|---|---|---|
| | Server-based technology and related products | | Production and distribution of organic fertilizer | | Consolidated | |
| | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 |
| | (Unaudited) | (Unaudited) | (Unaudited) | (Unaudited) | (Unaudited) | (Unaudited) |
| | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* |
| Turnover | 3,777 | 3,066 | – | – | 3,777 | 3,066 |
| Segment results | (934) | (1,121) | (235) | – | (1,169) | (1,121) |
| Other income | | | | | 255 | 342 |
| Unallocated expenses | | | | | (1,194) | (864) |
| Loss before taxation | | | | | (2,108) | (1,643) |
| Taxation | | | | | – | – |
| Loss for the period | | | | | (2,108) | (1,643) |

| | As at 30 June, | | | | | |
|---|---|---|---|---|---|---|
| | Server-based technology and related products | | Production and distribution of organic fertilizer | | Consolidated | |
| | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 |
| | (Unaudited) | (Unaudited) | (Unaudited) | (Unaudited) | (Unaudited) | (Unaudited) |
| | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* |
| Assets | | | | | | |
| Segment assets | 1,775 | 1,409 | 17,583 | – | 19,358 | 1,409 |
| Unallocated assets | | | | | 60,183 | 25,120 |
| Total assets | | | | | 79,541 | 26,529 |
| Liabilities | | | | | | |
| Segment liabilities | 4,744 | 3,082 | 3,712 | – | 8,456 | 3,082 |
| Unallocated liabilities | | | | | 24,271 | 295 |
| Total liabilities | | | | | 32,727 | 3,377 |

**(b) Geographical segments**

For the six months ended 30 June 2007, the Group's turnover and operating assets are located in the Special Administrative Region of Hong Kong and other regions in the People's Republic of China ("PRC"). Accordingly, no analysis by geographical segments is included in these financial statements.

**5. LOSS BEFORE TAXATION**

This is stated after charging:

| | Three months ended 30 June | | Six months ended 30 June | |
|---|---|---|---|---|
| | **2007** | **2006** | **2007** | **2006** |
| | *HK$'000* | *HK$'000* | *HK$'000* | *HK$'000* |
| Depreciation | 33 | 45 | 64 | 95 |

**6. TAXATION**

No provision for taxation has been made as the Group had no assessable profit for the six months ended 30 June 2007 (2006: Nil).

**7. DIVIDEND**

The Board does not recommend the payment of an interim dividend for the three months and six months ended 30 June 2007 respectively (2006: Nil).

**8. LOSS PER SHARE**

The computation of the basic loss per share for the three months ended 30 June 2007 is based on the loss for the period of approximately HK$990,000 (2006: HK$725,000) and on the weighted average number of 663,738,698 shares (2006: 589,966,720 shares).

The computation of the basic loss per share for the six months ended 30 June 2007 is based on the loss for the period of approximately HK$1,993,000 (2006: HK$1,643,000) and on the weighted average number of 627,056,499 shares (2006: 551,293,393 shares).

No diluted loss per share was presented as the exercise of the outstanding share options and the conversion of the outstanding warrants of the Company are anti-dilutive.

**9. INTANGIBLE ASSETS**

Intangible assets represent the goodwill arising on the acquisition of the entire equity interest in Silky Sky Investments Limited and its subsidiaries.

**10. INVENTORIES**

Inventories comprise finished goods and are stated at cost.

## 11. TRADE AND OTHER RECEIVABLES

| | The Group | |
|---|---|---|
| | **30 June 2007** | **31 December 2006** |
| | *HK$'000* | *HK$'000* |
| Trade receivables | 1,414 | 775 |
| Deposits, prepayments and other receivables | 10,981 | 3,863 |
| | 12,395 | 4,638 |

The Group has a policy of allowing a credit period from 30 to 120 days to its trade customers. The aging analysis of the trade receivables is as follows:

| | The Group | |
|---|---|---|
| | **30 June 2007** | **31 December 2006** |
| | *HK$'000* | *HK$'000* |
| 0-30 days | 361 | 175 |
| 31-60 days | 791 | 559 |
| 61-90 days | 83 | 10 |
| Over 90 days | 179 | 31 |
| | 1,414 | 775 |

## 12. TRADE AND OTHER PAYABLES

| | The Group | |
|---|---|---|
| | **30 June 2007** | **31 December 2006** |
| | *HK$'000* | *HK$'000* |
| Trade payables | 273 | 269 |
| Accrued charges and other creditors | 7,128 | 3,720 |
| | 7,401 | 3,989 |

The Group has an average credit period ranging from 30 to 90 days from its trade creditors. The aging analysis of the trade payables is as follows:

| | The Group | |
|---|---|---|
| | **30 June 2007** | **31 December 2006** |
| | *HK$'000* | *HK$'000* |
| 0-30 days | 152 | 126 |
| 31-60 days | 55 | 31 |
| 61-90 days | 53 | 112 |
| Over 90 days | 13 | – |
| | 273 | 269 |

**13. PROMISSORY NOTE**

On 21 May 2007, the Company issued a promissory note with a face amount of HK$24,031,250 to Mr. Yang Pei Gen in respect of the acquisition of the entire equity interest in Silky Sky Investments Limited. The promissory note is interest bearing at 2% per annum and is repayable within two years from the date of issuance.

## 4. INDEBTEDNESS

### Borrowings

As at the close of business on 30 November 2007, being the latest practicable date for the purpose of this statement of indebtedness prior to the printing of this circular, the Enlarged Group had outstanding borrowings of approximately HK$8,401,000, details of which are set out below:

| | *HK$'000* |
|---|---|
| Financial assistance from government (unsecured) | 1,295 |
| Promissory notes | 7,106 |
| | 8,401 |

As at 30 November 2007, the Enlarged Group had outstanding borrowings and debts of other loan of approximately HK$1,295,000 due to the HKSAR Government. The Innovation and Technology Fund ("ITF") of the HKSAR Government has provided financial assistance to the Group to assist in a specific product development. The funding is unsecured, non-interest bearing and repayable to ITF when revenue is generated from the specific product.

The Company issued a promissory note with a face amount of HK$24,031,250 which is interest bearing at 2% per annum and matures on 20 May 2009. As at 30 November 2007, the Company had outstanding promissory note of approximately HK$7,105,993 of which a total of approximately HK$74,743 was the accrued interest.

### Commitments

As at 30 November 2007, the Enlarged Group had operating lease commitments and capital commitments of approximately HK$474,810 and RMB22,154,587 respectively.

### Disclaimer

Save as aforesaid and apart from intra-group liabilities, at the close of business on 30 November 2007, the Enlarged Group had no other outstanding mortgages, charges, debentures or other loan capital or bank overdrafts or loans or other similar indebtedness, finance lease or hire purchase commitments, liabilities under acceptance or acceptance credits, debt securities, guarantees or other material contingent liabilities.

## 5. MATERIAL ADVERSE CHANGE

As at the Latest Practicable Date, the Directors are not aware of any material adverse change in the financial or trading position of the Group since 31 December 2006, the date to which the latest published audited financial statements of the Group were made up.

## 6. WORKING CAPITAL

After due and careful consideration, the Directors are of the opinion that, taking into account the Enlarged Group's internal resources, the existing banking facilities available and the estimated net proceeds of the Open Offer, the Enlarged Group has sufficient working capital for its present requirements in the next twelve months from the date of this circular.

*The following is the text of a report, prepared for the sole purpose of inclusion in this circular, received from the independent reporting accountants, Vision A. S. Limited.*

***Vision A. S. Limited*** **Certified Public Accountants**
**泓信會計師行有限公司**

18 January 2008

The Board of Directors
KanHan Technologies Group Limited
15/F., Sun House
181 Des Voeux Road Central
Hong Kong

Dear Sirs,

We report on the unaudited pro forma statement of assets and liabilities (the "Unaudited Pro Forma Financial Information") of KanHan Technologies Group Limited (the "Company") and its subsidiaries (hereinafter collectively referred to as the "Group") and Proud Dragon Limited (the "Target") and its subsidiaries (the "Target Group") (together with the Group hereinafter referred to as the "Enlarged Group") which has been prepared by the directors of the Company for illustrative purposes only, to provide information about how the proposed acquisition of the Target might have affected the financial information presented, for inclusion as APPENDIX IV to the circular of the Company dated 18 January 2008 (the "Circular"). The basis of preparation of the Unaudited Pro Forma Financial Information is set out on pages 102 to 107 to the Circular.

**RESPECTIVE RESPONSIBILITIES OF DIRECTORS OF THE COMPANY AND REPORTING ACCOUNTANTS**

It is the responsibility solely of the directors of the Company to prepare the Unaudited Pro Forma Financial Information in accordance with rule 7.31 of the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (the "GEM Listing Rules") and with reference to Accounting Guideline 7 "Preparation of Pro Forma Financial Information for Inclusion in Investment Circulars" issued by the Hong Kong Institute of Certified Public Accountants.

It is our responsibility to form an opinion, as required by rule 7.31(7) of the GEM Listing Rules, on the Unaudited Pro Forma Financial Information and to report our opinion to you. We do not accept any responsibility for any reports previously given by us on any financial information used in the compilation of the Unaudited Pro Forma Financial Information beyond that owed to whom those reports were addressed by us at the dates of their issue.

## BASIS OF OPINION

We conducted our engagement in accordance with Hong Kong Standard on Investment Circular Reporting Engagements ("HKSIR") 300 "Accountants' Reports on Pro Forma Financial Information in Investment Circulars" issued by the Hong Kong Institute of Certified Public Accountants. Our work consisted primarily of comparing the unadjusted financial information with source documents, considering the evidence supporting the adjustments and discussing the Unaudited Pro Forma Financial Information with the directors of the Company. This engagement did not involve independent examination of any of the underlying financial information.

We planned and performed our work so as to obtain the information and explanations we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Unaudited Pro Forma Financial Information has been properly compiled by the directors of the Company on the basis stated, that such basis is consistent with the accounting policies of the Group and that the adjustments are appropriate for the purpose of the Unaudited Pro Forma Financial Information as disclosed pursuant to rule 7.31(1) of the GEM Listing Rules.

The Unaudited Pro Forma Financial Information is for illustrative purpose only, based on the judgements and assumptions of the directors of the Company, and, because of its hypothetical nature, does not provide any assurance or indication that event will take place in the future and may not be indicative of the financial position of the Enlarged Group as at 30 June 2007 or any future date.

## OPINION

In our opinion:

- the Unaudited Pro Forma Financial Information has been properly compiled by the directors of the Company on the basis stated;
- such basis is consistent with the accounting policies of the Group; and
- the adjustments are appropriate for the purpose of the Unaudited Pro Forma Financial Information as disclosed pursuant to rule 7.31(1) of the GEM Listing Rules.

Yours faithfully,
**Vision A. S. Limited**
*Certified Public Accountants*
*Hong Kong*

**Cheung Man Yau, Timothy**
Practising Certificate No.: P01417

## INTRODUCTION TO THE UNAUDITED PRO FORMA FINANCIAL INFORMATION ON THE ENLARGED GROUP

The following unaudited pro forma financial information of the Enlarged Group as if the Acquisition has been completed on 30 June 2007, has been prepared based on the unaudited consolidated financial statements of the Group for the six months ended 30 June 2007 and the financial information of the Target Group for the period ended 30 September 2007. The unaudited financial statements of the Group has included the financial result of Silky Sky as the acquisition of Silky Sky was completed in May 2007. The accompanying unaudited pro forma financial information of the Enlarged Group has been prepared to illustrate the effect of the proposed acquisition of the Target at a consideration of HK47,600,000.

The accompanying unaudited pro forma financial information of the Enlarged Group is based on a number of assumptions, estimates, uncertainties and currently available information, and is provided for illustrative purposes. Accordingly, as a result of the uncertain nature of the accompanying unaudited pro forma financial information of the Enlarged Group, it may not give a true picture of the actual financial position or results of the Enlarged Group's operations that would have been attained had the Proposed Acquisition actually occurred on the dates indicated herein. Further, the accompanying unaudited pro forma financial information of the Enlarged Group does not purport to predict the Enlarged Group's future financial position or results of operations.

The unaudited pro forma financial information of the Enlarged Group should be read in conjunction with the Accountants' Reports of Proud Dragon and Zhong Tian Water Supply as set out in Appendix I and II and other financial information included elsewhere in this Circular.

## UNAUDITED PRO FORMA FINANCIAL STATEMENT ON THE ENLARGED GROUP

| | The Group As at 30 June 2007 HK$'000 | Proud Dragon Group As at 30 September 2007 HK$'000 | Zhong Tian As at 30 September 2007 HK$'000 | Pro-forma adjustments HK$'000 | Notes | Total HK$'000 |
|---|---|---|---|---|---|---|
| **NON-CURRENT ASSETS** | | | | | | |
| Property, plant and equipment | 762 | – | 49,377 | – | | 50,139 |
| Prepaid land lease payments | – | – | 695 | – | | 695 |
| Goodwill | 53,572 | – | – | 34,064 | *(8)* | 87,636 |
| | 54,334 | – | 50,072 | 34,064 | | 138,470 |
| **CURRENT ASSETS** | | | | | | |
| Inventories, at cost | 153 | – | – | – | | 153 |
| Accounts receivable | 1,414 | – | 158 | – | | 1,572 |
| Prepayments, deposits and other receivable | 10,981 | – | 1,047 | – | | 12,028 |
| Prepaid land lease payments | – | – | 25 | – | | 25 |
| Bank balances and cash | 12,659 | – | 1,110 | (6,200) | *(2)* | 7,569 |
| | 25,207 | – | 2,340 | (6,200) | | 21,347 |
| **CURRENT LIABILITIES** | | | | | | |
| Accounts payable | 273 | 23 | 17,341 | – | | 17,637 |
| Deposits received, accruals and other payables | 7,128 | – | 5,149 | – | | 12,277 |
| Due to a director | – | – | 1,156 | – | | 1,156 |
| Due to shareholders | – | – | 1,057 | 600 | *(7)* | 1,657 |
| Financial assistance from government | 336 | – | 568 | – | | 904 |
| | 7,737 | 23 | 25,271 | 600 | | 33,631 |
| **NET CURRENT ASSETS/(LIABILITIES)** | 17,470 | (23) | (22,931) | (6,800) | | (12,284) |
| **TOTAL ASSETS LESS CURRENT LIABILITIES** | 71,804 | (23) | 27,141 | 27,264 | | 126,186 |
| **NON-CURRENT LIABILITIES** | | | | | | |
| Financial assistance from government | 959 | – | 22,975 | – | | 23,934 |
| Convertible bonds | – | – | – | 8,432 | *(3)* | 8,432 |
| Promissory note | 24,031 | – | – | 15,600 | *(4)* | 39,631 |
| | 24,990 | – | 22,975 | 24,032 | | 71,997 |
| **NET ASSETS/(LIABILITIES)** | **46,814** | **(23)** | **4,166** | **3,232** | | **54,189** |
| **CAPITAL AND RESERVES** | | | | | | |
| Share Capital | 37,436 | – | 7,368 | (7,368) | *(5)* | 37,436 |
| Reserves | 2,815 | (23) | (3,202) | 4,793 | *(6)* | 4,383 |
| | 40,251 | (23) | 4,166 | (2,575) | | 41,819 |
| **MINORITY INTERESTS** | 6,563 | – | – | 5,807 | *(9)* | 12,370 |
| **TOTAL EQUITY** | **46,814** | **(23)** | **4,166** | **3,232** | | **54,189** |

*Notes:*

1. Under HKFRS 3 Business Combinations ("HKFRS 3"), the Group will apply the purchase method to account for the acquisition of the Target Group. In applying the purchase method, the identifiable assets, liabilities and contingent liabilities of Proud Dragon Group will be recorded on the consolidated balance sheet of the Group at their fair values at the date of completion. Any goodwill or discount arising on the acquisition will be determined as the excess or deficit of the purchase price to be incurred by the group over the Group's interests in the net fair value of the identifiable assets, liabilities and contingent liabilities of Proud Dragon Group at the date of completion. Negative goodwill resulting from the business combinations should be recognized immediately in the consolidated income statement.

   The total consideration of HK$47,600,000 comprises the Sale Consideration and the Subscription Consideration for the Proposed Acquisition:

   (i) The Sale Consideration of HK$31,800,000 shall be settled in the following manner:

      (a) HK$6,200,000 as deposits which have already been paid by the Purchaser to the Vendor at of the date of this circular;

      (b) HK$10,000,000 Convertible Bond to be issued by the Company to the Vendor upon Completion; and

      (c) HK$15,600,000 Promissory Note to be issued by the Company to the Vendor upon Completion.

   (ii) The Subscription Consideration of HK$15,800,000 shall be settled in cash upon the conditions (c) and (h) under the sub-section headed "Conditions precedent" having been fulfilled.

2. The pro forma adjustment of HK$6,200,000 represents the payment as deposits for the Sale Consideration as described in note (1)(i)(a) above.

3. The Convertible Bonds are to be issued as described in note 1(i)(b) above. Under Hong Kong Accounting Standards 32 and 39, the liability and equity component of convertible bonds are accounted for separately. The liability component is calculated at the discounted present value of the cash flows of future principal and interest payments at the market rate of interest applicable to similar liabilities that do not have a conversion option. The equity component is calculated as the excess of the issued proceeds over the liability component.

   The present value of the liability component is approximately HK$8,432,000, with the balance of HK$1,568,000 accounted for as a component of equity.

4. The pro forma adjustment of HK$15,600,000 represents the issuance of Promissory Note to the Vendor as described in note 1(i)(c) above.

5. The pro forma adjustment of approximately HK$7,368,000 represents the elimination of share capital of Proud Dragon Group and Zhong Tian Water Supply on consolidation.

6. The pro forma adjustment of approximately HK$4,793,000 represents the equity component of Convertible Bond amounting to approximately HK$1,568,000 and elimination of the pre-acquisition reserves of Proud Dragon Group and Zhong Tian Water Supply on consolidation of approximately HK$3,225,000.

7. The pro forma adjustment of approximately HK$600,000 represents the capital commitments arising from acquisition of 5.7% equity interest in Zhong Tian Water Supply from the minority shareholders.

   As disclosed in note 11 to the Accountant's Report of Proud Dragon, the total capital contributions payable to Zhong Tian Water Supply is RMB15,000,000 (equivalent to approximately HK$15,789,000), of which RMB570,000 (equivalent to approximately HK$600,000) will be paid to the minority shareholders.

After completion of the Acquisition and fulfillment of conditions (c) and (h) under the sub-section headed "Conditions precedent" further described on page 9 of the Circular, the capital commitment payable to Zhong Tian Water Supply will be satisfied by the Subscription Consideration of HK$15,800,000 in cash paid by the Company to Proud Dragon for the allotment of Subscription Shares, which resulted in an increase in Share Capital of Proud Dragon and an increase in Investment in subsidiaries in the books of Proud Dragon.

8. The pro forma adjustment of approximately HK$31,823,000 and HK$2,241,000 represents goodwill arising from the acquisition of Proud Dragon Group and Zhong Tian Water Supply respectively, which are arrived as follows:

| **Acquisition of Proud Dragon** | *HK$'000* |
|---|---|
| Sale Consideration for the acquisition of Proud Dragon Group | 31,800 |
| Add: share of net identifiable liabilities of Proud Dragon Group | 23 |
| | 31,823 |

| **Acquisition of Zhong Tian Water Supply** | *HK$'000* |
|---|---|
| Capital commitments on the acquisition of Zhong Tian Water Supply as disclosed in note 7 above | 15,789 |
| Less: share of 70% the net identifiable assets of Zhong Tian Water Supply | (2,916) |
| share of 70% of the capital contribution | (10,632) |
| | 2,241 |

9. The pro forma adjustment of approximately HK$5,807,000 represents the minority shareholder's share of 30% of the net identifiable assets of Zhong Tian Water Supply upon fulfilment of the capital contribution.

*The following is the accountant's report on Silky Sky received from Cheung & Siu as extracted from the circular of the Company dated 20 April 2007. Such accountants' report is incorporated to this circular pursuant to Rule 31(3)(b) of Appendix 1B of GEM Listing Rules.*

Cheung & Siu **Certified Public Accountants**
張、蕭會計師事務所

20 April 2007

The Board of Directors
KanHan Technologies Group Limited
15/F., Sun House
181 Des Voeux Road Central
Hong Kong

Dear Sirs,

We set out below our report on the financial information regarding Silky Sky Investments Limited ("Silky Sky") and its subsidiaries (hereinafter collectively referred to as the "Silky Sky Group") for the period from 18 August 2006 (date of incorporation of Silky Sky) to 31 December 2006 and for the two months ended 28 February 2007 (the "Relevant Periods") for inclusion in the circular of KanHan Technologies Group Limited (the "Company") dated 20 April 2007 (the "Circular") in connection with the proposed acquisition of the entire issued share capital of Silky Sky (the "Acquisition") by Rise Assets Limited, a wholly-owned subsidiary of the Company.

Silky Sky was incorporated in the British Virgin Islands on 18 August 2006 with limited liability and acts as an investment holding company. The registered office of Silky Sky is located at P.O. Box 957, Offshore Incorporations Centre, Road Town, Tortola, British Virgin Islands. As at the date of this report, Silky Sky is wholly and beneficially owned by Mr. Yang Pei Gen.

Sky Rich Limited ("Sky Rich") was incorporated in Hong Kong on 16 May 2006 with limited liability and with an authorised share capital of HK$10,000 divided into 10,000 shares of HK$1 each. Silky Sky has become the holding company of Sky Rich since Silky Sky acquired one share, representing the entire issued share capital, of Sky Rich on 10 October 2006. The principal activity of Sky Rich is investment holding.

On 23 November 2006, Sky Rich entered into an agreement with 渭南豐光科技有限責任公司 (Wei Nan Feng Guang Science and Technology Limited Liability Company#) ("Wei Nan"), to form an equity joint venture company named Beijing Shiji Jiangshan Resource Recycling Technology Ltd ("Beijing Shiji") in the People's Republic of China ("PRC"). Beijing Shiji was established on 25 December 2006 with a registered capital of RMB30 million. Pursuant to the joint venture agreement, Sky Rich agreed to invest RMB22.5 million, representing 75% of the registered capital whereas Wei Nan agreed to invest RMB7.5 million, representing 25% of the registered capital. As at the date of this report, Sky Rich has made capital contribution of HK$9,530,000 to Beijing Shiji.

\# *English translation of company names are for identification purpose only*

On 22 January 2007, Sky Rich entered into a share transfer agreement with Fortune Pacific Limited ("Fortune Pacific"). Pursuant to the agreement, Sky Rich agreed to sell and transfer 24% equity interest of Beijing Shiji to Fortune Pacific at a consideration of RMB7.2 million of which RMB1.44 million will be paid to Sky Rich and RMB5.76 million will be contributed to Beijing Shiji directly as further capital investment. Sky Rich's equity interest in Beijing Shiji will be decreased from 75% to 51% upon the completion of the share transfer. The share transfer was completed on 21 March 2007.

As at the date of this report, Silky Sky has interests in the following subsidiaries:

| Name of subsidiaries | Place and date of incorporation/ registration | Nominal value of issued/ registered capital | Attributable equity interest held by Silky Sky | Principal activities |
|---|---|---|---|---|
| Sky Rich Limited | Hong Kong 16 May 2006 | HK$1 | 100% (directly) | Investment holding |
| Beijing Shiji Jiangshan Resource Recycling Technology Ltd* | PRC 25 December 2006 | RMB30,000,000 | 51% (indirectly) | Waste recycling and production and distribution of organic fertilizer |

* *This subsidiary is a joint venture company with a registered capital of RMB30 million. Sky Rich had injected a capital of RMB9.5 million as at the date of this report.*

All companies of Silky Sky Group have adopted 31 December as their financial year end date.

Up to the date of this report, no audited financial statements have been prepared for the companies comprising the Silky Sky Group as they were either incorporated/established shortly before 28 February 2007 or are not subject to statutory audit requirements under the relevant rules and regulations in their jurisdictions of incorporation.

For the purpose of this report, the directors of Silky Sky have prepared the consolidated financial statements of the Silky Sky Group for the Relevant Periods (the "Underlying Financial Statements") in accordance with Hong Kong Financial Reporting Standards ("HKFRSs"), which also include all Hong Kong Accounting Standards ("HKASs") and Interpretations issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA"). For the purpose of this report, we have performed independent audit procedures on the Underlying Financial Statements in accordance with Hong Kong Standards on Auditing issued by the HKICPA.

The financial information for the Relevant Periods (the "Financial Information") set out in Sections A to B below has been prepared by the directors of Silky Sky based on the Underlying Financial Statements. We have examined the Financial Information and have carried out such additional procedures as are necessary in accordance with the Auditing Guideline 3.340 "Prospectuses and the Reporting Accountant" as recommended by the HKICPA.

The preparation of the Underlying Financial Statements and the Financial Information which give a true and fair view is the responsibility of the directors of Silky Sky. In preparing the Underlying Financial Statements and the Financial Information, it is fundamental that appropriate accounting policies are selected and applied consistently. The directors of the Company are responsible for the contents of the Circular in which this report is included. It is our responsibility to form an independent opinion, based on our examination, on the Financial Information and to report our opinion to you.

In our opinion, the Financial Information gives, for the purpose of this report, a true and fair view of the state of affairs of Silky Sky and of Silky Sky Group as at 31 December 2006 and 28 February 2007 and of the consolidated results and cash flows of Silky Sky Group for each of the Relevant Periods.

## A. FINANCIAL INFORMATION

### CONSOLIDATED INCOME STATEMENTS

| | Notes | Period from 18 August 2006 (date of incorporation) to 31 December 2006 HK$ | Two months ended 28 February 2007 HK$ |
|---|---|---|---|
| TURNOVER | 5 | – | – |
| Cost of sales | | – | – |
| Gross profit | | – | – |
| Other revenue | 5 | 6,059 | 770 |
| Administrative expenses | | (22,853) | (886,803) |
| LOSS BEFORE TAXATION | 6 | (16,794) | (886,033) |
| Tax | 8 | – | – |
| LOSS FOR THE PERIOD | | (16,794) | (886,033) |
| Attributable to: | | | |
| Equity holders of Silky Sky | | (16,794) | (664,482) |
| Minority interest | | – | (221,551) |
| | | (16,794) | (886,033) |

## CONSOLIDATED BALANCE SHEETS

| | Notes | As at 31 December 2006 HK$ | As at 28 February 2007 HK$ |
|---|---|---|---|
| NON-CURRENT ASSETS | | | |
| Property, plant and equipment | 9 | – | 228,618 |
| Total non-current assets | | – | 228,618 |
| CURRENT ASSETS | | | |
| Prepayments | 11 | – | 2,061,360 |
| Other receivables | 12 | – | 960,075 |
| Cash and bank balances | 13 | 5,557 | 5,206,524 |
| Total current assets | | 5,557 | 8,227,959 |
| CURRENT LIABILITIES | | | |
| Accrued liabilities and other payables | | 22,343 | 22,343 |
| Due to the shareholder | 14 | – | 9,256,721 |
| Total current liabilities | | 22,343 | 9,279,064 |
| NET CURRENT LIABILITIES | | (16,786) | (1,051,105) |
| Net liabilities | | (16,786) | (822,487) |
| EQUITY | | | |
| Issued capital | 15 | 8 | 8 |
| Reserves | | (16,794) | (600,944) |
| Equity attributable to equity holders of Silky Sky | | (16,786) | (600,936) |
| Minority interest | | – | (221,551) |
| Total equity | | (16,786) | (822,487) |

**BALANCE SHEETS**

| | Notes | As at 31 December 2006 HK$ | As at 28 February 2007 HK$ |
|---|---|---|---|
| NON-CURRENT ASSETS | | | |
| Investments in subsidiaries | *10* | 1 | 1 |
| CURRENT ASSETS | | | |
| Due from a subsidiary | *10* | – | 9,530,000 |
| Cash and bank balances | *13* | 7 | 7 |
| | | 7 | 9,530,007 |
| CURRENT LIABILITIES | | | |
| Accrued liabilities and other payables | | 7,500 | 7,500 |
| Due to the shareholder | *14* | – | 9,530,000 |
| | | 7,500 | 9,537,500 |
| NET CURRENT LIABILITIES | | (7,493) | (7,493) |
| Net liabilities | | (7,492) | (7,492) |
| EQUITY | | | |
| Issued capital | *15* | 8 | 8 |
| Reserves | *16* | (7,500) | (7,500) |
| Total equity | | (7,492) | (7,492) |

## CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

| | Issued capital | Exchange reserve | Accumulated losses | Minority interest | Total |
|---|---|---|---|---|---|
| | *HK$* | *HK$* | *HK$* | *HK$* | *HK$* |
| Issue of shares upon incorporation | 8 | – | – | – | 8 |
| Loss for the period | – | – | (16,794) | – | (16,794) |
| At 31 December 2006 and at 1 January 2007 | 8 | – | (16,794) | – | (16,786) |
| Exchange realignment | – | 80,332 | – | – | 80,332 |
| Loss for the period | – | – | (664,482) | (221,551) | (886,033) |
| At 28 February 2007 | 8 | 80,332 | (681,276) | (221,551) | (822,487) |

## CONSOLIDATED CASH FLOW STATEMENTS

| | Period from 18 August 2006 (date of incorporation) to 31 December 2006 | Two months ended 28 February 2007 |
|---|---|---|
| | *HK$* | *HK$* |
| OPERATING ACTIVITIES | | |
| Loss before tax | (16,794) | (886,033) |
| Adjustments for: | | |
| Depreciation | – | 7,071 |
| Interest income | (6,059) | (770) |
| Operating cash flows before movements in working capital | (22,853) | (879,732) |
| Increase in prepayments | – | (2,061,360) |
| Increase in other receivables | – | (960,075) |
| Increase in accrued liabilities and other payables | 22,343 | – |
| Cash used in operations | (510) | (3,901,167) |
| Interest paid | – | – |
| NET CASH USED IN OPERATING ACTIVITIES | (510) | (3,901,167) |
| INVESTING ACTIVITIES | | |
| Interest received | 6,059 | 770 |
| Purchases of items of property, plant and equipment | – | (235,689) |
| Increase in amount due to the shareholder | – | 9,256,721 |
| NET CASH FROM INVESTING ACTIVITIES | 6,059 | 9,021,802 |
| FINANCING ACTIVITIES | | |
| Proceeds from issue of shares | 8 | – |
| NET CASH FROM FINANCING ACTIVITIES | 8 | – |
| NET INCREASE IN CASH AND CASH EQUIVALENTS | 5,557 | 5,120,635 |
| Cash and cash equivalents at beginning of period | – | 5,557 |
| Effect of foreign exchange rate changes, net | – | 80,332 |
| CASH AND CASH EQUIVALENTS AT END OF PERIOD | 5,557 | 5,206,524 |
| ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS | | |
| – Cash and bank balances | 5,557 | 5,206,524 |

## B. NOTES TO THE FINANCIAL INFORMATION

### 1. GENERAL INFORMATION AND BASIS OF PRESENTATION OF FINANCIAL INFORMATION

Silky Sky is a limited liability company incorporated in the British Virgin Islands. The registered office of Silky Sky is located at P.O. Box 957, Offshore Incorporation Centre, Road Town, Tortola, British Virgin Islands.

Silky Sky and its subsidiaries are engaged in investment holding, waste recycling and production and distribution of organic fertilizer during the Relevant Periods.

The Financial Information has been prepared on a going concern basis because Rise Assets Limited (a wholly-owned subsidiary of the Company) who will become the controlling shareholder of Silky Sky upon completion of the Acquisition, will provide adequate funds to ensure Silky Sky to meet its financial obligations as they fall due for the foreseeable future.

### 2. ADOPTION OF NEW OR REVISED STANDARDS

The Financial Information has been prepared in accordance with HKFRSs issued by the HKICPA, accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. The Financial Information has been prepared under the historical cost convention.

New HKFRSs issued but not yet effective are not early adopted. The directors of Silky Sky Group anticipate that the application of these new HKFRSs will have no material impact on the Financial Information.

### 3. PRINCIPAL ACCOUNTING POLICIES

#### (a) Basis of consolidation

The consolidated financial statements incorporate the financial statements of Silky Sky and its subsidiaries for the Relevant Periods. The results of subsidiaries are consolidated from the date of acquisition, being the date on which Silky Sky Group obtains control, and continue to be consolidated until the date that such control ceases.

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

All significant inter-company transactions and balances within the Silky Sky Group are eliminated on consolidation.

Minority interests in the net assets of consolidated subsidiaries are presented separately from the Silky Sky Group's equity therein. Losses applicable to the minority in excess of the minority's interest in the subsidiary's equity are allocated against the interests of the Silky Sky Group except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses.

#### (b) Subsidiaries

A subsidiary is an entity over which Silky Sky has the power to control the financial and operating policies, directly or indirectly, so as to obtain benefits from its activities.

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

**(c) Impairment of assets**

Where an indication of impairment exists, or when annual impairment testing for an asset is required, the asset's recoverable amount is estimated. An asset's recoverable amount is calculated as 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 group of assets, in which case, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

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

An assessment is made at each balance sheet date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If any such indication exists, the asset's recoverable amount is estimated. A previously recognised impairment loss of an asset other than goodwill is reversed only if there has been a change in the estimates used to determine the recoverable amount of that asset, however not to an amount higher than the carrying amount that would have been determined net of any depreciation, had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is credited to the income statement in the period in which it arises.

**(d) Related parties**

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

(i) directly, or indirectly through one or more intermediaries, the party

– controls, is controlled by, or is under common control with, the Silky Sky Group;

– has an interest in the Silky Sky Group that gives it significant influence over the Silky Sky Group; or

– has joint control over the Silky Sky Group;

(ii) the party is a jointly-controlled entity;

(iii) the party is a member of the key management personnel of the Silky Sky Group;

(iv) the party is a close member of the family of any individual referred to in (i) or (iii) above;

(v) the party is an entity that is controlled, jointly controlled or significantly influenced by or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (iii) or (iv) above; or

(vi) the party is a post-employment benefit plan for the benefit of the employees of the Silky Sky Group, or of any entity that is a related party of the Silky Sky Group.

**(e) Property, plant and equipment and depreciation**

Property, plant and equipment are stated at cost less accumulated depreciation and any impairment losses.

The cost of an item of property, plant and equipment comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditure incurred after items of property, plant and equipment have been put into operation, such as repairs and maintenance, is normally charged to the income statement in the period in which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of an item of property, plant and equipment and the cost of the item can be measured reliably, the expenditure is capitalised as an additional cost of that asset or as a replacement.

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:

| | |
|---|---|
| Furniture and fixtures | 20% |
| Office equipment | 20% |

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected. Gain or loss on derecognition of property, plant and equipment, calculated as the difference between the net disposal proceeds and the carrying amount of the item, is included in the income statement in the period the item is derecognised.

**(f) Operating leases**

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

**(g) Cash and cash equivalents**

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

For the purpose of the balance sheets, cash and bank balances comprise cash on hand and at banks, including term deposits, which are not restricted as to use.

**(h) Income tax**

Income tax comprises current and deferred tax. Income tax is recognised in the income statement or in equity if it relates to items that are recognised in the same or a different period, 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.

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

Deferred tax liabilities are recognised for all taxable temporary differences:

- except where the deferred tax liability arises from the initial recognition of 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, except where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

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

- where the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability 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, associates and interests in joint ventures, 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 utilized.

The carrying amount of deferred tax assets is reviewed at each balance sheet date 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 utilized. Conversely, previously unrecognised deferred tax assets are reassessed at each balance sheet date and are recognised to the extent that it is probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilized.

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 at the balance sheet date.

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.

**(i) Revenue recognition**

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

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

(ii) interest income, on time proportion basis taking into account the principal outstanding and the effective interest rate applicable.

**(j) Foreign currencies**

Foreign currency transactions are recorded at the applicable rates of exchange ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated into Hong Kong dollars at the applicable rates of exchange ruling at that date. Exchange differences are dealt with in the income statement.

On consolidation, the financial statements of overseas subsidiaries are translated into Hong Kong dollars using the net investment method. The income statements of the overseas subsidiaries are translated into Hong Kong dollars at the weighted average exchange rates for the Relevant Periods, and its balance sheet is translated into Hong Kong dollars at the exchange rates ruling at the balance sheet dates. The resulting translation differences are included in the exchange fluctuation reserve.

For the purpose of the consolidated cash flow statements, the cash flows of the overseas subsidiaries are translated into Hong Kong dollars at the exchange rates ruling at the dates of the cash flows. Frequently recurring cash flows of the overseas subsidiaries which arise throughout the Relevant Periods are translated into Hong Kong dollars at the weighted average exchange rates for the Relevant Periods.

## 4. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES

**Judgements**

In the process of applying Silky Sky Group's accounting policies, the 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**

In determining whether an asset is impaired or whether the event previously causing the impairment no longer exists, the management has to exercise judgement in the area of asset impairment, particularly in assessing: (1) whether an event has occurred that may affect the asset value, or such an 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 derecognition; 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 have a material effect on the net present value used in the impairment test.

## 5. TURNOVER AND OTHER REVENUE

Silky Sky Group did not generate any turnover during the Relevant Periods. An analysis of the Silky Sky Group's other revenue is shown as follows:

| | Period from 18 August 2006 (date of incorporation) to 31 December 2006 | Two months ended 28 February 2007 |
|---|---|---|
| | *HK$* | *HK$* |
| Turnover | – | – |
| Other revenue | | |
| Interest income | 6,059 | 770 |
| | 6,059 | 770 |

## 6. LOSS BEFORE TAXATION

Loss before taxation is arrived at after charging:

| | Period from 18 August 2006 (date of incorporation) to 31 December 2006 | Two months ended 28 February 2007 |
|---|---|---|
| | *HK$* | *HK$* |
| Depreciation | – | 7,071 |
| Auditors' remuneration | – | – |
| Minimum lease payments under operating leases on: | | |
| Land and buildings | – | 133,097 |
| Exchange losses, net | – | 16,532 |
| Preliminary expenses | 14,000 | 33,552 |
| Staff cost (excluding directors' remuneration – *note 7*) | | |
| Salaries and allowances | – | 371,499 |

## 7. DIRECTORS' REMUNERATION AND FIVE HIGHEST PAID EMPLOYEES

During the Relevant Periods, no remuneration was paid or payable to the directors of Silky Sky Group.

There was no arrangement under which a director of Silky Sky Group waived or agreed to waive any remuneration during the Relevant Periods.

The details of the remuneration of the five highest paid individuals excluding directors of Silky Sky Group for the Relevant Periods are as follows:

| | Period from 18 August 2006 (date of incorporation) to 31 December 2006 | Two months ended 28 February 2007 |
|---|---|---|
| | *HK$* | *HK$* |
| Wages and salaries | – | 164,980 |

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

| | Number of individuals | |
|---|---|---|
| | Period from 18 August 2006 (date of incorporation) to 31 December 2006 | Two months ended 28 February 2007 |
| HK$Nil to HK$1,000,000 | – | 5 |

During the Relevant Periods, no remuneration was paid by the Silky Sky Group to the directors or five highest paid individuals as an inducement to join or upon joining the Silky Sky Group or as compensation for loss of office.

## 8. TAX

No provision for Hong Kong and overseas profits tax has been made as the Silky Sky Group did not generate any assessable profits arising from its operations during the Relevant Periods.

There are no material unprovided deferred tax assets and liabilities at the respective balance sheet dates.

## 9. PROPERTY, PLANT AND EQUIPMENT

**Silky Sky Group**

| | Furniture and fixtures *HK$* | Office equipment *HK$* | Total *HK$* |
|---|---|---|---|
| **Cost:** | | | |
| At 18 August 2006 | – | – | – |
| Additions during the period | – | – | – |
| At 31 December 2006 and 1 January 2007 | – | – | – |
| Additions during the period | 91,991 | 143,698 | 235,689 |
| At 28 February 2007 | 91,991 | 143,698 | 235,689 |
| **Accumulated depreciation:** | | | |
| At 18 August 2006 | – | – | – |
| Charge for the period | – | – | – |
| At 31 December 2006 and 1 January 2007 | – | – | – |
| Charge for the period | 2,760 | 4,311 | 7,071 |
| At 28 February 2007 | 2,760 | 4,311 | 7,071 |
| **Net book value:** | | | |
| At 28 February 2007 | 89,231 | 139,387 | 228,618 |
| At 31 December 2006 | – | – | – |

## 10. INTERESTS IN SUBSIDIARIES

| | As at 31 December 2006 *HK$* | As at 28 February 2007 *HK$* |
|---|---|---|
| Unlisted shares, at cost | 1 | 1 |
| Due from a subsidiary | – | 9,530,000 |
| | 1 | 9,530,001 |

The amount due from a subsidiary was unsecured, interest-free and has no fixed terms of repayment. The carrying amount of the amount due from a subsidiary approximates its fair value.

Particulars of the subsidiaries are as follows:

| Name of subsidiaries | Place and date of incorporation/ registration | Nominal value of issued/ registered capital | Attributable equity interest held by Silky Sky | Principal activities |
|---|---|---|---|---|
| Sky Rich Limited | Hong Kong 16 May 2006 | HK$1 | 100% (directly) | Investment holding |
| Beijing Shiji Jiangshan Resource Recycling Technology Ltd* | PRC 25 December 2006 | RMB30,000,000 | 75% (indirectly) | Waste recycling and production and distribution of organic fertilizer |

* *This subsidiary is a joint venture company with a registered capital of RMB30 million. Sky Rich had injected a capital of RMB9.5 million as at 28 February 2007.*

**11. PREPAYMENTS**

Prepayments of Silky Sky Group as at 28 February 2007 are amounts prepaid for the acquisition of production machinery and technology.

**12. OTHER RECEIVABLES**

| | Silky Sky Group | |
|---|---|---|
| | As at 31 December 2006 | As at 28 February 2007 |
| | *HK$* | *HK$* |
| Prepayment to staff for business purposes | – | 849,346 |
| Rental deposit | – | 35,425 |
| Rent prepayment | – | 5,365 |
| Other receivables | – | 69,939 |
| | – | 960,075 |

**13. CASH AND CASH EQUIVALENTS**

| | Silky Sky Group | | Silky Sky | |
|---|---|---|---|---|
| | As at 31 December 2006 | As at 28 February 2007 | As at 31 December 2006 | As at 28 February 2007 |
| | *HK$* | *HK$* | *HK$* | *HK$* |
| Cash and bank balances | 5,557 | 5,206,524 | 7 | 7 |

Cash at banks earns interest at floating rates based on daily bank deposit rates. The carrying amounts of the cash and cash equivalents approximate to their fair values.

The cash and bank balances of Silky Sky Group amounting to HK$Nil and HK$2,676,151 as at 31 December 2006 and 28 February 2007 respectively are denominated in Renminbi. RMB is not freely convertible into other currencies. Under the PRC Foreign Exchange Control Regulations and Administration of Settlement, Sale and Payment of Foreign Exchange Regulations, Silky Sky Group is permitted to exchange RMB for other currencies through banks authorized to conduct foreign exchange business.

## 14. DUE TO THE SHAREHOLDER

The amount due to the shareholder is unsecured, interest-free and has no fixed terms of repayment.

## 15. SHARE CAPITAL

| | **As at 31 December 2006** *HK$* | **As at 28 February 2007** *HK$* |
|---|---|---|
| Authorised: | | |
| 50,000 ordinary shares of US$1 each | 390,000 | 390,000 |
| Issued and fully paid: | | |
| 1 ordinary share of US$1 each | 8 | 8 |

Silky Sky was incorporated on 18 August 2006 with authorised share capital of US$50,000 divided into 50,000 ordinary shares of US$1 each. Upon incorporation, 1 ordinary share was issued at par for cash as subscriber's share.

## 16. RESERVES

| **Silky Sky** | **Accumulated losses** *HK$* |
|---|---|
| Loss for the period | (7,500) |
| At 31 December 2006 and 1 January 2007 | (7,500) |
| Loss for the period | – |
| At 28 February 2007 | (7,500) |

## 17. RELATED PARTY TRANSACTIONS

Other than the transactions and balances detailed elsewhere in the Financial Information, the Silky Sky Group had no significant transactions with related parties during the Relevant Periods.

## 18. OPERATING LEASE ARRANGEMENTS

The Silky Sky Group leases an office premise and two quarters under operating lease arrangements. The lease for the office premise is negotiated for a term of three years and the lease for the two quarters is negotiated for a term of one year.

At the balance sheet dates, Silky Sky Group had total future minimum lease payments under non-cancellable operating leases falling due as follows:

| | **As at 31 December 2006** *HK$* | **As at 28 February 2007** *HK$* |
|---|---|---|
| Within one year | – | 457,287 |
| In the second to fifth years, inclusive | – | 708,502 |
| | – | 1,165,789 |

## 19. CAPITAL COMMITMENTS

In addition to the operating lease arrangements detailed in note 18 above, the Silky Sky Group had the following capital commitments at each of the balance sheet dates:

| | **As at 31 December 2006** *HK$* | **As at 28 February 2007** *HK$* |
|---|---|---|
| Contracted but not provided for in the financial statements | | |
| – Acquisition of production machinery | – | 2,991,700 |
| – Acquisition of production technology *(note)* | – | 253,036 |
| – Further capital contribution to Beijing Shiji | 22,773,279 | 13,243,279 |

*Note:*

During the Relevant Periods, the Silky Sky Group entered into an agreement to acquire production technology from a company in which a director of Beijing Shiji has beneficial interest. The contract sum was RMB1,250,000 of which a deposit of RMB1 million has been paid during the Relevant Periods resulting in a commitment of RMB250,000 (equivalent to HK$253,036) as at 28 February 2007.

Other than those disclosed above, the Silky Sky Group had no significant commitments or contingent liabilities as at each of the balance sheet dates.

**20. FINANCIAL RISK AND MANAGEMENT**

The Silky Sky Group's overall risk management programme seeks to minimise potential adverse effects on the financial performance of the Silky Sky Group.

**(i) Interest rate risk**

The Silky Sky Group has no interest bearing borrowing. The Silky Sky Group's income and cash flows are substantially independent of changes in market interest rates. Currently, the Silky Sky Group does not have a hedging policy. However, the management monitors interest rate exposure and will consider hedging significant bank borrowings should the need arises.

**(ii) Foreign currency risk**

The Silky Sky Group incurs foreign currency risk on transactions and balances that are denominated in currencies other than Hong Kong dollars. The currencies giving rise to this risk are primarily Renminbi and United States Dollar. The Silky Sky Group currently does not have a foreign currency hedging policy.

**(iii) Credit risk**

The Silky Sky Group has no concentration of credit risk.

**(iv) Liquidity risk**

The Silky Sky Group actively manages its operating cash flows and the availability of funding so as to ensure that all repayment and funding needs are met. As part of its overall liquidity management, the Silky Sky Group maintains sufficient level of cash to meet its working capital requirements.

**(v) Fair values**

The carrying amounts of the financial assets and liabilities in the Financial Information approximate their fair values.

**21. SUBSEQUENT EVENTS**

A share transfer agreement dated 22 January 2007 was entered into between Sky Rich and Fortune Pacific Limited ("Fortune Pacific"), pursuant to which Sky Rich agreed to transfer 24% equity interest in Beijing Shiji to Fortune Pacific for a consideration of RMB7.2 million of which RMB1.44 million will be paid to Sky Rich and RMB5.76 million will be contributed to Beijing Shiji directly as further capital investment. Upon the completion of share transfer on 21 March 2007, Sky Rich retains 51% equity interest in Beijing Shiji and Sky Rich's commitment for further capital contribution to Beijing Shiji is reduced to RMB7.245 million.

**22. SUBSEQUENT FINANCIAL STATEMENTS**

No audited financial statements have been prepared for the Silky Sky Group in respect of any period subsequent to 28 February 2007.

Yours faithfully,
**Cheung & Siu**
*Certified Public Accountants*
(Practising)
Hong Kong

*The following are the unaudited pro forma financial information on the Group as enlarged by the acquisition of Silky Sky and its subsidiary, received from Cheung & Siu as extracted from the circular of the Company dated 20 April 2007.*

*Cheung & Siu* **Certified Public Accountants**
張、蕭會計師事務所

20 April 2007

The Board of Directors
KanHan Technologies Group Limited
15/F., Sun House
181 Des Voeux Road Central
Hong Kong

Dear Sirs,

We report on the unaudited pro forma statement of assets and liabilities (the "Unaudited Pro Forma Financial Information") of KanHan Technologies Group Limited (the "Company") and its subsidiaries (hereinafter collectively referred to as the "Group") and Silky Sky Investments Limited (the "Target") and its subsidiaries (the "Target Group") (together with the Group hereinafter referred to as the "Enlarged Group") which has been prepared by the directors of the Company for illustrative purposes only, to provide information about how the proposed acquisition of the Target might have affected the financial information presented, for inclusion as Appendix III to the circular of the Company dated 20 April 2007 (the "Circular"). The basis of preparation of the Unaudited Pro Forma Financial Information is set out on pages 73 to 76 to the Circular.

**Respective Responsibilities of Directors of the Company and Reporting Accountants**

It is the responsibility solely of the directors of the Company to prepare the Unaudited Pro Forma Financial Information in accordance with rule 7.31 of the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (the "GEM Listing Rules") and with reference to Accounting Guideline 7 "Preparation of Pro Forma Financial Information for Inclusion in Investment Circulars" issued by the Hong Kong Institute of Certified Public Accountants.

It is our responsibility to form an opinion, as required by rule 7.31(7) of the GEM Listing Rules, on the Unaudited Pro Forma Financial Information and to report our opinion to you. We do not accept any responsibility for any reports previously given by us on any financial information used in the compilation of the Unaudited Pro Forma Financial Information beyond that owed to whom those reports were addressed by us at the dates of their issue.

**Basis of Opinion**

We conducted our engagement in accordance with Hong Kong Standard on Investment Circular Reporting Engagements ("HKSIR") 300 "Accountants' Reports on Pro Forma Financial Information in Investment Circulars" issued by the Hong Kong Institute of Certified Public Accountants. Our work consisted primarily of comparing the unadjusted financial information with source documents, considering the evidence supporting the adjustments and discussing the Unaudited Pro Forma Financial Information with the directors of the Company. This engagement did not involve independent examination of any of the underlying financial information.

We planned and performed our work so as to obtain the information and explanations we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Unaudited Pro Forma Financial Information has been properly compiled by the directors of the Company on the basis stated, that such basis is consistent with the accounting policies of the Group and that the adjustments are appropriate for the purpose of the Unaudited Pro Forma Financial Information as disclosed pursuant to rule 7.31(1) of the GEM Listing Rules.

The Unaudited Pro Forma Financial Information is for illustrative purpose only, based on the judgements and assumptions of the directors of the Company, and, because of its hypothetical nature, does not provide any assurance or indication that event will take place in the future and may not be indicative of the financial position of the Enlarged Group as at 31 December 2006 or any future date.

**Opinion**

In our opinion:

- the Unaudited Pro Forma Financial Information has been properly compiled by the directors of the Company on the basis stated;

- such basis is consistent with the accounting policies of the Group; and

- the adjustments are appropriate for the purpose of the Unaudited Pro Forma Financial Information as disclosed pursuant to rule 7.31(1) of the GEM Listing Rules.

Yours faithfully,
**Cheung & Siu**
*Certified Public Accountants*
(Practising)
Hong Kong

## INTRODUCTION TO THE UNAUDITED PRO FORMA FINANCIAL INFORMATION ON THE ENLARGED GROUP

The following unaudited pro forma financial information of the Enlarged Group has been prepared based on the audited financial statements of the Group for the year ended 31 December 2006 and the financial information of the Target Group for the period ended 28 February 2007. The accompanying unaudited pro forma financial information of the Enlarged Group has been prepared to illustrate the effect of the proposed acquisition of the Target and the Sale Loan at a consideration of HK61,000,000 which shall be satisfied by deposit already paid, cash and allotment and issue of the shares of the Company and issue of promissory note by the Company.

The accompanying unaudited pro forma financial information of the Enlarged Group is based on a number of assumptions, estimates, uncertainties and currently available information, and is provided for illustrative purposes. Accordingly, as a result of the uncertain nature of the accompanying unaudited pro forma financial information of the Enlarged Group, it may not give a true picture of the actual financial position or results of the Enlarged Group's operations that would have been attained had the Proposed Acquisition actually occurred on 31 December 2006 or any future period. Further, the accompanying unaudited pro forma financial information of the Enlarged Group does not purport to predict the Enlarged Group's future financial position or results of operations.

The unaudited pro forma financial information of the Enlarged Group should be read in conjunction with the Accountants' Report on the Target Group as set out in Appendix I and other financial information included elsewhere in this Circular.

| | The Group As at 31 December 2006 | The Target Group As at 28 February 2007 | Pro-forma adjustments | | Total |
|---|---|---|---|---|---|
| | *HK$'000* | *HK$'000* | *HK$'000* | *Notes* | *HK$'000* |
| NON-CURRENT ASSETS | | | | | |
| Property, plant and equipment | 158 | 229 | – | | 387 |
| Goodwill | – | – | 52,131 | *(iv)* | 52,131 |
| Total non-current assets | 158 | 229 | 52,131 | | 52,518 |
| CURRENT ASSETS | | | | | |
| Inventories | 62 | – | – | | 62 |
| Trade and other receivables | 4,638 | 3,021 | – | | 7,659 |
| Cash and bank balances | 22,707 | 5,207 | (20,000) | *(vii)* | 7,914 |
| Total current assets | 27,407 | 8,228 | (20,000) | | 15,635 |
| CURRENT LIABILITIES | | | | | |
| Trade and other payables | 3,989 | 22 | – | | 4,011 |
| Financial assistance from government | 236 | – | – | | 236 |
| Due to a shareholder | – | 9,257 | (9,257) | *(vi)* | – |
| Total current liabilities | 4,225 | 9,279 | (9,257) | | 4,247 |
| NET CURRENT ASSETS/ (LIABILITIES) | 23,182 | (1,051) | (10,470) | | 11,388 |
| TOTAL ASSETS LESS CURRENT LIABILITIES | 23,340 | (822) | 41,388 | | 63,906 |
| NON-CURRENT LIABILITIES | | | | | |
| Financial assistance from government | 1,059 | – | – | | 1,059 |
| Promissory note | – | – | 24,031 | *(viii)* | 24,031 |
| Total non-current liabilities | 1,059 | – | 24,031 | | 25,090 |
| Net assets/(liabilities) | 22,281 | (822) | 17,357 | | 38,816 |
| EQUITY | | | | | |
| Issued capital | 29,498 | – | 6,788 | *(ii)* | 36,286 |
| Reserves | (7,217) | (601) | 10,782 | *(iii)* | 2,964 |
| | 22,281 | (601) | 17,570 | | 39,250 |
| Minority interests | – | (221) | (213) | *(v)* | (434) |
| Total equity | 22,281 | (822) | 17,357 | | 38,816 |

*Notes:*

Under HKFRS 3 Business Combinations ("HKFRS 3"), the Group shall apply the purchase method to account for the acquisition of the Target Group. In applying the purchase method, the identifiable assets, liabilities and contingent liabilities of the Target Group will be recorded on the consolidated balance sheet of the Group at their fair values at the date of completion. Any goodwill or discount arising on the acquisition shall be determined as the excess or deficit of the purchase price to be incurred by the group over the Group's interests in the net fair value of the identifiable assets, liabilities and contingent liabilities of the Target Group at the date of completion. Negative goodwill resulting from the business combinations should be recognized immediately in the consolidated income statement.

Details of the acquisition and their effects on the pro forma financial information are as follows:

(i) the total consideration for the Sale Share and the Sale Loan is HK$61,000,000 which shall be settled in the following manner:

(a) HK$20,000,000 as deposits which have already been paid by the Purchaser to the Vendor at of the date of this circular;

(b) HK$16,968,750 by procuring the Company to allot and issue 135,750,000 Consideration Shares at an issue price of HK$0.125 per Consideration Share; and

(c) HK$24,031,250 by issuing the Promissory Note to the Vendor.

(ii) the pro forma adjustment of approximately HK$6,788,000 represents the nominal value of 135,750,000 Consideration Shares at HK$0.05 per share of the Company amounting to HK$6,787,500 arising from issuance of the said Shares as described in note (i)(b) above and the elimination of share capital of the Target Group on consolidation.

(iii) the pro forma adjustment of approximately HK$10,782,000 represents the share premium arising from issuance of the Consideration Shares amounting to approximately HK$10,181,000, and the elimination of the pre-acquisition reserves of the Target Group on consolidation of approximately HK$601,000 (note (iv)).

(iv) the pro forma adjustment of approximately HK$52,131,000 represents goodwill arising from the acquisition of the Target Group which is arrived as follows:

| | *HK$'000* |
|---|---|
| Consideration for the acquisition of the Target Group | 61,000 |
| Add: share of net identifiable liabilities of the Target Group *(note (iii))* | 601 |
| | 61,601 |
| Less: Sale Loan acquired of HK$9,257,000 as described in note *(vi)* below | (9,257) |
| Pro forma adjustment of minority interest as described in note *(v)* below | (213) |
| | 52,131 |

(v) the pro forma adjustment of minority interest represents the minority shareholder's share of 24% of the net losses of approximately HK$886,000 of the Subsidiary upon the completion of the share transfer agreement dated 22 January 2007 entered into between Sky Rich and Fortune Pacific Limited.

(vi) the pro forma adjustment of HK$9,257,000 represents the Sale Loan to be assigned to the Group according to the Formal Agreement.

(vii) the pro forma adjustment of HK$20,000,000 represents the payment of the consideration as described in note (i)(a) above.

(viii) the pro forma adjustment of approximately HK$24,031,000 represents the payment of the consideration by issuing the Promissory Note to the Vendor as described in note (i)(c) above.

*The following is the text of a letter, prepared for the sole purpose of inclusion in this circular, received from Greater China Appraisal Limited.*

GREATER CHINA APPRAISAL LIMITED
漢 華 評 值 有 限 公 司

Room 2703
Shui On Centre
6-8 Harbour Road
Wanchai
Hong Kong

18 January 2008

The Directors
KanHan Technologies Group Limited
15th Floor
Sun House
181 Des Voeux Road Central
Hong Kong

Dear Sirs,

In accordance with the instructions from KanHan Technologies Group Limited ("the Company") to value the property interests of Dangtu Xian Zhongtian Water Supply Company ("Zhong Tian Water Supply") in the People's Republic of China (the "PRC"), we confirm that we have carried out inspections, made relevant enquiries and obtained such further information as we consider necessary for the purpose of providing the market values of such properties as at 31 October 2007 (referred to as the "valuation date").

It is our understanding that this valuation is for acquisition purpose.

This letter which forms part of our valuation report explains the basis and methodology of valuation, and clarifies our assumptions made, title investigation of properties and the limiting conditions.

## BASIS OF VALUATION

The valuation of such properties is our opinion of the market value which we would define as intended to mean "the estimated amount for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm's-length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion."

## VALUATION METHODOLOGY

Due to the nature of buildings and structures constructed, there is no readily identifiable market comparable to them, we have applied the cost method of valuation in assessing the property. It is a method of using current replacement costs to arrive at the value to the business in occupation of the property as existing at the date of valuation.

This method of valuation, cost method, is based on an estimate of the market value for the existing use of the land, plus the current gross replacement costs of the improvements, less allowances for physical deterioration and all relevant forms of obsolescence and optimization.

The cost method generally furnishes the most reliable indication of value for property in the absence of a known market based on comparable.

## ASSUMPTIONS

Our valuation has been made on the assumption that the owner sells the properties on the open market in their existing states without the benefit of any deferred terms contracts, leaseback, joint ventures, management agreements or any similar arrangement which would serve to increase the value of the properties.

Continued use assumes the properties will be used for the purposes for which the properties are designed and built, or to which they are currently adapted. The valuation on the property in continued use does not represent the amount that might be realized from piecemeal disposition of the property on the open market.

As the properties are held under long term land use rights, we have assumed that the owners of the properties have free and uninterrupted rights to use or transfer the properties for the whole of the unexpired term of the respective land use rights. In our valuation, we have assumed that the properties can be freely disposed of and transferred to third parties on the open market without any additional payment to the relevant government authorities. Unless stated as otherwise, vacant possession is assumed for the properties concerned.

We have assumed that all consents, approvals and licenses from relevant government authorities for the buildings and structures erected thereon have been granted. Also, we have assumed that all buildings and structures fall within the site are held by the owner or permitted to be occupied by the owner.

In the course of valuation, we have assumed that all the properties are currently held by Zhong Tian Water Supply, which have the rights to occupy, use, sell, lease, charge, mortgage or otherwise dispose of the interests within their respective terms of land use rights granted by the government without the need to seek further approval from and paying additional premium to the government.

It is assumed that all applicable zoning and use regulations and restrictions have been complied with unless nonconformity has been stated, defined, and considered in the appraisal report. Moreover, it is assumed that the utilization of the land and improvements is within the boundaries of the site held by the owner or permitted to be occupied by the owner. In addition, we assumed that no encroachment or trespass exists, unless noted in the report.

No environment impact study has been ordered or made. Full compliance with applicable national, provincial and local environmental regulations and laws is assumed unless otherwise stated, defined, and considered in the report. It is also assumed that all required licences, consents, or other legislative or administrative authority from any local, provincial, or national government or private entity or organization either have been or can be obtained or renewed for any use which the report covers.

Other special assumptions of each property, if any, have been stated out in the footnotes of the valuation certificate for the respective properties.

## TITLESHIP INVESTIGATION

For the properties held by Zhong Tian Water Supply in the PRC, we have been provided with copy of land use documents. However, due to the current registration system of the PRC, no investigations have been made for the legal title or any material liabilities attached to the property.

In the course of our valuation, we have relied upon the legal opinions as stated in the title report given by Fujian Minjiang Law Firm (the "PRC Lawyer") in relation to the legal title to the properties located in the PRC under valuation.

All legal documents disclosed in this report, if any, are for reference only and no responsibility is assumed for any legal matters concerning the legal title to the properties set out in this report.

## LIMITING CONDITIONS

We have not carried out detailed site measurements to verify the correctness of the land or building areas in respect of the relevant properties but have assumed that the areas shown on the legal documents provided to us are correct. Based on our experience of valuation of similar properties, we consider the assumptions so made to be reasonable. All documents and contracts have been used as reference only and all dimensions, measurements and areas are approximations.

We have inspected the exterior and, where possible, the interior of the properties included in the attached valuation certificates. However, no structural survey has been made and we are therefore unable to report as to whether the properties is free from rot, infestation or any other structural defects. Also, no tests were carried out on any of the services.

No site investigations have been carried out to determine the suitability of the ground conditions or the services for any property development. No soil analysis or geological studies were ordered or made in conjunction with this report, nor were any water, oil, gas or other subsurface mineral use rights or conditions investigated.

We do not investigate any industrial safety, environmental and health related regulations in association with any particular manufacturing process of the Zhong Tian Water Supply. It is assumed that all necessary licenses, procedures and measures were implemented in accordance with government legislation and guidance.

Having examined all relevant documentation, we have relied to a very considerable extent on the information provided and have accepted advice given to us by Zhong Tian Water Supply on such matters as planning approvals, statutory notices, easements, tenure, occupation, lettings, construction costs, rentals, site and floor areas and in the identification of those properties in which Zhong Tian Water Supply has valid interests. Floor areas of the property stated herein are ascertained by us by scaling off the registered floor plans of the subject development.

We have had no reason to doubt the truth and accuracy of the information provided to us by Zhong Tian Water Supply. We were also advised by the Company or Zhong Tian Water Supply that no material factors have been omitted from the information to reach an informed view, and have no reason to suspect that any material information has been withheld.

No allowances have been made in our valuation for any charges, mortgages or amounts owing on any of the properties valued nor for any expenses or taxation which may be incurred in effecting a sale.

Unless otherwise stated, it is assumed that all the properties are free of encumbrances, restrictions and outgoings of an onerous nature which could affect their values.

Since the property is located in a relatively under-developed market, the PRC, those assumptions are often based on imperfect market evidence. A range of values may be attributable to the property depending upon the assumptions made. While the valuer has exercised his professional judgment in arriving at the value, report readers are urged to consider carefully the nature of such assumptions which are disclosed in the valuation report and should exercise caution in interpreting the valuation report.

## OPINION OF VALUE

Valuation figures of the properties held by Zhong Tian Water Supply are shown in the attached summary of valuation and their respective valuation certificates.

**REMARKS**

Our valuation has been prepared in accordance with generally accepted valuation procedures. In valuing the properties, we have complied with the requirements contained in the HKIS Valuation Standards on Properties (1st Edition 2005) published by the Hong Kong Institute of Surveyors and effective from 1 January 2005.

All amounts are denominated in Chinese Renminbi.

We enclose herewith the summary of valuation and valuation certificates.

This valuation report is issued subject to our General Service Conditions.

Yours faithfully,
For and on behalf of
**GREATER CHINA APPRAISAL LIMITED**
**K.K. Ip** *BLE LLD*
*Chartered Valuation Surveyor*
*Registered Professional Surveyor*
*Managing Director*

*Note:* Mr. K.K. Ip, a Chartered Valuation Surveyor and a Registered Professional Surveyor, has substantial experience in valuation of properties in the PRC since 1992.

## SUMMARY OF VALUATION

**Property held by Zhong Tian Water Supply in the PRC**

| No. | Property | Market value in existing state as at 31 October 2007 *(RMB)* |
|---|---|---|
| 1. | Land, buildings and structures<br>Dagongwei Zhongxin Water Plant<br>Lin Cun<br>Shiqiao Town<br>Dangtu County<br>Ma'anshan<br>Anhui Province<br>The PRC | No commercial value |
| 2. | Land and buildings<br>Water Source Station<br>Sanxing Cun<br>Huangchi Town<br>Dangtu County<br>Ma'anshan<br>Anhui Province<br>The PRC | No commercial value |
| 3. | Land, buildings and structures<br>Huyang Water Plant<br>Dongwanghou<br>Huyang County<br>Dangtu Xian<br>Ma'anshan<br>Anhui Province<br>The PRC | No commercial value |
| 4. | Land, buildings and structures<br>Niandou Water Plant<br>Gongyuan Cun<br>Niandou County<br>Dangtu Xian<br>Ma'anshan<br>Anhui Province<br>The PRC | No commercial value |
| | **Grand Total:** | **No commercial value** |

## VALUATION CERTIFICATE

**Property held by Zhong Tian Water Supply in the PRC**

| No. | Property | Description | Particulars of Occupancy | Market value in existing state as at 31 October 2007 *(RMB)* |
|---|---|---|---|---|
| 1. | Land, buildings and structures Dagongwei Zhongxin Water Plant Lin Cun Shiqiao Town Dangtu County Ma'anshan Anhui Province The PRC | The property comprises a parcel of land ("the Land"), 7 buildings (the "Buildings") and various structures erected on the Land. The Buildings were completed in 2007.<br><br>The land area of the Land is approximately 38,000 square metres and the total gross floor area ("GFA") of the buildings is approximately 5,215 square metres. Detailed breakdown is as follows: | The property is currently occupied by Zhong Tian Water Supply as a water supply plant. | No commercial value<br><br>*(see note v)* |

| Buildings | No. of Blocks | No. of Storey | GFA *(sq.m.)* |
|---|---|---|---|
| Office | 1 | 4 | 1,253 |
| Dormitory | 2 | 3 | 2,496 |
| Pump room | 2 | 1-2 | 1,056 |
| Power room | 1 | 1 | 131 |
| Chemical room | 1 | 1 | 279 |
| Total | 7 | | 5,215 |

The various structures comprise water tanks, filtration tanks, precipitation tanks, internal road, boundary walls, greenery and etc.

The property is held under a land lease for a term of 30 years from 14 March 2006 to 13 March 2037 at a total rent of RMB570,000 for water plant purpose.

*Notes*:

(i) Zhong Tian Water Supply has obtained the operating rights of the water supply business in Shiqiao Area under a franchise agreement entered into between the People's Government of Shiqiao Town of Dangtu County ("Party A"), Water Resources Bureau of Dangtu County ("Party B") and Zhong Tian Water Supply ("Party C") dated 14 March 2006.

(ii) According to a land lease entered into between the People's Government of Shiqiao Town of Dangtu County and Zhong Tian Water Supply dated 18 April 2007, the Land was agreed to be leased to Zhong Tian Water Supply with a term of 31 years from 14 March 2006 to 13 March 2037 at a total rent of RMB570,000 for water plant purpose.

(iii) The Buildings were built by Zhong Tian Water Supply on the Land according to the franchise agreement mentioned in (i). As advised by Zhong Tian Water Supply, no further approvals are required.

(iv) Opinions of the PRC Lawyer are summarized as follows:

(a) According to a land lease (the "Lease") entered into between the People's Government of Shiqiao Town of Dangtu County and Zhongtian Water Supply dated 18 April 2007, the Land (with land area of 38,000 square metres) was agreed to be leased to Zhongtian Water Supply with a term of 31 years from 14 March 2006 to 13 March 2037 for water plant purpose.

(b) According to the relevant PRC laws, the maximum term of lease is 20 years. Therefore, the lease term of the Land is 20 years though it appears to be 31 years on the Lease. However, the Lease can be extended upon expiry after 20 years.

(c) Zhong Tian Water Supply has the right to use the Land under the Lease only, it does not has the right to sub-lease, mortgage and transfer the Land.

(d) The Land under the Lease is restricted to be used for water supply purpose which is not in violation of the prescribed usage of the Land nor any of the PRC laws and regulations.

(v) Since the Buildings were built by Zhong Tian Water Supply on lessor's land, we have assigned no commercial value to the Buildings. For reference purpose, assuming free from encumbrances, the depreciated replacement cost of the Buildings as at the valuation date would be approximately RMB10,300,000.

## VALUATION CERTIFICATE

| No. | Property | Description | Particulars of Occupancy | Market value in existing state as at 31 October 2007 *(RMB)* |
|---|---|---|---|---|
| 2. | Land and buildings Water Source Station Sanxing Cun Huangchi Town Dangtu County Ma'anshan Anhui Province The PRC | The property comprises a parcel of land ("the Land") and 2 buildings (the "Building") erected on the Land. The Building was completed in 2006.<br><br>The land area of the Land is approximately 4,553 square metres and the total gross floor area ("GFA") of the buildings is approximately 268 square metres.<br><br>The property is held under a land lease for a term of 30 years from 31 December 2006 to 31 December 2037 at a total rent of RMB47,810 for water source purpose. | The property is currently occupied by Zhong Tian Water Supply as a water source station. | No commercial value<br><br>*(see note v)* |

*Notes:*

(i) Zhong Tian Water Supply has obtained the operating rights of the water supply business in Huangchi Area under a franchise agreement entered into between the People's Government of Huangchi Town of Dangtu County ("Party A"), Water Resources Bureau of Dangtu County ("Party B") and Zhong Tian Water Supply ("Party C") dated 14 March 2006.

(ii) According to a land lease entered into between the People's Government of Huangchi Town of Dangtu County and Zhong Tian Water Supply dated 5 February 2007, the Land was agreed to be leased to Zhong Tian Water Supply with a term of 31 years from 31 December 2006 to 31 December 2037 at a total rent of RMB47,810 for water source purpose.

(iii) The Building were built by Zhong Tian Water Supply on the Land according to the franchise agreement mentioned in (i). As advised by Zhong Tian Water Supply, no further approvals are required.

(iv) Opinions of the PRC Lawyer are summarized as follows:

(a) According to a land lease (the "Lease") entered into between the People's Government of Huangchi Town of Dangtu County and Zhongtian Water Supply dated 5 February 2007, the Land (with land area of 4,553 square metres) was agreed to be leased to Zhongtian Water Supply with a term of 31 years from 31 December 2006 to 31 December 2037 for water source purpose.

(b) According to the relevant PRC laws, the maximum term of lease is 20 years. Therefore, the lease term of the Land is 20 years though it appears to be 31 years on the Lease. However, the Lease can be extended upon expiry after 20 years.

(c) Zhong Tian Water Supply has the right to use the Land under the Lease only, it does not has the right to sub-lease, mortgage and transfer the Land.

(d) The Land under the Lease is restricted to be used for water supply purpose which is not in violation of the prescribed usage of the Land nor any of the PRC laws and regulations.

(v) Since the Buildings were built by Zhong Tian Water Supply on lessor's land, we have assigned no commercial value to the Buildings. For reference purpose, assuming free from encumbrances, the depreciated replacement cost of the Buildings as at the valuation date would be approximately RMB670,000.

## VALUATION CERTIFICATE

| No. | Property | Description | Particulars of Occupancy | Market value in existing state as at 31 October 2007 *(RMB)* |
|---|---|---|---|---|
| 3. | Land, buildings and structures Huyang Water Plant Dongwanghou Huyang County Dangtu Xian Ma'anshan Anhui Province The PRC | The property comprises a parcel of land ("the Land"), 4 buildings (the "Buildings") and various structures erected on the Land. The Buildings were completed in 2006.<br><br>The land area of the Land is approximately 3,333 square metres and the total gross floor area ("GFA") of the buildings is approximately 243 square metres. Detailed breakdown is as follows: | The property is currently occupied by Zhong Tian Water Supply as a water supply plant. | No commercial value<br><br>*(see note v)* |

| Buildings | No. of Blocks | No. of Storey | GFA *(sq.m.)* |
|---|---|---|---|
| Office | 1 | 1 | 104 |
| Pump room | 1 | 1 | 33 |
| Chemical | 1 | 1 | 75 |
| Ancillary | 1 | 1 | 31 |
| Total | 4 | | 243 |

The various structures comprise water tanks, filtration tanks, precipitation tanks, internal road, boundary walls, greenery and etc.

The property is held under a land lease for a term of 31 years from 23 August 2005 to 22 August 2036 at a total rent of RMB50,000 for water plant purpose.

*Notes:*

(i) Zhong Tian Water Supply has obtained the operating rights of the water supply business in Huyang Area under a franchise agreement entered into between the People's Government of Huyang Town of Dangtu County ("Party A"), Water Resources Bureau of Dangtu County ("Party B") and Zhong Tian Water Supply ("Party C") dated 23 August 2003.

(ii) According to a land lease entered into between the People's Government of Huyang Town of Dangtu County and Zhong Tian Water Supply dated 25 August 2005, the Land was agreed to be leased to Zhong Tian Water Supply with a term of 31 years from 23 August 2005 to 22 August 2036 at a total rent of RMB50,000 for water plant purpose.

(iii) The Buildings were built by Zhong Tian Water Supply on the Land according to the franchise agreement mentioned in (i). As advised by Zhong Tian Water Supply, no further approvals are required.

(iv) Opinions of the PRC Lawyer are summarized as follows:

(a) According to a land lease (the "Lease") entered into between the People's Government of Huyang Town of Dangtu County and Zhongtian Water Supply dated 25 August 2005, the Land (with land area of 3,333 square metres) was agreed to be leased to Zhongtian Water Supply with a term of 31 years from 23 August 2005 to 22 August 2036 for water plant purpose.

(b) According to the relevant PRC laws, the maximum term of lease is 20 years. Therefore, the lease term of the Land is 20 years though it appears to be 31 years on the Lease. However, the Lease can be extended upon expiry after 20 years.

(c) Zhong Tian Water Supply has the right to use the Land under the Lease only, it does not has the right to sub-lease, mortgage and transfer the Land.

(d) The Land under the Lease is restricted to be used for water supply purpose which is not in violation of the prescribed usage of the Land nor any of the PRC laws and regulations.

(v) Since the Buildings were built by Zhong Tian Water Supply on lessor's land, we have assigned no commercial value to the Buildings. For reference purpose, assuming free from encumbrances, the depreciated replacement cost of the Buildings as at the valuation date would be approximately RMB840,000.

## VALUATION CERTIFICATE

| No. | Property | Description | Particulars of Occupancy | Market value in existing state as at 31 October 2007 *(RMB)* |
|---|---|---|---|---|
| 4. | Land, buildings and structures Niandou Water Plant Gongyuan Cun Niandou County Dangtu Xian Ma'anshan Anhui Province The PRC | The property comprises a parcel of land ("the Land"), 4 buildings (the "Buildings") and various structures erected on the Land. The Buildings were completed in 2006.<br><br>The land area of the Land is approximately 3,733 square metres and the total gross floor area ("GFA") of the buildings is approximately 260 square metres. Detailed breakdown is as follows: | The property is currently occupied by Zhong Tian Water Supply as a water supply plant. | No commercial value<br><br>*(see note v)* |

| Buildings | No. of Blocks | No. of Storey | GFA *(sq.m.)* |
|---|---|---|---|
| Office | 1 | 1 | 104 |
| Pump room | 1 | 1 | 76 |
| Chemical room | 1 | 1 | 80 |
| Total | 4 | | 260 |

The various structures comprise water tanks, filtration tanks, precipitation tanks, internal road, boundary walls, greenery and etc.

The property is held under a land lease for a term of 31 years from 23 September 2005 to 22 September 2036 at a total rent of RMB56,000 for water plant purpose.

*Notes:*

(i) Zhong Tian Water Supply has obtained the operating rights of the water supply business in Niandou Area under a franchise agreement entered into between the People's Government of Niandou Town of Dangtu County ("Party A"), Water Resources Bureau of Dangtu County ("Party B") and Zhong Tian Water Supply ("Party C") dated 23 September 2003.

(ii) According to a land lease entered into between the People's Government of Niandou Town of Dangtu County and Zhong Tian Water Supply dated 22 September 2005, the Land was agreed to be leased to Zhong Tian Water Supply with a term of 31 years from 23 September 2005 to 22 September 2036 at a total rent of RMB56,000 for water plant purpose.

(iii) The Buildings were built by Zhong Tian Water Supply on the Land according to the franchise agreement mentioned in (i). As advised by Zhong Tian Water Supply, no further approvals are required.

(iv) Opinions of the PRC Lawyer are summarized as follows:

(a) According to a land lease (the "Lease") entered into between the People's Government of Niandou Town of Dangtu County and Zhongtian Water Supply dated 22 September 2005, the Land (with land area of 3,733 square metres) was agreed to be leased to Zhongtian Water Supply with a term of 31 years from 23 September 2005 to 22 September 2036 for water plant purpose.

(b) According to the relevant PRC laws, the maximum term of lease is 20 years. Therefore, the lease term of the Land is 20 years though it appears to be 31 years on the Lease. However, the Lease can be extended upon expiry after 20 years.

(c) Zhong Tian Water Supply has the right to use the Land under the Lease only, it does not has the right to sub-lease, mortgage and transfer the Land.

(d) The Land under the Lease is restricted to be used for water supply purpose which is not in violation of the prescribed usage of the Land nor any of the PRC laws and regulations.

(v) Since the Buildings were built by Zhong Tian Water Supply on lessor's land, we have assigned no commercial value to the Buildings. For reference purpose, assuming free from encumbrances, the depreciated replacement cost of the Buildings as at the valuation date would be approximately RMB1,420,000.

## 1. RESPONSIBILITY STATEMENT

This circular, for which the Directors collectively and individually accept full responsibility, includes particulars given in compliance with the GEM Listing Rules for the purpose of giving information with regard to the Company. The Directors, having made all reasonable enquiries, confirm that, to the best of their knowledge and belief:

(1) the information contained in this circular is accurate and complete in all material respects and not misleading;

(2) there are no other matters the omission of which would make any statement in this circular misleading; and

(3) all opinions expressed in this circular have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

## 2. DISCLOSURE OF INTERESTS

### (A) Directors and chief executive of the Company

As at the Latest Practicable Date, the following Directors had or was deemed to have interests or short positions in the Shares, underlying Shares or debentures of the Company and its associated corporations (within the meaning of Part XV of the SFO) (i) which were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which they were taken or deemed to have under such provisions of the SFO); or (ii) which were required, pursuant to section 352 of the SFO, to be entered in the register referred to therein; or (iii) which were, pursuant to rules 5.46 to 5.67 of the GEM Listing Rules relating to securities transactions by Directors to be notified to the Company and the Stock Exchange:

*(i) Long positions in the Shares*

| Name of Director | Nature of interest | Number of Shares held | Approximate percentage of issued share capital of the Company |
|---|---|---|---|
| Mr. Yang | Beneficial | 177,125,000 | 13.31% |
| Mr. Pang | Beneficial | 10,500,000 | 0.79% |
| Mr. Ma | Beneficial | 870,000 | 0.07% |
| Mr. Mo | Beneficial | 21,385,920 | 1.61% |
| Ms. Au | Beneficial | 22,500,000 | 1.69% |

Save as disclosed above, as at the Latest Practicable Date, none of the Directors nor the chief executive of the Company had or was deemed to have any interests or short positions in the Shares, underlying Shares or debentures of the Company and its associated corporations (within the meaning of Part XV of the SFO) (i) which were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which they were taken or deemed to have under such provisions of the SFO); or (ii) which were required, pursuant to section 352 of the SFO, to be entered in the register referred to therein; or (iii) which were, pursuant to rules 5.46 to 5.67 of the GEM Listing Rules relating to securities transactions by Directors to be notified to the Company and the Stock Exchange.

**(B) Substantial Shareholders**

As at the Latest Practicable Date, so far as is known to the Directors, as at the Latest Practicable Date, the following person (not being Directors or chief executive of the Company) had, or was deemed to have, interests or short positions in the Shares or underlying Shares 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 who were 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 any member of the Group:

| Name of Shareholder | Nature of interest | Number of Shares held | Position | Approximate percentage of issued share capital of the Company |
|---|---|---|---|---|
| Mr. Lau *(Note 1)* | Through a corporation | 299,478,238 | Long | 22.51% |
| Ms. Chan Yiu Kan Katie *(Note 1)* | Interest of spouse | 299,478,238 | Long | 22.51% |
| Manciple *(Note 1)* | Beneficial | 299,478,238 | Long | 22.51% |

*Note:*

1. Manciple is wholly and beneficially owned by Mr. Lau. Manciple beneficially owns 299,478,238 Shares. Under the SFO, Mr. Lau is deemed to be interested in 299,478,238 Shares. Ms. Chan Yiu Kan Katie, the wife of Mr. Lau, is also deemed to be interested in 299,478,238 Shares.

Save as disclosed above, as at the Latest Practicable Date, the Directors 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 or short positions in the Shares or underlying Shares (including any interests in options in respect of such capital), 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 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 any member of the Enlarged Group.

## 3. DIRECTORS' SERVICE CONTRACTS

As at the Latest Practicable Date, none of the Directors has entered into any service contract or management agreement, proposed or otherwise with any member of the Enlarged Group (excluding contracts expiring or terminable by the employer within one year without payment of compensation other than statutory compensation).

## 4. COMPETING INTERESTS

As at the Latest Practicable Date, none of the Directors or the management Shareholders (as defined in the GEM Listing Rules) or substantial Shareholder or any of their respective associates has any interest in business which competes with or may compete with the business of the Group or has any other conflict of interests which any person has or may have with the Group.

## 5. LITIGATION

As at the Latest Practicable Date, no member of the Enlarged Group was engaged in any litigation or arbitration of material importance and no litigation, arbitration or claim of material importance was known to the Directors to be pending or threatened against any member of the Enlarged Group.

## 6. INTERESTS IN CONTRACTS AND ASSETS

Rise Assets has issued promissory note of HK$24,031,250 to Mr. Yang on 21 May 2007 for part of the consideration in relation to the acquisition of entire interest in Silky Sky. As at the Latest Practicable Date, Rise Assets has repaid HK$23,000,000 to Mr. Yang. Save as disclosed, as at the Latest Practicable Date, no contract or arrangement of significance in relation to the Enlarged Group's business to which any member of the Enlarged Group was a party and in which any of the Directors had a material interest, whether directly or indirectly, subsisted as at the Latest Practicable Date.

None of the Directors nor expert referred to in paragraph 9 has any direct or indirect interests in any assets which had been acquired or disposed of by or leased to, or which are proposed to be acquired or disposed of by or leased to, any member of the Enlarged Group during the period since 31 December 2006, the date to which the latest published audited financial statements of the Group were made up, up to and including the Latest Practicable Date.

## 7. MATERIAL CONTRACTS

The following contracts (not being contracts in the ordinary course of business) have been entered into by members of the Enlarged Group within the two years immediately preceding the Latest Practicable Date which are or may be material:

(a) the underwriting agreement dated 20 January 2006 and entered into with the Company, Mr. Mo, Kingston Securities Limited, Quam Securities Company Limited and Hantec Capital Limited in relation to the rights issue of 442,475,040 rights Shares at HK$0.057 per rights Share;

(b) the warrant placing agreement dated 28 August 2006 and entered into among the Company as the issuer, Glory Force Limited as the subscriber and Mr. Yip as the guarantor in relation to the subscription of 117,800,000 unlisted warrants of the Company by Glory Force Limited at an issue price of HK$0.015 per warrant and subscription price of HK$0.155 per Share;

(c) the conditional legally binding memorandum of understanding dated 2 February 2007 and the formal sale and purchase agreement dated 21 March 2007 and entered into between Mr. Yang and Rise Assets, a wholly owned subsidiary of the Company in respect of the acquisition of Silky Sky for a total consideration of HK$61 million;

(d) the MOU;

(e) the Agreement; and

(f) the underwriting agreement dated 29 October 2007 entered into between the Company, Quam Securities Company Limited and Partners Capital International Limited in relation to the Open Offer.

Save as disclosed above, there are no other contracts (not being contracts in the ordinary course of business) being entered into by the members of the Group within the two years preceding the date of this circular, which are or may be material.

## 8. SHARE CAPITAL

The authorised share capital of the Company as at the Latest Practicable Date and immediately following the allotment and issue of the Conversion Shares are as follows:

| | | |
|---|---|---|
| ***Authorised*** | | *HK$* |
| 2,000,000,000 | Shares | 100,000,000 |
| ***Issued and to be issued, fully paid or credited as fully paid*** | | |
| 1,330,375,080 | Shares in issue as at the Latest Practicable Date | 66,518,754 |
| 40,000,000 | Conversion Shares to be allotted and issued | 2,000,000 |
| 1,370,375,080 | Shares | 68,518,754 |

## 9. EXPERTS

The following are the qualifications of the experts who have given an opinion or advice contained in this circular:

| **Name** | **Qualification** |
|---|---|
| Vision A. S. Limited | Certified Public Accountants |
| Greater China Appraisal Limited | Chartered Valuation Surveyor<br>Registered Professional Surveyor Valuer |
| Fujian Minjiang Law Firm | PRC lawyer |

As at the Latest Practicable Date, Vision A. S. Limited, Fujian Minjiang Law Firm and Greater China Appraisal Limited did not have any interests, either direct or indirect, in any assets which have been acquired or disposed of by or leased to or are proposed to be acquired or disposed of by or leased to any member of the Enlarged Group since 31 December 2006, the date to which the latest published audited consolidated financial statements of the Enlarged Group were made up.

As at the Latest Practicable Date, Vision A. S. Limited, Fujian Minjiang Law Firm and Greater China Appraisal Limited were not interested beneficially or non-beneficially in any shares in the Company or any of its subsidiaries or any right or option (whether legally enforceable or not) to subscribe for or to nominate persons to subscribe for securities in any member of the Group.

Vision A. S. Limited, Fujian Minjiang Law Firm and Greater China Appraisal Limited have given and have not withdrawn their written consents to the issue of this circular with the inclusion of their respective letters and/or reports and/or reference to their name in the form and context in which they respectively appears.

## 10. MISCELLANEOUS

(a) The registered office of the Company is located at Caledonian Bank & Trust Limited, Caledonian House, P.O. Box 1043, George Town, Grand Cayman, Cayman Islands.

(b) The head office and principal place of business of the Company in Hong Kong is 15/F., Sun House, 181 Des Voeux Road Central, Hong Kong.

(c) The branch share registrar and transfer office in Hong Kong of the Company is Tricor Standard Limited located at 26th Floor, Tesbury Centre, 28 Queen's Road East, Wanchai, Hong Kong.

(d) The company secretary and qualified accountant of the Company is Ms. Au Shui Ming, Anna, who is a certified practicing accountant of CPA Australia and a fellow member of the Hong Kong Institute of Certified Public Accountants.

(e) The compliance officer of the Company is Mr. Mo Wai Ming, Lawrence who is also an executive Director.

(f) The Company has established an audit committee with written terms of reference prepared and adopted with reference to the guidelines recommended by the Hong Kong Institute of Certified Public Accountants. The audit committee provides an important link between the Board and the Company's auditors in matters coming within the scope of the Group's audit. It also reviews the effectiveness of both the external and internal audit and of internal controls and risk evaluation. The audit committee comprises three members, namely Mr. Hsu William Shiu Foo, Mr. Lee Kun Hung and Mr. Kwok Chi Sun, Vincent who are all independent non-executive Directors. Further details of them are set out below:

Mr. Hsu William Shiu Foo, aged 57, is an independent non-executive Director and audit committee member of the Company. Mr. Hsu has over 10 years of global business experience in tourism and service-oriented related fields in various international corporations. Mr. Hsu holds a Bachelor degree in Arts from Brigham Young Univesity, Hawaii and a Master degree in Hotel Administration from Cornell University, New York. Mr. Hsu is currently an independent non-executive director of other listed companies.

Mr. Lee Kun Hung, aged 41, is an independent non-executive Director and audit committee member of the Company. Mr. Lee has over 15 years of manufacturing experience in the watch industry. Mr. Lee holds a Bachelor of Arts degree from Boston College, Massachusetts, US. Mr. Lee has not held any directorship in any listed company in the last three years.

Mr. Kwok Chi Sun, Vincent, aged 45, is an independent non-executive Director and audit committee member of the Company. Mr. Kwok is a sole proprietor of Vincent Kwok & Co., and is a Certified Public Accountant. He is an independent non-executive director of other listed companies.

(g) The English texts of this circular and the accompanying form of proxy shall prevail over their respective Chinese texts in case of inconsistency.

## 11. DOCUMENTS AVAILABLE FOR INSPECTION

Copies of the following documents are available for inspection at the principal place of business of the Company at 15/F., Sun House, 181 Des Voeux Road Central, Hong Kong during normal business hours on any weekday other than public holidays, from the date of this circular up to and including the date of the EGM:

(a) the memorandum and articles of association of the Company;

(b) the service contracts referred to in the paragraph headed "Directors' service contracts" in this appendix;

(c) the material contracts referred to in the paragraph headed "Material contracts" in this appendix;

(d) the accountants' report of Proud Dragon Group, the text of which is set out in appendix I to this circular;

(e) the accountants' report of Zhong Tian Water Supply, the text of which is set out in appendix II;

(f) the annual reports of the Company for each of the three financial years ended 31 December 2006;

(g) the interim report of the Company for the six months ended 30 June 2007;

(h) the letter from Vision A. S. Limited in respect of the unaudited pro forma financial information on the Enlarged Group, the text of which is set out in appendix IV to this circular;

(i) the accountants' report of Silky Sky, the text of which is set out in appendix V to this circular;

(j) the unaudited pro forma financial information of the Group as enlarged by the acquisition of Silky Sky, the text of which is set out in appendix VI to this circular;

(k) the valuation report issued by Greater China Appraisal Limited, the text of which is set out in appendix VII to this circular;

(l) the written consents from Vision A. S. Limited, Fujian Minjiang Law Firm and Greater China Appraisal Limited referred to in paragraph 9 of this appendix;

(m) the circular dated 20 April 2007 in relation to the acquisition of the entire interest in Silky Sky;

(n) the prospectus of the Company dated 26 November 2007 in relation to the Open Offer; and

(o) this circular.

# KANHAN TECHNOLOGIES GROUP LIMITED
# 看漢科技集團有限公司*

*(Proposed to be renamed as Shen Nong China (Group) Limited 神農中國(集團)有限公司)*
*(incorporated in the Cayman Islands with limited liability)*
(Stock Code: 8175)

**Notice is hereby given** that an extraordinary general meeting (the "**Meeting**") of KanHan Technologies Group Limited (the "**Company**") will be held at 15th Floor, Sun House, 181 Des Voeux Road Central, Hong Kong on Monday, 4 February 2008 at 11:00 a.m. for the purpose of considering and, if thought fit, passing the following resolution:

## ORDINARY RESOLUTION

"**THAT**

(a) the conditional sale and purchase agreement (the "**Agreement**") dated 29 October 2007 and entered into among Rise Assets Limited ("**Rise Assets**"), a wholly-owned subsidiary of the Company, as purchaser, Mr. Yip Yuk Tong (the "**Vendor**") as vendor and Proud Dragon Limited ("**Proud Dragon**"), supplemented by the supplemental agreement (the "**Supplemental Agreement**") dated 14 January 2008 and entered into among Rise Assets, the Vendor and Proud Dragon, in relation to the acquisition of 318 ordinary shares (the "**Proud Dragon Shares**") of US$1.00 each in the share capital of Proud Dragon at a consideration of HK$31,800,000 by Rise Assets from the Vendor and in relation to the subscription of 158 Proud Dragon Shares by Rise Assets from Proud Dragon at a consideration of HK$15,800,000 (copy of the Agreement and the Supplemental Agreement have been produced to the Meeting marked "A" and "B" and signed by the chairman of the Meeting for the purpose of identification) and the transactions contemplated thereunder, be and are hereby approved, confirmed and ratified;

(b) any one or more of the directors (the "**Directors**") of the Company be and is/are hereby authorised to do all other acts and things and execute all documents which he/they consider(s) necessary or expedient for the implementation of and giving effect to the Agreement as supplemented by the Supplemental Agreement and the transactions contemplated thereunder;

(c) the issue of a convertible bond (the "**Convertible Bond**") in the principal amount of HK$10,000,000 by the Company in accordance with the terms and conditions of the Agreement as supplemented by the Supplemental Agreement and the transactions contemplated thereunder be and is hereby approved; and

(d) any one or more of the Directors be and is/are hereby authorised to take all steps necessary or expedient in his/their opinion to implement and/or give effect to the issue of the Convertible Bond, including but not limited to the allotment and issue of ordinary shares (the "**Shares**") of HK$0.05 each in the share capital of the Company of which may fall to be issued upon the exercise of the conversion rights attached to the Convertible Bond."

By order of the Board
**KanHan Technologies Group Limited**
**Pang Hong Tao**
*Chairman*

Hong Kong, 18 January 2008

* *For identification purpose only*

*Registered office:*
Caledonian Bank & Trust Limited
Caledonian House
P.O. Box 1043
George Town
Grand Cayman
Cayman Islands

*Head office and principal place of business in Hong Kong:*
15/F., Sun House
181 Des Voeux Road Central
Hong Kong

*Notes:*

1. A member entitled to attend and vote at the Meeting convened by the above notice is entitled to appoint one or more proxy to attend and, subject to the provisions of the articles of association of the Company, vote in his stead. A proxy need not be a member of the Company but must be present in person at the Meeting to represent the member. If more than one proxy is so appointed, the appointment shall specify the number and class of shares in respect of which each such proxy is so appointed.

2. A form of proxy for use at the Meeting is enclosed. In order to be valid, the form of proxy must be duly completed and signed in accordance with the instructions printed thereon and deposited together with a power of attorney or other authority, if any, under which it is signed, or a notarially certified copy of such power or authority, at the offices of the Company's Hong Kong share registrar in Hong Kong, Tricor Standard Limited at 26th Floor, Tesbury Centre, 28 Queen's Road East, Wanchai, Hong Kong not less than 48 hours before the time appointed for holding the Meeting or any adjournment thereof. Completion and return of a form of proxy will not preclude a member from attending in person and voting at the above Meeting or any adjournment thereof, should he so wish.

3. In the case of joint holders of shares, any one of such holders may vote at the Meeting, either personally or by proxy, in respect of such share as if he was solely entitled thereto, but if more than one of such joint holders are present at the meeting personally or by proxy, that one of the said persons so present whose name stands first in the register of members of the Company in respect of such Shares shall alone be entitled to vote in respect thereof.