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OVERVIEW

We are principally engaged as a main contractor in the provision of (i) waterworks engineering services; (ii) road works and drainage services; (iii) LPM Services; and (iv) building works. We are also engaged in site formation works for the public and private sectors in Hong Kong.

Kwan On, a member of our Group, is one of the Group C contractors (confirmed) for waterworks engineering services and one of the Group C contractors (confirmed) for road works and drainage services. Group C contractors are the highest ranking contractors in terms of tender limits, and can tender for public works with contracts sum of any value exceeding HK\$185 million. Kwan On is also one of the Group A contractors (probationary) for building works and Group B contractors (confirmed) for site formation works. In addition, Kwan On is one of the contractors on the Specialist List for “Landslip Preventive/ Remedial Works to Slopes/Retaining Walls” category. Members of our Group also hold other licences and certificates granted by BD and EMSD. Please refer to the paragraph headed “Licences and certificates held by our Group” below under this section for further details.

During the Track Record Period, most of the works undertaken by us were civil engineering projects for WBDB. Revenue generated from Government contracts, including those awarded by WSD, CEDD, ArchSD and DSD, represented approximately 95.5%, 97.7% and 99.9% respectively of our total revenue for each of the two years ended 31 March 2014 and the six months ended 30 September 2014. The duration of our projects for the public sector generally ranged from 6 months to 48 months, depending on the size of the contract and the complexity of the works undertaken. Projects undertaken by us for the private sector generally included slope stabilization, upgrading and remedial works for HA, school, hospital and private residence.

The following table sets forth a breakdown of our revenue by categories of services provided during the Track Record Period:

Types of services	Year ended 31 March		Six months ended 30 September	
	2013	2014	2013	2014
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
	<i>(unaudited)</i>			
Waterworks engineering services	158,892	208,084	87,007	119,767
Road works and drainage	43,237	107,914	31,981	135,043
LPM Services	109,751	63,335	31,116	74,603
Building works	—	13,950	3,381	2,950
	<u>311,880</u>	<u>393,283</u>	<u>153,485</u>	<u>332,363</u>

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During the Track Record Period and up to the Latest Practicable Date, we had completed 12 projects for both the public and private sectors in Hong Kong with a total value of works certified of approximately HK\$819.54 million. As at the Latest Practicable Date, we had 14 projects in progress, of which 11 were tendered by Kwan On and 3 were tendered by our Group’s joint venture or joint operations. For details of the projects undertaken by us, please refer to the sub-section headed “Contracts completed and contracts in progress” under this section below.

Depending on our manpower availability, the expertise required, the level of complexity of works involved, cost effectiveness and licencing requirements, we may appoint subcontractors to carry out certain parts of the contracts works. We have maintained a list of approved subcontractors, the selection of which are based on a set of criteria including previous job references, reputation in the industry, price competitiveness, quality of work and skill sets of workers of the subcontractors. As at the Latest Practicable Date, there were over 20 subcontractors on our list of approved subcontractors, with our five largest subcontractors having maintained business relationship with us for up to nine years. In order to closely monitor the performance of the subcontractors and to ensure that the subcontractors comply with the requirements and provisions set out in the respective main contracts and the relevant laws, rules and regulations, we have specific subcontractor management plan for each contract undertaken by us. Our project manager is responsible for supervising and monitoring the works provided by our subcontractors and for ensuring their compliance with the requirements and provisions of the respective main contracts and the relevant laws, rules and regulations. For details of the arrangement between our subcontractors and us, please refer to the sub-section headed “Control over subcontractors” under this section below.

During the Track Record Period, the principal construction materials used by our subcontractors and us include various kinds of pipes (including mild steel pipes, ductile iron pipes and polyethylene pipes), fittings, steel bars, concrete and asphalt, which are sourced from a number of suppliers. During the Track Record Period, there were more than 20 materials suppliers on our approved list of suppliers, with our five largest suppliers having maintained business relationship with us for up to nine years. Before admitting a supplier to our approved list, we will take into account a host of factors including its product quality, punctuality of delivery, job references and reputation in the industry. Please refer to the paragraph headed “Material suppliers” under the sub-section headed “Suppliers” in this section below.

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MAJOR SERVICES

Waterworks engineering services

Our waterworks engineering services mainly involve the replacement and rehabilitation of aged water mains, including laying associated service pipes and making service connections to the water mains. Our services also include construction of pumping stations, service reservoirs, mainlaying and all the associated civil, structural, geotechnical, landscaping, electrical and mechanical works including site formation, excavation, pipe jacking, and permanent and temporary accesses.

Set out below are the main types of our waterworks works:



1. *Laying of water mains*

Contract number: 10/WSD/10

Replacement and rehabilitation of water mains, Stage 4 Phase 1 – mains in Shatin and Sai Kung



2. *Construction of pumping stations*

Contract number: 6/WSD/06

Construction of salt water supply system for Penny's Bay



3. *Construction of service reservoirs*

Contract number: 6/WSD/11

Construction of water supply system to housing development at Anderson Road

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Road works and drainage services

Our road works and drainage services generally include construction of local roads with junction improvement and the associated footpaths and planting areas; restoration of area; slope stabilisation works; and construction of associated drains, sewers and water mains and landscaping works.

Set out below are the main types of our road and drainage works:



1. *Construction of roads with junction*

Contract number: TK/2008/01
Tseung Kwan O Development – Site Formation and infrastructure works at Pak Shing Kok



2. *Construction of associated drains, sewers and water mains and landscaping works*

Contract number: TK/2008/01
Tseung Kwan O Development – Site Formation and infrastructure works at Pak Shing Kok

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LPM Services

Our LPM Services generally include upgrading of slopes and retaining walls and include installation of soil nails and raking drains, rock slope stabilisation works and slope cutting in association with surface drainage channel construction and landscaping works.

Set out below are the main types of our LPM Services:



1. *Slope maintenance*

Contract number: GE/2011/03
Landslip Prevention and Mitigation Programme, 2008, Package C, landslip prevention and mitigation works in Kowloon and Hong Kong



2. *Installation of soil nails*

Contract number: GE/2011/03
Landslip Prevention and Mitigation Programme, 2008, Package C, landslip prevention and mitigation works in Kowloon and Hong Kong

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Site formation works

Site formation works broadly involve demolition of existing structures, excavation to the design formation level and/or filling to form a new site for later development and associated drainage and slope stabilization works.

Set out below is the main type of our site formation works:



1. *Site formation works*

Contract number: TK/2008/01
Tseung Kwan O Development – Site Formation and infrastructure works at Pak Shing Kok

Building works

General building contractors may carry out general building works and street works which do not include any specialised works designated for registered specialist contractors. We provide building works for both the public and private sectors in Hong Kong.

Our Directors consider that the financial, technical and management requirements for a contractor to engage in civil engineering projects for the public sector in Hong Kong create effective barriers to international and local contractors who are not currently on the Contractor List and Specialist List from entering the sector. Our Directors also consider that the contract sums of civil engineering projects for the public sector in Hong Kong are always larger than those of projects for the private sector. As such, we focus on undertaking civil engineering projects for the public sector in Hong Kong and our revenue is largely derived from the provision of waterworks engineering services, roads and drainage services and LPM Services for the public sector in Hong Kong during the Track Record Period.

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COMPETITIVE STRENGTHS

Our Directors believe that with our experienced management team and extensive project experience in the implementation of waterworks projects, road works and drainage projects and landslip preventive and mitigative projects, our Group has established a reputation in the civil engineering and construction industry in Hong Kong. In particular, our Directors believe that our Group possesses the following competitive strengths:

Established operating history and proven track record

We have an operating history of over 30 years. Since the acquisition of Kwan On in 1993, we have undertaken more than 30 projects including civil engineering contracts of waterworks engineering, roads and drainage works and landslip preventive and mitigative works in Hong Kong. Kwan On’s quarterly performance ratings as appraised by WBDB were above the industry averages in the recent ten consecutive quarters up to the third quarter of 2014. Our Directors consider that our proven track record and our ability to execute works of satisfactory quality are the crucial factors to our success in the industry.

Diversified experience and capabilities

We are one of the Group C contractors (confirmed) for waterworks and one of the Groups C contractors (confirmed) for roads and drainage services on the Contractor List. As at the Latest Practicable Date, there were 22 and 41 Group C contractors (confirmed) under the categories of “Waterworks” and “Roads and Drainage”, respectively, in the Contractor List. We are also one of the Group A contractors (probationary) for building works and Group B contractors (confirmed) for site formation works on the Contractor List. In addition, we are one of the approved specialist contractors on the Specialist List for LPM Services. We also possess other licenses granted by BD and EMSD which could benefit us to obtain contracts from the private sector. Details of the licences and certificates held by us are set out in the subsection headed “Licences and certificates held by our Group” under this section below. Throughout the years of operations, we have accumulated experience in a variety of civil engineering projects, including waterworks projects, road works and drainage projects and landslip preventive and mitigative projects. Our Directors consider that with the abovementioned qualifications and accumulated experience, we will be able to continue undertaking civil engineering projects of various kinds.

Experienced management team

Our management team has extensive experience in the civil engineering industry. Mr. Tony Wong, who is an executive Director, has more than 20 years of experience in handling various civil engineering projects in Hong Kong. Mr. Kwong and Mr. Chung, both are executive Directors, have more than 20 years of experience in the construction industry in Hong Kong respectively. As at the Latest Practicable Date, all members of our senior management team had received tertiary education and/or above or obtained professional qualifications. For further details of the biographies and relevant industry experience of our management team, please refer to the section headed “Directors and senior management” in this document. Our Directors consider that the qualifications and experience of our senior

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management team help us formulate competitive tenders, which are essential to securing new contracts, and in carrying out efficient and timely implementation and management of project works.

Stable relationships with our subcontractors and construction materials suppliers

We have established stable business relationships for up to nine years with our five largest subcontractors during the Track Record Period. Having stable working relationship with our subcontractors enables us to have comprehensive assessment of their ability and quality of works and also allow us to enjoy stable subcontracting services. We also maintain stable relationships for up to nine years with our five largest materials suppliers during the Track Record Period to ensure adequate supply of materials to us, in terms of both quality and quantity. Please refer to the sub-section headed “Suppliers” under this section below for further details.

BUSINESS STRATEGIES

Our business objective is to achieve sustainable growth in our current businesses by strengthening our position as a main contractor in the provision of civil engineering services in Hong Kong. We intend to achieve our business objective by pursuing the following strategies:

Expanding our business scale and diversifying our source of income

Kwan On was upgraded to Group C contractor (confirmed) under the “Roads and Drainage” category and Group B contractor (confirmed) under the “Site Formation” category on 26 February 2013 and 19 June 2013 respectively, which has further enhanced our ability to tender for and secure works projects with larger contract values under these two categories. Our Directors plan to expand our business scale through securing more works contracts with contract sum of HK\$300 million or above and diversify our source of income by tendering for more contracts originated from CEDD and DSD in view of the upcoming opportunities arising from projects and continuous capital expenditure from the two departments. Please refer to the section headed “Industry Overview” in this document for the details of works and opportunities under the aforesaid two departments.

Further strengthening our manpower

Apart from the requirements on the employed capital and working capital, Kwan On is also required to employ a minimum number of full time management and technical personnel with the necessary qualifications as stipulated in the ETWB Handbook in order to be retained on the Contractor List (both on confirmed and probationary status). As such, with the expansion of our business scale in the future, we plan to recruit additional management and technical personnel to fulfill the requirements for retaining on the Contractor List. In addition, in order to uphold the work quality of the projects undertaken by our Group and to provide a safety and healthy working environment for our workers, subcontractors and the public, we intend to recruit additional personnel to strengthen our quality assurance and safety teams.

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Acquisition of additional equipment and machinery to strengthen our ability of project implementation

We intend to source and purchase additional equipment and machinery to strengthen our project implementation ability in anticipation of the expansion of our business scale in the future. Such equipment and machinery include but not limited to backhoe, air compressor and crane. We intend to allocate approximately HK\$2.1 million or 8.0% of the net proceeds from the [REDACTED] for the acquisition of additional equipment and machinery. Please refer to the section headed “Statement of business objective and use of proceeds” in this document for details of the relevant time frame, estimate capital expenditure and implementation plan.

As at the Latest Practicable Date, we have not identified any target for acquisition and do not have any acquisition plan.

LICENCES AND CERTIFICATES HELD BY OUR GROUP

The following tables summarise the details of the licences held by the members of our Group as approved contractors as at the Latest Practicable Date:

Relevant authority	Relevant List	Licence/ Certificate	Holder	Date of Expiry (Note 7)
WBDB	Approved Contractors for Public Works – Waterworks Category	Group C (confirmed) (Notes 1, 2 and 8)	Kwan On	Not applicable
WBDB	Approved Contractors for Public Works – Roads and Drainage Category	Group C (confirmed) (Notes 1, 3 and 8)	Kwan On	Not applicable
WBDB	Approved Contractors for Public Works – Site Formation Category	Group B (confirmed) (Notes 1, 4 and 8)	Kwan On	Not applicable
WBDB	Approved Contractors for Public Works – Buildings Category	Group A (probationary) (Notes 1, 5 and 8)	Kwan On	Not applicable
WBDB	Approved Suppliers of Materials and Specialist Contractors for Public Works – Landslip Preventive/Remedial Works to Slopes/ Retaining Walls	Confirmed (Note 6)	Kwan On	Not applicable

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Notes:

1. The financial criteria for retention on the Contractor List for the respective categories (on confirmed and probationary status) are established by WBDB. Such financial criteria primarily concern the levels of employed capital and working capital of a contractor. To ascertain that the required financial criteria and requirements are met, our Group is required to:
 - (a) submit the original or a certified true copy of their latest audited accounts;
 - (b) submit certified statements of outstanding workload;
 - (c) provide supplementary information as and when required to enable WBDB to carry out ad hoc financial assessment; and
 - (d) answer all reasonable enquiries from WBDB.

Apart from the aforesaid financial criteria, our Group is also required to employ a minimum number of full time management and technical personnel with the required qualifications as stipulated in the ETWB Handbook in order to be retained on the Contractor List (on confirmed and probationary status).

2. As at the Latest Practicable Date, the minimum management and technical personnel criteria for the "Waterworks" category were fulfilled by Mr. Tony Wong and Mr. Kwong, respectively.
3. As at the Latest Practicable Date, the minimum management and technical personnel criteria for the "Roads and Drainage" category were fulfilled by Mr. Tony Wong and Mr. Sit Cheung Yee, Simon, project manager of our Group, respectively.
4. As at the Latest Practicable Date, the minimum management and technical personnel criteria for the "Site Formation" category were fulfilled by Mr. Tony Wong and Mr. Chung, respectively.
5. As at the Latest Practicable Date, the minimum management and technical personnel criteria for the "Buildings" category were fulfilled by Mr. Tony Wong and Mr. Mak Kam Ho, Danny, procurement manager (building materials and plants) of our Group, respectively.
6. As at the Latest Practicable Date, the minimum management and technical criteria for the "Landslip Preventive/Remedial Works to Slopes/Retaining Walls" category were fulfilled by Mr. Tony Wong and our other employees respectively.
7. These licences granted by WBDB do not have specified expiry dates and their retention are subject to fulfillment of criteria provided in the ETWB Handbook and regulatory actions taken by WBDB.
8. Apart from Mr. Tony Wong, the Group have submitted the proposed nomination letter to Development Bureau, Government Secretariat in relation to the nomination of Ms. Tai Mei Kiu and Dr. Wong Chun Hung, who can fulfil the requirement as stipulated in the ETWB Handbook, as top management in addition to Mr. Tony Wong.

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Relevant authority	Type of registration	Holder	Date of registration	Date of expiry (Note)
BD	Registered Specialist Contractor – Demolition	Kwan On	8 June 2000	28 March 2015
BD	Registered Specialist Contractor – Foundation	Kwan On	8 June 2000	13 March 2018
BD	Registered General Building Contractor	Kwan On	27 October 2005	4 November 2017
BD	Registered Specialist Contractor – Site Formation	Kwan On	26 May 2000	25 February 2018
BD	Registered Specialist Contractor – Demolition	UEL	28 January 2002	3 December 2016
BD	Registered General Building Contractor	UEL	30 October 2000	6 November 2015
BD	Registered Specialist Contractor – Site Formation	UEL	19 March 2001	25 July 2016
EMSD	Registered Electrical Contractor	UEL	20 November 1998	19 November 2016

Note: Pursuant to section 8C(2)(c) of the Building Ordinance, a registered contractor shall apply to the BD for renewal of registration not later than 28 days prior to the date of expiry of the registration. As at the Latest Practicable Date, applications for renewal in respect of these registration have been submitted to BD.

As advised by the Hong Kong Legal Advisers, provided that Kwan On and UEL fulfill all prerequisite requirements as set out by the relevant authority, there is no legal impediment for Kwan On and UEL to renew the requisite licences upon their expiry. The respective Government departments will issue reminders for renewal of our licences before their expiry dates. Our Administration Department will arrange the application for renewal accordingly before expiry.

Our Directors confirm that each member of our Group has been granted all the required licences and approvals for carrying on our business activities and confirm that such required licences and approvals were valid and subsisting as at the Latest Practicable Date. Up to the Latest Practicable Date, our Group did not have any historical incidents of non-satisfaction of the statutory minimum employed capital and working capital requirements for maintenance of our approved contractor status.

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During the Track Record Period, our contracts for public sector were tendered by and awarded to (i) Kwan On, a member of our Group which held the licences granted by WBDB; or (ii) an unincorporated joint venture formed by Kwan On and U-Tech, namely Kwan On – U-Tech 1; or (iii) the joint operations formed by Kwan On and its business partners, namely Kwan On – China Geo and Kwan On – U-Tech 2. When a contract is awarded to Kwan On, Kwan On may undertake the contract works by itself or subcontract the contract works to any one of UEL, UECL and UEWL. Contractors who tender for contracts from the Government are required to hold the relevant licences granted by WBDB as approved contractors. Contractors are not required to subcontract works only to subcontractors which are holders of the relevant licences granted by WBDB as approved contractors. Accordingly, other subsidiaries of our Group, which act as subcontractors of Kwan On in the execution of works contracts, are not required to obtain licences granted by WBDB. As for contract 10/WSD/10, Kwan On – U-Tech 1 undertakes part of the works while subcontracts the remaining works to subcontractors and U-Tech is one of its subcontractors. As for contracts 4/WSD/11 and 9/WSD/13, the joint operations subcontract all of the works to subcontractor(s) who will be responsible for the necessary labour, plant, materials and all the expenses to complete the project. Further details of Kwan On – U-Tech 1, Kwan On – China Geo and Kwan On – U-Tech 2 can be found under the paragraph headed “Mode of operation of Kwan On – U-Tech 1, Kwan On – China Geo and Kwan On – U-Tech 2” in this section below.

CONTRACTS COMPLETED AND CONTRACTS IN PROGRESS

During the Track Record Period, most of the works undertaken by us were civil engineering projects for the public sector. The duration of our projects in the public sector generally ranged from 6 months to 48 months, depending on the size of the contract and the complexity of the works undertaken. Projects undertaken by us for the private sector generally included slope stabilisation, upgrading and remedial works for HA, schools, hospitals and private residences.

Contracts completed

Set out below are the details of the contracts completed by us during the Track Record Period and up to the Latest Practicable Date:

Contract number	Customer	Particulars of the contract	Contract period (Note 1)	Time of completion (Note 2)	Amount of works certified (Note 3)	Reason(s) for extension of time (Note 10)
SX X121	ArchSD	Slope upgrading works of geotechnical feature No.11SE-A/F435 at the Woodside, Mount Parker Road	17 August 2011 to 12 May 2012	18 July 2012	HK\$12.83 million	Inclement weather and variation orders
YL/2008/01	CEDD	Kau Hui Development, Engineering Works in Area 16, Yuen Long, Phase 2 Extension of Road L3	12 September 2011 to 9 July 2013 (Note 9)	9 July 2013	HK\$2.66 million	Variation orders
TK/2008/01	CEDD	Tseung Kwan O Development – Site Formation and infrastructure works at Pak Shing Kok	27 March 2009 to 21 September 2012	26 September 2012	HK\$165.22 million	Inclement weather, variation orders and unpredictable obstructions

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Contract number	Customer	Particulars of the contract	Contract period (Note 1)	Time of completion (Note 2)	Amount of works certified (Note 3)	Reason(s) for extension of time (Note 10)
20090074	HA	Landslip preventive works for slopes and retaining walls – Term contract for slop maintenance and improvement works for Region D	7 December 2009 to 7 June 2012	14 March 2013	HK\$27.12 million	Inclement weather and variation orders
Not applicable	Tung Wah Hospital	Slope upgrading works for Feature No.11SW-A/CR82 at Tung Wah Hospital, 12 Po Yan Street, Sheung Wan, Hong Kong	27 September 2010 to 26 April 2011	4 June 2012 (Note 7)	HK\$4.81 million	Inclement weather and variation orders
GE/2011/03	CEDD	Landslip Prevention and Mitigation Programme, 2008, Package C, Landslip Prevention and Mitigation Works in Kowloon and Hong Kong Island	27 October 2011 to 25 April 2013	17 July 2013	HK\$60.95 million	Inclement weather, variation orders and identification of potential unexploded ordinance
DC/2009/25	DSD	Construction of Intercepting Drains at Shun Tat Street, Tuen Mun and Remaining Works at Sha Po Tsuen, Yuen Long	12 September 2011 to 15 November 2012 (Note 9)	19 August 2013	HK\$10.87 million	Inclement weather and variation orders
24/WSD/09	WSD	Salt Water Supply for Northwest New Territories – Construction of Tan Kwai Tsuen Salt Water Service Reservoir and Associated Works	11 January 2010 to 11 October 2012	12 November 2013	HK\$104.81 million	Inclement weather and variation orders and unpredictable obstructions
YL/2009/01	CEDD	Hang Hau Tsuen Channel at Lau Fau Shan	29 December 2009 to 27 December 2012	30 May 2013	HK\$79.41 million	Inclement weather and variation orders
20100095	HA	Underground Utilities Investigation Term Contract (2011-2013)	31 August 2011 to 31 August 2013	31 August 2013	HK\$8.22 million	Not applicable
26/WSD/06	WSD	Replacement and Rehabilitation of water Mains, Stage 2, Mains in Wong Tai Sin, Kowloon Bay and Kwun Tong	6 June 2007 to 4 April 2011	4 July 2011	HK\$217.93 million	Inclement weather
11/WSD/08	WSD	Replacement and Rehabilitation of water Mains, Stage 3 – Mains in HK Zoological & Botanical Gardens & Mid-level Areas	4 May 2009 to 2 May 2012	30 April 2012	HK\$124.71 million	Non-possession of site, late issuance of excavation permit and variation orders
Total					HK\$819.54 million	

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Contracts in progress as at the Latest Practicable Date

Set out below are the details of our contracts in progress as at the Latest Practicable Date:

1. Contracts tendered by Kwan On

Contract number	Customer	Particulars of the contract	Contract period (Note 1)	Extended date for completion	Reason for extension of time	Estimated contract sum (Note 4)	Value of works certified	Percentage of works certified (Note 5)	Outstanding contract value	Revenue expected to be recognised	
										Year ending 31 March 2015	Year ending 31 March 2016
GE/2010/21	CEDD	Landslip Prevention and Mitigation Programme, 2008, Packages J and M, Landslip prevention and mitigation works in Wan Chai	11 November 2011 to 11 May 2014 (Note 13)	17 June 2014	Inclement weather	HK\$151.09 million	HK\$142.33 million	94.2%	HK\$8.76 million	HK\$27.49 million	–
6/WSD/11	WSD	Construction of water supply system to housing development at Anderson Road	30 December 2011 to 29 April 2015	3 October 2015	Inclement weather	HK\$147.26 million	HK\$129.97 million	88.3%	HK\$17.29 million	HK\$32.79 million	HK\$8.92 million
15/WSD/11	WSD	Replacement and rehabilitation of water mains, stage 4 phase 2 – mains on Outlying Islands	4 October 2012 to 5 April 2016	Not applicable	Not applicable	HK\$164.47 million	HK\$66.68 million	40.5%	HK\$97.79 million	HK\$31.48 million	HK\$49.70 million
DC/2012/05	DSD	Sewerage at Yuen Long Kau Hui and Shap Pat Heung	6 September 2012 to 6 September 2016	Not applicable	Not applicable	HK\$142.35 million	HK\$100.11 million	70.3%	HK\$42.24 million	HK\$41.59 million	HK\$24.66 million
SD B807	AcHS	Demolition of Block B of ex-Kennedy Town police married quarters, Kennedy Town, Hong Kong	24 September 2013 to 19 August 2014 (Note 14)	Not applicable	Not applicable	HK\$11.01 million	HK\$10.82 million	98.3%	HK\$0.19 million	HK\$3.13 million	–
KL/2012/03	CEDD	Kai Tak Development – Stage 4 infrastructure at former north apron area	19 September 2013 to 2 September 2017	Not applicable	Not applicable	HK\$830.17 million	HK\$184.14 million	22.2%	HK\$646.03 million	HK\$182.75 million	HK\$215.10 million
GE/2012/11	CEDD	Landslip Prevention and Mitigation Programme, 2009, Package C, Landslip Prevention and Mitigation Works in Lantau and Het Ling Chau	19 November 2013 to 18 November 2015	Not applicable	Not applicable	HK\$86.82 million	HK\$34.58 million	39.8%	HK\$52.24 million	HK\$30.10 million	HK\$26.43 million
GE/2013/06	CEDD	Landslip Prevention and Mitigation Programme, 2008, Package J, Landslip Prevention and Mitigation Works in New Territories	13 December 2013 to 11 June 2015	Not applicable	Not applicable	HK\$109.26 million	HK\$45.74 million	41.9%	HK\$63.52 million	HK\$38.53 million	HK\$6.69 million
GE/2013/17	CEDD	Landslip Prevention and Mitigation Programme, 2008, Package M, Landslip Prevention and Mitigation Works in Lantau North	27 December 2013 to 26 December 2015	4 January 2016	Inclement weather	HK\$75.04 million	HK\$29.51 million	39.3%	HK\$45.53 million	HK\$34.18 million	HK\$23.49 million
2013/0375	HA	Main Engineering Infrastructure in association with the Proposed Developments at Area 56 in Tung Chung	2 September 2014 to 1 March 2016	Not applicable	Not applicable	HK\$40.00 million	HK\$2.62 million	6.5%	HK\$37.38 million	HK\$10.00 million	HK\$29.55 million
GE/2013/16	CEDD	Landslip Prevention and Mitigation Programme, 2008, Package N, Landslip Prevention and Mitigation Works in Sham Wat, Tai O East, Upper Keung Shan and Keung Shan Road East in West Lantau	18 December 2014 to 19 June 2017	Not applicable	Not applicable	HK\$208.07 million	–	0.0%	HK\$208.07 million	HK\$17.85 million	HK\$82.10 million
Total						HK\$1,965.54 million	HK\$746.50 million				

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2. Contracts tendered by our Group’s joint venture or joint operations

Contract number	Customer	Tendered by	Particulars of the contract	Contract period	Estimated contract sum	Estimated total revenue to be received by our Group	Estimated total expenses to be recognised by our Group	Estimated total profit attributable to our Group
10/WSD/10	WSD	Kwan On – U-Tech 1	Replacement and rehabilitation of water mains, Stage 4 Phase 1 – mains in Shatin and Sai Kung (Note 6)	22 August 2011 to 21 April 2015	HK\$276.59 million	HK\$276.59 million	HK\$209.68 million	HK\$66.91 million
4/WSD/11 (Note 14)	WSD	Kwan On – China Geo	Construction of Butterfly Valley Fresh Water Primary Service Reservoir extension and associated mainlaying (Note 11)	24 September 2013 to 22 January 2017	HK\$285.80 million	HK\$145.76 million	HK\$140.23 million	HK\$5.53 million
9/WSD/13 (Note 14)	WSD	Kwan On – U-Tech 2	Water supply to Pak Shek Kok reclamation area, Tai Po – stage 2 phase 2 (Note 12)	31 December 2013 to 15 October 2016	HK\$56.18 million	HK\$28.09 million	HK\$26.40 million	HK\$1.69 million
					HK\$618.57 million	HK\$450.44 million	HK\$376.31 million	HK\$74.13 million

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Notes:

1. Contract period is the period from the date of commencement under the notice for commencement of works issued by the customer or the date of novation agreement (whichever is applicable) to the original contract completion date provided in the contract or works order for projects with HA.
2. Time of completion is determined with reference to the report on contractor’s performance issued by relevant customer except for contract 20100095, YL/2008/01 and 26/WSD/06 and explicitly excludes maintenance period/defect liability period. For contract YL/2008/01, which is a novated contract, time of completion is determined with reference to the notification of expiry of the maintenance period for the works except landscape works. For contract 26/WSD/06, the time of completion indicated the expiry of contract period, actual works were completed in December 2012. For contract 20100095, the time of completion refers to the ending date of the relevant contract period.
3. Amount of works certified is based on the certificates of payment received from the relevant customer up to the Latest Practicable Date.
4. The estimated contract sum is based on (i) the tender sum awarded and gazetted; (ii) the estimated final contract sum (for WBDB jobs) in the report on contractor’s performance, adjusted based on drawings, variation orders, proposed works and related information provided by customers whichever is the latest; or (iii) budget forecast prepared by our Quantity Surveying and Tendering Department. For HA jobs, the estimated contract sum is based on the tender sum or aggregate of estimated value of works order issued by HA if the amount of works orders received exceeds the original tender sum.
5. The percentage of works certified as at the Latest Practicable Date is based on the certificates issued by the customer on the relevant projects. It represents the amount of works certified as a percentage of the estimated contract sum. For details of contract certification and payment, please refer to the paragraph headed “Application for contract payment and certification” under the sub-section headed “Operations” in this section below.
6. Kwan On – U-Tech 1 is an unincorporated joint venture formed between Kwan On and U-Tech, in July 2011 for the purpose of submitting tenders and the subsequent execution of the works relating to the contract 10/WSD/10. Please refer to the paragraph headed “Kwan On – U-Tech 1” under the section headed “History and development” in this document and the sub-section headed “Mode of operation of Kwan On – U-Tech 1, Kwan On – China Geo and Kwan On – U-Tech 2” under this section headed below for details.
7. For private sector works, completion is by reference to final payment certificate.
8. Claims for extension of time for completion had been submitted to the customers and were under assessment by the customers.
9. Novated contracts.
10. To provide for certain unforeseen circumstances which are beyond the control of the contractor, an “extension of time” clause may be included in contracts for public sector. In addition, a clause in relation to “extension of time” may be included for both public and private works arising out of variation orders.
11. Kwan On – China Geo is a joint operation formed between Kwan On and China Geo in August 2013 for the purpose of preparing and submitting the tender relating to the contract 4/WSD/11. Please refer to the paragraph headed “Kwan On – China Geo” under the section headed “History and development” in this document and the sub-section headed “Mode of operation of Kwan On – U-Tech 1, Kwan On – China Geo and Kwan On – U-Tech 2” under this section below for details.
12. Kwan On– U-Tech 2 is a joint operation formed between Kwan On and U-Tech in December 2013 for the purpose of preparing and submitting the tender relating to the contract 9/WSD/13. Please refer to the paragraph headed “Kwan On – U-Tech 2” under the section headed “History and development” in this document and the sub-section headed “Mode of operation of Kwan On – U-Tech 1, Kwan On – China Geo and Kwan On – U-Tech 2” under this section below for details.
13. The extended completion date of 17 June 2014 was the date previously agreed with the customers. We had applied to the customer for a further extension of time and such application was being considered by the customer as at the Latest Practicable Date.

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14. We had notified the customer for substantial completion of the works on 9 August 2014 and was pending for the issuance of the certificate of completion by the customer as at the Latest Practicable Date.
15. The estimated total revenue represents our Group’s participating interest in the estimated contract sum for contract 4/WSD/11 or contract 9/WSD/13 (as the case may be) pursuant to the terms of the agreement entered into between Kwan On and the relevant joint operator, which has been accounted for and recognised as the revenue of our Group in accordance with HKFRS 11. Expenses incurred by the relevant joint operation are recognised in our Group’s financial statements as cost of services based on our Group’s participating interests in the relevant joint operation as aforesaid. Hence, the profit attributable to our Group from contracts 4/WSD/11 and 9/WSD/13 will be the revenue less the expenses recognised respectively.

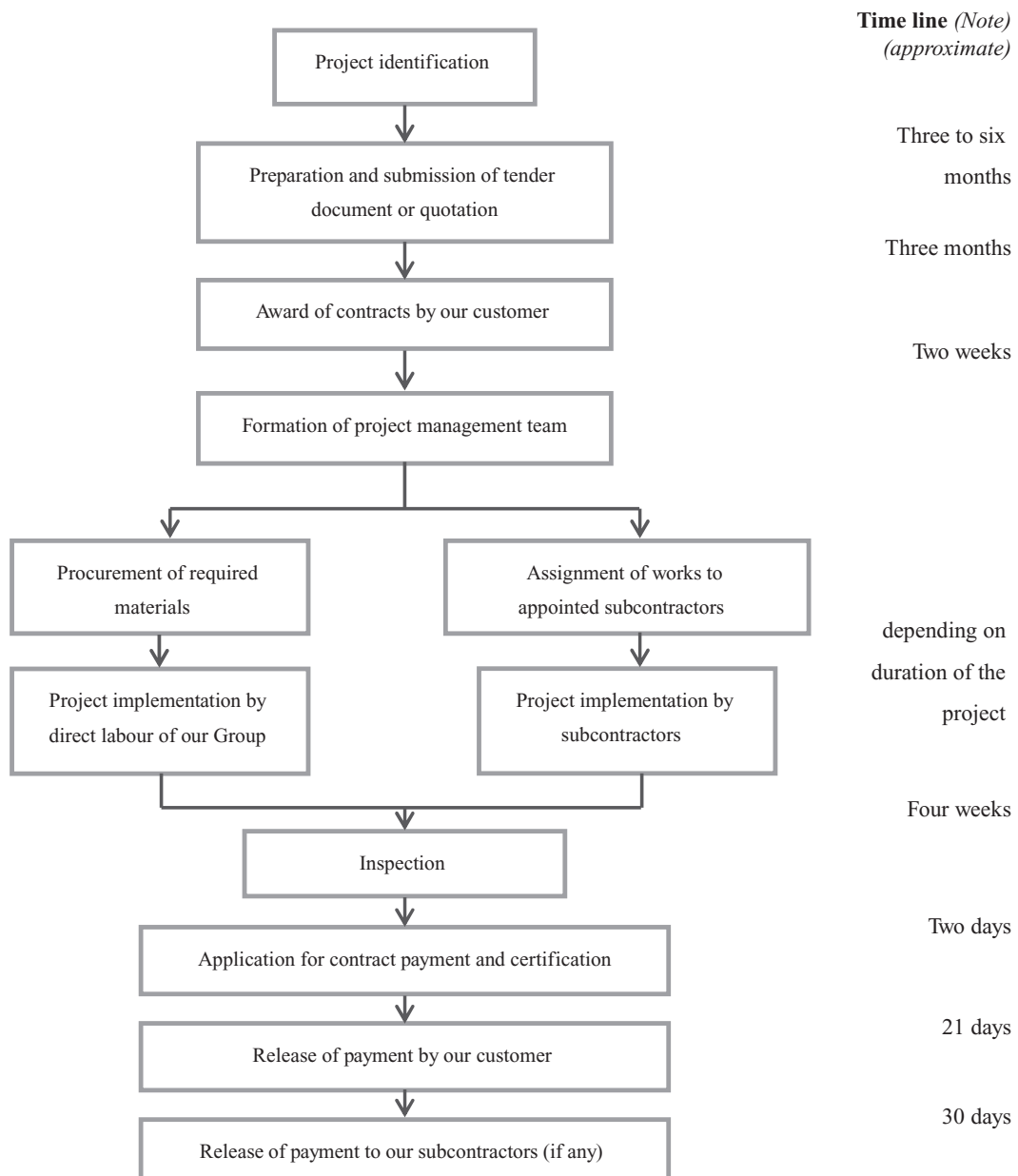
For further details of the respective accounting treatments of our joint venture and joint operations, please refer to the sub-section headed “Mode of operation of Kwan On – U-Tech 1, Kwan On – China Geo and Kwan On – U-Tech 2” under this section below.

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OPERATIONS

We are principally engaged as a main contractor in the provision of (i) waterworks engineering services; (ii) road works and drainage services; (iii) LPM Services; and (iv) building works in Hong Kong. We are also engaged in site formation works for the public sector in Hong Kong.

The typical operational procedures for the abovementioned types of our principal business are largely identical. The following diagram illustrates the typical operational procedures undertaken by us:



Note: The time line may vary for different projects depending on factors such as terms of contract, nature of works and other unforeseeable circumstances.

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Project identification

Projects for the public sector in Hong Kong are generally identified by our Quantity Surveying and Tendering Department through reviewing the Government Gazette and the Government's website on which tender notices from different Government departments are published. A typical tender notice includes brief description of the works required, the expected commencement date and contract period, the contact details of the relevant parties from which forms of tender and further particulars of the project may be obtained and the closing time and date of the tender. Information in respect of projects for the private sector in Hong Kong subject to tender may be received directly from clients by way of invitation letters, phone calls or verbal invitation.

Preparation and submission of tender document or quotation

Once the tender documents including the forms of tender and further particulars from the Government department concerned or clients in private sector are obtained by us, our Quantity Surveying and Tendering Department will commence preliminary work for the preparation of tender submissions such as understanding the specifications and requirements of the project by visiting to the site at which the project is to be undertaken. Depending on the complexity of the project, external consultants such as architects, engineers and costing consultants may be engaged by us.

Market information and data relevant to our business and, in particular, preparation of tenders such as price trend of construction materials, wage trend and our tender record are maintained and updated regularly by us to facilitate the preparation of competitive tenders. After conducting the aforesaid analysis, our quantity surveyor will prepare a preliminary pricing list with the preliminary prices for each item inserted in the bill of quantities and submit to our contract manager for review. Our contract manager will scrutinise the preliminary pricing list and bill of quantities and make adjustments (if necessary) based on experience and recent market information for final review and approval of our executive Directors. As at the Latest Practicable Date, there were 12 staff in our Quantity Surveying and Tendering Department headed by a quantity surveying manager.

For contracts for the public sector in Hong Kong, we, through Kwan On, which holds the licences granted by WBDB or through the joint venture or the relevant joint operation formed by Kwan On and its business partner, will submit the tender documents to the Government upon finalising the bill of quantities and other documents required for submission. In order to be recommended for the award of a contract, our Accounting Department will in connection with the tender for each public sector works contract also submit the original or a certified true copy of the latest audited accounts and latest half-yearly management accounts, certified statements of outstanding workload and supplementary information of Kwan On and respond to all reasonable enquiries from the Government to demonstrate that the requisite amount of employed and working capital is met. The employed capital and working capital requirements are determined based on the latest statement of outstanding workload and would take into account the annual value of the new tender. In addition, our Accounting Department will from time to time review the level

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of employed capital and working capital, which will also be subsequently reviewed by Mr. Tony Wong, one of our executive Directors, to ensure that the requisite financial criteria and requirement are met at all times.

We will submit the duly completed form of tender together with quotation, bill of quantities or other documents required directly to our private sector clients for bidding contracts.

A table summarizing the number of tenders submitted by, and awarded to, our Group and the overall success rate for each of the two years ended 31 March 2014 and since 1 April 2014 to Latest Practicable Date is set out below:

	Number of tenders submitted	Number of contracts awarded	Overall success rate (%)
Year ended 31 March 2013	20	2	10.0
Year ended 31 March 2014	34	8	23.5
From 1 April 2014 to Latest Practicable Date	28	2	7.1

Kwan On was upgraded to Group C contractor (confirmed) under the “Roads and Drainage” category on 26 February 2013 and thus the number of tenders submitted for works contracts under such category was increased during the year ended 31 March 2014. Our Directors consider that there is no assurance that the tenders submitted by us are competitive and contracts will be awarded to us. Accordingly, there is no assurance that the tender success rate will improve in the future. In the event that we are unsuccessful in tendering, we will review our tendering strategies and will continue to prepare and submit tenders for projects that we consider are profitable in the future.

Award of contracts by our customer

Award of contracts is generally notified to us by a letter of acceptance for both public and private sectors in Hong Kong and is also published in the Government Gazette for public sector contracts. To formalise the award of contracts for the public sector in Hong Kong, an article of agreement incorporating terms and conditions specified in the general and special conditions of contract, the tender, the bill of quantities and other tender documents will be executed between the Government and our Group. When a contract is awarded to Kwan On, Kwan On may undertake the contract by itself or subcontract the contract works to any one of UEL, UECL and UEWL. During the Track Record Period, 3 contracts (contracts 10/WSD/10, 4/WSD/11 and 9/WSD/13) were awarded to the joint venture or joint operations formed by Kwan On and its business partners, namely, Kwan On – U-Tech 1, Kwan On – China Geo and Kwan On – U-Tech 2. As for the contract 10/WSD/10, Kwan On – U-Tech 1 undertakes part of the works while subcontracts the remaining works to subcontractors and U-Tech is one of its subcontractors. As for the contracts 4/WSD/11 and 9/WSD/13, the joint operations subcontract all of the works to subcontractor(s) who will be responsible for the necessary labour, plant, materials and all the expenses to

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complete the project. For further details of the Kwan On – U- Tech 1, Kwan On – China Geo and Kwan On – U-Tech 2 please refer to the sub-section headed “Mode of operation of Kwan On – U-Tech 1, Kwan On – China Geo and Kwan On – U-Tech 2” under this section below.

Formation of project management team

Once a contract is awarded and the relevant article of agreement has been executed, a project management team will be formed which typically comprises full-time staff of our Group, including but not limited to a project manager, a site agent, quantity surveyor(s), site engineer(s), a site foremen, a safety officer, an environmental officer and workers selected by the project manager. Depending on the nature of project, the project management team may also involve a technical manager, a traffic arrangement implementation co-coordinator and an excavation permit application controller. The project management team is also responsible for the identification of and obtaining approvals, permits, licenses and certificates required by the Government for the contract. The site agent will be responsible for the on-site supervision, work progress monitoring, issues resolution and the overall co-ordination of the day-to-day work of the project.

Procurement of required materials

The project management team will prepare works programmes, material procurements and the construction equipment specifically required for the project. Material requests will be made accordingly by the project management team to our Purchasing Department whereby our Purchasing Department will solicit quotations from the suppliers on our approved list for the requested materials and equipment. We will then submit a proposal together with the certificates and catalogues of the materials manufacturer, technical data sheets and test certificates for the materials and job references of the material supplier to our customer for approval before using such material. The customer may review and approve the aforesaid proposal subject to the test results and its inspection on the workmanship of material delivered on site. Where purchase orders will be placed whenever necessary, we will also regularly review the inventory level to ensure that a sufficient level of inventory is maintained for implementing contract works and for contingencies. Depending on the terms of arrangement with our subcontractors, we may be required to purchase materials for our subcontractors for carrying out our projects which will be satisfied by our subcontractors by way of deduction of the subcontracting fees payable by us to them from time to time.

In order to prevent costs overrun of the projects, our Group will enter into bulk purchase contracts with suppliers of major materials to fix their prices to mitigate the risk of subsequent price hikes. In addition, our Accounting Department will be responsible for compiling project costs summary to monitor the actual costs incurred against income and check for any cost overrun. Any cost overrun for the project will be investigated. The project costs summary is required to be approved by our Group’s financial controller and Mr. Tony Wong, one of our executive Directors.

During the Track Record Period, most of our works contracts for the public sector provide for a contract price adjustment mechanism, details of which are set out in the paragraph headed “Contract price adjustment mechanism” under this section below. The sum

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payable in each interim payment by our customers will be increased or decreased by a price fluctuation factor. There is no price adjustment clause stipulated in the contracts with our subcontractors. During the Track Record Period, our failure to fully shift the additional costs in relation to project TK/2008/01 to our customer led to loss in such project. The loss from such project had an adverse impact on our Group's profit margin for the year ended 31 March 2013. For details, please refer to the section headed "Financial Information" in this document.

Assignment of works to approved subcontractors

Depending on our manpower availability, the expertise required, the level of complexity of work involved, cost effectiveness and licencing requirements, we may appoint subcontractors to carry out certain parts of the contract works. We have maintained a list of approved subcontractors, the selection of which are based on a set of criteria including previous job references, reputation in the industry, price competitiveness, quality of work and skill sets of workers of the subcontractors. The list of approved subcontractors is reviewed and updated when necessary based on the performance assessment of each subcontractor by us. We generally sub-contract the works to our subcontractors by way of negotiation.

For public sector contracts, we enter into an article of agreement for subcontracting and for private sector contracts, we may enter into a subcontracting agreement with some of the subcontractors appointed which generally, require such subcontractor to observe all the requirements and provisions of the relevant main contract entered into between us and our customers except for situations where the subcontracting rates and specifications of subcontracted works are particularly stated in the subcontracting agreement, if any. During the Track Record Period, certain subcontractors had not entered into any subcontracting agreement with us, the risks associated with such omission is disclosed in the section headed "Risk factors" in this document and the corresponding recommendations are set out under the subsection headed "Internal control measures" under this section below. Notwithstanding these subcontractors had not entered into written subcontracting agreements with us, they will normally submit written quotations to us which set out the maximum subcontracting unit rate for their works. We will issue a payment statement to each subcontractor containing the quantity of work done by such subcontractor, the unit rate, the value of work, retention withheld, any materials charged back and the then net payable amount to such subcontractor on a job basis. Our project manager is responsible for supervising and monitoring the works provided by our subcontractors and for ensuring their compliance with the requirements and provisions of respective main contract and the relevant laws, rules and regulations. We may make advances to subcontractors on a short-term basis to alleviate their cash flow problems. In the event where the collectability of advances is doubtful, the doubtful amount will be deducted from the amount payable to the relevant subcontractor under the abovementioned payment statement immediately and therefore no provision was made in the past due to such advances.

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Project implementation

The project management team, headed by a project manager, is responsible for all aspects of the project including preparation of the project plan, resources allocation, budget monitoring and overall project execution and administration. The site agent who is normally stationed at the site is responsible for site supervision and monitoring work progress. Meetings between our customers and the project manager are held to review work progress, to resolve issues identified during implementation of the project and to revise the work program, if necessary.

Our customer may, in the course of project implementation, order variation to any part of the works that is necessary for the completion of the works (“**variation orders**”). The variation orders may include: (i) additions, omissions, substitutions, alterations, changes in quality, form, character, kind, position, dimension, level or line; (ii) changes to any sequence, method or timing of construction specified in the main contract; and (iii) changes to the site or entrance to and exit from the site. Our customer’s engineer may determine the sum of variation orders which shall be added to or deducted from the contract sum mainly with respect to rate of works of the same or similar character as set out in the main contract. A variation order will be notified to our site agent by a letter from our customer’s engineer describing the detailed works to be carried out as a result of such variation order. Our Quantity Surveying and Tendering Department will obtain quotation from subcontractors and then prepare and submit the rate for such variation order to our customer for approval. At the end of each month, we will apply to our customer for the amount of variation order carried out and receive progress payment. The value of the variation orders has to be agreed between our customers and us. However, if both parties failed to reach an agreement, our customer’s engineer is authorized to fix the value as he thinks fit and notify us accordingly. The principal contract terms and settlement of variation orders are generally in line with the terms of the main contract. The financial impact of variation orders on our results is disclosed in the paragraph headed “Significant factors affecting operating results and financial conditions of our Group” under the section headed “Financial information” in this document.

Inspection

During the course of project implementation, our quantity surveyor will conduct inspection on all works completed on a regular basis to ensure that the works performed by our Group comply with the requirements as set out in the relevant contract. At the request of our customers, further inspection may be conducted together with the customers’ representative.

Application for contract payment and certification

We receive progress payment pursuant to the terms of each contract for both public and private sectors and our application for progress payment is normally made by our quantity surveyor manager on a monthly basis. After examination by the engineers or any other authorised person of our customers, a payment certificate would be issued to us certifying the portion of work completed which normally takes around 21 days from the date of application.

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Release of payment by our customer

Under the current practice, payments for public sector projects will be made by our customer to us within 21 days from the date of issue of the payment certificate as stipulated in the relevant contracts. For private sector projects, payments will generally be made by our customer to us according to the terms of the relevant contracts ranging from 30 days to 60 days from the date of issue of the payment certificate.

Release of payment to subcontractors (if any)

We normally pay our subcontractors on a monthly basis with reference to the value of the work done. We will verify the actual works completed by our subcontractors as certified by the customers, and deduct any materials consumed by or purchased on behalf of them, expenses paid on behalf of them and advances made to them (if any). Payment will be made to our subcontractors after the verification process has been conducted.

Our Directors consider and the Sponsor concurs that the existing project management and control procedures are adequate and effective to ensure the smooth operation of our Group.

MODE OF OPERATION OF KWAN ON – U-TECH 1, KWAN ON – CHINA GEO AND KWAN ON – U-TECH 2

During the Track Record Period, Kwan On – U-Tech 1, Kwan On – China Geo and Kwan On – U-Tech 2 had been awarded three contracts (namely contracts 10/WSD/10, 4/WSD/11 and 9/WSD/13) with a total estimated contract sum of approximately HK\$618.57 million, details of which are described under the paragraphs headed “Kwan On – U-Tech 1”, “Kwan On – U-Tech 2” and “Kwan On – China Geo” in the section headed “History and Development” in this document. China Geo is a state-owned enterprise established in the PRC with headquarter in Beijing, which is principally engaged the provision of domestic and international engineering services. U-Tech is a company incorporated in Hong Kong and a wholly-owned subsidiary of an energy supply group in Hong Kong. U-Tech is principally engaged in provision of a full range of customer services such as consultancy, construction and maintenance in various engineering projects.

Contract 10/WSD/10

Kwan On – U-Tech 1 was awarded the contract for the Replacement and Rehabilitation of Water Mains, Stage 4 Phase 1 – Mains in Shatin and Sai Kung by WSD with an estimated contract sum of approximately HK\$276.59 million. The administration of the contract 10/WSD/10 by Kwan On – U-Tech 1 is under the management and direction of the board of Kwan On – U-Tech 1 (the “**10/WSD/10 Management Committee**”), which comprises a total of three members nominated by Kwan On, being Mr. Tony Wong (as Chairman of the 10/WSD/10 Management Committee), Mr. Kwong and Mr. Chung and two members nominated by U-Tech. According to the joint venture agreement entered into between Kwan On and U-Tech dated 29 July 2011, Kwan On and U-Tech are entitled to share 70% and 30% respectively of the profits and losses arising out of or in connection with the contract 10/WSD/10. Having considered that (i) Kwan On – U-Tech 1 has

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established the 10/WSD/10 Management Committee which decides the operational and financial policies of Kwan On – U-Tech 1; (ii) decision by the 10/WSD/10 Management Committee is made by votes of the members of the 10/WSD/10 Management Committee; (iii) the 10/WSD/10 Management Committee comprises 5 members, of which, 3 are nominated by Kwan On and the other 2 are nominated by U-Tech, as provided in the joint venture agreement; and (iv) profit and loss resulting from Kwan On – U-Tech 1 is shared between Kwan On and U-Tech in the ratio specified in the joint venture agreement, our Directors are of the view that Kwan On, through its majority voting right of the 10/WSD/10 Management Committee stated above, has the power to control the operational and financial activities of Kwan On – U-Tech 1 and is subject to variable returns from Kwan On – U-Tech 1. Therefore, Kwan On has control over Kwan On – U-Tech 1 and Kwan On – U-Tech 1 has been classified a subsidiary of Kwan On and its financial position and results of operation are consolidated into the financial statements of our Group in accordance HKFRS 10 “Consolidated Financial Statements”.

Under HKFRS 11 “Joint Arrangements”, joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control. In addition, an entity that is a party to an arrangement assesses whether the contractual arrangement gives all the parties, or a group of the parties, control of the arrangement collectively. All the parties, or a group of the parties, control the arrangement collectively when they must act together to direct the activities that significantly affect the returns of the arrangement (i.e. the relevant activities). As Kwan On has control over Kwan On – U-Tech 1 and Kwan On – U-Tech 1 is classified as a subsidiary of Kwan On, the joint venture arrangement under Kwan On – U-Tech 1 does not fall within the scope of HKFRS 11. Kwan On – U-Tech 1 undertakes part of the works while subcontracts the remaining works to subcontractors, one of which is U-Tech, the joint venture partner. Kwan On – U-Tech 1 entered into a subcontracting agreement with U-Tech on 24 August 2011 in respect of the subcontracting works under the contract 10/WSD/10 which constitutes a connected transaction for the Company, details of which can be found under the paragraph headed “Subcontracting arrangements” under the section headed “Connected Transactions” in this document.

For each of the two years ended 31 March 2014 and the six months ended 30 September 2014, revenue generated from Kwan On – U-Tech 1 amounted to approximately HK\$74.6 million, HK\$71.6 million and HK\$40.0 million, respectively. Net profit contributed by Kwan On – U-Tech 1 amounted to approximately HK\$14.2 million, HK\$11.9 million and HK\$10.8 million respectively for each of the two years ended 31 March 2014 and the six months ended 30 September 2014.

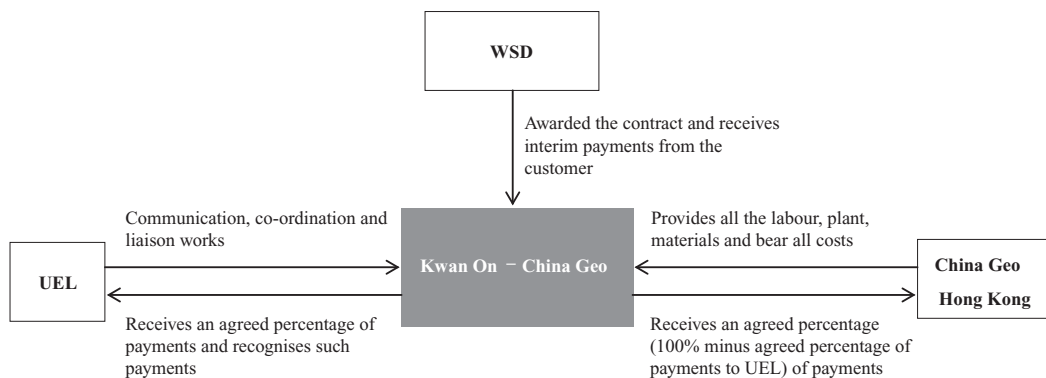
Contract 4/WSD/11

Kwan On – China Geo was a joint operation formed by Kwan On and China Geo on 12 August 2013 for the purpose of preparing and submitting the tender in relation to the construction of Butterfly Valley Fresh Water Primary Service Reservoir Extension and Associated Mainlaying (contract 4/WSD/11). Both Kwan On and China Geo agreed to appoint China Geology (Hong Kong) Industry Ltd. (“**China Geo Hong Kong**”), a wholly-owned subsidiary of China Geo as the major subcontractor of this contract. The estimated contract sum for the contract 4/WSD/11 amounted to approximately HK\$285.80

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million. According to the agreement entered into between Kwan On and China Geo on 12 August 2013, Kwan On and China Geo are entitled to share 51% and 49% of the surplus, loss, assets, liabilities, rights and obligations arising from Kwan On – China Geo.

The mode of operation of Kwan On – China Geo is different from Kwan On – U-Tech 1 in that the burden of costs of this project is shifted from Kwan On – China Geo to the subcontractors and that an agreed percentage of return will be received by our Group. Set out below is a simplified diagram illustrating the operation mode of the contract 4/WSD/11:



Note: According to the subcontracting agreements, UEL receives an agreed percentage of payment from the customer. In the preparation of our Group’s combined financial statements, our Group recognises our share of revenue and expenses arising from Kwan On – China Geo in accordance with the participating interest of 51% as mentioned above under HKFRS 11 “Joint Arrangements”. The profit attributable to our Group from this contract is represented by the revenue less expense recognised, which is equivalent to the payment in accordance with the agreed percentage as aforesaid.

As illustrated above, the contract was awarded to Kwan On – China Geo by WSD. Kwan On – China Geo acts as the main contractor for this contract. Kwan On and China Geo are jointly and severally liable to the Government for the due observance and punctual performance of the obligations of Kwan On – China Geo.

According to the subcontracting agreements made by Kwan On – China Geo with UEL and China Geo Hong Kong respectively, UEL provides one project manager who will be responsible for communication, co-ordination, assisting planning and arrangement of the project works, inclusive of ongoing decision making jointly with China Geo about the progress of the project in this project in return for an agreed percentage of payments paid by the customer in respect of this contract while China Geo Hong Kong will be responsible for all the works of this contract and providing all the labour, plant, materials and bearing all costs for the completion of the project in return for an agreed percentage of payments paid by the customer in respect of this contract. The said agreed percentages of payments payable to UEL and China Geo Hong Kong make up the whole 100% of payments made by the customer in respect of this contract (the “**Kwan On – China Geo Agreed Percentages**”) and thus all payments received from the customer in respect of this contract are to be distributed between UEL and China Geo Hong Kong based on the Kwan On – China Geo Agreed Percentages as a return for their respective works done in accordance with the above respective subcontracting agreements.

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Our Directors consider that the above arrangement facilitates the distribution of all payments received from the customer under this contract directly between our Group and China Geo Hong Kong in accordance with the Kwan On – China Geo Agreed Percentages, thereby resulting in no profit or loss at the level of Kwan On – China Geo.

No financial statements were prepared for Kwan On – China Geo during the Track Record Period because Kwan On – China Geo had been established for less than one year and there were no statutory requirements in Hong Kong for unincorporated entities such as the joint operation to prepare audited financial statements. Prior to the maintenance of separate books and records for Kwan On – China Geo before the first year of its establishment, our Group recognised its share of revenue and expenses attributable to Kwan On – China Geo based on its source documents, including but not limited to interim payment certificates issued by the customer, subcontracting agreements and bank statements of Kwan On – China Geo, rather than based on the books and records maintained for Kwan On – China Geo, which usually should also include the accounting ledger, trial balance and financial statements. Revenue of Kwan On – China Geo was determined using the percentage of completion method under HKAS 11 “Construction Contracts” with reference to the amounts certified in the interim payment certificates issued by the customer. On the other hand, since the subcontractors appointed by Kwan On – China Geo for the execution of contract 4/WSD/11 are responsible for all the works and will provide necessary labour, plant and materials and bear all the costs for the completion of the contracts, the expenses of Kwan On – China Geo comprise the subcontracting charges only. Expenses of Kwan On – China Geo, which comprised only its subcontracting charges, could be completely and reliably determined by multiplying the agreed percentages stipulated in the respective subcontracting agreements with the monthly interim payment certificates. Given that the revenue and expenses of Kwan On – China Geo could be determined accurately and reliably based on the source documents as described above, the management of the Company did not at the time of establishment of Kwan On – China Geo and prior to the first year of its establishment consider it necessary to maintain separate books and records, which usually should also include the accounting ledger, trial balance and financial statements, for Kwan On – China Geo. Despite the absence of statutory requirements for the preparation of audited financial statements for unincorporated entities but for the sake of implementing a robust financial control system for our Group (including entities in which our Group has a participation interest) upon the Listing, our Directors have decided to prepare financial statements for Kwan On – China Geo and to maintain separate books and records, which should usually also include the accounting ledger, trial balance and financial statements, for Kwan On – China Geo after its first year of establishment.

Under the above arrangement, our Group shares the income deriving from this contract with China Geo Hong Kong based on the interim payment certificates issued by the customer and the expenses of Kwan On – China Geo based on the subcontracting agreements between Kwan On – China Geo and the relevant parties with respect to our Group’s participating interest in accordance with the agreement entered into between Kwan On and China Geo on 12 August 2013. In addition, disbursement of cash and operation of the bank account of Kwan On – China Geo require the joint signature of Kwan On and China Geo, which could prohibit Kwan On – China Geo from incurring any debt or encumbrance on its assets. Our Directors are of the view that it is not uncommon to adopt this mode of operation in the local construction industry to utilize respective expertise and

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resources of the business partners. These resources include (i) the pool of human resources of the business partners, in particular project managers and/or quantity surveyors and (ii) the reputation, experience and job references of the business partners in the construction industry. In addition to the aforesaid benefits, the primary reason for using a contractual arrangement such as the joint operation instead of a limited company is that one of the eligibility requirements to tender for public sector contracts in Hong Kong is satisfied by a joint operation where one of its contractual parties holds the requisite licences granted by WBDB whereas it will not be satisfied by a limited company despite it is formed by an approved contractor because these licences may not be transferred to or used by other third parties including the subsidiaries of such approved contractor. Therefore, the joint operation with Kwan On, which is the holder of the requisite licenses granted by WBDB, as one of the partners can satisfy the relevant licensing requirements and will be eligible to tender for the contract 4/WSD/11.

Having considered that (i) both Kwan On and China Geo jointly decided the terms of tender sum and subcontracting fee for execution of this contract; and (ii) Kwan On and China Geo are jointly responsible for ongoing decision making about the progress of the project which will affect the fulfilment of contract obligations jointly by both Kwan On and China Geo under this contract such that the inability to achieve due observance and punctual performance of the obligations under the contract will result in liabilities to both Kwan On and China Geo, our Directors are of the view that Kwan On has joint control of the contractual arrangement under HKFRS 11 "Joint Arrangements". There is no initial investment made by Kwan On to Kwan On – China Geo. Furthermore, Kwan On has confirmed that it has no dominant influence or control over Kwan On – China Geo by virtue of the provisions of the agreement entered into with China Geo, nor is it able to direct its overall policies or alter the terms of the aforesaid agreement. As such, Kwan On – China Geo has been classified as a subsidiary of our Company under the Companies Ordinance, applicable accounting standards or for the purpose of the GEM Listing Rules.

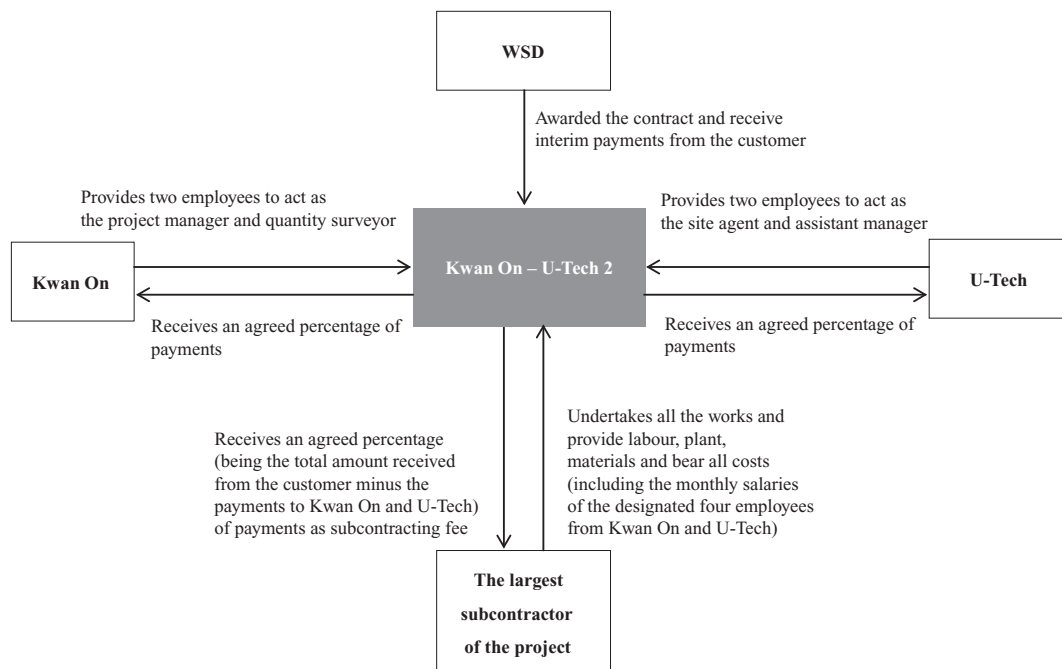
Contract 9/WSD/13

Kwan On – U-Tech 2 is a joint operation formed by Kwan On and U-Tech on 16 December 2013 for the purpose of submitting the tender and the subsequent execution of the works in relation to the water supply to Pak Shek Kok reclamation area, Tai Po – Stage 2 Phase 2 (contract 9/WSD/13). The estimated contract sum for the contract amounted to approximately HK\$56.18 million. According to the agreement entered into between Kwan On and U-Tech on 16 December 2013, Kwan On and U-Tech are entitled to share 50% each of the surplus, loss, assets, liabilities, rights and obligations arising from Kwan On – U-Tech 2.

Both parties agreed to appoint a major subcontractor to undertake almost all the contract works as well as the amount to be paid to such subcontractor. Kwan On and U-Tech then jointly approved the project budget and other necessary documents for tendering the contract and submitting the tender to WSD.

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Set out below is a simplified diagram illustrating the operation mode of the contract 9/WSD/13:



Note: According to the subcontracting agreements, Kwan On receives an agreed percentage of payment from the customer. In the preparation of our Group’s combined financial statements, our Group recognises our shares of revenue and expenses arising from Kwan On – U-Tech 2 in accordance with the participating interest of 50% as mentioned above under HKFRS 11 “Joint Arrangements”. The profit attributable to our Group from this contract is represented by the revenue less expense recognised, which is equivalent to the payment in accordance with the agreed percentage as aforesaid.

Kwan On – U-Tech 2 acts as the main contractor for this contract. Kwan On and U-Tech are jointly and severally liable to the Government for the due observance and punctual performance of the respective obligations of Kwan On – U-Tech 2.

According to the subcontracting agreements entered by Kwan On – U-Tech 2 with Kwan On, U-Tech and the largest subcontractor in this project respectively, Kwan On and U-Tech will mainly be responsible for project management and the largest subcontractor in this project will undertake all works of this project and will be responsible for the necessary labour, plant, materials and will bear all costs (including the monthly salaries of the four designated employees of Kwan On and U-Tech) for the completion of the project in return for an agreed percentage of payment paid by the customer in respect of this contract. The said agreed percentages of payments payable to Kwan On, U-Tech and the largest subcontractor in this project make up the whole 100% of payments made by the customer in respect of this contract (the “**Kwan On – U-Tech 2 Agreed Percentages**”) and thus all the payments received from the customer in respect of this contract are to be distributed among Kwan On, U-Tech and the largest subcontractor based on the Kwan On – U-Tech 2 Agreed Percentages as a return for their respective works done in accordance with the above respective subcontracting agreements.

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Our Directors consider that the above arrangement facilitates the distribution of all payments received from the customer under this contract directly among our Group, U-Tech and the largest subcontractor of the project in accordance with the Kwan On – U-Tech 2 Agreed Percentages, thereby resulting in no profit or loss at the level of Kwan On – U-Tech 2.

No financial statements were prepared for Kwan On – U-Tech 2 during the Track Record Period because Kwan On – U-Tech 2 had been established for less than one year. Prior to the maintenance of separate books and records for Kwan On – U-Tech 2 before the first year of its establishment, our Group recognised its share of revenue and expenses attributable to Kwan On – U-Tech 2 based on its source documents, including but not limited to interim payment certificates issued by the customer, subcontracting agreements and bank statements of Kwan On – U-Tech 2, rather than based on the books and records maintained for Kwan On – U-Tech 2, which usually should also include the accounting ledger, trial balance and financial statements. Revenue of Kwan On – U-Tech 2 was determined using the percentage of completion method under HKAS 11 "Construction Contracts" with reference to the amounts certified in the interim payment certificates issued by the customer. On the other hand, since the subcontractors appointed by Kwan On – U-Tech 2 for the execution of contract 9/WSD/13 are responsible for all the works and will provide necessary labour, plant and materials and bear all the costs for the completion of the contracts, the expenses of Kwan On – U-Tech 2 comprise its subcontracting charges only. Expenses of Kwan On – U-Tech 2, which comprised only the subcontracting charges, could be completely and reliably determined by multiplying the agreed percentages stipulated in the respective subcontracting agreements with the monthly interim payment certificates. Given that the revenue and expenses of Kwan On – U-Tech 2 could be determined accurately and reliably based on the source documents as described above, the management of the Company did not at the time of establishment of Kwan On – U-Tech 2 and prior to the first year of its establishment consider it necessary to maintain separate books and records, which usually should also include the accounting ledger, trial balance and financial statements, for Kwan On – U-Tech 2. Despite the absence of statutory requirements for the preparation of audited financial statements for unincorporated entities but for the sake of implementing a robust financial control system for the Group (including entities in which the Group has a participation interest) upon Listing, our Directors have decided to prepare financial statements for Kwan On – U-Tech 2 and to maintain separate books and records, which should usually also include the accounting ledger, trial balance and financial statements, for Kwan On – U-Tech 2 after its first year of establishment.

Under the above arrangement, our Group shares the income deriving from this contract with U-Tech and the largest subcontractor of the project based on the interim payment certificates issued by the customer and expenses of Kwan On – U-Tech 2 based on the subcontracting agreements between Kwan On – U-Tech 2 and the relevant parties with respect to our Group's participating interest in accordance with the agreement entered into between Kwan On and U-Tech on 16 December 2013. In addition, disbursement of cash and operation of the bank account of Kwan On – U-Tech 2 require the joint signature of Kwan On and U-Tech, which could prohibit Kwan On – U-Tech 2 from incurring any debt or encumbrance on its assets. Our Directors are of the view that it is not uncommon to adopt this mode of operation in the construction industry to utilize respective expertise and resources of the business partners and subcontractors. These resources include (i) the pool of human resources of the business partners, in particular project managers and/or quantity surveyors and (ii) the reputation, experience and job references of the business partners in the

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construction industry. In addition to the aforesaid benefits, the primary reason for using a contractual arrangement such as the joint operation instead of a limited company is that one of the eligibility requirements to tender for public sector contracts in Hong Kong is satisfied by a joint operation where one of its contractual parties holds the requisite licences granted by WBDB whereas it will not be satisfied by a limited company despite it is formed by an approved contractor because these licences may not be transferred to or used by other third parties including the subsidiaries of such approved contractor. Therefore, the joint operation with Kwan On, which is the holder of the requisite licenses granted by WBDB, as one of the partners can satisfy the relevant licensing requirements and will be eligible to tender for the contract 9/WSD/13.

Kwan On – U-Tech 2 has entered into subcontracting agreements with Kwan On, U-Tech and the largest subcontractor of this project respectively to set out the scope of works to be undertaken by and agreed percentage of return to be granted to them. Pursuant to the articles of agreement entered into between Kwan On – U-Tech 2 and Kwan On, Kwan On will designate two employees to act as the project manager and quantity surveyor of the project in return for an agreed percentage of the payments paid by the customer in respect of this contract. Pursuant to the subcontracting agreements entered into between Kwan On – U-Tech 2 and U-Tech, U-Tech will designate two employees to act as the site agent and assistant manager of the project in return for an agreed percentage of the interim payments paid by the customer in respect of this contract. Pursuant to the subcontracting agreement entered into between Kwan On – U-Tech 2 and the largest subcontractor of the project, such subcontractor agreed that it would undertake all of the works of this project and would be responsible for the necessary labour, plant, materials and would bear all costs (including the monthly salaries of the four designated employees of Kwan On and U-Tech) in return for an agreed percentage of the payments received from the customer (being the total amount received from the customers minus the payments to Kwan On and U-Tech) as subcontracting fee.

Having considered that the unanimous consent of both Kwan On and U-Tech is required in respect of (i) the approval of project budgets; and (ii) selection, determination of remuneration and appointment/removal of subcontractors, the Directors are of the view that Kwan On and U-Tech have joint control over Kwan On – U-Tech 2 and HKFRS 11 “Joint Arrangements” will apply. In addition, there is no evidence to demonstrate that Kwan On has significant influence over the financial and operating policies of the relevant activity of Kwan On – U-Tech 2, for which HKAS 28 “Investments in Associates and Joint Ventures” applies. There is no initial investment by Kwan On to the Kwan On – U-Tech 2. Furthermore, neither of the parties has dominant influence or control over Kwan On – U-Tech 2 by virtue of the provisions of the agreement entered into between Kwan On and U-Tech, nor is it able to direct the overall policies or alter the terms of the aforesaid agreements. As such, Kwan On – U-Tech 2 has not been classified as a subsidiary of our Group either under the Companies Ordinance, applicable accounting standards or for the purpose of the GEM Listing Rules.

According to the terms of the contract agreed with the Government in respect of contracts 4/WSD/11 and 9/WSD/13, Kwan On and its business partners are jointly and severally liable to the Government for the due observance and punctual performance of the respective obligations of Kwan On – U-Tech 2 and Kwan On – China Geo. Should the subcontractors who are appointed by the relevant joint operation to undertake the works under the relevant contract be in default of their subcontracting obligations towards the

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relevant joint operation due to bankruptcy, liquidation or any other reason which lead to losses, damages, costs and expense suffered by the Government, Kwan On and its business partners shall indemnify the Government against such losses, damages, costs and expenses arising out of any act, default or omission on the part of the relevant joint operation in the performance of the relevant contract. In addition, a partnership is dissolved as regards all the partners by the death or bankruptcy of any partner subject to any agreement between the partners under section 35(1) of the Partnership Ordinance (Chapter 38 of the Laws of Hong Kong). Accordingly, in the event that the business partners of the joint operations become bankrupt or liquidated, the relevant joint operation will be dissolved and Kwan On, being the sole surviving partner, shall continue to perform its obligations under the relevant works contracts on its own account.

Our Directors confirm that relevant financial reporting standards are properly adopted in the preparation of the accountant’s report of our Group.

CONTRACT TERMS

Generally the contracts with our customers contain terms and conditions relating to the contract price, contract period, the scope of work and the payment terms. There may also be retention money clause, contract price fluctuation adjustment, performance bonds/liquidated damages requirements and maintenance/defect liability period provisions in some of our contracts.

Retention money

According to the terms and conditions of the contracts which are still in progress, during the Track Record Period, the retention money for public sector contracts is 1% of the total contract sum whereas the retention money for private sector contracts is usually 5% of the total contract sum. Pursuant to the terms of each contract for the public sector, retention money withheld will be released within 21 days upon issue of the certificate for the payment of retention money subject to the customers’ satisfaction of the works.

Contract price adjustment mechanism

During the Track Record Period, save for one contract with ArchSD and two contracts for the private sector in Hong Kong, all of our works contracts provide for a contract price adjustment mechanism (both upward and downward adjustments) with reference to price indices listed in the “Index Numbers of the Costs of Labour and Materials used in Public Sector Construction Projects” published by CSD (“**CSD Price Indices**”) applicable to period of time which is close to the period covered by the relevant interim payment. The contract price adjustment mechanism does not fully mitigate the inflation of construction costs, including labour and materials costs because of the difference between the time when the construction costs are incurred and the applicable time of the CSD Price Indices referred by the contract price fluctuation adjustment for the calculation of each interim payment. As such, the contract price adjustment mechanism is independent of the actual amounts paid and is not a back-to-back reimbursement of the actual additional costs incurred by such works contract. The contract price also would not be adjusted for events that do not relate to the prices of construction materials and labour, such as changes in macroeconomic conditions or the Government’s expenditure policies on any particular works project or public infrastructure generally.

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For each of the two years ended 31 March 2014 and the six months ended 30 September 2014, the sum of contract price fluctuation adjustment paid by our clients under the abovementioned contract price adjustment mechanism for our works contracts amounted to approximately HK\$18.08 million, HK\$28.53 million and HK\$21.16 million respectively, which covered approximately 6.41%, 8.36% and 6.76% of our cost of services respectively for the same period. Our Directors consider that additional construction costs arising from inflation for those works contracts which provide for a contract price adjustment mechanism could be partly compensated by our customers during the Track Record Period.

Performance bonds/liquidated damages requirement

In order to secure due and timely performance of the main contractor, some customers may request the main contractor to take out performance bonds issued by a bank or an insurance company in favour of the customers, and to include a liquidated damages clause to project itself against the main contractor's late completion of works in the contracts for both public and private sectors.

Our Group would issue a performance bond only if it is required by the contract. During the Track Record Period, there was only one contract (contract 20100095) with HA that required a performance bond. As at the Latest Practicable Date, there were two contracts (contracts 20100095 and 20130375) with HA that required performance bonds. Generally, the amount of performance bond required for a project undertaken by us would not exceed 5% of the tendered amount and the performance bond normally expires six months from the date of issue of the last certificate of completion or upon the expiry of the contract period, whichever is later. As at 31 March 2013 and 2014 and 30 September 2014, we had guarantees on performance bonds of approximately HK\$0.6 million, HK\$0.6 million and HK\$0.6 million respectively. During the Track Record Period and up to the Latest Practicable Date, no performance bond had been called by our customers by reason of late completion of any of the contracts undertaken by us.

During the Track Record Period and up to the Latest Practicable Date, no liquidated damages had been claimed by our customer against us.

Maintenance/defects liability period

Our customers would normally require a maintenance/defects liability period of 12 months during which we are responsible to rectify works defects and we would require an identical defect liability/maintenance period from our subcontractors in respect of the portion of works completed by such subcontractors.

If any defects are identified, our project manager will agree on a rectification works programme with the customers so that the defects are remedied at the most convenient time. Where the defect requires remedy by our subcontractor, the relevant subcontractor will be responsible for rectifying the defects and will bear all the associated rectification costs.

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MACHINERY AND EQUIPMENT

Principal machinery

Our works require the use of various equipment and machinery. At the commencement of each project, our project manager will review the construction method for such project and determine the machinery to be used, and in the event that machinery or equipment in addition to those possessed by our Group is required for undertaking the project, we may acquire such machinery or equipment or lease the same from local suppliers depending on factors such as availability of the machinery in the market, acquisition/leasing cost and maintenance costs. During the Track Record Period and up to the Latest Practicable Date, we purchased machinery such as excavators, crane, trucks and butt fusion machine from local suppliers and we leased machinery such as air compressors and generators for undertaking certain projects of our Group.

The estimated remaining useful lives of our principal machinery and equipment ranged from approximately 1 year to 4 years. A machinery or equipment will be replaced when the cost for repairs and maintenance exceeds the cost for replacement.

Repairs and maintenance

We perform annual checks on our machines in accordance with relevant regulations in force from time to time. Repairs and maintenance of machinery and equipment are outsourced to independent service providers who are general engineering companies. The total costs for operating and maintenance of machinery and equipment for each of the two years ended 31 March 2013 and 2014 and the six months ended 30 September 2014 amounted to approximately HK\$1.1 million, HK\$0.9 million and HK\$0.7 million respectively.

Service capacity and utilisation rate

Our Directors consider that due to the nature of our business and operations, it is not feasible and practicable to quantify the service capacity and utilisation rate for the following reasons:

- (i) the service capacity of our Group could be adjusted and increased by acquisition and/or leasing of additional machinery and equipment and outsourcing to subcontractors;
- (ii) different types of machinery and equipment have different functions and therefore it is not feasible to quantify the capacity of each piece of machinery and equipment by making reference to an objective and comparable scale or standard of measurement; and
- (iii) it is impracticable to quantify the output of each worker due to their different ages, skills and experience.

SEASONALITY

Our Directors are of the view that the civil engineering industry in Hong Kong does not exhibit any significant seasonality.

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PRICING POLICY

The bill of quantities and quotations prepared by us for works contracts are determined on a case-by-case basis by taking into account (i) the complexity and difficulties of the project; (ii) the completion time requested by customers; (iii) the estimated number and types of workers required and respective wage trend; (iv) the estimated cost of construction materials; (v) the estimated subcontracting cost, if necessary; (vi) the estimated number and types of workers required; and (vii) the prevailing market conditions.

MARKETING

We did not conduct any marketing or promotional activity during the Track Record Period. Most of the works undertaken by us were civil engineering projects for the public sector in Hong Kong which were normally awarded through open tendering procedures. In respect of projects for the private sector in Hong Kong, we obtain information regarding the tender directly from clients by way of invitation letters, phone calls or verbal invitation. Our Directors consider that our licences held, proven track record and ability to execute works of satisfactory quality could enhance our competitiveness in the open tendering and help us attract customers in private sector.

CUSTOMERS

Our customers are mainly various Departments of the Government. During the Track Record Period, all of our customers are located in Hong Kong and all of the settlements between our customers and us took place in Hong Kong. During the Track Record Period, our largest customer accounted for approximately 50.9%, 52.9% and 55.5% respectively of our revenues for the two years ended 31 March 2014 and the six months ended 30 September 2014. Our five largest customers together accounted for approximately 100%, 99.2% and 99.9% of our revenues for each of the two years ended 31 March 2014 and the six months ended 30 September 2014 respectively. The general credit terms granted by us are on an average of 21 days to customers in public sector and on an average of 30 days to customers in private sector respectively. Payments by our customers are usually settled by bank transfer or cheque.

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Set out below is a breakdown of the revenue attributable to our five largest customers during the Track Record Period and their respective background information:

For the year ended 31 March 2013

	<i>HK\$'000</i>	<i>%</i>
WSD	158,892	50.9
CEDD	123,158	39.5
HA	13,998	4.5
DSD	12,512	4.0
ArchSD	<u>3,320</u>	<u>1.1</u>
Total turnover attributable to our top five customers	<u><u>311,880</u></u>	<u><u>100.0%</u></u>

For the year ended 31 March 2014

	<i>HK\$'000</i>	<i>%</i>
WSD	208,084	52.9
CEDD	105,110	26.7
DSD	62,761	16.0
ArchSD	8,351	2.1
Customer A	<u>6,070</u>	<u>1.5</u>
Total turnover attributable to our top five customers	<u><u>390,376</u></u>	<u><u>99.2%</u></u>

For the six months ended 30 September 2014

	<i>HK\$'000</i>	<i>%</i>
CEDD	184,380	55.5
WSD	119,767	36.0
DSD	23,823	7.1
ArchSD	3,979	1.2
HA	<u>408</u>	<u>0.1</u>
Total turnover attributable to our top five customers	<u><u>332,357</u></u>	<u><u>99.9%</u></u>

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Set out below is the background information of the five largest customers of our Group during the Track Record Period:

Customer	Principal business	Location	Service provided by our Group	Years of business relationship with our Group	Typical credit terms offered by the Group and payment method
WSD	Waterworks	Hong Kong	Waterworks engineering	19	Payment is due 21 days after certification, paid by bank transfer
CEDD	Geotechnical and roads and drainage	Hong Kong	Slope maintenance and road works	16	Payment is due 21 days after certification, paid by bank transfer
HA	Civil engineering	Hong Kong	Slope maintenance	12	Payment is due 21 days after certification, paid by bank transfer
DSD	Wastewater and stormwater drainage services	Hong Kong	Road works	10	Payment is due 21 days after certification, paid by bank transfer
ArchSD	Buildings and related facilities	Hong Kong	Slope maintenance and building demolition	7	Payment is due 21 days after certification, paid by bank transfer
Customer A	Incorporated owners of a residence	Hong Kong	Building maintenance	2	Payment is due 30 days after certification, paid by cheque

During the Track Record Period, the customer base of our Group was highly concentrated. Revenue generated from Government contracts, including those awarded by WSD, CEDD, ArchSD and DSD, represented approximately 95.5%, 97.7% and 99.9% of our Group’s total revenue for each of the two years ended 31 March 2014 and the six months ended 30 September 2014 respectively. Our Directors consider that our reliance on the Government during the Track Record Period is attributable to a combination of factors including (i) the financial, technical and management requirements for a contractor engaging in civil engineering projects of the Government provide effective barriers for those contractors who are not on the Contractor List and the Specialist List from entering the sector; and (ii) the contract sums of projects of the Government are always larger than those projects for private sector.

Our Directors are of the view that reliance on the Government is not uncommon for construction companies which are mainly engaged in projects for the public sectors in Hong Kong given that (i) all contracts for the public sector in Hong Kong are generally commissioned by the Government and other public bodies in Hong Kong; (ii) contracts for the public sector in Hong Kong are normally awarded through open tendering procedures; and (iii) the increasing opportunities arising from the Government’s expenditure on projects

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for the public sector in the future, details of which are set out in the section headed "Industry Overview" in this document. In addition, two members of our Group hold various licenses and certificates to undertake projects of different categories and the revenue of our Group during the Track Record Period was derived from contracts awarded by different departments of the Government.

None of our Directors or their close associates or any Shareholder holding more than 5% of our Company's issued share capital had any interests in our five largest customers as at the Latest Practicable Date.

SUPPLIERS

Our suppliers are categorised into (i) materials suppliers for provision of construction materials used in our projects and (ii) subcontractors for provision of specific services required by our contracts.

During the Track Record Period, our largest supplier accounted for approximately 12.3%, 9.2% and 20.9% of our cost of services and our five largest suppliers accounted for approximately 36.3% and 31.9% and 47.5% of our cost of services respectively. During the Track Record Period, all of our five largest suppliers are subcontractors who provide services required by our works contracts. Set out below is a breakdown of our Group's cost of sales by our five largest suppliers during the Track Record Period:

For the year ended 31 March 2013

	<i>HK\$'000</i>	<i>%</i>
Supplier A	34,682	12.3
Supplier B	25,176	8.9
Supplier C	20,698	7.4
Supplier D	11,832	4.2
Supplier E	<u>9,842</u>	<u>3.5</u>
Total cost of services attributable to our top five suppliers	<u>102,230</u>	<u>36.3</u>

For the year ended 31 March 2014

	<i>HK\$'000</i>	<i>%</i>
Supplier A	31,275	9.2
U-Tech	23,292	6.8
Supplier F	21,757	6.4
Supplier B	17,586	5.1
Supplier G	<u>15,002</u>	<u>4.4</u>
Total cost of services attributable to our top five suppliers	<u>108,912</u>	<u>31.9</u>

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For the six months ended 30 September 2014

	<i>HK\$'000</i>	<i>%</i>
U-Tech	65,528	20.9
Supplier A	32,935	10.5
Supplier H	29,641	9.5
Supplier F	13,364	4.3
Supplier I	7,308	2.3
Total cost of services attributable to our top five suppliers	148,776	47.5

Connected transactions

Except for U-Tech, all of the five largest suppliers are Independent Third Parties and have business relationships with us from two to nine years. Except for Supplier F, the credit terms granted by our largest suppliers are generally 30 days from the date of invoice. Payments to our suppliers are usually made by cheque. Saved as disclosed in the section headed “Connected Transactions” in this document, none of our Directors or their close associates or any Shareholder holding more than 5% of our Company’s issued share capital had any interests in our five largest suppliers as at the Latest Practicable Date. Set out below is the background information of our five largest suppliers during the Track Record Period:

Supplier	Principal business	Major service provided	Location	Years of business relationship with our Group	Typical credit terms
Supplier A	Civil engineering services	Pipe works and main laying	Hong Kong	5	30 days
Supplier B	Civil engineering services and construction	Earth works and structure works	Hong Kong	5	30 days
Supplier C	Civil engineering services	Flexible barrier	Hong Kong	3	30 days
Supplier D	Provision of construction and transportation services	Pipe works and main laying	Hong Kong	4	30 days
Supplier E	Civil engineering services	Asphalt supply and laying	Hong Kong	6	30 days
U-Tech	Civil engineering services	Pipe works/main laying	Hong Kong	5	30 days
Supplier F	Civil engineering services	Pipe works/main laying	Hong Kong	9	7 days
Supplier G	Civil engineering services	Trenchless pipe work	Hong Kong	2	30 days
Supplier H	Civil engineering services	Earth works and structure works	Hong Kong	1	30 days
Supplier I	Electrical and mechanical engineering services	Electrical and mechanical works	Hong Kong	4	30 days

Materials suppliers

During the Track Record Period, there were more than 200 materials suppliers on our approved list of suppliers. Before admitting a materials supplier to our approved list, we will take into account a host of factors including its product quality, punctuality of delivery, job references and reputation in the industry.

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During the Track Record Period, the principal construction materials used by our subcontractors and us include various kinds of pipes (including mild steel pipes, ductile iron pipes and polyethylene pipes), fittings, steel bars, concrete and asphalt, which are sourced from a number of suppliers. All of our materials suppliers are located in Hong Kong and all of our purchases are denominated in HK\$.

Our Group typically entered into bulk purchase orders with materials suppliers where the prices would be fixed within the bulk ordered quantity in order to mitigate the effect arising from the increase in material prices. Our works contracts for the public sector in Hong Kong typically provide for a contract price adjustment mechanism with reference to the Price Indices. Please refer to the paragraph headed “Contract price adjustment mechanism” under the sub-section headed “Contract terms” in this section above for further details. During the Track Record Period, our failure to fully shift the additional costs in relation to project TK/2008/01 to our customers led to losses on such project.

Our largest materials supplier accounted for approximately 17.6%, 13.1% and 26.3% of our total purchases respectively and our five largest materials suppliers accounted for approximately 55.3%, 46.1% and 52.8% of our total purchases for each of the two years ended 31 March 2014 and the six months ended 30 September 2014 respectively. All of our five largest materials suppliers are Independent Third Parties. We have established business relationship with our five largest materials suppliers from one year to nine years. We have entered into legally binding supply contracts with certain suppliers for supply of concrete pipes and steel bars, with term of over one year. The duration of these supply contracts ranged from one year to four years. The specifications, purchases price and quantity of construction materials are usually specified in such contracts. Generally, there is no automatic renewal of the contract term or minimum purchase requirement under these supply contracts. Save as disclosed, no long-term contract has been entered into between us and our materials suppliers.

None of our Directors or their close associates or any Shareholder holding more than 5% of our Company’s issued share capital had any interests in our five largest materials suppliers as at the Latest Practicable Date. During the Track Record Period, we had not experienced any significant shortage or delay in the supply of materials by our materials suppliers.

Subcontractors

Depending on our manpower availability, the expertise required, the level of complexity of work involved, cost effectiveness and licencing requirements, we may appoint subcontractors to carry out certain parts of the contract works, including excavation, formwork, rebar fencing, etc. We have maintained a list of approved subcontractors, the selection of which are based on a set of criteria including previous job references, reputation in the industry, price competitiveness, quality of work and skill sets of workers of the subcontractors. As at the Latest Practicable Date, there were over 20 subcontractors on our list of approved subcontractors, with our five largest subcontractors having maintained business relationship with us for up to nine years. Please refer to the paragraph headed “Subcontracting agreements” under the sub-section headed “Control over subcontractors” in this section below for details of subcontracting arrangements between us and our

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subcontractors. Our subcontracting costs amounted to approximately HK\$187.6 million, HK\$221.8 million and HK\$231.8 million respectively, representing approximately 66.5%, 64.9% and 74.0% of the total cost of services for each of the two years ended 31 March 2014 and the six months ended 30 September 2014 respectively. During the same period, the subcontracting costs paid to our largest subcontractor accounted for approximately 18.5%, 14.1% and 28.2% of our total subcontracting costs and the subcontracting costs paid to our five largest subcontractors accounted for approximately 54.2%, 48.3% and 63.6% of our total subcontracting costs respectively. All of our five largest subcontractors are small to medium-sized local firms and have had business relationships with us for up to nine years. Except for U-Tech, all of our five largest subcontractors are Independent Third Parties.

None of our Directors or their close associates or any Shareholder holding more than 5% of our Company’s issued share capital had any interests in our five largest subcontractors as at the Latest Practicable Date. During the Track Record Period and up to the Latest Practicable Date, we had not experienced any incidents whereby our subcontractors have caused significant delay in completing the required services which resulted in any material adverse impact on our operations or financial position.

SENSITIVITY ANALYSIS

During the Track Record Period, the cost of services of our Group consists of (i) subcontracting charges; (ii) direct staff costs; (iii) material costs; (iv) plant and depreciation; (v) overhead costs; (vi) provision for obsolete stocks; and (vii) other contract costs.

The subcontracting charges payable by us to our subcontractors are determined with reference to the works performed by such subcontractor measured at a rate provided under such subcontracting agreement in which allowance for price fluctuation is generally not provided. As such, the subcontracting charges usually do not vary with the fluctuations of labour costs or material costs.

The following tables illustrate the impact of hypothetical fluctuations in direct staff costs and material costs on our profit before tax during the Track Record Period.

Fluctuations in direct staff costs

Hypothetical fluctuations in	+5%	+15%	+20%	-5%	-15%	-20%
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Changes in profit before tax						
Year ended 31 March 2013	(2,798)	(8,393)	(11,190)	2,798	8,393	11,190
Year ended 31 March 2014	(2,879)	(8,638)	(11,517)	2,879	8,638	11,517
Six months ended 30						
September 2014	(1,782)	(5,345)	(7,126)	1,782	5,345	7,126

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Fluctuations in material costs

Hypothetical fluctuations in	+5%	+15%	+20%	-5%	-15%	-20%
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Changes in profit before tax						
Year ended 31 March 2013	(1,323)	(3,968)	(5,291)	1,323	3,968	5,291
Year ended 31 March 2014	(1,203)	(3,609)	(4,813)	1,203	3,609	4,813
Six months ended 30						
September 2014	(1,064)	(3,193)	(4,257)	1,064	3,193	4,257

The above sensitivity analysis is for illustrative purpose only. As most of our works contracts provide for a contract price adjustment mechanism, details of which are set out in the paragraph headed “Contract price adjustment mechanism” under the sub-section headed “Contract terms” in this section above, our Directors consider that additional construction costs incurred by us for those works contracts which provide for a contract price adjustment mechanism due to inflation could be partly compensated by our customer in normal circumstances.

INVENTORY CONTROL

Our inventories mainly comprised various pipes and fittings for water supply system for waterworks engineering projects. The undertaking of our construction projects also required other major materials, including concrete, asphalt and steel bars. Concrete and asphalt are ordered and delivered as required and are used immediately upon delivery. Steel bars are ordered when demanded as the delivery lead time is short. Where purchase orders will be placed whenever necessary, we will also regularly review the inventory level to ensure that a sufficient level of inventory is maintained for implementing contract works and for contingencies. Depending on the terms of arrangement with our subcontractors, we may be required to purchase materials for our subcontractors for carrying out our projects and typically charge the total costs of such materials together with a handling fee to our subcontractors, which will be settled by our subcontractors by way of deduction of the subcontracting fees payable by us to them from time to time. The ownership of the materials purchased by us on behalf of our subcontractors shall, until they have been collected by our subcontractors, remain with us and form part of our inventories.

Provision for stock obsolescence will be made at each reporting date after our Directors take into account a number of factors concerning stock obsolescence which include (i) no usage/sale during the last 12-month period and lack of future expected movement and (ii) stocks known to be obsolete or damaged or unusable. Stock provision shall be made to reduce stock from cost to net realisable value when a stock is identified as obsolete or there are concerns that a stock could be sold or used. The provision for such obsolete stock can be written back if a future need is identified.

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CONTROL OVER SUBCONTRACTORS

Subcontracting agreements

As at the Latest Practicable Date, we had entered into subcontracting agreements with 18 subcontractors. A typical subcontracting agreement contains (i) subcontracting services undertaken by the subcontractor; (ii) duration of the agreement, which is usually coterminous with the duration of related main contract entered into between us and our customer; (iii) basis of determining the subcontracting fees, which is usually the value of works completed by such subcontractor as certified by our customer; (iv) monthly payment date, which is usually 7 days after completion of our verification of works completed by such subcontractor; (v) retention money withheld, which is 5% of the monthly subcontracting fee payable by us to such subcontractor and will be released as to half within 3 months after the issue of completion certificate by our customer and as to half after the completion of the main contract and maintenance period; and (vi) maintenance period and service provided by such subcontractor. It is also stipulated in a subcontracting agreement that the terms and conditions, specification and plan of the related main contract shall apply to such subcontracting agreement. The subcontractor shall assume the same duties and responsibilities as shall be borne by us under the main contract.

During the Track Record Period, certain subcontractors had not entered into any subcontracting agreement with us. Subcontracting charges paid to subcontractors who had not entered into subcontracting agreements for each of the two years ended 31 March 2014 and the six months ended 30 September 2014 amounted to approximately HK\$149.4 million, HK\$120.2 million and HK\$73.8 million respectively, representing approximately 79.7%, 54.2% and 31.8% of the total subcontracting charges incurred respectively. Please refer to the paragraph headed “Some of our subcontractors had not entered into written subcontracting agreements with us during the Track Record Period and the interests of our Group may not be well protected if any conflict or dispute arises” under the section headed “Risk factors” in this document and the subsection headed “Internal control” under this section below.

Subcontractor management plan

In order to closely monitor the performance of the subcontractors and to ensure that the subcontractors comply with the requirements and provisions set out in the respective main contracts, and the relevant laws, rules and regulations, we have specific subcontractor management plan for each contract undertaken by us, which mainly covers various aspects such as:

- (i) Scope of works to be subcontracted;
- (ii) Approach to control subcontractors by requiring the subcontractors to abstain from subcontracting the whole of the works subcontracted to them, by requiring the subcontractors to report upwards their subcontracting arrangements and any subsequent changes, and by requesting the subcontractors to submit written declarations of no “hidden” subcontracts for any part of the works subcontracted to them;

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- (iii) Proposed measures for supervision of the works and monitoring the performance of subcontractors, particularly the aspects of the works programming, quality and safety of the works and environmental protection;
- (iv) Criteria for the selection of subcontractors;
- (v) Details of our management team of the relevant contract who shall be responsible for direct supervision and management of subcontractors;
- (vi) Declaration that members of staff in our management team are prohibited to be given a subcontract to any part of the works or to have a vested interest in any of the subcontractors irrespective of tiers; and
- (vii) Proposed measures to ensure our subcontractors' timely payments of wages to the site personnel and timely payments by our subcontractors to subcontractors of lower tiers.

Details of our quality and safety control measures over our subcontractors are disclosed in the subsections headed "Quality Assurance" and "Safety Policy" in this section below. Our project manager will be responsible for monitoring and supervision of the works provided by our subcontractors and their compliance with the requirements and provisions set out in the respective main contracts and the relevant laws, rules and regulations.

Measures to prevent the hiring of illegal workers

According to section 38A of the Immigration Ordinance, a construction site controller (i.e. the principal or main contractor and includes a subcontractor, owner, occupier or other person who has control over or is in charge of a construction site) shall take all practicable steps to (i) prevent having illegal immigrants from being on site or (ii) prevent illegal workers who are not lawfully employable from taking employment on site.

We require our subcontractors to carefully check the identity documents of their workers to ensure that no illegal workers are hired to work on the sites for which we are responsible. Our labour officers will check the identity card of on-site workers to prevent our subcontractors from using illegal workers. During the Track Record Period, no illegal workers were reported on the sites for which we are responsible.

Environmental performance control

We have an environmental management plan for each contract undertaken by our Group, which sets out our general environmental policies, organisational structure and responsibilities of Environmental Protection Team, in-house rules and regulations, environmental performance monitoring, implementation measures, waste management measures and review of requirements. We instruct our subcontractors to adopt environmental protection measures in order to satisfy EPD's requirement and minimize the effects on the air, noise, water quality as well as nuisance of waste within and outside the site. Our environmental supervisors carry out daily site inspection to ensure that follow-up action has

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been taken by promptly to rectify any defects and deficiencies identified, potential pollution on site. In addition, our environmental officers carry out environmental inspection of the site to assess the environmental impact due to the execution of works.

QUALITY ASSURANCE

Our Directors believe that our success and growth depend on our ability to fulfill the needs of our customers by providing quality services. We have established formal quality management system in accordance with the requirements of ISO9001:2008 quality management system applicable to construction of civil engineering works (site formation, waterworks, roads and drainage) in Hong Kong and construction of landslip preventive and remedial works to slopes and retaining walls in Hong Kong to ensure the quality of our work.

We normally assign a project manager to oversee the quality management of projects undertaken by us. We generally procure the materials and equipment required in the project from the suppliers on our approved list. We also conduct regular sample checks on the materials used to ensure a consistent quality. We also provide a maintenance or defects liability period of twelve months to our customers after completion of each project. Kwan On's quarterly performance ratings as appraised by WBDB were higher than the industry averages in the recent ten consecutive quarters up to the third quarter of 2014.

To ensure all the works are carried out and completed in accordance with the contract requirements with proper working sequence as required under the contract, we will invite our customers to inspect our works. For each project, our project management team will hold monthly meetings with our subcontractors to ensure their understanding of our requirements and concerns, particularly in relation to compliance with safety and environmental standards and prohibition of employment of illegal workers. Our project management team reviews the performance of subcontractors in terms of a number of criteria such as sufficiency of manpower, progress, workmanship, response to instructions and planning and management annually by completing a subcontractor assessment report. In cases of major non-performance by an approved subcontractor, the project management team will review its suitability to remain on our approved list.

SAFETY POLICY

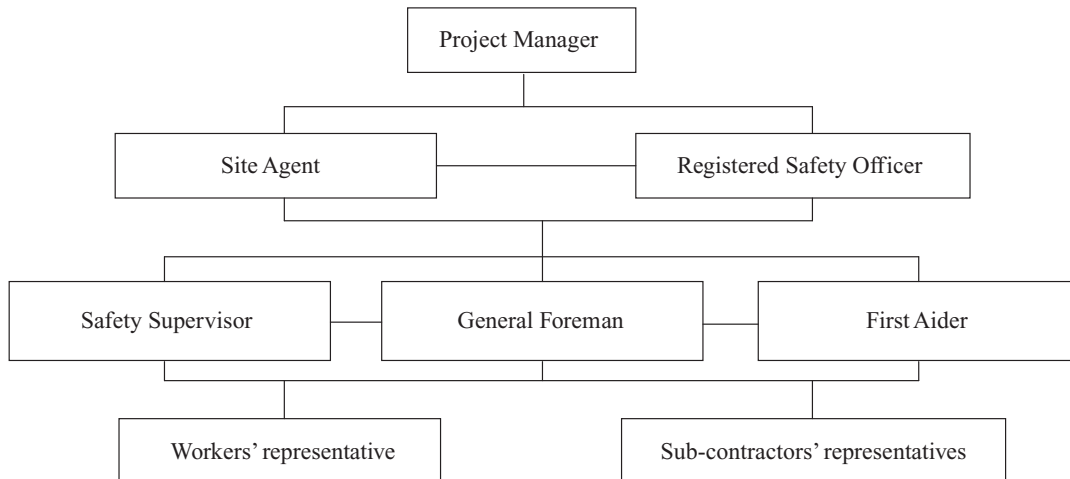
Our Directors are of the view that safety is the first priority during the delivery of our services. We are committed to providing a safe and healthy working environment to our staff and workers of our subcontractors by managing various kinds of risks in relation to implementation of our projects.

Our safety management system is documented in written procedures and supplemented with oral instructions, trainings and demonstrations. We have comprehensive safety plan for each contract undertaken by us, which covers general safety policies, safety organisational chart, safety training, in-house safety rules and regulations, safety and health inspections, job hazards analysis, personal protective equipment, accident investigation, emergency preparedness, safety promotion, health assurance programme, control of subcontractors and

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process control programme. Communications of safety working procedures and risk control measures are made through the site safety committee, safety trainings, daily coordination meeting and internal circulations and reports.

A site safety committee is formed for each construction site before a contract is awarded. Members of the site safety committee meet every month for communication and reporting on safety and health issues amongst all levels from top management down to labour force. Set out below is the organizational chart of a typical site safety committee for each project:



Members of the site safety committee may vary from project to project. In general, a project manager has more than 10 years of experience in civil engineering and construction and obtained a bachelor's degree or above in engineering related discipline. Please refer to the section headed “Directors and senior management” in this document for the background and industry experience of our project managers. The safety officers shall be registered under the Factories and Industrial Undertakings Regulations (Chapter 59A of the Laws of Hong Kong). The safety officers employed by us shall have at least three years of experience in construction works and have completed training courses in relation to occupational safety.

Project manager

The main responsibilities of the project manager are (i) initiating and reviewing the safety policies for prevention of injury, ill health, damage and wastage; (ii) setting targets for reduction of accident rates; (iii) ensuring that the site safety plan is regularly reviewed and kept up to date and implemented; (iv) ensuring that all levels of staff receive adequate and appropriate training; (v) ensuring that line management is conversant with the relevant requirements of current legislation and the site safety plan and that all are assigned appropriate duties and responsibilities for implementation of safety policies; (vi) carrying out disciplinary action against those subcontractors and their employees who have repeatedly violated relevant safety regulations; and (vii) maintaining regular communication with the site safety officer.

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Site agent

The site agent reports to the project manager for implementing the pertinent requirements of the safety plan. He is responsible for (i) receiving verbal and written report or checklist from the safety officer and implementing the recommendations to enhance the safety and health of the employees on site; (ii) reporting accidents and dangerous occurrence within 24 hours; (iii) chairing the monthly site safety committee meeting; (iv) carrying out daily site safety inspection and chairing the daily safety co-ordination meeting; (v) issuing warning letters to workers for health and safety violations and imposing penalties or even removing offenders from site for subsequent misdemeanors; and (vi) taking urgent action to protect the safety of the site and preventing unsafe working practices or other violations of the safety plan or statutory regulations.

Registered safety officer

The site's registered safety officers report directly to the project manager or project director. They are mainly responsible for (i) carrying out safety inspections and preparing inspection reports; (ii) supervising and monitoring implementation of the safety plan and risk control measures; (iii) ensuring that subcontractors and all persons working on site comply with the requirements of the safety plan; (iv) investigating accidents and injuries and reporting with recommendations for prevention of re-occurrence; (v) preparing training programmes and conducting training; (vi) maintaining a record of all examinations and test certificates for plant and temporary structures and safety diary for recording all matters related to safety and health; (vii) maintaining a register of first aiders, competent persons and examiners required under the relevant legislations and persons responsible for conducting different levels of safety training; (viii) conducting internal safety audits at intervals of not less than once every six months; and (ix) contacting the Labour Department, manufacturers and trade associations once it is required. As at the Latest Practicable Date, our Group had five safety officers registered under the Factories and Industrial Undertakings Regulations (Chapter 59A of the Laws of Hong Kong).

Safety supervisor

The site's safety supervisors are accountable to the registered safety officers. They are mainly responsible for (i) carrying out daily inspection and completion of the daily inspection checklist; (ii) supervising workers to ensure their observance of the safety standards; (iii) promoting and improving site safety conciseness and awareness; (iv) preparing weekly safety report to the safety officer; and (v) conducting daily and weekly cleaning and tidying of the site and checking of the site after each day's work.

General foreman

The site's general foreman is responsible for (i) incorporating safety and health instructions in routine orders; (ii) reporting to the safety officer and site agent of any workers or subcontractors who consistently fail to perform safety or ignoring safety instructions; (iii) supervising any particular task which would associate with potential

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hazards so as to ensure the health and safety of the workers engaged; (iv) reporting defects in plant or equipment; and (v) reporting any accident in the first notice to the safety officer and site agent.

First Aider

The site's first aider is responsible for (i) providing first aid treatment to the injured and accompanying the injured to hospital; (ii) maintaining records of site injuries; (iii) reporting all injuries to safety supervisor or safety officer immediately; and (iv) maintaining an adequate stock of first aid equipment.

Workers' representative and subcontractors' representatives

Workers' representative and subcontractors' representatives attend the site's safety committee meeting to provide opinions for improvement of site's safety.

We have also implemented a stringent set of safety control measures over our subcontractors to ensure the entire safety performance of our projects. Pursuant to section 24 of the Employees' Compensation Ordinance, when an employee of a subcontractor is injured at work, the principal contractor shall be liable for any claim of compensation made by the injured employee under the Employees' Compensation Ordinance. Therefore, for any action regarding personal injuries instituted by the employees of our subcontractors or subcontractors of lower tiers, we would always be named as one of the defendants due to its liability to settle the claim of compensation pursuant to section 24 of the Employees' Compensation Ordinance even without any fault on our part. Such payment is recoverable from our subcontractors pursuant to section 24 of the Employees' Compensation Ordinance. Since either we or the direct employers of the employees in question should have taken out employee's compensation insurance policy, the payment should be ultimately recoverable from the insurance companies.

We implement the following safety control measures in order to ensure our subcontractors to comply with the safety standards:

- (i) We have set up general rules for subcontractors and their employees to observe on site. All subcontractors and their employees are informed of the details and responsibilities stated in the outline safety plan prepared for each contract before commencement of the works and during site specific induction training. Subsequent amendments to such outline safety plan will be posted on safety notice board for every site and introduced to workers during on-site safety training;
- (ii) Safety supervisors and safety representatives appointed under each contract carry out daily safety inspection to ensure that all identified or potential safety hazards/abnormalities are rectified within the required time frame;
- (iii) Our on-site safety officers carry out weekly site inspection. A safety inspection report is used by the safety officers to check and monitor the compliance of our safety rules;

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- (iv) We conduct monthly site safety and environmental management committee meetings with customers and monthly site safety and environmental meeting with our subcontractors and workers to discuss safety issues and review their safety performance;
- (v) An evaluation is conducted for assessment of the safety performance of each subcontractor every two months; and
- (vi) We carry out disciplinary action against those subcontractors and their employees who have repeatedly failed to comply with our safety rules. Our site agents and safety officers have the authority to issue safety warning notice to subcontractors and their employees to ensure their compliance with the safety rules.

Our Group's handling and recording system for accidents and dangerous occurrence are designed to satisfy both statutory and contractual obligations and apply to all subcontractors engaged in the project.

In the event of personal injury or an accident happened in the workplace which could have resulted in serious injury or damages to the works or plant or a dangerous occurrence, the general foreman or safety supervisor will immediately initiate the reporting procedure by verbally advising site agent and safety officer. Upon receiving notification of an accident, incident or other dangerous occurrences on site, the site agent will verbally report to the engineer's site staff or engineer's representative immediately. A written preliminary report within 24 hours of the accident or incident with adequate information will be submitted to the engineer's representative.

For personal injury or an accident, a completed statutory Form 2 (a prescribed form in the Employees' Compensation Ordinance) in duplicate copies together with the supplementary information on accidents on construction site will be submitted to the Labour Department and engineer's representative within 7 days of the accident for employee compensation. A complete injury or accident report form with safety recommendations for accident recurrence and a copy of all the correspondence to the Government departments will be submitted to the engineer's representative. We will report minor accidents to Labour Department with temporary incapacity not more than 3 days using Form 2B with a copy to the engineer' representative for record following the same procedures as for the reportable accidents describe above.

For dangerous occurrence, we will report in writing to the Occupational Safety and Health Branch of Labour Department within 24 hours, irrespective of whether there are casualties or not, on the Labour Department's standard "Dangerous Occurrence Report Form".

An investigation team comprises safety officer, site agent, safety supervisor and the immediate supervisor of the injured, other specialist as appropriate will be formed for accident investigation. Investigation will be conducted by (i) taking photos and making sketches for narration; (ii) examining the equipment/tool/material involved in the accident; (iii) reporting on the environment of the accident scene; (iv) interviewing the injured person, eye-witness and any other parties involved; (v) consulting expert opinion when necessary;

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and (vi) identifying the specific employer of those involved. After investigating the accident, our safety officer will complete an accident investigation report. The site agent will arrange an appropriate competent person to inspect the workplace to determine whether it is safe for work before allowing work to restart at the incident place. Such inspection will include a check on the stability of the workplace, the function of the plant and machinery, the installation of the electric devices and etc.

We have established procedures to ensure that all accidents, incidents, dangerous occurrence and near misses are recorded in the prescribed forms. Each entry will show the name and occupation of the injured party, the name of employer, the date and time of the injury, the precise nature and cause of the injury, the estimated period of incapacity (if any) and the first aid treatment administered. The entry will also indicate whether the injury was reportable under the Factories and Industrial Undertakings Regulations. Our safety officer will collate the above information into a consolidated report for the project manager and submit the same to the engineer. Our safety officer will maintain comprehensive accident and incidents statistical data based on the monthly returns. The database will provide information on the cumulative total number of reportable injury accidents on the project and cumulative reportable injury accident/incident and frequency rates.

A case study approach is employed by us in site safety meetings monthly or when necessary with on-site workers. Lessons learned from recent injuries or accidents occurred on our site or in the construction industry will be reported in such meetings to strengthen site safety conciseness and awareness. Our safety officer will prepare recommendations to improve our existing project safety plan and prevent re-occurrence of similar injuries or accidents. Furthermore, we will review our safety policy regularly and will make amendments to our safety policy to incorporate new rules and regulations applicable to the industry when necessary.

In accordance with section 13 of the Factories and Industrial Undertakings (Safety Management) Regulation (Chapter 59AF of the Laws of Hong Kong), semi-annual corporate safety audits for our Group are carried out by an external registered safety auditor to collect and assess the information on and suggest improvements to our safety management system during the Track Record Period. Such external safety auditor has been registered as a safety auditor under section 4(1) of the Factories and Industrial Undertakings (Safety Management) Regulation (Chapter 59AF of the Laws of Hong Kong) since 14 November 2003. Normally, one project undertaken by us and related workplace will be selected and visited by the safety auditor to verify the implementation of safety management system. In addition, pursuant to schedule 3 of the Factories and Industrial Undertaking (Safety Management) Regulation (Chapter 59AF of the Laws of Hong Kong), additional safety audits will be conducted towards the projects with contract value of HK\$100 million or more. The objectives and scope of audit include: (i) to determine the conformity of the safety management system elements with the requirements of the Code of Practice on Safety Management issued by the Occupational Safety and Health Branch of the Labour Department; (ii) to determine the efficiency, effectiveness and reliability of the safety management system in meeting the planned arrangements and specified safety objectives and requirements; (iii) to assess the safety performance against the regulatory requirements; and (iv) to provide our Group with an opportunity to continuously improve the safety management system through correction actions. During the audit, physical site inspections,

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system documents examination and interview of site personnel were conducted. A corporate safety report which contains audit details, audit tool, status of project being audited, objectives and scope of audit, audit process and criteria, findings and recommendations and follow-up action plan will be prepared and submitted to the Safety Management Administration Office of the Labour Department of the Government. As evaluated by the external safety auditors, our corporate safety performance during the Track Record Period ranged up to 81.51%.

In recognition of our safety performance, we received the 10th and 11th Hong Kong Occupational Safety and Health Award – Safety Performance Award (Construction) from the Occupational Safety & Health Council in 2011 and 2012. Please refer to the subsection headed “Awards and recognition” in this section below for further details of our safety awards.

Although we have established comprehensive safety management system and implemented various safety control measures to mitigate safety risks, the occurrence of accidents or injuries to workers on our sites cannot be completely eliminated due to the nature of the works of the construction industry. We have taken out insurance for our workers as required by the contracts and the Employees’ Compensation Ordinance (Chapter 282 of the Laws of Hong Kong). For each of the two years ended 31 March 2014 and since 1 April 2014 up to the Latest Practicable Date, we recorded one, nil and nil non-fatal reportable accident(s) respectively. No fatal accidents were recorded during the Track Record Period and up to the Latest Practicable Date.

A table comparing the overall accident rates for the construction industry against us with regard to accident rate per 1,000 workers per year is set out below:

	Construction industry average <i>(Note 1)</i>	Our Group <i>(Note 2)</i>
Year 2012	44.3	6.1 <i>(Note 3)</i>
Year 2013	40.8	0 <i>(Note 4)</i>
Year 2014 up to the Latest Practicable Date	Not available	0 <i>(Note 5)</i>

Notes:

1. Extract from “Report on Accident Statistics and Analysis for Public Works Contracts for 2013” published by the Safety Section of the Development Bureau in June 2014.
2. Cumulative number of accidents per 1,000 workers per year, based on a conversion of 1.67 accidents per 100,000 man-hours worked equivalent to 60 accidents per 1,000 workers per year.
3. Based on one cumulative non-fatal reportable accident and 593,958 man-hours worked converted in accordance with note 2 above.
4. No reportable accident occurred in 2013.

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5. On 12 November 2014, a general worker of a subcontractor of our Group was injured when a hydraulic soil excavator operated by him was tipped over during lunch hour. As the worker operated the hydraulic soil excavator without our or our subcontractor's authorisation and the accident happened during non-business hour, the accident was disregarded for the purpose of computation of the accident rate.

Based on the above, our Directors are of the view that our accident rate is lower than the construction industry average during the Track Record Period and up to the Latest Practicable Date.

The following table shows the lost time injury frequency rate ("LTIFR") for the accidents occurred to us:

	Number of lost time injuries	Number of man-hours worked	LTIFR (Note)
Year 2012	4	1,295,959	3.09
Year 2013	1	1,138,072	0.88
Year 2014 up to the Latest Practicable Date	0	1,412,137	0

Note: The LTIFR is calculated based on the number of lost time injuries multiplied by 1,000,000 divided by the number of man-hours worked.

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During the Track Record Period and up to the Latest Practicable Date, we had five outstanding claims for personal injuries and employees compensation involving five incidents, of which a sum (inclusive of sick leave allowance and medical fees but exclusive of the damages that may be payable by us under civil claims) of approximately HK\$0.9 million had been paid by our Company during the Track Record Period and up to the Latest Practicable Date. The table below sets out the work injuries occurred at our sites and compensated by our Company during the Track Record Period and up to the Latest Practicable Date relating to the said five incidents:

Case	Year	Date of incident	Nature of incident	Compensation paid by our Company up to the Latest Practicable Date <i>(Note 1)</i>	Amount reimbursed by insurance company	Rectification actions
A	2012	9 December 2012	Fall from height	HK\$378,350	To be assessed	Use of safety belt and attach to a suitably located anchorage
B <i>(Note 2)</i>	2012	13 July 2012	Leg injured by timber cutting saw	HK\$468,528	To be assessed	<ul style="list-style-type: none"> ● Select the correct weight, size and tool for the job ● Ensure that handles have a smooth finish, should be easy to grasp and should have no sharp edges or corners
C	2012	28 June 2012	Flying particles causing injury to eye	HK\$218,120 <i>(Note 4)</i>	Nil <i>(Note 3)</i>	<ul style="list-style-type: none"> ● Keep maintenance to avoid blockage of the pipeline ● Worker should wear conceal type goggles ● Conduct safety training on precaution on blowout of grouting hose
D	2012	15 May 2012	Hit by falling objects	HK\$395,830	Nil <i>(Note 5)</i>	Surround scaffolds and elevated work area with toe-boards and safety nets to prevent objects falling off from height
E	2014	12 November 2014	Tipping over of hydraulic soil excavator	Nil	N/A <i>(Note 6)</i>	Remind staff to leave construction sites during lunch hour

Notes:

1. Compensation paid by our Group comprised sick leave allowance, medical fees and compensation (if any) but excluded the damages that may be payable by us under civil claims and is calculated up to the nearest thousand;
2. This is the non-fatal reportable accident recorded in Year 2012;
3. The injured person is an employee of a subcontractor of our Group. The insurance company rejected the employees' compensation claim on the ground that the insurance coverage does not extend to a subcontractor's employer liability;

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4. A District Court Action (DCEC 1971/2013) was commenced by the injured person against UEL and one other respondent in respect of the claim for employees' compensation under the Employees' Compensation Ordinance (Chapter 282 of the Laws of Hong Kong) for personal injury sustained by him, details of which were disclosed in the subsection headed "Legal proceedings" under this section below;
5. The insurance company rejected the employee's compensation claim as the accident had not been reported within the required period. The injured person was an employee of a subcontractor of our Company. We have not been informed by such subcontractor at the time of the accident and consequently we have failed to notify the accident to the insurance Company within the required period;
6. The injured person is an employee of a subcontractor of our Group. The accident was caused by the tipping over of a hydraulic soil excavator operated by the injured person during lunch hour without our or our subcontractor's authorisation. [As at the Latest Practicable Date, we had not received any complaint from the Government nor claim from the injured person in relation this accident.]

All of the above accidents and injuries had been reported to the Labour Department. According to the Certificate of Review of Assessment issued by the Employees' Compensation (Ordinary Assessment) Board (the "EC Board") dated 12 March 2014, the loss of earning capacity permanently caused by the injury under Case B has been revised from 3% to 3.5%, pursuant to an appeal filed by the applicant on 7 October 2013 against the initial assessment by the EC Board under section 16G of the Employees' Compensation Ordinance. Therefore, the total amount of compensation payable under Case B would be approximately HK\$59,000. According to the Certificate of Assessment issued by the EC Board dated 19 November 2013, the loss of earning capacity permanently caused by the injury under Case C is 25%. Therefore, the total amount of compensation would be HK\$306,000 for Case C. As advised by the legal advisers to our Company as to our Group's litigation, it is difficult to estimate the maximum potential liabilities of our Group for Cases A and D at this stage since the compensation payable by our Group will be subject to an assessment of the permanent loss of earning capacity by the EC Board. It would not be feasible to assess the maximum amount of compensation and penalties potentially payable by our Group with reference to similar cases since the decisions of the EC Board are not published and available in public record. Further, each of these assessments is based on individual circumstances and cannot be generalised, save for clear-cut cases of permanent total incapacity where the respective percentages of the loss of earning capacity are set out in the First Schedule to the Employees' Compensation Ordinance.

In our case, none of the above cases fall within the First Schedule to the Employees' Compensation Ordinance. As such, it is considered that our Group should rely on the assessment of the EC Board, and that the results of any attempt by our Group to assess the above cases by adopting the percentages of the loss of earning capacity for cases of permanent total incapacity as specified in the First Schedule of the Employees' Compensation Ordinance would be misleading and exaggerating.

Having said that, our Group has appointed a medical expert to assess the maximum potential liability of our Group in respect of Case D. According to an assessment report dated 23 January 2014 and issued by a private medical practitioner, the loss of earning capacity permanently caused by the injury under Case D is 3%. Subject to the assessment by the EC Board, it is estimated that the amount of compensation under Case D would be

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approximately HK\$12,000. Our Group will appoint a medical expert to assess the maximum potential liability of our Group in respect of Case A, subject to the obtaining of the consent from the injured employee under Case A.

All insurance claims are handled by our Human Resources & Administration Department, headed by the Head of Human Resources. Upon receipt of an injury case, our Human Resources Officer will submit the relevant information to the insurance company directly or through the broker. The insurance company will then send request for further information and our Human Resources Officer will prepare the requested information for submission to the insurance company.

Our Company will implement enhanced internal controls on handling insurance claims before Listing. We will procure our general foremen to check regularly with each subcontractor whether there were accidents/injuries occurred on our construction sites to ensure timely reporting of accidents/injuries by our subcontractors. In the event that subcontractors fail to report accidents timely or comply with our safety policy, we will consider disciplinary action including termination of works by such subcontractors. In addition, our Group will purchase employees’ compensation policy to cover employees of subcontractors in the future to mitigate the risk.

During the Track Record Period, there had been three claims for property damages in relation to damage to the vehicles of our Group with an aggregate claim amount of approximately HK\$71,000, of which approximately HK\$40,000 had been reimbursed by an insurance company in respect of one claim during the same period. In respect of the remaining two claims, the Group has paid approximately HK\$9,000 for the settlement of one claim and has submitted to the insurance company the other claim which is now under the insurance company’s consideration. During the Track Record Period, no material injury and fatal accidents had happened on our sites.

Our Directors confirmed that save as disclosed in this subsection and the subsection headed “Legal Proceedings” in this section below, we have complied with all the relevant laws, rules and regulations relating to safety and health in all material respects. None of the Directors, senior management members and personnel involved has been investigated and sued by the relevant government authorities and/or injured victims. Upon perusal of the results of the latest litigation search conducted against each member of our Group, the Hong Kong Legal Advisers confirmed that they are not aware of any material non-compliance by our Group in relation to the relevant laws, rules and regulations relating to safety and health as at the Latest Practicable Date save as disclosed in this subsection and the subsection headed “Legal Proceedings” in this section below.

As summarised in the above paragraphs, our safety management system is documented in written procedures and supplemented with oral instructions, trainings and demonstrations. We have comprehensive safety plan for each contract and established handling and recording system for accidents and dangerous occurrence. We have engaged external registered safety auditor to conduct semi-annual corporate safety audits and additional safety audits towards the projects with contract value of HK\$100 million or more. We have also adopted additional preventive measures to improve the workers’ awareness on safety and strengthen

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the control over our subcontractors. On such basis, our Directors believe, and the Sponsor concurs that, the existing safety measures are adequate and effective to ensure ongoing compliance with relevant laws and regulations by our Group.

During the Track Record Period and up to the Latest Practicable Date, there were seven prosecution cases laid by different departments of the Government against our Group, six of which were either acquitted after trial or the prosecutions were dismissed. Accordingly, no rectification actions would be needed by our Group for these six prosecution cases. Our Group has no potential liability (including civil liability) for the abovementioned prosecution cases. As at the Latest Practicable Date, the following prosecution case against Kwan On – U-Tech 1 was still pending:

Department of the Government	Contract number	Case number	Date of incident	Date of hearing	Offence/Cause
Labour Department	10/WSD/10	KTS 12067/2014	25 February 2014	12 February 2015 (Note)	Being the contractor responsible for the site where workers employed thereat were liable to come into contact with live electric cable or apparatus, failed to take such measures as will prevent the workers from being endangered by the cable or apparatus

Note: The above case was originally scheduled to be heard on 18 December 2014 but has been adjourned to 12 February 2015 pending resolution of a point of law regarding the capacity of a joint venture company by the Hong Kong Court of Final Appeal in another legal proceeding unrelated to our Group.

The offence in respect of the above case number KTS 12067/2014 is stipulated in sections 47(1), 68(1)(a) and 68(2)(a) of Construction Sites (Safety) Regulations (Cap. 59I of the Laws of Hong Kong). The maximum fine for the above prosecution case is HK\$200,000 pursuant to rule 68(2)(a) of Construction Sites (Safety) Regulations.

Save as disclosed above, our Directors confirm that no prosecution has been laid against our Group by any relevant authorities in respect of violation of applicable laws or regulations.

Furthermore, having considered that (i) risks of accidents or injuries to workers are inherent due to the nature of works in the construction industry; (ii) our Group have implemented various safety measures to mitigate safety risks; (iii) our Group has not recorded any fatal accident and our accident rate is lower than the average for public works contracts during the Track Record Period and up to the Latest Practicable Date, our Directors are of the view, and the Sponsor concurs that, the past litigations, prosecutions and non-compliance safety issues do not involve any dishonesty on the part of our Directors or impugn on their integrity or competence and do not affect their suitability to act as directors of a listed issuer under Rules 5.01 and 5.02 of the GEM Listing Rules.

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INTERNAL CONTROL

We strive to maintain the integrity of our business, results of operations and reputation by strictly adhering to internal control system in respect of our construction engineering services. As such, we have implemented an effective internal control system by developing and enhancing, from time to time, different sets of internal control procedures and manuals covering a number of key control areas such as financial management, tendering, budgeting, purchase and procurement management, control over subcontractors, safety and environment compliance management, with a view to ensuring compliance by our Group with applicable laws and regulations.

In preparation for the Listing and to further improve our internal control system, we have engaged BDO Financial Services Limited (the "**Internal Control Adviser**") on 13 September 2012 to undertake a review on the internal control system of our Group. During the internal control review, our Internal Control Adviser has reviewed the internal control system of our Group according to the agreed scope which included: (1) entity-level controls; (2) tendering, budgeting and running construction projects; (3) subcontracting and accounts payable; (4) procurement and accounts payable; (5) project expenses reimbursement; (6) expenditure on human resources and payroll cycle; (7) treasury and cash management; (8) financial reporting and disclosure; (9) budgeting and profit forecast; and (10) general computer controls. The Internal Control Adviser has recommended measures to improve and rectify significant weakness of the internal control systems identified during the review, and the significant weaknesses and recommended measures identified have been summarised in the following paragraphs:

In respect of the imperfection in recognition of revenue, the Internal Control Adviser observed that our Group in the past has recognised contract revenue with reference to the monthly interim payment ("**IP**") certificate issued by the customers concerned. The period covered by the IP certificate may span across different financial reporting periods. Recognizing revenue based on the receiving date of the IP certificate may result in cutoff issue. Moreover, there were no periodic reviews of the estimated total contract revenue and costs. This practice may not be in line with HKAS 11 which stipulated that contract revenue shall be recognised by reference to the stage of completion of the contract activity at the end of the reporting period. In addition, any expected loss on the contract may not be recognised as an expense immediately. We have identified five entities within the Group namely, Kwan On, Kwan On – U-Tech 1, UEL, UECL and UEWL having the aforesaid issue and engaged BDO Tax Limited ("**Tax Adviser**") as our tax adviser to review and comment on whether the financial difference quantified by us between our previous contract revenue recognition that did not comply with HKAS 11 and the revenue recognition based on the stage of completion method under HKAS 11 (the "**Financial Difference**") would attract additional tax liability for the years of assessment 2010/11 and/or 2011/12 and any resulting Section 82A penalty imposed by the IRD.

According to the aforesaid tax review, the Tax Adviser is of the view that there is additional tax liability for Kwan On-U-Tech 1 for the year of assessment 2011/12 as a result of the Financial Difference. There may be also a potential Section 82A penalty up to treble the amount of the tax undercharged due to the understatement of profits in filing the Profits Tax Return for the year of assessment 2011/12 by Kwan On – U-Tech 1. The maximum

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Section 82A penalty that may be imposed on Kwan On – U-Tech 1 by the IRD as a result of the understatement of the assessable profits for the year of assessment 2011/12 is HK\$2,581,731 which is derived by arithmetically trebling the amount of tax undercharged of HK\$860,577 based on the estimated assessment issued by the IRD on 10 February 2014. However, if the IRD imposes the penalty, on the basis that Kwan On – U-Tech 1 voluntarily reported the understatement of profits, the percentage of penalty is generally in the range of 30% to 60% of the tax undercharged according to the penalty policy of the IRD. The percentage may be adjusted upwards or downwards after taking into consideration of the aggravating and mitigating factors. The tax representative of Kwan On – U-Tech 1 has already informed the IRD under its letter dated 9 December 2013 on the additional profit by submitting a revised profits tax computation for the year of assessment 2011/12 which takes into account of the Financial Difference and other prior year adjustments mainly for the recognition of the proceeds received from customer to income as resulted from receipt in advance. Kwan On – U-Tech 1 has received the estimated assessment from the IRD dated 10 February 2014 for the year of assessment 2011/12 based on the revised profits tax computation submitted. The total tax payable of HK\$860,577 for the year of assessment 2011/12 was settled by Kwan On – U-Tech 1 in about March 2014. Our Group has accounted for such additional tax liability of HK\$860,577 in the financial information presented in the Accountant's Report. Our Group has not made any provision for the Section 82A penalty given that such potential tax penalty may or may not be incurred and such amount could not be ascertained unless we have received the relevant notice from IRD.

As for Kwan On, the Tax Adviser is of the view that it will have a tax refund of HK\$7,463 and additional tax liability of HK\$44,643 for the years of assessment 2010/11 and 2011/12 respectively resulting from the Financial Difference without taking into account of other prior year adjustments. The tax impact of the Financial Difference on Kwan On can only be ascertained after taking into account of all other prior year adjustments which may have tax implications for the same year of assessment affected, which are mainly discount of non-current portion of retention money receivable and payables and staff annual leave and long service payments provision. The tax representative of Kwan On has already filed revised tax computations for the years of assessment of 2010/11 and 2011/12 under its covering letter dated 11 November 2013 as a result of the Financial Difference and other prior year adjustments claiming reduction of assessable profits of HK\$3,599,641 for year of assessment 2010/11 and HK\$528,352 for the year of assessment 2011/12 by setting them off against the assessable profits for the year of assessment 2012/13 in the 2012/13 Profits Tax Return. The IRD has issued an assessment for the year of assessment 2012/13 on 29 November 2013 in accordance with the Profits Tax Return filed under the IRD's assessing programme of "Assess First Audit Later". In the assessment, the assessable profits for the year of assessment 2012/13 are reduced by the reduction of assessable profits of HK\$3,599,641 for year of assessment 2010/11 and HK\$528,352 for the year of assessment 2011/12. Under the programme of "Assess First Audit Later", assessments will be issued based on the information reported in the Profits Tax Returns first and, assessments may be selected for tax examination later. Should Kwan On fail to claim the reduction of assessable profits for the years of assessment 2010/11 and 2011/12, it will incur additional tax liabilities of HK\$681,118 $[(HK\$3,599,641 + HK\$528,352) \times 16.5\%]$ for the year of assessment of 2012/13. However, such potential tax liabilities are subject to the examination of the IRD. As at the Latest Practicable Date, we had not received any response from the IRD in examining the claim.

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The Tax Adviser is of the view that there is no additional tax liability for the other three entities, namely UEL, UECL and UEWL as the Financial Difference represents changing the assessable profits situations of UEL and UECL to tax loss positions for the year of assessment 2011/12, and to increase the tax loss claimed by UEWL for the years of assessment 2010/11 and 2011/12.

The Indemnifiers will indemnify the Group against, among other things, any further tax liabilities and any Section 82A penalty which may be payable by the five entities in respect of any income, profits or gains earned, accrued or received or deemed to have been earned, accrued or received on or before the Listing Date pursuant to the Deed of Indemnity.

To prevent the recurrence of this non-compliance incident, we have assigned our financial controller to prepare a revenue recognition schedule to adjust for the time difference between the date of certificate and reporting date so that comparison between the percentage completion by costs and by certificate could be conducted. We have also assigned our Quantity Surveying and Tendering Department and our responsible project managers to prepare budgets to the estimated contract sum and total cost for each project. Details of the significant judgments and estimates involved in revenue recognition are disclosed in the paragraph headed "construction contracts" under the section headed "Financial information".

A follow-up review was performed by the Internal Control Adviser for the enhanced internal controls for the period from January 2013 to August 2013 for the abovementioned non-compliance issue identified during the review of the Internal Control Adviser. After the follow-up review, the Internal Control Adviser concurs with our Directors' and our Sponsor's view that the enhanced internal controls have been properly designed and operated effectively by our Company.

In respect of the deficiencies in financial reporting, the Internal Control Adviser observed that our Company has not yet documented a comprehensive monthly financial closing procedure. In addition, there is neither month-end nor period-end financial closing. The Internal Control Adviser has recommended that our Group should adopt monthly closing procedure and prepare closing checklist as a tool to ensure all financial data is being captured under accrual basis. We have adopted the monthly closing procedure. Month-ending closing checklist is prepared by our Accounting Manager and reviewed by our Financial Controller. Our Accounting Department compiles reports in standard format which include a profit and loss account and balance sheet to present to our Board on a monthly basis. Our Accounting Officer prepares a monthly cash count record sheet attaching a printed general ledger which is checked by our Assistant Accountant and reviewed by our Accounting Manager.

In respect of the deficiencies in the preparation of financial budget and forecast, the Internal Control Adviser observed that no formal budget and plan had been prepared for our Company as a whole. In fact, the budget is only prepared for each individual project. The Internal Control Adviser recommended that an annual budget and cash flow forecast shall be prepared by our Company and reviewed and approved by our Board. Variance analysis was also recommended by the Internal Control Adviser to be performed regularly. We have formalized the procedure of preparing, reviewing and updating of budget and cash flow

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forecast in our internal control manual. Our Accounting Manager has prepared a profit forecast and cash flow forecast for the year ended 31 March 2013, which was reviewed by our Financial Controller and approved by the Managing Director. The profit forecast and cash flow forecast will be prepared on an ongoing basis. On a quarterly basis, actual figures are compared to the budget and cash flow forecast. Amendment to the budget and forecast would be considered.

In respect of the shortcomings in the purchase of materials, the Internal Control Adviser observed that no formal periodic assessment on the existing vendors to ensure the vendors can meet the criteria set by our Company. Besides, the Internal Control Adviser also recommended that all purchase requisition forms shall be duly filled and processed at the site office before sending to our purchase department at the head office. The Internal Control Adviser also suggested that all purchase orders shall be validated by stamping the company chop by authorized staff before sending to the vendor. We have assigned our Quantity Surveying Manager and Purchasing Clerk, respectively, to prepare subcontractor assessment form and vendor assessment form. The assessment will be conducted annually. We have also requested our Purchasing Department to keep a list of personnel at the site office who is authorised to initiate purchase of materials and to process duly signed purchase requisition form hereinafter. In addition, we have asked our Project Director to sign and affix the company chop on every purchase order to signify his approval. The company chop concerned shall be kept by the Project Director.

In respect of the deficiencies in the maintenance of subcontractors' masterfile and periodic assessment of our subcontractors, the Internal Control Adviser observed that there was no review procedure before adding the subcontractor's details into the list of subcontractors. In addition, more than one list of approved subcontractors were maintained by the Quantity Surveying Department. Update on the list was not centralized and may create different versions. Furthermore, the Internal Control Adviser observed that there was no periodic review on the subcontractors' masterfile. The Internal Control Adviser recommended that formal procedures for subcontractor assessment shall be established. All qualified subcontractors should be added to the masterfile of subcontractors, which should be maintained centrally. Periodic review of such masterfile should be conducted at least annually and the process should be formally documented. We have formalized the procedure of periodic assessment of existing subcontractors. The assessments for existing subcontractors have been performed annually by our Quantity Surveying Department. If the assessment result of a subcontractor is unsatisfactory, such subcontractor will be removed from the subcontractors' masterfile by our Quantity Surveying Manager.

In respect of the failure to enter into written subcontracting agreement with certain subcontractors, the Internal Control Adviser has recommended that we should, as soon as possible, execute contracts with all subcontractors with terms and conditions that are mutually agreed before commencement of work. We will enter into written subcontracting agreements with all subcontractors going forward unless rejected by the counterparties. Our Directors consider that based on their past experience in communicating with those subcontractors, they declined to enter into written subcontracting agreements due to their limited knowledge to formulate all terms, rights and obligations in writing and our Directors also consider that the practice of engaging subcontractors without written agreement is not uncommon in the construction industry. For those subcontractors who have not entered into

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subcontracting agreements with us, quotations were submitted by them to us before commencement of works. Works were carried out by them at the same time as details of the quotation were finalised. Although verbal contracts shall be as equally valid and binding as written contracts, the interests of our Group may not be well protected if any conflict or dispute arises out of the verbal contracts. It would be difficult for us to prove the existence and/or the contents of the verbal terms in court since such terms had not been recorded in writing. We will issue a payment statement containing the quantity of work done by respective subcontractor, the unit rate, the value of work, retention withheld, any materials charged back and the then net payable amount to each subcontractor on a job basis. However, in the future, where a subcontractor refuses to enter into written subcontracting agreement with us, we will consider replacing such subcontractor with other suitable subcontractors who possess similar skills, experience and adequate workforce to complete the subcontracting works and are willing to enter into written subcontracting agreements with us. As at the Latest Practicable Date, we had entered into subcontracting agreements with over 20 subcontractors.

Save as disclosed above, the Internal Control Adviser has identified the following significant weaknesses in relation to our internal control system:

- the corporate governance framework of a listed company has not yet been fully established;
- we have not yet established policies and controls regarding the compliance of the GEM Listing Rules;
- our operation manual has not yet been fully implemented and distributed to all staff;
- there are few limitations in the accounting system currently used by our Company;
- monitoring controls among the accounting system shall be enhanced;
- filing for financial documentation shall be enhanced;
- the recognition basis of accounts payable is upon the receipt of the vendor invoice and cut off issues may arise when the invoice date and the goods delivery date are not in the same accounting period;
- there is no evidence of three-way matching (purchase order to invoice) to ensure that the invoice rate agrees with the ordered rate before payments are made to vendors;
- the risk of overspending during construction increases if cost-related expenses were not properly allocated to each project;
- lack of independent review on accuracy of the salary calculation for head office staff;

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- data security for payroll system shall be enhanced;
- failure to prepare the cash flow forecast for each entity in our Group on a monthly basis;
- the delegation of power is too centralized which may lead to the possibility of management override; and
- there is no formal policy on information security.

Regarding the abovementioned significant weakness of the internal control system identified during the review of the Internal Control Adviser, the enhanced internal controls have been fully implemented by our Company since January 2013.

A follow-up review (the “**1st Follow-up Review**”) was performed by the Internal Control Adviser in January 2013 to check whether our Company has remedial deficiencies identified for the period from November 2012 to December 2012. The result of the 1st Follow-up Review is that all the deficiencies (including those significant weaknesses mentioned above) have been rectified by our Company.

In August 2013, an additional follow-up review (the “**2nd Follow-up Review**”) was performed by the Internal Control Adviser for the enhanced internal controls for the period from January 2013 to August 2013 for the abovementioned significant weaknesses of the internal control system identified during the review by the Internal Control Adviser. After the 2nd Follow-up Review, the Internal Control Adviser concurs with the Directors’ view that the enhanced internal controls have been properly designed and operated effectively by our Company.

During the 2nd Follow-up Review, the Internal Control Adviser has also performed review on the internal control measures of our safety system and tested the enhanced internal controls for the period from January 2013 to August 2013. After the review of the documents and information provided by our Company in relation to our safety system and visits to our head office and certain project sites, the Internal Control Adviser concurs with the Directors’ view that the internal controls over our safety system have been properly designed and operated effectively.

Our executive Directors are responsible for the formulation and overseeing the implementation of our internal control measures. We will engage legal advisers and a compliance adviser upon Listing to provide us with updates on the changes in the applicable laws and regulations from time to time to see if any change is required to be made to our operation and internal control procedures. Upon Listing, we will also engage internal control advisers to review our internal control systems on a regular basis and a compliance adviser to advise us on matters relating to the GEM Listing Rules.

Our Directors are of the view that the internal control measures are adequate and effective to enhance the internal control of our Group. The Sponsor has reviewed the internal control and follow-up reports prepared by the Internal Control Adviser, discussed

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with the Internal Control Adviser on the adequacy and effectiveness of the internal control measures and concurred with the Directors' view that the Company's enhanced internal controls, when fully implemented, to be sufficient and effective.

RISK MANAGEMENT

In the course of conducting our construction engineering businesses, we are exposed to various types of risks, including credit risks, operational risks, market risks, liquidity risks and regulatory risks, the details of which have been disclosed under the section headed "Risk factors" in this document.

Save for establishing and implementing internal control procedures as mentioned in the paragraph headed "Internal control" above, our executive Directors are responsible for overseeing and reviewing the implementation of our Group's internal control and risk management measures. Although there are risks associated with our business operations, we have adopted the following measures to prevent or mitigate such risks:

(a) Risk of reliance on the contracts granted by the Government

Our Directors are of the view that the reliance on the Government is not uncommon for construction companies which are mainly engaged in public sector projects. Two members of our Group hold various licenses and certificates to undertake projects of different categories. During the Track Record Period, the revenue of our Group was derived from contracts granted by various Departments of the Government, including WSD, CEDD, ArchSD and DSD through open tendering process. During the Track Record Period, we had not encountered any conflict with the Government regarding our execution of the works contracts nor had we had any works contracts terminated by the Government. Save for the contracts granted by the Government for public sector, we will from time to time tender for works contracts for private sector which are considered by our Directors to be profitable.

(b) Risk of reliance on subcontractors to implement certain parts of contracts

In general, our Directors consider that the quality of works performed by our subcontractors is stable. We have put in place specific subcontractor management plan for each contract undertaken by us and implemented quality, safety and environmental control measures to monitor the performance of our subcontractors and ensure that they comply with the requirements and provision set out in the respective main contracts. Details of our control measures over subcontractors are disclosed in the paragraphs headed "Control over subcontractors", "Quality assurance" and "Safety policy" in this section above.

(c) Risk of labour shortage

We adopt a strategy in retention of staff by providing training and subsidies to staff. We had not encountered any shortage of labour supply during the Track Record Period. As at the Latest Practicable Date, we had a total of 628 employees comprising 264 staff employed on full-time basis and 364 casual workers, with longest years of services of

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approximately 30 years and average years of service of approximately 2 years, respectively. In addition, we may subcontract certain part or parts of a works contracts to subcontractors depending on our manpower availability.

(d) Risk of fluctuation in cost of materials and labour

During the Track Record Period, save for two contracts with ArchSD and two contracts for the private sector in Hong Kong, all of our works contracts for the public sector provide for a contract price adjustment mechanism (both upward and downward adjustments) with reference to the Price Indices. In addition, in order to manage fluctuations of materials prices, we entered into bulk purchase orders with material suppliers and call for delivery of materials whenever necessary. The prices would be fixed within the bulk ordered quantity even if the prices inflated subsequently.

(e) Risk of failure to maintain safe construction sites

In order to manage the risks relating to implementation of our projects, we have put in place a comprehensive safety management system, including implementing safety plan and forming a site safety committee for each contract, having site safety meetings with on-site workers monthly or as and when necessary and engaging external registered safety auditor to assess and suggest improvements to our safety management system. Details of our safety policy are set out in the subsection headed “Safety policy” under this section above. We have also taken out insurance for our workers as required by the contracts and the Employees’ Compensation Ordinance (Chapter 282 of the Laws of Hong Kong).

During the Track Record Period and up to the Latest Practicable Date, our business and financial position has not been materially affected by each of the above risks.

ENVIRONMENTAL PROTECTION

Our business operations are subject to certain environmental protection laws and regulations in Hong Kong, such as Air Pollution Control Ordinance, Noise Control Ordinance, Water Pollution Control Ordinance, Waste Disposal Ordinance and Environmental Impact Assessment Ordinance, details of which are set out in the section headed “Regulatory Overview” in this document. We are committed to the minimisation of the impact on the environment resulting from our business activities and continual improvement of environmental performance to fulfill our responsibilities to both the community and environment.

The principal environmental management measures implemented by our Group are as follows:

- (i) Comply with all applicable environmental related legal requirements and contractual obligations to which our Company subscribes;
- (ii) Prevent, reduce and eliminate pollution or any other degradation of environment resulting from our business activities;

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- (iii) Reduce waste and minimise the consumption of resources;
- (iv) Educate, train and motivate employees to carry out tasks in an environmentally responsible manner;
- (v) Provide sufficient resources and facilities for the implementation of environmental nuisance abatement and waste management;
- (vi) Obtain and renew the necessary environmental licences, registrations and permit;
and
- (vii) Encourage environmental protection among suppliers and subcontractors.

For all of the public sector contracts, we are required to submit an environmental management plan to the engineer appointed by us which sets out the measures to be taken and the responsible personnel to be designated by us to ensure that our works are carried out in the interests of environmental protection. We are also required to report monthly to the engineer on the effectiveness of the implementation of the environmental management plan throughout the duration of the contract. In order to make continual improvement on environmental issues and meet the changing site practices, the environmental officer and the site agent will review and update the abovementioned environmental management plan monthly or as and when necessary or as directed by the engineer appointed by the contractor. An environment protection team which consists of a project director, a contract manager, a project manager, a site agent, an environmental officer, a foremen and an environmental supervisor will be formed to implement the environmental management plan of respective contract. We also require our subcontractors to strictly comply with our environmental protection policy. Our environmental officer is responsible for monitoring the ongoing compliance with the environmental management plan, compiling the monthly environmental report for submission to the engineer and providing the environmental training for the staff and on-site workers.

The annual cost of compliance with applicable environmental laws and regulations in Hong Kong were approximately HK\$95,000, HK\$240,000 and HK\$60,000 for each of the two years ended 31 March 2014 and the six months ended 30 September 2014 respectively, which was mainly attributable to the cost of disposal of construction waste. Our Directors consider that the cost of compliance with applicable environmental laws and regulations going forward will be subject to the nature and category of contracts awarded to us.

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AWARDS AND RECOGNITION

Over the past years, we have received the following awards from the following Governmental department and non-profit organisations:

Year of Grant	Description	Organization
2011	2011 HKCA Construction Safety Innovation Award – Certificate of Appreciation	Hong Kong Construction Association
	The 10th Hong Kong Occupational Safety and Health Award – Safety Performance Award (Construction)	Occupational Safety & Health Council
2012	Best Landslip Preventive Measures Contractor of 2011 – Winning Contractor	CEDD
	The 11th Hong Kong Occupational Safety and Health Award – Safety Performance Award (Construction)	Occupational Safety & Health Council

INSURANCE

We have taken out and maintained employees' compensation insurance and contractor's all risks insurance for each project. The insurance policy generally covers the entire contract period, including the defects liability period following completion of the project.

Our Directors confirm that, during the Track Record Period and up to the Latest Practicable Date, we had taken out and maintained insurance policies in respect of employees' compensation and contractors' all risks for the projects in which members of our Group act as main contractors in accordance with the applicable laws and regulations and relevant contractual terms which is in line with industry practice. During the Track Record Period, the contractors' all risks policies cover our subcontractors and the employer of the contract to the extent of (i) vibration or removal or weakening of support; (ii) employer's property; and (iii) employer's employees as visitors, but exclude injuries to the employees of our subcontractors. Our Directors consider that it is not uncommon for contractors' all-risks policies to exclude subcontractors' employees in the civil engineering industry. In addition, we have insurance cover for our liabilities under employees' compensation and personal injury claims which meet the statutory minimum insurance coverage of HK\$100 million on a per incident basis.

Pursuant to section 40(1B) of the Employees' Compensation Ordinance, we as principal contractor has the discretion to take out insurance policy for an amount not less than HK\$200 million per event to cover our liability and that of our sub-contractors under the Ordinance and at common law.


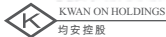


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Nevertheless, pursuant to section 24(1) of the Employees’ Compensation Ordinance, we as principal contractor shall be liable to pay to our sub-contractor’s employees any compensation under the Ordinance. In light of our exposure under section 24(1) of the Employees’ Compensation Ordinance, during the Track Record Period and up to the Latest Practicable Date, the coverage of the current employees’ compensation insurance maintained by us for our projects in progress had been extended to the employees of our subcontractors. We will continue to maintain employees’ compensation insurance covering our subcontractors’ employees going forward. As such, our Directors consider that the insurance premium to be paid will be higher than those paid during the Track Record Period.

The total insurance cost incurred by us amounted to approximately HK\$8.1 million, HK\$13.2 million and HK\$7.8 million respectively for each of the two years ended 31 March 2014 and the six months ended 30 September 2014. Our Directors confirm that the above insurance coverage is adequate for the operation of our business and is in line with the industry norm.

INTELLECTUAL PROPERTY RIGHTS

Trademarks

As at the Latest Practicable Date, we had registered (i) the  trademark numbered 302466072 under classes 37 and 42; (ii) the  trademark numbered 302417670 under Classes 37 and 42; (iii) the  trademark numbered 302505014 under Classes 19 and 37; and (iv) the  trademark numbered 302783638 under Class 16 in Hong Kong. Details of such trademarks are set out in the subsection headed “Intellectual property rights of our Group” in Appendix IV to this document.

Domain name

As at the Latest Practicable Date, we had registered the domain name, kwanonconstruction.com in Hong Kong. Details of such domain name are set out in the subsection headed “Intellectual property rights of our Group” in Appendix IV to this document.

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PROPERTY INTERESTS

As at the Latest Practicable Date, our Group did not own any property interests and leased six properties in Hong Kong, details of which are set out below:

No.	Location of property	Gross floor area (<i>sq.ft.</i>)	Lessor	Date of expiry of lease	Usage
1.	3D & Carport P11, Yiko Industrial Building, 10 Ka Yip Street, Chai Wan, Hong Kong	5,952	Shiu Mau	31 December 2015	Documents storage
2.	Unit B, 8th Floor, North Point Industrial Building, No. 78 Marble Road, No. 499 King's Road, Hong Kong	4,500	An Independent Third Party	6 December 2015	Site office
3.	Unit B3, 11th Floor, Reality Tower, No. 4 Sun On Street, Chai Wan, Hong Kong	510	An Independent Third Party	21 February 2015	Documents storage
4.	5/F, So Hong Commercial Building, 41, 43, 45, 47 Jervois Street, Hong Kong	2,907	An Independent Third Party	31 July 2017	Head office and principal place of business
5.	4/F, So Hong Commercial Building, 41, 43, 45, 47 Jervois Street, Hong Kong	2,907	An Independent Third Party	31 July 2017	Head office and principal place of business
6.	Unit 6, 16/F, Block 45, Heng Fa Chuen, No. 100 Shing Tai Road, Hong Kong	777	Ms. Chiu	30 April 2015	Staff quarters

The aforesaid properties are used for non-property activities as defined under Rule 8.01B(2) of the GEM Listing Rules. According to section 6(2) of the Companies (Exemptions of Companies and Prospectuses from Compliance with Provisions) Notice (Chapter 32L of the Laws of Hong Kong), this document is exempted from compliance with the requirements of section 342(1)(b) of the Companies (Winding Up and Miscellaneous Provisions) Ordinance in relation to paragraph 34(2) of the Third Schedule to the Companies (Winding Up and Miscellaneous Provisions) Ordinance, which require a valuation with respect to all our Group's interests in land or buildings, for the reason that as at the Latest Practicable Date, each of our properties has a carrying amount below 15% of our combined total assets.

During the Track Record Period, we had not experienced any difficulty in renewing our leases.

BUSINESS

LABOUR

The Minimum Wage Ordinance came into effect on 1 May 2011 and the current statutory wage level is fixed at HK\$30 per hour. Furthermore, our Directors confirm that as at the Latest Practicable Date, there was no material operational and financial impact on us as a result of the implementation of the Minimum Wage Ordinance at the current wage level and we have been in compliance with the requirements under the Minimum Wage Ordinance since its enactment.

We had not encountered any shortage of labour supply during the Track Record Period. We are committed to retaining our staff by providing training and subsidies to staff.

In the course of carrying out our works, we may sometimes require our subcontractors to designate its employees to perform works which our subcontractors have contracted to perform. We as the main contractor will be liable to pay wages of such employees of our subcontractors and make contributions to the Mandatory Provident Fund ("MPF") for such employees if our subcontractors fail to do so. According to section 43C of the Employment Ordinance, a principal contractor or a principal contractor and every superior subcontractor jointly and severally is/are liable to pay any wages that become due to an employee who is employed by a subcontractor on any work which the subcontractor has contracted to perform, if such wages are not paid by the subcontractor within the period specified in the Employment Ordinance. In order to (i) ensure that the payments to workers are made timely and accurately and (ii) to prevent the employment of illegal workers, we may, subject to agreement with the subcontractors and the casual workers, pay wages to the casual workers directly. In doing so, our subcontractor will confirm the payroll of such employees at the end of each wage period and consent to our deduction of the payroll and relevant contributions to the MPF for such employees from the subcontracting fee payable by us to such subcontractor. Our Human Resources and Administration Department is responsible for rectifying and compiling the payroll and MPF contributions of such employees of our subcontractors.

Given that it is the principal contractor's liability to pay any wages due to employees employed by subcontractors, our Directors believe that the aforesaid arrangements with subcontractors for employment of employees will ensure the timely payment of wages to their employees and enable us to prevent our subcontractors from using illegal workers on our sites.

We have a zero tolerance policy on the recruitment of illegal workers. When recruiting workers, we will carefully check the identification documents provided by the candidates. We will report to the police when we come across any candidate with suspicious identity. During the Track Record Period, no illegal workers have been reported for the projects we are contracted for.

During the Track Record Period and up to the Latest Practicable Date, we had not encountered any labour strike action on our construction sites.

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STAFF

Staff

As at the Latest Practicable Date, our Group had employed a total of 628 employees, comprising 264 staff employed on a full-time basis and 364 casual workers. Since all the contract works undertaken by our Group are located in Hong Kong, all of our employees work in Hong Kong. The following table shows a breakdown of our employees as at 31 March 2013 and 2014, 30 September 2014 and the Latest Practicable Date by functions:-

Function	As at 31 March		As at 30	As at the
	2013	2014	September	Latest
			2014	Practicable
				Date
Managing director	1	1	1	1
Project management	33	35	39	36
Quantity surveying and tendering	13	13	13	14
Purchasing	5	6	6	6
Safety	7	10	7	7
Finance	9	12	12	12
Human resources and administration	14	14	14	15
Direct workers	249	357	503	537
Total	<u>331</u>	<u>448</u>	<u>595</u>	<u>628</u>

Relationship with staff

Our Directors believe that our Group maintains good working relations with its employees. Our Group has not experienced any significant problems with its employees or disruption to its operations due to labour disputes, nor has it experienced any difficulties in the recruitment and retention of experienced staff. Our Directors believe that our Group has a good working relationship with its employees.

Training and recruitment policies

We generally recruit our employees from the open market by placing recruitment advertisements. Our Group assesses the available manpower on a continuous basis to determine whether additional personnel are required to cope with the business development of our Group.

We provide various types of trainings to our employees, including (i) conducting in-house continuous professional development seminars; (ii) subsidizing our staff for pursuing further studies in related field; and (iii) provision of safety training programme to

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staff to enhance their safety awareness. Our total training expenses for each of the two years ended 31 March 2014 and the six months ended 30 September 2014 amounted to approximately HK\$338,000, HK\$289,000 and HK\$401,000 respectively.

RESEARCH AND DEVELOPMENT

During the Track Record Period and up to the Latest Practicable Date, we did not engage in any research and development activities.

COMPETITION

During the Track Record Period, our Group primarily focused on providing waterworks engineering services, road works and drainage services and landslip preventive, remedial works to slopes and retaining walls services for the public sector in Hong Kong. Our Directors consider the minimum requirements on the financial, technical and management aspects of a contractor for inclusion on the Contractor List and the Specialist List provide effective entry barriers for international and local contractors who are not currently on the aforesaid lists from entering the sector as a main contractor. We compete primarily with those contractors who hold licences of the same status under the same categories on the Contractor List and the Specialist List as us. Based on the information available from WBDB’s website as at the Latest Practicable Date, there were a total of 22 Group C contractors (confirmed) under the category of “Waterworks” and a total of 41 Group C contractors (confirmed) under the category of “Roads and drainage” on the Contractor List. Our Directors are of the view that we compete directly with the contractors listed on the Contractor List. Some evaluations of tenders are based on a formula approach, in which a tenderer’s performance rating is taken into account to a significant extent. Therefore, the low performance rating received will reduce the competitiveness of contractors in tendering for works contracts from the Government. As disclosed in the paragraph headed “competitive strengths” in this section above, Kwan On’s quarterly performance ratings as appraised by WBDB were higher than the industry averages in the recent ten consecutive quarters up to the third quarter of 2014. Our Directors are of the view that Kwan On’s recent above-industry-average performance ratings enhance its competitiveness in tendering a project.

Based on the Government’s actual expenditure of approximately HK\$3,951.1 million for the fiscal year 2013 and the estimated expenditure of approximately HK\$4,499.5 million for the fiscal year 2014 on the projects of water supply, our revenue generated from provision of waterworks engineering services for the public sector for each of the two years ended 31 March 2014 and the six months ended 30 September 2014 of approximately HK\$158.9 million, HK\$208.1 million and HK\$119.8 million represented approximately 4.0%, 4.6% and 2.7% respectively of the above expenditure.

Based on the Government’s actual expenditure of approximately HK\$1,263.8 million for the fiscal year 2013 and the Government’s estimated expenditure of approximately HK\$858.3 million for the fiscal year 2014 on capital projects of stormwater drainage, our revenue generated from provision of roads and drainage works for the public sector for each

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of the two years ended 31 March 2014 and the six months ended 30 September 2014 of approximately HK\$43.2 million, HK\$107.9 million and HK\$135.0 million represented approximately 3.4%, 12.6% and 15.7% respectively of the above expenditure.

Based on the Government’s actual expenditure of approximately HK\$1,029.0 million for the fiscal year 2013 and the Government’s estimated expenditure of approximately HK\$1,000.0 million for the fiscal year 2014 on capital projects for landslip prevention and mitigation works, our revenue generated from LPM Services for the public sector for each of the two years ended 31 March 2014 and the six months ended 30 September 2014 of approximately HK\$109.8 million, HK\$63.3 million and HK\$74.6 million represented approximately 10.7%, 6.3% and 7.5% respectively of the above expenditure.

KEY BUSINESS DRIVERS

Government’s continuous expenditure on civil engineering works in Hong Kong

During the Track Record Period, our Group derived most of our revenue from the works contracts granted by the Government. According to the Government Budgets for the fiscal year 2014-15, the Government’s expenditure on (i) water supply projects under construction; (ii) capital projects of stormwater drainage; and (iii) landslip prevention and mitigation works in Hong Kong for the fiscal year 2013, amounted to approximately HK\$3,951.1 million, approximately HK\$1,263.8 million and approximately HK\$1,029 million respectively. It is expected that the Government will continue to expend on civil engineering projects in Hong Kong in the coming years. Accordingly, our business development will benefit from such continuous expenditure and upcoming projects from the Government.

Our established operating history and proven track record

We have undertaken more than 30 civil engineering projects in Hong Kong since our acquisition of Kwan On in 1993. Kwan On’s quarterly performance ratings as appraised by WBDB were above the industry averages in the recent ten consecutive quarters up to the third quarter of 2014. Some evaluations of tenders are based on a formula approach, in which a tenderer’s performance rating is taken into account to a significant extent. Our Directors consider that the our above-industry-average performance ratings and the proven track record of Kwan On in the execution of contracts will enhance our competitiveness in tendering for works contracts from the Government, which will encourage our Group’s business development in the future.

Our business strategy to diversify source of income by leveraging different types of licences held by Kwan On

In view of the upcoming projects and continuous capital expenditure from CEDD and DSD, our Directors plan to diversify our source of income by tendering for more contracts originated from these two departments. The licences held by Kwan On which had been upgraded to Group C contractors (confirmed) under the “Roads and Drainage” category and Group B contractor (confirmed) under the “Site Formation” category on 26 February 2013

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and 19 June 2013 respectively further enhance our ability to tender for and secure works projects with larger contract values under these two categories and foster the future business growth of our Group.

LEGAL PROCEEDINGS

As at the Latest Practicable Date, our Group was engaged in the following litigation and/or proceedings that could have a material adverse effect on our business, results of operations or financial condition:

- (i) a Court of First Instance Action (HCCT 4/2006) was commenced by a subcontractor of a subcontractor of Kwan On in January 2006 against Kwan On, and the said subcontractor as other defendant, for a sum of approximately HK\$9.52 million or such sum as is due, allegedly as damages for breach of certain oral agreement made by Kwan On for paying the plaintiff should the other defendant fail or refuse to do so. Kwan On denied any liability to pay the plaintiff on the ground that Kwan On had never agreed to be responsible for paying the plaintiff should the other defendant fail or refuse to do so. Kwan On agreed to participate in the payment process in respect of labourer wages for the works and would, if called up, assist the plaintiff in paying its labourers their wages and the agreement made by Kwan On with the plaintiff was recorded under minutes. Kwan On was never called upon by the plaintiff to assist such payments. The plaintiff also claims interest and costs against Kwan On. As advised by the legal advisers to Kwan On as to the said action, they are of the view that the documents which the parties have disclosed so far do not support the plaintiff's case. The plaintiff has left the action in abeyance since September 2009;
- (ii) a Court of First Instance Action (HCPI 279/2013) was commenced by an employee of a subcontractor of Kwan On in or about April 2013 against Kwan On and one other respondent in respect of a claim for personal injury sustained by him in an accident happened on 14 December 2011 arising out of and in the course of his employment. No specific amount of claim was stated in the writ of proceedings. By a consent order of the High Court of Hong Kong dated 16 December 2014, Kwan On and the other respondent were ordered to pay the plaintiff a sum of HK\$1,215,000 (inclusive of interest) in full and final settlement of his claim against Kwan On and the other respondent in respect of the above action, of which payments of HK\$915,000 were already made to the plaintiff by Kwan On's insurer. Kwan On was informed by a letter dated 15 January 2015 from the legal advisers to the said action that its insurer was in the course of arranging the final payment of HK\$300,000 for its legal advisers to discharge the only outstanding balance of such settlement sum;
- (iii) a District Court Action (DCPI 2268/2012) was commenced by an employee of the Director of Lands in or about October 2012 against Kwan On, Secretary for Justice (sued on behalf of Director of Lands Department) and one other defendant in respect of a claim for personal injury sustained by him in his course of employment arising out of the alleged negligence and/or breach of statutory duty and/or breach of common duty of care under the Occupiers Liability Ordinance

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(Chapter 314 of the Laws of Hong Kong) in an accident happened on 11 November 2009 at a construction site alleged to be occupied and managed by Kwan On. No specific amount of claim was stated in the writ of proceeding and no judgment has been entered against Kwan On in respect of the above action. By a letter dated 9 November 2012 from the Department of Justice (on behalf of the Director of Lands) to Kwan On, Kwan On was informed that the plaintiff proposed a settlement offer of HK\$231,711.32 by a letter dated 8 October 2012 from the plaintiff's legal advisers to the Department of Justice. By a further letter dated 14 November 2014 from the plaintiff's solicitor to Kwan On's solicitors and the Department of Justice, the plaintiff made a sanctioned offer in the sum of HK\$185,000 (inclusive of interest but on top of the compensation under the Employees' Compensation Ordinance in the sum of HK\$69,137.68 and exclusive of legal cost) in full and final settlement of the plaintiff's whole claim. Kwan On has not accepted the aforesaid offers and no settlement has been reached;

- (iv) a District Court Action (DCEC 1971/2013) was commenced by an employee of a subcontractor of UEL in November 2013 against UEL as the second respondent, Kwan On as the intended third respondent and the said subcontractor as the first respondent in respect of a claim for employees' compensation under the Employees' Compensation Ordinance (Chapter 282 of the Laws of Hong Kong) for personal injury sustained by the employee in an accident happened on or about 28 June 2012 arising out of and in the course of his employment. According to the Certificate of Assessment of the Employees' Compensation (Ordinary Assessment) Board dated 19 November 2013, the loss of earning capacity permanently caused by the injury is 25%. No specific amount of claim was stated in the writ of proceeding. By a letter dated 13 November 2014 from the plaintiff's legal advisers to UEL's legal advisers as to the said action, the plaintiff has agreed, without prejudice to any issue that may arise in the plaintiff's common law claim, to accept a sum of approximately HK\$341,000 (exclusive of legal cost) in settlement of the claim and the plaintiff's legal advisers have confirmed the receipt from UEL a sum of HK\$341,000 on 3 December 2014;
- (v) a Court of First Instance Action (HCPI 173/2014) was commenced by an employee of a subcontractor of Kwan On in about February 2014 against such subcontractor as the first defendant and Kwan On as the second defendant in respect of a claim for personal injury sustained by him in his course of employment in an accident happened on 26 April 2011 at a construction site alleged to be occupied and managed by the said subcontractor. No specific amount of claim was stated in the writ of proceedings. No settlement has been reached and no judgment has been entered against Kwan On in respect of the above action. As assessed by the legal advisers to Kwan On as to the said action, assuming full deduction (if allowed by the court) of the payment received by the applicant of this case under the previous settled claim against Kwan On and its subcontractor commenced by him under the Employees' Compensation Ordinance (Chapter 282 of the Laws of Hong Kong) of approximately HK\$396,000, it is estimated that the net compensation payable under the said action to be approximately HK\$1,253,000;

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- (vi) a Court of First Instance Action (HCPI 351/2014) was commenced by an employee of a subcontractor of UEL in about April 2014 against such subcontractor as the first defendant and UEL as the second defendant in respect of a claim for personal injury sustained by him in his course of employment in an accident happened on 28 June 2012 at a construction site alleged to be occupied and managed by the said subcontractor. Approximately HK\$2.7 million plus interest is claimed under this action. No settlement has been reached and no judgment has been entered against Kwan On in respect of the above action. The plaintiff of the said action is the applicant of the District Court Action (DCEC 1971/2013) mentioned above; and
- (vii) a District Court Action (DCEC 991/2014) was commenced by an employee of UCRL in about May 2014 against UCRL as the first respondent and Kwan On as the second respondent in respect of a claim for employees' compensation under the Employees' Compensation Ordinance (Chapter 282 of the Laws of Hong Kong) for personal injury sustained by the employee in an accident happened on or about 13 July 2012 arising out of and in the course of his employment. According to the Certificate of Review of Assessment of the Employees' Compensation (Ordinary Assessment) Board dated 12 March 2014, the loss of earning capacity permanently caused by the injury is 3.5%. Accordingly, it is estimated that the compensation payable under the said action will amount to approximately HK\$59,000. Our Directors confirm that our Group has taken out the necessary employees' compensation policy to cover its liability against the said proceeding; and
- (viii) a District Court Action (DCEC 2494/2014) was commenced by an employee of UCRL in about December 2014 against UCRL as the first respondent and Kwan On as the second respondent in respect of a claim for employees' compensation under the Employees' Compensation Ordinance (Chapter 282 of the Laws of Hong Kong) for personal injury sustained by the employee in an accident that happened on or about 9 December 2012 arising out of and in the course of his employment. No specific amount of claim was stated in the writ of proceeding. According to the Certificate of Assessment of the Employees' Compensation (Ordinary Assessment) Board dated 27 October 2014, the loss of earning capacity permanently caused by the injury is 2%. Accordingly, it is estimated that the compensation payable under the said action will amount to approximately HK\$37,000.

The Indemnifiers have undertaken to fully indemnify our Group against all the costs and liabilities incurred by our Group in relation to those outstanding or unsettled legal and arbitration proceedings, investigations, prosecutions and/or claims to the extent that such costs and liabilities are resulting from or by reference to any event or circumstances occurred on or before the date on which the [REDACTED] becomes unconditional that exceed the relevant amounts of provisions made in our Company's audited accounts for the Track Record Period and are not otherwise indemnified by any other parties under any contractual obligations.

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As at the Latest Practicable Date, save as disclosed above, no member of our Group was engaged in any litigation, arbitration or claim of material importance, and no litigation, arbitration or claim of material importance was known to our Directors to be pending or threatened by or against our Group, that would have a material adverse effect on its business, result of operations or financial condition.

NON-COMPLIANCE MATTERS

Our Directors confirm that during the Track Record Period and up to the Latest Practicable Date, our Group had obtained all necessary approvals, permits, consents, licences and registrations required for our business and operations in Hong Kong and all of them were in force.

Prior to and during the Track Record Period, our Group had leased two workshops situated in an industrial building in Chai Wan (the “**Chai Wan Workshops**”) for use as our previous head office, which usage was not in strict compliance with the user provisions stipulated in the occupation permit issued by BD and the Government Lease granted by the Government to which the Chai Wan Workshops are held subject. In order to rectify such non-compliance, our Group has relocated to and operated at our present head office situated in a commercial building in Sheung Wan since 15 November 2014 and used the Chai Wan Workshops for storage of documents. As at the Latest Practicable Date, we had not received any claims, demands or proceedings from the landlord of the Chai Wan Workshops and/or the relevant Government authorities in respect of such past non-compliance.

Our Group’s present use of the leased property in North Point (the “**North Point Property**”) as site office is not in strict compliance with the user provisions stipulated in the occupation permit issued by the BD as well as the Government Lease granted by the Government to which such property is held subject.

The Government Lease of the North Point Property provides that the properties shall not be used for any purposes other than for factory premises, while the relevant occupation permit stipulates the user of the properties as factory space for non-domestic use. In addition, under the relevant tenancy agreement, the North Point Property shall be used for industrial use only. Our Group is currently using the North Point Property as a site office for use by the representatives of WSD, which is not in strict compliance with the relevant user provisions. The site office is provided by our Group for fulfilling part of our contractual obligations under project 15/WSD/11 that, among other matters, our Group shall provide a site office located in North Point as approved by the engineer of WSD throughout the course of the works under the said contract. Notwithstanding the breach of user as illustrated above, our Company confirms that the landlord has not raised complaint as to such breach against our Group, and there are no subsisting disputes between the landlord and our Group which demands the rectification of the breach nor termination of the said tenancy agreement nor re-entrance of the North Point Property or any part of it. Our Directors confirm that the North Point Property has not breached any statutory safety requirement. Our Directors currently consider that it is difficult for our Group to rectify the non-compliance of the North Point Property, as the proposed property for relocation is subject to acceptance by the customer in accordance with the contract with the customer.

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The tenancy agreement in respect of the North Point Property will expire on 6 December 2015 and our Group intends to relocate our site office at North Point upon the expiry of the tenancy agreement. Based on our Directors' current estimation, it is expected that the relocation cost will amount to approximately HK\$65,000 and the difference in leasing expenses will amount to approximately HK\$18,000 per month.

The Lands Department of the Government acting on behalf of the Government has the right to re-enter the leased property in the event of any default of the terms and conditions of the aforesaid Government Lease. The Building Authority may also by order in writing (the "**Order**") serve on the landlord and our Group as occupier to require them to discontinue the present use of the leased property within one month from the service of such Order should the Building Authority considers that the leased property is unsuitable by reason of its construction for its present use. In addition, the landlord of the North Point Property shall have the right to terminate the relevant tenancy agreement, and to claim against our Group for loss and damages resulting from the breach. As advised by the Hong Kong Legal Advisers, our Group as tenant or the Directors shall be held liable on conviction to a maximum fine of HK\$50,000 (and a further fine of HK\$5,000 for each day of continuous failure to comply with the Order) and imprisonment of one year should we fail to comply with the Order within one month from the service of the same without reasonable excuse.

Our Group confirms that it had not received any such Order as at the Latest Practicable Date and further undertakes that it shall discontinue the use of the North Point Property should it receive any such Order from the Building Authority. In relation to the aforesaid, as our Group may have to seek alternative premises for its site office if our Group is required to vacate the North Point Property, the Indemnifiers have given indemnity in favour of our Group under the Deed of Indemnity pursuant to which, among others, that they will jointly and severally indemnify our Group against all relocation costs, loss of profit and business, penalties and fines and all losses and damages which may be suffered by any members of our Group as a result of or in connection with the past and present breaches of any terms of the tenancy agreements in respect of the Chai Wan Workshops and the North Point Property, the user provisions of the Government Leases and occupation permits of the Chai Wan Workshops and the North Point Property, including but not limited to the past or present usage of these leased properties as site office which were and are inconsistent with their respective permitted use.

In order to ensure on-going compliances with laws and regulations after Listing, our Group will implement the following internal control measures:

- (i) conduct search for permitted use of property before entering into any tenancy agreement;
- (ii) obtain necessary consents/approval from the landlord; and
- (iii) appoint legal adviser to review and advise on the tenancy agreement to be entered into.

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Views of our Directors and the Sponsor

Our Directors consider that the abovementioned non-compliance incidents would not affect the suitability of our executive Directors under Rule 5.01, 5.02 and 11.07 of the GEM Listing Rules or the suitability of listing of our Company under Rule 11.06 of the GEM Listing Rules and that the various internal control measures adopted by us are adequate and effective under Rule 6A.15(5) of the GEM Listing Rules having taken into account the fact that (i) we have taken the abovementioned internal control measures to avoid recurrence of the non-compliance incidents; (ii) no additional material non-compliance incident has taken place since the measures are taken; and (iii) the above non-compliance incidents were unintentional, did not involve any fraudulent act on the part of our executive Directors and did not raise any question as to the integrity of our executive Directors.

The Sponsor, after considering the above and having reviewed the internal control measures, concurs with the view of our Directors that (i) the various internal control measures adopted by us are adequate and effective under Rule 6A.15(5) of the GEM Listing Rules; (ii) our executive Directors have the standard of integrity and competence commensurate with positions as directors of a listed issuer under Rules 5.01 and 5.02 of the GEM Listing Rules; and (iii) the abovementioned non-compliance incidents would not affect the suitability of our Directors under Rules 5.01, 5.02 and 11.07 of the GEM Listing Rules and the suitability of Listing of our Company under Rule 11.06 of the GEM Listing Rules.