

CHINA SECURITY & SURVEILLANCE TECHNOLOGY, INC.

Form 10-K

March 02, 2010

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

Q ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended: December 31, 2009

£ TRANSITION REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission File Number: 001-33774

CHINA SECURITY & SURVEILLANCE TECHNOLOGY, INC.

(Exact Name Of Registrant As Specified In Its Charter)

Delaware

(State or other jurisdiction of incorporation or organization)

98-0509431

(I.R.S. Employer Identification Number)

13/F, Shenzhen Special Zone Press Tower, Shennan Road,

Futian District, Shenzhen,

People's Republic of China, 518034

(86) 755-8351-0888

(Registrant's telephone number, including area code)

Name of Each Exchange on Which Registered:

Securities registered pursuant to Section 12(b) of the

New York Stock Exchange

Act:

Common Stock, \$.0001 par value

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer, or a smaller reporting company. See definition of “accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

Yes No

At June 30, 2009, the last business day of the registrant’s most recently completed second fiscal quarter, there were 50,517,323 shares of the registrant’s common stock outstanding, and the aggregate market value of such shares held by non-affiliates of the registrant (based upon the closing price of such shares as reported on the New York Stock Exchange) was approximately \$392.8 million. Shares of the registrant’s common stock held by the registrant’s executive officers and directors have been excluded because such persons may be deemed to be affiliates of the registrant. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

There were 68,494,270 shares of common stock outstanding as of February 26, 2010.

DOCUMENTS INCORPORATED BY REFERENCE:

Portions of the registrant’s Proxy Statement for its Annual Meeting of Shareholders to be filed with the Commission within 120 days after the close of the registrant’s fiscal year are incorporated by reference into Part III of this Annual Report on Form 10-K.

CHINA SECURITY & SURVEILLANCE TECHNOLOGY, INC.
FORM 10-K
FOR THE YEAR ENDED DECEMBER 31, 2009
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INTRODUCTORY NOTE

Except as otherwise indicated by the context, references to CSR, we, us, our, our Company, or the Company are to China Security & Surveillance Technology, Inc., a Delaware corporation, and its consolidated subsidiaries. Unless the context otherwise requires, all references to:

- Allied Rich are to Allied Rich Limited, a Hong Kong corporation and an indirect, wholly owned subsidiary of the Company;
- Chain Star are to Chain Star Investments Limited, a Hong Kong corporation and an indirect, wholly owned subsidiary of the Company;
- Cheng Feng are to Shanghai Cheng Feng Digital Technology Co. Ltd., a corporation incorporated in the People's Republic of China and an indirect, wholly owned subsidiary of the Company;
- Chuang Guan are to Shenzhen Chuang Guan Intelligence Network Technology Co., Ltd., a corporation incorporated in the People's Republic of China;
- Coson are to Shenzhen Coson Electronic Co. Ltd., a corporation incorporated in the People's Republic of China and an indirect, wholly owned subsidiary of the Company;
- CSSD are to China Security & Surveillance Distribution (PRC) Inc., a corporation incorporated in the People's Republic of China and a direct, wholly owned subsidiary of the Company;
- CSSM are to China Security & Surveillance Manufacturing (PRC) Inc., a corporation incorporated in the People's Republic of China and a direct, wholly owned subsidiary of the Company;
- CSSS are to China Security & Surveillance Services (PRC) Inc., a corporation incorporated in the People's Republic of China and a direct, wholly owned subsidiary of the Company;
- CSST HK are to China Security & Surveillance Technology (HK) Ltd., a Hong Kong corporation and an indirect, wholly owned subsidiary of the Company;
- CSST PRC are to China Security & Surveillance Technology (PRC) Inc., a corporation incorporated in the People's Republic of China and a direct, wholly owned subsidiary of the Company;
- DIT are to DIT Industry(H.K.) Limited, a Hong Kong corporation and an indirect, wholly owned subsidiary of the Company;
- DM are to Beijing DM Security & Technology Co., Ltd., a corporation incorporated in the People's Republic of China;
- Golden are to Golden Group Corporation (Shenzhen) Limited, a corporation incorporated in the People's Republic of China and an indirect, wholly owned subsidiary of the Company;
- Guanling are to Beijing Aurine Divine Land Technology Co., Ltd., a corporation incorporated in the People's Republic of China and an indirect, wholly owned subsidiary of the Company;
- HiEasy are to HiEasy Electronic Technology Development Co., Ltd., a corporation incorporated in the People's Republic of China and an indirect, wholly owned subsidiary of the Company;
- Hongtianzhi are to Shenzhen Hongtianzhi Electronics Co., Ltd., a corporation incorporated in the People's Republic of China and an indirect, wholly owned subsidiary of the Company;
- Huge Long are to Huge Long Limited, a Hong Kong corporation and an indirect, wholly owned subsidiary of the Company;
- Jin Lin are to Shenzhen Jin Lin Technology Co., Ltd., a corporation incorporated in the People's Republic of China and an indirect, wholly owned subsidiary of the Company;
- Kit Grant are to Kit Grant Limited, a Hong Kong corporation and an indirect, wholly owned subsidiary of the Company;
- Link Billion are to Link Billion Investment Limited, a Hong Kong corporation and an indirect, wholly owned subsidiary of the Company;

- Long Top are to Long Top Limited, a Hong Kong corporation and an indirect, wholly owned subsidiary of the Company;
- Longhorn are to Shenzhen Longhorn Security Technology Co., Ltd., a corporation incorporated in the People's Republic of China and an indirect, wholly owned subsidiary of the Company;
- Minking are to Changzhou Minking Electronics Co., Ltd., a corporation incorporated in the People's Republic of China and an indirect, wholly owned subsidiary of the Company;
- Multiwin are to Multiwin International Holdings Limited, a Hong Kong corporation and an indirect, wholly owned subsidiary of the Company;
- Ocean Pacific are to Ocean Pacific Technology Limited, a Hong Kong corporation and an indirect, wholly owned subsidiary of the Company;
- Safetech are to China Safetech Holdings Limited, a British Virgin Islands corporation and a direct, wholly owned subsidiary of the Company;
- Sharp Eagle are to Sharp Eagle (HK) Limited, a Hong Kong corporation and an indirect, wholly owned subsidiary of the Company;
- Sincere On are to Sincere On Limited, a Hong Kong corporation and an indirect, wholly owned subsidiary of the Company;
- Stonesonic are to Guangdong Stonesonic Digital Technique Co., Ltd., a corporation incorporated in the People's Republic of China and an indirect, wholly owned subsidiary of the Company;
- Tsingvision are to Hangzhou Tsingvision Intelligence System Co., Ltd., a corporation incorporated in the People's Republic of China and an indirect, wholly owned subsidiary of the Company;
- WDH are to Shenzhen Wandaiheng Industry Limited, a corporation incorporated in the People's Republic of China and an indirect, wholly owned subsidiary of the Company;
- BVI are to the British Virgin Islands;
- PRC and China are to the People's Republic of China;
- RMB are to Yuan Renminbi of China;
- U.S. dollar, \$ and US\$ are to United States dollars;
- Exchange Act are to the Securities Exchange Act of 1934, as amended; and
- Securities Act are to the Securities Act of 1933, as amended.

Special Note Regarding Forward Looking Statements

In addition to historical information, this report contains forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act. We use words such as believe, expect, anticipate, project, target, plan, optimistic, intend, aim, will or similar expressions which are intended to identify forward-looking statements. Such statements include, among others, those concerning market and industry segment growth and demand and acceptance of new and existing products; any projections of sales, earnings, revenue, margins or other financial items; any statements of the plans, strategies and objectives of management for future operations; any statements regarding future economic conditions or performance; uncertainties related to conducting business in China, as well as all assumptions, expectations, predictions, intentions or beliefs about future events. You are cautioned that any such forward-looking statements are not guarantees of future performance and involve risks and uncertainties, as well as assumptions, that, if they were to ever materialize or prove incorrect, could cause the results of the Company to differ materially from those expressed or implied by such forward-looking statements. Such risks and uncertainties, among others, include:

- Our ability to attract new customers;
- Our ability to employ and retain qualified employees;
- Our ability to successfully integrate companies that we have acquired and to avoid or mitigate potential damages arising from risks associated with acquired companies and the legal structures utilized to effectuate acquisitions of these companies;

- Our ability to keep pace with technological developments in the surveillance and safety industry, and to develop and commercialize new products;
- Competition and competitive factors in the markets in which we compete;
- General economic and business conditions in China and in the local economies in which we regularly conduct business, which can affect demand for the Company's products and services;
- Changes in laws, rules and regulations governing the business community in China in general and the surveillance and safety industry in particular; and
- The risks identified in Item 1A. Risk Factors included herein.

All statements other than statements of historical fact are statements that could be deemed forward-looking statements. The Company assumes no obligation and does not intend to update these forward-looking statements, except as required by law.

PART I

ITEM 1. BUSINESS

Overview of Our Business

We are primarily engaged, through our indirect Chinese subsidiaries, in the manufacturing, distributing, installing, and servicing of surveillance and safety products and systems and developing surveillance and safety related software in China. Our customers are primarily comprised of: (1) governmental entities, such as customs agencies, courts, public security bureaus, and prisons; (2) non-profit organizations, including schools, museums, sports arenas, and libraries; and (3) commercial entities, such as airports, hotels, real estate, banks, mines, railways, supermarkets, and entertainment venues.

A majority of our revenues are derived from the provision of surveillance and safety packaged solutions, including manufacturing, installation and after-sale service maintenance of surveillance and safety systems. Because the majority of our revenues are derived from installations, they are generally non-recurring. Our revenues are not concentrated within any one customer or group of related customers. Maintenance services in our packaged solutions are included for the first year following installation. Our customers may separately purchase maintenance services after the first year.

Our sales network covers most of China's populated areas, and we do not rely on any particular region for revenues. Our subsidiaries collectively have more than 140 branch offices and distribution points.

We have experienced strong growth over the past several years. Our revenues increased from \$240.19 million in fiscal year 2007 to \$580.87 million in fiscal year 2009, representing a compounded growth rate of approximately 55.5%. We strive to provide customer-driven, one-stop services to our clients and actively pursue acquisition prospects and other strategic opportunities.

Our Corporate History and Corporate Structure

We were originally incorporated in the BVI on April 8, 2002 under the name Apex Wealth Enterprises Limited. Prior to our reverse acquisition of Safetech in September 2005, our business strategy and ownership changed several times. In September 2005, we acquired all of the capital stock of Safetech in exchange for shares of our capital stock. This share exchange transaction resulted in a change of the ownership control of the Company. As a result of the Safetech acquisition and series of subsequent acquisitions of PRC surveillance and safety companies, our business became the business of our indirect, wholly-owned Chinese subsidiaries. In November 2006, we changed our domicile from the BVI to Delaware by merging into a newly incorporated Delaware corporation, China Security & Surveillance Technology, Inc. We are currently headquartered in Shenzhen, China.

All of our business operations are conducted through our Chinese subsidiaries. The chart below presents our corporate structure as of December 31, 2009:

*by way of Declaration of Trust

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Segment Information

In fiscal year 2009, our operations were comprised of three reportable segments:

- The Installation Segment provides design, sale, installation, service and monitoring of electronics surveillance and safety systems to residential, commercial, industrial and governmental customers;
- The Manufacturing Segment provides design, manufacturing and sales of surveillance and safety products, including intrusion security, access control and video management systems;
- The Distribution Segment provides distribution and sales of surveillance and safety products and services, including intrusion security, access control and video management systems;

In 2009, we added two new segments: a software segment and a service segment. The software segment provides development and sales of surveillance and safety software and systems (the Software Segment) and the service segment provides surveillance and safety services and maintenance (the Service Segment). Both the Software Segment and the Service Segment are currently in the development stage. During 2009, the assets and operating results of the development stage Software and Service Segments were not significant. Therefore, for financial reporting purposes, these are accounted for within the Installation Segment. With these five segments, we are able to provide one-stop service to our customers, including not only products, but also services, installations, maintenance, software, system upgrading, and other related solutions, which we believe many of our competitors cannot match.

For financial information relating to our business segments, see Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations and Note 18 of the Consolidated Financial Statements appearing elsewhere in this annual report. For a discussion of the risks attendant to our foreign operations, please see Item 1A Risk Factors.

Installation Segment

Our Installation Segment performs installations of surveillance and safety products and systems for customer projects. It also provides project design, material supply, engineering, and operating maintenance services. The Installation Segment offers a variety of services over its six divisions, including the Safe City Projects (see discussion of the Safe City Project below), Conventional Projects, Total Solutions, Home Security, Community Security and Research and Development for both government and corporate customers. Our Installation Segment has provided these services in China for about 9 years and has successfully completed an estimated 50 projects in 2009.

In 2004, the Chinese government promulgated the Safe City (or Plan 3111) initiative, which requires about 660 cities throughout China to install and operate street surveillance, and we are a government-recommended Safe City vendor.

Our Installation Segment consists of two operating subsidiaries: Golden and CSST PRC. In 2009, Golden and CSST PRC together accounted for approximately 76.1% of our revenues from the supply and installation of surveillance and safety systems for various projects involving railways, schools, banks, highways, commercial buildings, and public security and government entities, among others.

Our Installation Segment is devoted to constructing Safe City projects as well as many other surveillance and safety projects in China. Our one-stop technical support and service system including project design, material supply, engineering and operating maintenance offers an all-covered solution.

Manufacturing Segment

Our Manufacturing Segment manufactures a variety of products, including detectors, access controllers, high-speed demo video cameras, box cameras, digital video recorders (DVRs), video management systems, monitors, screens, computer software and systems, and accessories. The Manufacturing Segment also designs, sells and develops these

products. It markets its products both individually and as bundled packages of services and features.

Our Manufacturing Segment also focuses on developing technology independently and in collaboration with our other business segments to improve product quality, functionality and efficiency, reduce costs, and develop new products.

In 2009, we derived approximately 15.1% of our revenues from sales of manufactured products, excluding products sold in connection with the installation projects described above. The acquisitions in 2008 and 2009 of Stonesonic, Longhorn, DIT and Coson increased, and are expected to continue to enhance, our manufacturing capacity.

The following eight subsidiaries operate in our Manufacturing Segment:

- *CSSM*. CSSM is responsible for the planning, manufacturing, marketing, research and development of surveillance and safety products produced by our Manufacturing Segment subsidiaries. CSSM also provides general corporate services to all other subsidiaries in the Manufacturing Segment. It was established to integrate the internal resources of our Manufacturing Segment and enhance our ability to provide one-stop shopping services. CSSM also acts as the main customer service contact for our Manufacturing Segment customers.
- *Minking*. Minking specializes in the production, research, and development of closed-circuit television, or CCTV products, such as IP network high-speed dome cameras, pressure high-speed dome cameras, and intelligent high-speed dome cameras.
- *HiEasy*. HiEasy is engaged in audio and video coder-decoder technology research and manufacturing.
- *Hongtianzhi*. Hongtianzhi is a security digital camera manufacturer. Its products include video cameras, digital video cameras, and monitors.
- *Stonesonic*. Stonesonic is a monitoring equipment solutions provider that engages in developing, manufacturing and promoting television broadcast terminals, screens, industrial monitoring, and medical treatment monitoring. It is one of the largest professional monitor manufacturers in China as measured by production output and a provider of CCTV monitors.
- *Longhorn*. Longhorn specializes in the manufacture and installation of safety alarm systems in China and manufactures intruder alarm products, including a full range of motion detectors, control panels, sirens, smoke and gas detectors, and alarm accessories.
- *DIT*. DIT focuses on consumer safety system integration and export and positions itself as a one-stop source surveillance and safety vendor. Its products and services cover consumer security systems and professional surveillance and safety solutions. DIT targets overseas markets. In 2009, all of DIT's products were sold to overseas markets, including United States, Europe and South Asia.
- *Coson*. Coson is an intelligent access control solution provider and provides control access solutions to a diverse group of clients that include government buildings, banks, post offices, universities, and large residential properties in China.

Distribution Segment

Our Distribution Segment is responsible for distribution and marketing of surveillance and safety products and solutions. Our Distribution Segment has established distribution offices nationwide. Our Distribution Segment's sales network covers most of China's populated areas and does not rely on any particular region for our business. The Distribution Segment sells surveillance and safety products, including intrusion security, access control, DVR, CCTV, and video management systems to our clients. Our Distribution Segment acts as the distributor for our own brands as well as other international brands and Chinese brands.

Currently, the following three major subsidiaries operate under the Distribution Segment:

- *CSSD*. CSSD is responsible for the distribution, marketing and sales of surveillance and safety products and solutions produced by our subsidiaries in China. It also provides general corporate services to all other subsidiaries in the Distribution Segment.
- *Cheng Feng*. Cheng Feng distributes all components of our video surveillance systems, including speed domes, DVRs, compression boards, video servers, and other fixed cameras.
- *Guanling*. Guanling is engaged in the business of selling CCTV systems, security alarm systems, common safety systems, public broadcast equipment, biometrics systems, plasma display TVs, and other related security products.

Our Distribution Segment is not only a one-stop shop for our own products but also a sales platform for many other Chinese and international brands in the Chinese surveillance and safety market.

Software Segment

We established a Software Segment in 2009 that develops and sells surveillance and safety software, including surveillance systems software, DVR systems software, NVR (net video recorder) systems software and ITS (intelligent traffic system) software. Our Software Segment develops software independently. The Software Segment markets its software independently and as a part of bundled packages with our other segments' products.

The Software Segment has deployed its software and solutions within government agencies, police departments, the financial industry, the telecommunication industry, the power industry and the transportation industry.

The following two subsidiaries operate in our Software Segment:

- *Tsingvision*. Tsingvision is mainly engaged in the research, development, manufacture, and sales of computer software for surveillance systems such as surveillance systems software and intelligent control platforms for network video software.
- *Jin Lin*. Jin Lin is engaged in the research, development, manufacture, and sales of information technology system software and intelligent traffic systems software.

Currently, our Software Segment is in the developmental stage. We plan to develop this segment into a significant part of our business by continuing to develop new technologies and software products.

Service Segment

We also established a Service Segment in 2009 that provides general services to our clients. Our Service Segment offers a full range of surveillance and safety services, including network alarm response services, safety and surveillance products and solutions post-sale, maintenance services, software upgrading services, project integration services, security guard services, safety and surveillance consulting services, and safety and surveillance trustee services.

Currently, CSSS is our only subsidiary operating in the Service Segment. We plan to develop CSSS into a major surveillance and safety customer services center for the industry.

Our Products

We manufacture the key components of surveillance and safety products, and rely on third-party electronic assembling companies to assemble the final products utilizing our technology. All of our final products are fully branded and developed independently. Our Manufacturing Segment manufactures most of our hardware products and our software is mainly produced by Tsingvision, one of the subsidiaries in our Software Segment. Our main products include standalone DVRs, embedded DVRs, mobile DVRs, digital cameras, intelligent control system software platforms, perimeter security alarm systems, monitors, and auxiliary apparatuses.

- Standalone DVRs

Our standalone DVR stores digital images captured by security cameras. It also controls the recording functions of the cameras and manages the storage of the data. This product has a pre-installed surveillance software system developed by us, which enables it to perform access control and recording functions. It also has: an upgradable hard drive which allows clients to customize the digital storage capacity; network server functions, which allow clients to access the digital images via Internet; MPEG-4 video compression, which allows for more efficient compression of the images and higher image quality; and 4-16 signal input channels, which allows 4 to 16 cameras to be connected to the standalone DVR. This product has the competitive features of small size, low cost and high reliability. The primary markets for this product are small- to medium-size businesses, non-profit organizations and private residences. It is generally used for small-scale surveillance and safety needs.

- Embedded DVRs

Similar to our standalone DVR, our embedded DVR provides recording and compression functions. It has a pre-installed surveillance software system developed by us, upgradable hard drive, network server function, MPEG-4 video compression, 4-36 signal input channels, and uses Microsoft's Windows operating system. As compared to our

standalone DVR, the embedded DVR has higher capacity to accommodate the recording functions for a greater number of cameras. In addition, it is operated via Microsoft's Windows operating system. The primary markets for these products are large projects and community security projects.

- Mobile DVRs

Similar to our standalone DVR, our mobile DVR is smaller in size and has a maximum of 4 ports. The mobile DVR can be installed in a vehicle and enables recording of digital video images within the vehicle's cabin. This product is easily installable, supports Global Positioning System/General Packet Radio Service, has 1 to 4 signal input channels, and has MPEG-4 video compression. The primary markets for this product are the transportation industry and governmental agencies.

- Real-Time Hard-Compression Coding Cards

Our real-time hard-compression coding card includes a Philips PNX 170X high frequency single digital signal processor (DSP) chip and works with 4-channel enhanced Common Intermediate Format images. This product contains an enhanced H.264 algorithm that is four times the complexity of the usual H.264 algorithm, and it is especially suitable for network transmission and recording for long periods. The product supports motion detection, target detecting, on-screen display, area mosaics, and watermark encryptions. It also contains advanced motherboard and display card compatibility technology, allowing it to work with a variety of major and common motherboards and display cards. It is especially suitable for network transmission in finance, manufacturing and transportation industries.

- DVR Compression Boards

Our DVR compression board is a professional digital security product that adopts the most advanced H.264 video compression algorithm and Ogg Vorbis audio compression technology. The product uses a fully optimized algorithm based on DSP technology to implement video and audio real-time coding and active video and audio preview and motion detection. Video images are directly transmitted from the board to the display frame buffer, and compressed stream data is also directly sent to the host computer's memory. The transmission does not use the host computer processor, saving significant computer processor resources. One personal computer can support up to 64 channels for video and audio input, and the parameters of each channel can be set independently and will not affect one another. We provide application software for these cards.

- Digital Cameras

Digital cameras can be easily installed in most locations on a customer's site. The range of cameras that we produce and sell includes high-speed dome cameras, which can view 360 degrees, pan, zoom, and tilt, all at high speed, color Charge Coupled Device (CCD) cameras, indoor color CCD dome cameras, color/black and white CCD flying saucer cameras, infrared CCD multi-function cameras, mini-digital signal processing cameras, indoor standalone sphere CCD cameras, and network high-speed sphere CCD cameras.

- Intelligent High-Speed Dome Cameras

Our intelligent high-speed dome camera is an integrated camera system using high-speed, spherical, 360-degree movement. The high-speed dome camera is developed with a shield and platform. The shield protects the camera while the platform provides greater control over the camera's direction and view. Our brand of intelligent high-speed dome camera has received from Changzhou Products Supervision & Inspection Institute a special certificate of International Electrotechnical Commission IP68 standard for dust tight and water proofing, and it uses pre-error automatic calibration to ensure stability, proper rotational movement and greater rotational working life.

Our intelligent high-speed dome camera is mostly used in mountainous, wet and unstable conditions. In addition, we are the general agent for the intelligent high-speed dome camera products of South Korea CNB and in charge of its sales in China.

- Intelligent Control System Software Platforms

Our intelligent control system software platforms are used for the management of all integration of security equipment and IP-based network security management software. We have the following two platform types: CF-SRP (an intelligent integrated security management system) and CF-SNP (an integrated network security platform management system). We will continue to strengthen our software development platform with a more organic combination with hardware and software to achieve greater success when bidding for Safe City projects.

- Perimeter Security Alarm Systems

Our perimeter security alarm system is a motion sensor which concentrates on protecting all of the accessible entry points and prevents intrusion at home. The alarm system is highly resistant to interference and influence by environmental effects and the surrounding magnetic field.

- Monitors

Our security monitors provide high-definition video, reliability and color reducibility. This product line includes SVM LCD monitors, SVM CRT monitors and other high-quality monitors. Our SVM series is based on the latest 3D digital graphic design technology. The structure of the product adopts the single-oriented design which embodies the light,

thin characteristics of both the LCD and CRT products.

Our other monitor products include LCD multiple screen combination panel walls, LCD advertising players, built-in quadruple LCD/CRT monitors, IP monitor, and progressive scanning color digital monitors.

- RFID Terminals and Data Collectors

Our RFID (Radio Frequency Identification) hand-held terminals and data collectors are based on the latest RFID technology including human, animal and object identification. They can read and write electronic tags matching ISO 18000-6C/EPC C1 Gen2 standard. Their multimedia functions are all based on advanced mobile operating systems.

Our RFID products could be widely used in many different places such as checkpoints, warehouses, hospitals, libraries, museums and super markets, etc., for checking, recording, tracing and other related safety management purposes.

None of these products accounted for more than 10% of our revenues in 2009.

Raw Materials and Our Principal Suppliers

We use manufactured electronic components in our products. The main components of our products include camcorders, monitors, frames, decoders, lenses and outdoor hoods.

Shenzhen is one of the biggest and most concentrated bases for electronic products in China. As a result, there are numerous suppliers and vendors of the components that are needed for our products. Because of the high level of competition among the suppliers, the prices of our principal components are relatively stable, and we are able to purchase these raw materials at reasonable prices. We have entered into written contracts with several major suppliers and vendors.

The main suppliers to our subsidiaries are: Zhongjie Communication Co. Ltd., Guangdong Fenghua Advanced Technology (Holding) Co. Ltd., Shenzhen Tianxu Trade Co. Ltd., Golden Supreme International Co. Ltd., Panasonic Corporation of China, Heshan Yingchuang Trade Co. Ltd., Tamron Optical (Shanghai) Co. Ltd., Shenzhen Apon Technology Co. Ltd., Shenzhen Trade-link Supply Chain Management Co. Ltd., and Sony Corporation of Hong Kong Ltd. None of our suppliers accounted for more than 10% of the total cost of goods sold in 2009.

Our Distribution, Marketing, Customers and Customer Programs

Our customers are primarily: (1) governmental entities, such as customs agencies, courts, public security bureaus, and prisons; (2) non-profit organizations, including schools, museums, sports arenas, and libraries; and (3) commercial entities, such as airports, hotels, real estate, banks, mines, railways, supermarkets, and entertainment venues. Because a large percentage of our revenues are derived from the installation of surveillance and safety systems which are generally non-recurring, we do not rely on one single or a small group of customers. No one single customer accounted for more than 10% of our total revenue in 2009. We generally do not generate significant revenues from any existing client after the installation project is completed unless that client has additional installation sites for which our services might be required.

We have developed a multi-tiered marketing plan, allowing us to effectively market products and services to our clients. We sell most of our products and services through our own distribution network. Our distribution and sales networks cover most of China's populated areas, and we do not rely on any particular region for our business. Our subsidiaries collectively have more than 140 branch offices and distribution points.

In addition to our own branch offices and employees, we cooperate with independent sales agents and have established close relationships with these sales agents in order to take advantage of their regional resources and provide products and services that are tailored to the needs of our customers in those regions.

Through this distribution and marketing network, we believe we can continue to promote our brand recognition, strengthen the management of our distribution network and improve our sales revenue and market share.

We have also been marketing and promoting our products through the following means:

- participating in various industrial shows to display our products;
- advertising in industrial magazines and periodicals to introduce and promote our products;
- publishing our own magazine, which is distributed to our suppliers and sales agents so that they can better understand our Company and strengthen their confidence in us; and
- utilizing the internet to promote our products, such as the public safety network and Chinese Security Association network.

Competition

There are many companies in China engaged in the business of manufacturing surveillance and safety products and designing and installing surveillance and safety systems. The surveillance and safety industry in China is still nascent, and no company has obtained the dominating position. In addition, it is difficult in the surveillance and safety industry for very large companies to reap benefits from their size, because most of surveillance and safety projects require the product to be specially tailored to meet customers' individual requirements.

In the surveillance and safety industry, competition is based on price, product quality, ability to distribute products, and ability to provide after-sales service.

We believe China Network Communication Corporation and China Telecommunications Corporation are the two major competitors with respect to our Installation Segment. Our major competitors in China with respect to our Manufacturing Segment are Samsung (Tianjin) Electronics Co., Ltd., Shenzhen Skyworth Qunxin Security Technology Co., Ltd., SAE Electronic Co., Ltd, and Hangzhou Hikvision Digital Technology Co., Ltd. We believe Zhejiang Dahua Technology Co., Ltd., a China-based surveillance equipment provider, is the major competitor of our Distribution Segment. Huawei Technologies Co., Ltd., Nanwang Information Industry Group Co., Ltd., Harbin Synjones Electronic Co., Ltd., and Shenzhen SED Electronic Equipment Co., Ltd. are the major competitors of our Software Segment.

Additional competition comes from international companies, such as General Electric and Honeywell. Some of our international competitors are larger than we are and possess greater name recognition, assets, personnel, sales, and financial resources. However, these competitors generally have higher prices for their products, and most of them do not have distribution networks in China that are as developed as ours.

We believe that the range of our product and service offerings, our brand recognition by the market, our capital resources, our relatively low labor costs, and our extensive distribution channels enable us to compete favorably in the market for the surveillance and safety products and services that we offer in China.

Intellectual Property

Our success depends, in part, on our ability to maintain and protect our proprietary technology and to conduct our business without infringing on the proprietary rights of others. We rely primarily on a combination of patents, trademarks and trade secrets, as well as employee and third-party confidentiality agreements, to safeguard our intellectual property. As of December 31, 2009, we held 98 patents and had 49 patent applications pending.

As of December 31, 2009, we held 32 trademarks and had 23 trademark applications pending.

We protect our trade secrets through confidentiality provisions of the employment contracts we enter into with our employees. In addition, our engineers are generally divided into different project groups, each of which generally handles only a portion of the project. As a result, no one engineer generally has access to the entire design process and documentation for a particular product.

Employees

We have approximately 3,500 full-time employees. Approximately 370 of them are administrative and accounting staff, approximately 340 of them are research and development staff and approximately 700 of them are engineers and sales staff.

Approximately 900 employees are located in Shenzhen, and the rest of our employees are located in various branches throughout China. Approximately 58% of our employees have bachelor degrees, and most of these majored in

computer science.

As required by applicable Chinese law, we have entered into employment contracts with most of our officers, managers and employees. We believe that we maintain a satisfactory working relationship with our employees, and we have not experienced any significant labor disputes or any difficulty in recruiting staff for our operations. Our employees in China participate in a state pension plan organized by Chinese municipal and provincial governments. We are required to contribute monthly to the plan at the rate of 23% of the average monthly salary. In addition, we are required by Chinese law to cover employees in China with various types of social insurance. We believe that we are in material compliance with the relevant PRC laws.

With the expansion of our business operations and several anticipated acquisitions, we expect that the number of our employees will increase in the next 12 months.

Backlog

As of December 31, 2009, 2008 and 2007, we had a backlog of unfilled orders for our products of \$192.85 million, \$88.54 million and \$60.5 million, respectively.

Research and Development

Currently, we have approximately 340 employees devoted to our research and development efforts, which are aimed at finding new varieties of products, improving existing products, improving overall product quality, and reducing production costs. We set up three research and development centers located in Shenzhen, Wuhan and Hangzhou, respectively. We spent approximately \$2.86 million, \$1.89 million, and \$0.35 million in research and development activities during 2009, 2008, and 2007, respectively.

Government Regulation

Some surveillance and safety products produced in China, such as DVRs, monitors, and alarm systems must satisfy testing required by the China Public Security Bureau, or CPSB, and manufacturers of such products must receive the Security Technology Protection Product Manufacturing Permit from the provincial branch of CPSB. We received a permit relating to these products from Guangdong branch of CPSB in May 2003. In addition, we have a license from the Guangdong province for the design, installation and repair of security protection systems.

Because most of our operating subsidiaries are located in the PRC, we are regulated by the national and local laws of the PRC.

There is no private ownership of land in China, and all land ownership is held by the government of the PRC, its agencies and collectives. Land use rights for commercial use can be obtained from the government for a period of up to 50 years, and are typically renewable. Land use rights can be transferred upon approval by the land administrative authorities of the PRC (State Land Administration Bureau) upon payment of the required land transfer fee. We have received the necessary land use right certificates for the properties described under Item 2 - Properties. See Item 2 - Properties for more details.

In addition, we are also subject to the PRC's foreign currency regulations. The PRC government has control over RMB reserves through, among other things, direct regulation of the conversion of RMB into other foreign currencies. Although foreign currencies which are required for current account transactions can be bought freely at authorized Chinese banks, the proper procedural requirements prescribed by Chinese law must be met. At the same time, Chinese companies are also required to sell their foreign exchange earnings to authorized Chinese banks and the purchase of foreign currencies for capital account transactions still requires prior approval of the Chinese government.

We believe that we are in material compliance with all registrations and requirements for the issuance and maintenance of all licenses required by the governing bodies, and that all license fees and filings are current.

Seasonality

Our operating results and operating cash flows historically have been subject to seasonal variations. Our revenues are usually higher in the second half of the year than in the first half of the year, and the first quarter is usually the slowest quarter because fewer projects are undertaken during and around the Chinese spring festival.

Available Information

Our internet website is www.csst.com. Our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, including exhibits, and amendments to those reports filed or furnished pursuant to Sections

13(a) and 15(d) of the Exchange Act, are available free of charge on our website as soon as reasonably practicable after such reports are electronically filed with, or furnished to, the SEC. Copies of these reports may also be obtained free of charge by sending written requests to our Secretary, China Security & Surveillance Technology, Inc., 13/F, Shenzhen Special Zone Press Tower, Shennan Road, Futian District, Shenzhen, People's Republic of China, 518034. The information posted on our web site is not part of this or any other report we file with or furnish with the SEC. Investors can also read and copy any materials filed by us with the SEC at the SEC's Public Reference Room which is located at 100 F Street, NE, Washington, DC 20549. Information about the operation of the Public Reference Room can be obtained by calling the SEC at 1-800-SEC-0330. Our filings can also be accessed at the SEC's internet website: www.sec.gov.

ITEM 1A. RISK FACTORS

RISKS RELATED TO OUR BUSINESS

Due to the nature of our business, we do not have significant amounts of recurring revenues from our existing customers, and we are highly dependent on new business development.

Most of our revenues are derived from the installation of surveillance and safety systems which are generally non-recurring. Our customers are primarily governmental entities, non-profit organizations and commercial entities, such as airports, customs agencies, hotels, real estate developments, banks, mines, railways, supermarkets, and entertainment enterprises. We manufacture and install security systems for these customers and generate revenues from the sale of these systems to our customers and, to a lesser extent, from maintenance of these systems for our customers. After we have manufactured and installed a system at any particular customer site, we have generated the majority of revenues from that particular client. We do not expect to generate significant revenues from any existing client in future years unless that client has additional installation sites for which our services might be required. Therefore, in order to maintain a level of revenues each year that is at or in excess of the level of revenues we generated in prior years, we must identify and be retained by new clients. If our business development, marketing and sales techniques do not result in an equal or greater number of projects of at least comparable size and value for us in a given year compared to the prior year, then we may be unable to increase our revenues and earnings or even sustain current levels in the future.

A decrease or delay in state or local mandating and funding of surveillance and safety system installation and operation may cause our revenues and profits to decrease.

We depend substantially on national, state and local government laws mandating and funding surveillance and safety system installation and operation in China. We expect that this dependence will continue for the foreseeable future. If China's priorities change, whether due to tightening budgets, shifting policy, or otherwise, initiatives such as the Safe City Project may be abandoned or cut back, and our financial condition and results of operations may suffer material adverse effects.

Our products often are subject to testing, inspection and approval.

We frequently supply products and services pursuant to agreements with general contractors or government agencies. The successful completion of our obligations under these contracts is often subject to satisfactory testing, inspection and approval of such products and services. Although we endeavor to satisfy the requirements of each of these contracts to which we are a party, no assurance can be given that the necessary approval of our products and services will be granted on a timely basis or at all, and that we will receive any payments due to us. In some cases, we may be dependent on others to complete these projects which may also delay payments to us. Any failure to obtain these approvals and payments may have a material adverse effect on our business and future financial performance.

We face risks related to general domestic and global economic conditions and to the current credit crisis.

Our current operating cash flows, which combined with access to the credit markets, provide us with significant discretionary funding capacity. However, the current uncertainty arising out of domestic and global economic conditions, including the recent disruption in credit markets, poses a risk to the economies in which we operate that has impacted demand for our products and services, and may impact our ability to manage normal relationships with our customers, suppliers and creditors. If the current situation deteriorates significantly, our business could be materially negatively impacted, including such areas as reduced demand for our products and services from a slow-down in the general economy, or supplier or customer disruptions resulting from tighter credit markets.

In order to grow at the pace expected by management, we will require additional capital to support our long-term business plan. If we are unable to obtain additional capital in future years, we may be unable to proceed with our long-term business plan, and we may be forced to curtail or cease our operations.

We will require additional working capital to support our long-term business plan, which includes identifying suitable targets for horizontal or vertical mergers or acquisitions, so as to enhance the overall productivity and benefit from economies of scale. Our working capital requirements and the cash flow provided by future operating activities, if any, will vary greatly from quarter to quarter, depending on the volume of business during the period and payment terms with our customers. We may not be able to obtain adequate levels of additional financing, whether through equity financing, debt financing or other sources. Additional financings could result in significant dilution to our earnings per share or the issuance of securities with rights superior to our current outstanding securities. In addition, we may grant registration rights to investors purchasing our equity or debt securities in the future. If we are unable to raise additional financing, we may be unable to implement our long-term business plan, develop or enhance our products and services, take advantage of future opportunities or respond to competitive pressures on a timely basis, if at all. In addition, a lack of additional financing could force us to substantially curtail or cease operations.

Our business could be adversely affected by reduced levels of cash, whether from operations or from borrowings.

Historically, our principal sources of funds have been cash flows from operations and borrowings from banks and other institutions. Our operating and financial performance may generate less cash and could result in our failing to comply with our credit agreement covenants. We were in material compliance with these covenants in fiscal year 2009 and expect to be in compliance with these covenants during fiscal year 2010. However, our ability to remain in compliance in the future will depend on our future financial performance and may be affected by events beyond our control. There can be no assurance that we will generate sufficient earnings and cash flow to remain in compliance with the credit agreement, or that we will be able to obtain future amendments to the credit agreement to avoid a default. In the event of a default, there can be no assurance that we could negotiate a new credit agreement or that we could obtain a new credit agreement with satisfactory terms and conditions within a reasonable time period.

We sometimes extend credit to our customers. Failure to collect the trade receivables or untimely collection of them could affect our liquidity.

We extend credit to some of our customers while generally requiring no collateral. Generally, our customers pay in installments, with a portion of the payment upfront, a portion of the payment upon receipt of our products by our customers and before the installation, and a portion of the payment after the installation of our products and upon satisfaction of our customer. Sometimes, a small portion of the payment will not be paid until after a certain period following the installation. We perform ongoing credit evaluations of our customers' financial condition and generally have no difficulties in collecting our payments. However, if we encounter future problems collecting amounts due from our clients or if we experience delays in the collection of amounts due from our clients, our liquidity could be negatively affected.

If our subcontractors fail to perform their contractual obligations, our ability to provide services and products to our customers, as well as our ability to obtain future business, may be harmed.

Many of our contracts involve subcontracts with other companies upon which we rely to perform a portion of the services that we must provide to our customers. There is a risk that we may have disputes with our subcontractors, including disputes regarding the quality and timeliness of work performed by those subcontractors. A failure by one or more of our subcontractors to satisfactorily perform the agreed-upon services may materially and adversely impact our ability to perform our obligations to our customers, could expose us to liability and could have a material adverse effect on our ability to compete for future contracts and orders.

If we are unable to attract and retain senior management and qualified technical and sales personnel, our operations, financial condition and prospects will be materially adversely affected.

Our future success depends in part on the contributions of our management team and key technical and sales personnel and our ability to attract and retain qualified new personnel. In particular, our success depends on the continuing employment of our CEO, Mr. Guoshen Tu, and our CFO, Mr. Terence Yap. There is significant competition in our industry for qualified managerial, technical and sales personnel, and we cannot assure you that we will be able to retain our key senior managerial, technical and sales personnel or that we will be able to attract, integrate and retain other such personnel that we may require in the future. If we are unable to attract and retain key personnel in the future, our business, operations, financial condition, results of operations and prospects could be materially adversely affected.

Our growth strategy has required us to make acquisitions and to make additional acquisitions in the future, which could subject us to significant risks, any of which could harm our business.

Our growth strategy includes identifying and acquiring or investing in suitable candidates on acceptable terms. In 2009, we acquired a 100% ownership interest in Coson. We have also entered into letters of intent to acquire several

other companies. Over time, we may acquire or make investments in other providers of products that complement our business and other companies in the security industry. The successful integration of these companies and any other acquired businesses require us to:

- integrate and retain key management, sales, research and development, production and other personnel;
- incorporate the acquired products or capabilities into our offerings from an engineering, sales and marketing perspective;
- coordinate research and development efforts;
- integrate and support pre-existing supplier, distribution and customer relationships; and
- consolidate duplicate facilities and functions and combine back office accounting, order processing and support functions.

Acquisitions involve a number of risks and present financial, managerial and operational challenges, including:

- diversion of management's attention from running our existing business;

- increased expenses, including travel, legal, administrative and compensation expenses resulting from newly hired employees;
- increased costs to integrate personnel, customer base and business practices of the acquired company with our own;
- adverse effects on our reported operating results due to possible write-down of goodwill associated with acquisitions;
- potential disputes with sellers of acquired businesses, technologies, services, products and potential liabilities; and
- dilution to our earnings per share if we issue common stock in any acquisition.

Moreover, performance problems with an acquired business, technology, product or service could also have a material adverse impact on our reputation as a whole. Any acquired business, technology, product or service could significantly underperform relative to our expectations, and we may not achieve the benefits we expect from our acquisitions. Geographic distance between business operations, the compatibility of the technologies and operations being integrated and the disparate corporate cultures being combined also presents significant challenges. Acquired businesses are likely to have different standards, controls, contracts, procedures and policies, making it more difficult to implement and harmonize company-wide financial, accounting, billing, information and other systems. If we cannot overcome these challenges, we may not realize actual benefits from past and future acquisitions, which will impair our overall business results.

Our acquisition strategy also depends on our ability to obtain necessary government approvals, as described under - Risks Related to Doing Business in China - We may be unable to complete a business combination transaction efficiently or on favorable terms due to complicated merger and acquisition regulations which became effective on September 8, 2006.

Due to our rapid growth in recent years, our past results may not be indicative of our future performance so evaluating our business and prospects may be difficult.

Our business has grown and evolved rapidly in recent years as demonstrated by our growth in sales revenue from approximately \$240.19 million in 2007, to \$427.35 million in 2008 and to \$580.87 million in 2009. We may not be able to achieve similar growth in future periods, and our historical operating results may not provide a meaningful basis for evaluating our business, financial performance and prospects. Therefore, you should not rely on our past results or our historical rate of growth as an indication of our future performance.

Management's estimates and assumptions affect reported amounts of expenses and changes in those estimates could impact operating results.

Goodwill and other indefinite-lived intangible assets are tested for impairment at least annually, and the results of such testing may adversely affect our financial results. We use a variety of valuation techniques in determining fair value. The impairment review is highly judgmental and involves the use of significant estimates and assumptions. These estimates and assumptions have a significant impact on the amount of any impairment charge recorded, and actual results may differ significantly from the estimates and assumptions used.

We recognize deferred tax assets and liabilities for the expected future tax consequences of events which are included in the financial statements or tax returns. In assessing the realizability of the deferred tax assets, management makes certain assumptions about whether the deferred tax assets will be realized. We expect the deferred tax assets currently recorded to be fully realizable; however, there can be no assurance that an increased valuation allowance would not need to be recorded in the future.

Our facilities, or facilities of our customers or suppliers, could be susceptible to natural disasters.

All of our facilities and many of the facilities of our customers and suppliers are located in China. Natural disasters, such as floods and earthquakes, occur frequently in China, and they pose substantial threats to businesses with operations there. As a developing country, China's emergency-response ability is limited, and its ability to provide emergency reconstruction and other aid to businesses affected by natural disasters is limited. Should a natural disaster severely damage one of our facilities, or damage a major facility of one or more of our significant customers or suppliers, our business could be materially disrupted.

Our insurance coverage may be inadequate to protect us against losses.

Like many other Chinese companies, we do not carry property insurance coverage for our facilities and inventories and do not have any business liability, loss of data or business interruption insurance coverage for our operations in China. If any claims for injury are brought against us, or if we experience any business disruption, litigation or natural disaster, we might incur substantial costs and diversion of resources.

Our quarterly operating results are likely to fluctuate, which may affect our stock price.

Our quarterly revenues, expenses, operating results and gross profit margins vary from quarter to quarter. As a result, our operating results may fall below the expectations of securities analysts and investors in some quarters, which could result in a decrease in the market price of our common stock. The reasons our quarterly results may fluctuate include:

- seasonality inherent in the surveillance and safety industry;
- variations in profit margins attributable to product mix;
- changes in the general competitive and economic conditions;
- delays in, or uneven timing in the delivery of, customer orders;
- the introduction of new products by us or our competitors; and
- delays in surveillance and safety funding and budgetary restraints on national and local government spending.

Period to period comparisons of our results should not be relied on as indications of future performance.

Future government regulations or other standards could have an adverse effect on our operations.

Our operations are subject to a variety of laws, regulations and licensing requirements of national and local authorities in the PRC. In certain jurisdictions, we are required to obtain licenses or permits and to meet certain standards in the conduct of our business. The loss of such licenses, or the imposition of conditions to the granting or retention of such licenses, could have an adverse effect on us. In the event that these laws, regulations and/or licensing requirements change, we may be required to modify our operations or to utilize resources to maintain compliance with such rules and regulations. In addition, new regulations may be enacted that could have an adverse effect on us.

Our limited ability to protect our intellectual property, and the possibility that our technology could inadvertently infringe technology owned by others, may adversely affect our ability to compete.

We rely on a combination of trademarks, copyrights, trade secret laws, confidentiality procedures and licensing arrangements to protect our intellectual property rights. A successful challenge to the ownership of our technology could materially damage our business prospects. Our competitors may assert that our technologies or products infringe on their patents or proprietary rights. We may be required to obtain from others licenses that may not be available on commercially reasonable terms, if at all. Problems with intellectual property rights could increase the cost of our products or delay or preclude our new product development and commercialization. If infringement claims against us are deemed valid, we may not be able to obtain appropriate licenses on acceptable terms or at all. Litigation could be costly and time-consuming but may be necessary to protect our technology license positions or to defend against infringement claims.

We may be exposed to liabilities under the Foreign Corrupt Practices Act and Chinese anti-corruption laws, and any determination that we violated any of these laws could have a material adverse effect on our business.

We are subject to the Foreign Corrupt Practice Act, or FCPA, and other laws that prohibit improper payments or offers of payments to foreign governments and their officials and political parties by U.S. persons and issuers as defined by the statute for the purpose of obtaining or retaining business. We are similarly subject to Chinese anti-corruption laws. We have operations, agreements with third parties and make sales in China, which may experience corruption. Our activities in China create the risk of unauthorized payments or offers of payments by one of the employees, consultants, sales agents or distributors of our Company, even though these parties are not always subject to our control. It is our policy to implement safeguards to discourage these practices by our employees. However, our existing safeguards and any future improvements may prove to be less than effective, and the employees, consultants, sales agents or distributors of our Company may engage in conduct for which we might be held responsible. Violations of the FCPA or Chinese anti-corruption laws may result in severe criminal or civil

sanctions, and we may be subject to other liabilities, which could negatively affect our business, operating results and financial condition. In addition, the U.S. government may seek to hold our Company liable for successor liability FCPA violations committed by companies in which we invest or that we acquire.

Safetech is a BVI company, while our operating subsidiaries are PRC or Hong Kong companies, and most of our officers and directors reside outside the United States. Therefore, certain judgments obtained against our Company by our shareholders may not be enforceable in the BVI or China.

Safetech is a BVI company, and our operating subsidiaries are PRC or Hong Kong companies. Most of our officers and directors reside outside of the United States. All or substantially all of our assets and the assets of these persons are located outside of the United States.

As a result, it may not be possible for investors to effect service of process within the United States upon our Company or such persons or to enforce against it or these persons the United States federal securities laws, or to enforce judgments obtained in United States courts predicated upon the civil liability provisions of the federal securities laws of the United States, including the Securities Act and the Exchange Act.

RISKS RELATED TO OUR RECENT HIGH YIELD NOTES

Covenants in our debt instruments restrict or prohibit our ability to engage in or enter into a variety of transactions.

On August 18, 2009, we entered into a notes purchase agreement with Citadel Equity Fund Ltd. (Citadel) as well as indentures and an investor rights agreement, pursuant to which we restructured our outstanding \$60 million Guaranteed Senior Unsecured Notes Due 2012 and \$50 million Guaranteed Senior Unsecured Notes Due 2012 into two new tranches of notes, consisting of the \$50 million Tranche A Zero Coupon Guaranteed Senior Unsecured Convertible Notes (the Tranche A Notes) and \$84 million Tranche B Zero Coupon Guaranteed Senior Unsecured Notes (the Tranche B Notes). We subsequently repurchased and cancelled the Tranche A Notes with \$47.5 million in November 2009. The Tranche B Notes remain outstanding.

The indenture governing the Tranche B Notes contains various covenants that may limit our discretion in operating our business. In particular, we are limited in our ability to merge, consolidate or transfer substantially all of our assets, issue stock of subsidiaries, incur additional debt and create liens on our assets to secure debt. In addition, if there is default, and we do not maintain certain financial covenants or we do not maintain borrowing availability in excess of certain pre-determined levels, we may be unable to incur additional indebtedness, make restricted payments (including paying cash dividends on our capital stock) or redeem or repurchase our capital stock.

The indenture governing the Tranche B Notes requires us to maintain certain financial ratios and limit our ability to make capital expenditures. These covenants and ratios could have an adverse effect on our business by limiting our ability to take advantage of financing, merger and acquisition or other corporate opportunities and to fund our operations. Any future debt could also contain financial and other covenants more restrictive than those imposed under the indenture governing the Tranche B Notes.

The Tranche B Notes and their corresponding debt could have significant consequences to investors. For example, they could:

- limit our ability to obtain additional financing for working capital, capital expenditures, and other general corporate requirements;
- increase our vulnerability to general adverse economic and industry conditions;
- require us to sell assets to reduce indebtedness or influence our decisions about whether to do so;
- restrict us from making strategic acquisitions or pursuing business opportunities;
- limit our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate;
- limit, along with the financial and other restrictive covenants in our indebtedness, among other things, our ability to borrow additional funds; and
- place us at a competitive disadvantage compared to competitors that may have proportionately less debt.

In addition, our ability to make scheduled payments or refinance our obligations depends on our successful financial and operating performance, cash flows, and capital resources, which in turn depend upon prevailing economic conditions and certain financial, business, and other factors, many of which are beyond our control. If our cash flows and capital resources are insufficient to fund our debt obligations, we may be forced to reduce or delay capital expenditures, sell material assets or operations, obtain additional capital, restructure our debt, or declare bankruptcy. In the event that we are required to dispose of material assets or operations to meet our debt service and other

obligations, the value realized on such assets or operations will depend on market conditions and the availability of buyers. Accordingly, we may be forced to sell at an unfavorable price.

RISKS RELATED TO OUR INDUSTRY

Seasonality affects our operating results.

Our sales are affected by seasonality. Our revenues are usually higher in the second half of the year than in the first half of the year because fewer projects are undertaken during and around the Chinese spring festival.

Our success relies on our management's ability to understand the highly evolving surveillance and safety industry.

The Chinese surveillance and safety industry is nascent and rapidly evolving. Therefore, it is critical that our management is able to understand industry trends and make good strategic business decisions. If our management is unable to identify industry trends and act in response to such trends in a way that is beneficial to us, our business will suffer.

If we are unable to respond to the rapid changes in our industry and changes in our customer's requirements and preferences, our business, financial condition and results of operations could be adversely affected.

If we are unable, for technological, legal, financial or other reasons, to adapt in a timely manner to changing market conditions or customer requirements, we could lose customers and market share. The surveillance and safety industry is characterized by rapid technological change. Sudden changes in customer requirements and preferences, the frequent introduction of new products and services embodying new technologies and the emergence of new industry standards and practices could render our existing products, services and systems obsolete. The emerging nature of products and services in the surveillance and safety industry and their rapid evolution will require that we continually improve the performance, features and reliability of our products and services. Our success will depend, in part, on our ability to:

- enhance our existing products and services;
- anticipate changing customer requirements by designing, developing, and launching new products and services that address the increasingly sophisticated and varied needs of our current and prospective customers; and
- respond to technological advances and emerging industry standards and practices on a cost-effective and timely basis.

The development of additional products and services involves significant technological and business risks and requires substantial expenditures and lead time. If we fail to introduce products with new technologies in a timely manner, or adapt our products to these new technologies, our business, financial condition and results of operations could be adversely affected. We cannot assure you that even if we are able to introduce new products or adapt our products to new technologies that our products will gain acceptance among our customers. In addition, from time to time, we or our competitors may announce new products, product enhancements or technological innovations that have the potential to replace or shorten the life cycles of our existing products, and that may cause customers to refrain from purchasing our existing products, resulting in inventory obsolescence.

We may not be able to maintain or improve our competitive position among strong competition in the surveillance and safety industry, and we expect this competition to continue to intensify.

The Chinese surveillance and safety industry is highly competitive. In addition, since China joined the World Trade Organization, we also face competition from international competitors. Some of our international competitors are larger than us and possess greater name recognition, assets, personnel, sales and financial resources. These entities may be able to respond more quickly to changing market conditions by developing new products and services that meet customer requirements or are otherwise superior to our products and services and may be able to more effectively market their products than we can because they have significantly greater financial, technical and marketing resources than we do. They may also be able to devote greater resources than we can to the development, promotion and sale of their products. Increased competition could require us to reduce our prices, result in our receiving fewer customer orders, and result in a loss of our market share. We cannot assure you that we will be able to distinguish ourselves in a competitive market. To the extent that we are unable to successfully compete against existing and future competitors, our business, operating results and financial condition could be materially adversely affected.

Our business and reputation as a manufacturer of high quality surveillance and safety products may be adversely affected by product defects or performance.

We believe that we offer high quality products that are reliable and competitively priced. If our products do not perform to specifications, we might be required to redesign or recall those products or pay substantial damages. Such an event could result in significant expenses, disrupt sales and affect our reputation and that of our products. In addition, product defects could result in substantial product liability. We do not have product liability insurance. If we face significant liability claims, our business, financial condition, and results of operations would be adversely affected.

Our product offerings involve a lengthy sales cycle and we may not anticipate sales levels appropriately, which could impair our profitability.

Some of our products and services are designed for medium to large commercial, industrial and government facilities desiring to protect valuable assets and/or prevent intrusion into high security facilities in China. Given the nature of our products and the customers that purchase them, sales cycles can be lengthy as customers conduct intensive investigations and deliberate between competing technologies and providers. For these and other reasons, the sales cycle associated with some of our products and services is typically lengthy and subject to a number of significant risks over which we have little or no control. If sales in any period fall significantly below anticipated levels, our financial condition and results of operations could suffer.

We could face liability for our failure to respond adequately to alarm activations.

The nature of the services we provide potentially exposes us to greater risks of liability for employee acts or omissions or system failures that may be inherent in other businesses. In the event of litigation with respect to such matters, our financial condition and results of operations could be materially and adversely affected. In addition, the costs of such litigation could have an adverse effect on us.

RISKS RELATED TO DOING BUSINESS IN CHINA

Adverse changes in political and economic policies of the PRC government could impede the overall economic growth of China, which could reduce the demand for our products and damage our business.

We conduct substantially all of our operations and generate most of our revenue in China. Accordingly, our business, financial condition, results of operations and prospects are affected significantly by economic, political and legal developments in China. The PRC economy differs from the economies of most developed countries in many respects, including:

- the higher level of government involvement;
- the early stage of development of the market-oriented sector of the economy;
- the rapid growth rate;
- the higher level of control over foreign exchange; and
- the allocation of resources.

As the PRC economy has been transitioning from a planned economy to a more market-oriented economy, the PRC government has implemented various measures to encourage economic growth and guide the allocation of resources. While these measures may benefit the overall PRC economy, they may also have a negative effect on us.

Although the PRC government has in recent years implemented measures emphasizing the utilization of market forces for economic reform, the PRC government continues to exercise significant control over economic growth in China through the allocation of resources, controlling payment of foreign currency-denominated obligations, setting monetary policy and imposing policies that impact particular industries or companies in different ways.

Any adverse change in the economic conditions or government policies in China could have a material adverse effect on the overall economic growth and the level of surveillance and safety investments and expenditures in China, which in turn could lead to a reduction in demand for our products and consequently have a material adverse effect on our business and prospects.

Uncertainties with respect to the PRC legal system could limit the legal protections available to you and us.

We conduct substantially all of our business through our operating subsidiaries in China. Our operating subsidiaries are generally subject to laws and regulations applicable to foreign investments in China and, in particular, laws applicable to foreign-invested enterprises. The PRC legal system is based on written statutes, and prior court decisions may be cited for reference, but have limited precedential value. Since 1979, a series of new PRC laws and regulations have significantly enhanced the protections afforded to various forms of foreign investments in China. However, since the PRC legal system continues to rapidly evolve, the interpretations of many laws, regulations and rules are not always uniform and enforcement of these laws, regulations and rules involve uncertainties, which may limit legal protections available to you and us. In addition, any litigation in China may be protracted and result in substantial costs and diversion of resources and management attention. In addition, all of our executive officers and all but one of our directors are residents of China and not of the United States, and substantially all the assets of these persons are located outside the United States. As a result, it could be difficult for investors to effect service of process in the United States or to enforce a judgment obtained in the United States against our Chinese officers, directors and

subsidiaries.

The PRC government exerts substantial influence over the manner in which we conduct our business activities.

The PRC government has exercised and continues to exercise substantial control over virtually every sector of the Chinese economy through regulation and state ownership. Our ability to operate in China may be harmed by changes in its laws and regulations, including those relating to taxation, import and export tariffs, environmental regulations, land use rights, property and other matters. We believe that our operations in China are in material compliance with all applicable legal and regulatory requirements. However, the central or local governments of the jurisdictions in which we operate may impose new, stricter regulations or interpretations of existing regulations that would require additional expenditures and efforts on our part to ensure our compliance with such regulations or interpretations.

Accordingly, government actions in the future, including any decision not to continue to support recent economic reforms and to return to a more centrally planned economy or regional or local variations in the implementation of economic policies, could have a significant effect on economic conditions in China or particular regions thereof and could require us to divest ourselves of any interest we then hold in Chinese properties or joint ventures.

Restrictions on currency exchange may limit our ability to receive and use our sales revenue effectively.

Most of our sales revenue and expenses are denominated in Renminbi. Under PRC law, the Renminbi is currently convertible under the current account, which includes dividends and trade and service-related foreign exchange transactions, but not under the capital account, which includes foreign direct investment and loans. Currently, our PRC operating subsidiaries may purchase foreign currencies for settlement of current account transactions, including payments of dividends to us, without the approval of the State Administration of Foreign Exchange (the SAFE), by complying with certain procedural requirements. However, the relevant PRC government authorities may limit or eliminate our ability to purchase foreign currencies in the future. Since a significant amount of our future revenue will be denominated in Renminbi, any existing and future restrictions on currency exchange may limit our ability to utilize revenue generated in Renminbi to fund our business activities outside China that are denominated in foreign currencies.

Foreign exchange transactions by PRC operating subsidiaries under the capital account continue to be subject to significant foreign exchange controls and require the approval of or need to register with PRC government authorities, including SAFE. In particular, if our PRC operating subsidiaries borrow foreign currency through loans from us or other foreign lenders, these loans must be registered with SAFE, and if we finance the subsidiaries by means of additional capital contributions, these capital contributions must be approved by certain government authorities, including the Ministry of Commerce, or their respective local counterparts. These limitations could affect our PRC operating subsidiaries' ability to obtain foreign exchange through debt or equity financing.

Failure to comply with PRC regulations relating to the establishment of offshore special purpose companies by PRC residents may subject our PRC resident stockholders to personal liability, limit our ability to acquire PRC companies or to inject capital into our PRC subsidiaries, limit our PRC subsidiaries' ability to distribute profits to us or otherwise materially adversely affect us.

In October 2005, SAFE issued the Notice on Relevant Issues in the Foreign Exchange Control over Financing and Return Investment Through Special Purpose Companies by Residents Inside China, generally referred to as Circular 75, which required PRC residents to register with the competent local SAFE branch before establishing or acquiring control over an offshore special purpose company, or SPV, for the purpose of engaging in an equity financing outside of China on the strength of domestic PRC assets originally held by those residents. Internal implementing guidelines issued by SAFE, which became public in June 2007 (known as Notice 106), expanded the reach of Circular 75 by (1) purporting to cover the establishment or acquisition of control by PRC residents of offshore entities which merely acquire control over domestic companies or assets, even in the absence of legal ownership; (2) adding requirements relating to the source of the PRC resident's funds used to establish or acquire the offshore entity; (3) covering the use of existing offshore entities for offshore financings; (4) purporting to cover situations in which an offshore SPV establishes a new subsidiary in China or acquires an unrelated company or unrelated assets in China; and (5) making the domestic affiliate of the SPV responsible for the accuracy of certain documents which must be filed in connection with any such registration, notably, the business plan which describes the overseas financing and the use of proceeds. Amendments to registrations made under Circular 75 are required in connection with any increase or decrease of capital, transfer of shares, mergers and acquisitions, equity investment or creation of any security interest in any assets located in China to guarantee offshore obligations, and Notice 106 makes the offshore SPV jointly responsible for these filings. In the case of an SPV which was established, and which acquired a related domestic company or assets, before the implementation date of Circular 75, a retroactive SAFE registration was required to have been completed

before March 31, 2006; this date was subsequently extended indefinitely by Notice 106, which also required that the registrant establish that all foreign exchange transactions undertaken by the SPV and its affiliates were in compliance with applicable laws and regulations. Failure to comply with the requirements of Circular 75, as applied by SAFE in accordance with Notice 106, may result in fines and other penalties under PRC laws for evasion of applicable foreign exchange restrictions. Any such failure could also result in the SPV's affiliates being impeded or prevented from distributing their profits and the proceeds from any reduction in capital, share transfer or liquidation to the SPV, or from engaging in other transfers of funds into or out of China.

We have asked our stockholders who are PRC residents as defined in Circular 75 to register with the relevant branch of SAFE, as currently required, in connection with their equity interests in us and our acquisitions of equity interests in our PRC subsidiaries. However, we cannot provide any assurances that they can obtain the above SAFE registrations required by Circular 75 and Notice 106. Moreover, because of uncertainty over how Circular 75 will be interpreted and implemented, and how or whether SAFE will apply it to us, we cannot predict how it will affect our business operations or future strategies. For example, our present and prospective PRC subsidiaries' ability to conduct foreign exchange activities, such as the remittance of dividends and foreign currency-denominated borrowings, may be subject to compliance with Circular 75 and Notice 106 by our PRC resident beneficial holders.

In addition, such PRC residents may not always be able to complete the necessary registration procedures required by Circular 75 and Notice 106. We also have little control over either our present or prospective direct or indirect stockholders or the outcome of such registration procedures. A failure by our PRC resident beneficial holders or future PRC resident stockholders to comply with Circular 75 and Notice 106, if SAFE requires it, could subject these PRC resident beneficial holders to fines or legal sanctions, restrict our overseas or cross-border investment activities, limit our subsidiaries' ability to make distributions or pay dividends or affect our ownership structure, which could adversely affect our business and prospects.

We may be unable to complete a business combination transaction efficiently or on favorable terms due to complicated merger and acquisition regulations which became effective on September 8, 2006.

On August 8, 2006, six PRC regulatory agencies, including the CSRC, promulgated the Regulation on Mergers and Acquisitions of Domestic Companies by Foreign Investors, which became effective on September 8, 2006. This new regulation, among other things, governs the approval process by which a PRC company may participate in an acquisition of assets or equity interests. Depending on the structure of the transaction, the new regulation will require the PRC parties to make a series of applications and supplemental applications to the government agencies. In some instances, the application process may require the presentation of economic data concerning a transaction, including appraisals of the target business and evaluations of the acquirer, which are designed to allow the government to assess the transaction. Government approvals will have expiration dates by which a transaction must be completed and reported to the government agencies. Compliance with the new regulations is likely to be more time consuming and expensive than in the past and the government can now exert more control over the combination of two businesses. Accordingly, due to the new regulation, our ability to engage in business combination transactions has become significantly more complicated, time consuming and expensive, and we may not be able to negotiate a transaction that is acceptable to our stockholders or sufficiently protect their interests in a transaction.

The new regulation allows PRC government agencies to assess the economic terms of a business combination transaction. Parties to a business combination transaction may have to submit to the Ministry of Commerce and other relevant government agencies an appraisal report, an evaluation report and the acquisition agreement, all of which form part of the application for approval, depending on the structure of the transaction. The regulations also prohibit a transaction at an acquisition price obviously lower than the appraised value of the PRC business or assets and in certain transaction structures, require that consideration must be paid within defined periods, generally not in excess of a year. The regulation also limits our ability to negotiate various terms of the acquisition, including aspects of the initial consideration, contingent consideration, holdback provisions, indemnification provisions and provisions relating to the assumption and allocation of assets and liabilities. Transaction structures involving trusts, nominees and similar entities are prohibited. Therefore, such regulation may impede our ability to negotiate and complete a business combination transaction on financial terms that satisfy our investors and protect our stockholders' economic interests.

In addition to the above risks, in many instances, we will seek to structure transactions in a manner that avoids the need to make applications or a series of applications with Chinese regulatory authorities under these new M&A regulations. If we fail to effectively structure an acquisition in a manner that avoids the need for such applications or if the Chinese government interprets the requirements of the new M&A regulations in a manner different from our understanding of such regulations, then acquisitions that we have effected may be unwound or subject to rescission. Also, if the Chinese government determines that our structure of any of our acquisitions does not comply with these new regulations, then we may also be subject to fines and penalties.

Failure to comply with Chinese regulations regarding the registration requirements for employee incentive plans may subject the PRC plan participants or us to fines and other legal or administrative sanctions.

In December 2006, the People's Bank of China promulgated the Administrative Measures for Individual Foreign Exchange, which set forth the respective requirements for foreign exchange transactions by Chinese individuals under either the current account or the capital account. In January 2007, the SAFE issued the Implementation Rules of the Administrative Measures for Individual Foreign Exchange, which, among other things, specified approval requirements for certain capital account transactions such as a Chinese citizen's participation in the employee stock ownership plans or stoc