CHINA SECURITY & SURVEILLANCE TECHNOLOGY, INC.
Form 10-Q
April 25, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended: March 31, 2011

[ ] 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 small business issuer as specified in its charter)

Delaware	**98-0509431**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Empl. Ident. No.)

13/F, Shenzhen Special Zone Press Tower, Shennan Road
Futian District, Shenzhen, China 518034
(Address of principal executive offices, Zip Code)

(86) 755-8351-0888
(Registrant's telephone number, including area code)

____
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 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 [X] 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 whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer [ ]	Accelerated Filer [X]
Non-Accelerated Filer [ ] (Do not check if a smaller reporting company)	Smaller reporting company [ ]

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

Yes [ ] No [X]

The number of shares outstanding of each of the issuer's classes of common equity, as of April 20, 2011 is as follows:

Class of Securities	Shares Outstanding
Common Stock, $0.0001 par value	**89,722,023**

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PART I

FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

CHINA SECURITY & SURVEILLANCE TECHNOLOGY, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
AS OF MARCH 31, 2011 (UNAUDITED) AND DECEMBER 31, 2010
Expressed in thousands of U.S. dollars
(Except for share and per share amounts)

ASSETS

		March 31, 2011		December 31, 2010
Cash and cash equivalents	$	278,739	$	65,626
Restricted cash		20,000		--
Accounts receivable, net		417,966		433,986
Inventories, net		43,026		59,368
Prepayments and deposits		56,809		56,241
Advances to suppliers and subcontractors		103,701		88,360
Other receivables		61,011		47,116
Total current assets		981,252		750,697
Deposits paid for business acquisitions, properties and intangible assets		153,657		146,243
Plant and equipment, net		75,136		75,294
Land use rights, net		7,957		7,896
Intangible assets, net		47,346		48,692
Goodwill		79,516		79,516
Deferred financing costs, net		2,669		2,684
TOTAL ASSETS	$	1,347,533	$	1,111,022

Continued

CHINA SECURITY & SURVEILLANCE TECHNOLOGY, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS (CONTINUED)
AS OF MARCH 31, 2011 (UNAUDITED) AND DECEMBER 31, 2010
Expressed in thousands of U.S. dollars
(Except for share and per share amounts)

LIABILITIES AND EQUITY

	March 31, 2011	December 31, 2010
CURRENT LIABILITIES		
Notes payable short term	$ 182,657	$ 196,329
Obligations under product financing arrangements short term	6,110	6,687
Guaranteed senior unsecured notes payable short term	21,907	37,408
Accounts and bills payable	40,608	32,240
Accrued expenses	58,472	49,421
Advances from customers	17,738	15,216
Taxes payable	26,230	28,648
Payable for acquisition of businesses, properties and land use rights	3,763	3,763
Deferred income	2,768	3,201
Total current liabilities	360,253	372,913
LONG TERM LIABILITIES		
Notes payable long term	299,903	60,570
Obligations under product financing arrangements long term	5,164	6,474
Guaranteed senior unsecured notes payable long term	3,285	6,580
Net deferred tax liabilities	668	282
Total liabilities	669,273	446,819
EQUITY		
Preferred stock, $0.0001 par value; 10,000,000 shares authorized, no shares issued and outstanding		
Common stock, $0.0001 par value; 290,000,000 shares authorized, 89,722,023 (March 31, 2011) and 89,521,115 (December 31, 2010) shares issued and outstanding	9	9
Additional paid-in capital	379,964	374,417
Retained earnings	245,050	243,371
Statutory surplus reserve fund	804	804
Accumulated other comprehensive income	52,450	45,619
Total equity of the Company	678,277	664,220
Noncontrolling interest	(17)	(17)
Total equity	678,260	664,203
TOTAL LIABILITIES AND EQUITY	$ 1,347,533	$ 1,111,022

See accompanying notes to condensed consolidated financial statements.

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CHINA SECURITY & SURVEILLANCE TECHNOLOGY, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
FOR THE THREE MONTHS ENDED MARCH 31, 2011 AND 2010
Expressed in thousands of U.S. dollars
(Except for share and per share amounts)

	Three Months Ended March 31	
	2011 (Unaudited)	2010 (Unaudited)
Revenues	$ 99,054	$ 120,190
Cost of goods sold (including depreciation and amortization for the three months ended March 31, 2011 and 2010 of $259 and $254, respectively)	67,567	91,211
Gross profit	31,487	28,979
Selling and marketing	2,696	2,714
General and administrative (including non-cash employee compensation for the three months ended March 31, 2011 and 2010 of $5,547 and $8,326, respectively)	17,698	16,322
Depreciation and amortization	2,968	2,980
Income from operations	8,125	6,963
Interest income	141	78
Interest expense	(5,114)	(2,295)
Other income, net	596	246
Income before income taxes	3,748	4,992
Income taxes	(2,069)	(1,717)
Net income	1,679	3,275
Add: net loss attributable to the noncontrolling interest	--	2
Net income attributable to the Company	1,679	3,277
Foreign currency translation gain	6,831	124
Comprehensive income attributable to the Company	8,510	3,401
Comprehensive loss attributable to the noncontrolling interest	--	(2)
COMPREHENSIVE INCOME	$ 8,510	$ 3,399
NET INCOME PER SHARE ATTRIBUTABLE TO THE COMPANY S COMMON SHAREHOLDERS		
BASIC	$ 0.02	$ 0.05
DILUTED	$ 0.02	$ 0.05
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING		
BASIC	84,310,000	63,961,000
DILUTED	89,696,000	68,369,000

See the accompanying notes to condensed consolidated financial statements.

CHINA SECURITY & SURVEILLANCE TECHNOLOGY, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE THREE MONTHS ENDED MARCH 31, 2011 (UNAUDITED)
Expressed in thousands of U.S. dollars
(Except for share and per share amounts)

	The Company s Shareholders							
	Common Stock							
	Shares	Par Value	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Statutory Surplus Reserve Fund	Non-Controlling Interest	Total Equity
BALANCE AT JANUARY 1, 2011	89,521,115	$ 9	$ 374,417	$ 243,371	$ 45,619	$ 804	$ (17)	$ 664,20
Issuance of restricted stock under Equity Incentive Plan and recognition of stock-based compensation	200,908	--	5,547	--	--	--	--	5,54
Foreign currency translation gain	--	--	--	--	6,831	--	--	6,83
Net income for the period	--	--	--	1,679	--	--	--	1,67
BALANCE AT MARCH 31, 2011	89,722,023	$ 9	$ 379,964	$ 245,050	$ 52,450	$ 804	$ (17)	$ 678,26

See the accompanying notes to condensed consolidated financial statements.

CHINA SECURITY & SURVEILLANCE TECHNOLOGY, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE THREE MONTHS ENDED MARCH 31, 2011 AND 2010
Expressed in thousands of U.S. dollars
(Except for share and per share amounts)

	Three Months Ended March 31	
	2011 (Unaudited)	2010 (Unaudited)
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 1,679	$ 3,275
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	3,227	3,234
Provision for obsolete inventories	(6)	--
Amortization of deferred financing costs	833	217
Non-cash compensation expense	5,547	8,326
Debt discount amortization	524	950
Deferred taxes	383	(310)
Changes in operating assets and liabilities:		
Decrease (increase) in:		
Accounts receivable	20,408	(48,573)
Inventories	16,947	(3,308)
Prepayments and deposits	1	(46)
Advances to suppliers and subcontractors	(14,447)	(14,634)
Other receivables	(13,409)	(3,626)
Increase (decrease) in:		
Accounts payable and accrued expenses	16,289	(13,846)
Advances from customers	2,369	5,675
Taxes payable	(2,708)	1,629
Deferred income	(465)	159
Net cash provided by (used in) operating activities	37,172	(60,878)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Additions to plant and equipment	(519)	(597)
Additions to intangible assets, other than through business acquisitions	(276)	(533)
Deposits paid for business acquisitions, properties and intangible assets, net	(5,935)	(6,526)
Net cash used in investing activities	(6,730)	(7,656)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Restricted cash	(20,000)	--
Proceeds from borrowings, net of financing costs	300,800	109,137
Repayment of borrowings	(77,992)	(32,229)
Repayment of guaranteed senior unsecured notes payable	(19,320)	(19,320)
Repayment of obligations under product financing arrangements	(1,716)	(1,251)
Net cash provided by financing activities	181,772	56,337
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	212,214	(12,197)
Effect of exchange rate changes on cash and cash equivalents	899	7
Cash and cash equivalents, beginning of period	65,626	154,483
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 278,739	$ 142,293

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CHINA SECURITY & SURVEILLANCE TECHNOLOGY, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)
FOR THE THREE MONTHS ENDED MARCH 31, 2011 AND 2010
Expressed in thousands of U.S. dollars
(Except for share and per share amounts)

	Three Months Ended March 31,			
		2011		2010
SUPPLEMENTARY CASH FLOW INFORMATION:		(Unaudited)		(Unaudited)
Interest paid	$	3,884	$	1,090
Income taxes paid	$	568	$	498

See the accompanying notes to condensed consolidated financial statements.

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CHINA SECURITY & SURVEILLANCE TECHNOLOGY, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
Expressed in thousands of U.S. dollars
(Except for share and per share amounts)

1. BASIS OF PRESENTATION

The accompanying financial statements as of March 31, 2011 and for the three months ended March 31, 2011 and 2010, have been prepared by CHINA SECURITY & SURVEILLANCE TECHNOLOGY, INC. (the Company) without an audit. Pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC), certain information and footnote disclosures normally included in the financial statements prepared in accordance with accounting principles generally accepted in the United States of America (US GAAP) have been condensed or omitted pursuant to such rules and regulations. These financial statements should be read in conjunction with the financial statements and the notes thereto included in the Company s audited annual financial statements for the year ended December 31, 2010, which are included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010, filed with the SEC on February 28, 2011. Amounts as of December 31, 2010 are derived from these audited consolidated financial statements.

In the opinion of management, all adjustments (which include only normal recurring adjustments) necessary to present fairly the financial position as of March 31, 2011, results of operations and cash flows for the three months ended March 31, 2011 and 2010, have been made. The results of operations for the three months ended March 31, 2011, are not necessarily indicative of the operating results for the full year.

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

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Use of Estimates

The preparation of financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Management makes these estimates using the best information available at the time the estimates are made; however actual results could differ materially from those estimates.

(b) Fair Value Measurement

The Company utilizes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described below:

Level 1: Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;

Level 2: Quoted prices in markets that are not active, or inputs that are observable, either directly or indirectly, for substantially the full term of the asset or liability; and

Level 3: Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (supported by little or no market activity).

At March 31, 2011 and December 31, 2010, the Company has no financial assets or liabilities subject to recurring fair value measurements.

The Company s financial instruments include cash and cash equivalents, accounts receivable, other receivables, accounts and bills payable, notes payable, obligations under product financing arrangements, and guaranteed senior unsecured notes payable. Management estimates that the carrying amounts of these non-related party financial instruments approximate their fair values due to their short-term nature and/or based on market interest rates currently available.

CHINA SECURITY & SURVEILLANCE TECHNOLOGY, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
Expressed in thousands of U.S. dollars
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2. SUMMARY OF SELECTED SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(c) Cash and Cash Equivalents, and Restricted Cash

The Company considers highly liquid investments purchased with original maturities of three months or less to be cash equivalents.

Restricted cash as of March 31, 2011 represents time deposits on account to secure short-term notes payable. Also see Note 10.

(d) Accounts Receivable

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of trade accounts receivable. The Company extends credit to its customers in the normal course of business and generally does not require collateral. The Company s credit terms in general are from 30 to 330 days, dependent upon the segment, the nature of the project, and the customer. The Company assesses the probability of collection from each customer at the outset of the arrangement based on a number of factors, including the customer s payment history and its current creditworthiness. If in management s judgment collection is not probable, the Company does not record revenue until the uncertainty is removed.

Management performs ongoing credit evaluations, and the Company maintains an allowance for potential credit losses based upon its loss history and its aging analysis. The allowance for doubtful accounts is the Company s best estimate of the amount of credit losses in existing accounts receivable. Management reviews the allowance for doubtful accounts each reporting period based on a detailed analysis of trade receivables. In the analysis, management primarily considers the age of the customer s receivable, and also considers the creditworthiness of the customer, the economic conditions of the customer s industry, general economic conditions and trends, and the business relationship and history with its customers, among other factors. If any of these factors change, the Company may also change its original estimates, which could impact the level of the Company s future allowance for doubtful accounts. If judgments regarding the collectability of receivables were incorrect, adjustments to the allowance may be required, which would reduce profitability.

Accounts receivable are recognized and carried at the original invoice amount less an allowance for any uncollectible amounts. An estimate for doubtful accounts receivable is made when collection of the full amount is no longer probable. Bad debts are written off as incurred.

As of March 31, 2011, one individual customer had an accounts receivable balance which represented approximately 23.4% of the Company s total accounts receivable. There were no other individual customers with a balance greater than 10% of total accounts receivable at March 31, 2011. As of December 31, 2010, one individual customer had an accounts receivable balance which represented approximately 13.5% of the Company s total accounts receivable. There was no other individual customer that had an accounts receivable balance greater than 10% of the Company s total accounts receivable at December 31, 2010.

From time to time, the Company enters into receivable factoring arrangements. The Company accounts for these arrangements under ASC 860, *Transfers and Servicing.* These arrangements are without recourse, the receivables are isolated from the Company, the transferee has the right to pledge or exchange the receivables, and the Company does not maintain effective control over the receivables. Therefore, these arrangements satisfy the conditions to be accounted for as a sale and the Company recognizes any gain or loss in earnings. The Company did not enter into any receivable factoring agreements during the three months ended March 31, 2011 and 2010.

(e) Inventories

Manufacturing, distribution and service segment inventories consist of raw materials, work in process and finished goods and are stated at the lower of cost, determined on a weighted average basis, or net realizable value. Net realizable value is the estimated selling price in the ordinary course of business less the estimated cost of completion and the estimated costs necessary to make the sale. When inventories are sold, their carrying amount is charged to expense in the period in which the revenue is recognized. Write-downs for declines in net realizable value or for losses of inventories are recognized as an expense in the period the impairment or loss occurs.

Installation segment contract costs are included within installations in process, a component of inventories, and include materials, labor and overhead related to the installations.

As of March 31, 2011 and December 31, 2010, inventories held under product financing arrangements (see Note 11) were $20,008 and $19,808, respectively.

During the three months ended March 31, 2011 and 2010, approximately 34% and 46%, respectively, of total inventory purchases were from five suppliers. Management believes that should the Company lose any one of its major suppliers, other suppliers are available that could provide similar products to the Company on comparable terms.

CHINA SECURITY & SURVEILLANCE TECHNOLOGY, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
Expressed in thousands of U.S. dollars
(Except for share and per share amounts)

2. SUMMARY OF SELECTED SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(f) Accounting for Software To Be Sold, Leased or Marketed

The Company accounts for software development costs in accordance with ASC 985-20 *Costs of Software to Be Sold, Leased or Marketed* . Costs related to establishing the technological feasibility of a software product are expensed as incurred as a part of research and development in general and administrative expenses. Costs that are incurred to produce the finished product after technological feasibility is established are capitalized and amortized over the estimated economic life of five years. The Company performs periodic reviews to ensure that unamortized software development costs remain recoverable from future revenue.

At March 31, 2011 and December 31, 2010, unamortized computer software costs were $5,297 and $5,331, respectively. During the three months ended March 31, 2011 and 2010, $397 and $313, of amortization expenses were charged to income, respectively.

(g) Goodwill

Goodwill represents the excess of the purchase price over the net fair value of the identifiable tangible and intangible assets acquired and the fair value of liabilities assumed in acquisitions. ASC 350-30-50 *Goodwill and Other Intangible Assets* , requires the testing of goodwill and indefinite-lived intangible assets for impairment at least annually. The Company tests goodwill for impairment in the fourth quarter of each year.

Under applicable accounting guidance, the goodwill impairment analysis is a two-step test. The first step of the goodwill impairment test involves comparing the fair value of each reporting unit with its carrying amount including goodwill. If the fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is considered not impaired; however, if the carrying amount of the reporting unit exceeds its fair value, the second step must be performed to measure potential impairment.

The second step involves calculating an implied fair value of goodwill for each reporting unit for which the first step indicated possible impairment. If the implied fair value of goodwill exceeds the goodwill assigned to the reporting unit, there is no impairment. If the goodwill assigned to a reporting unit exceeds the implied fair value of goodwill, an impairment charge is recorded for the excess.

(h) Revenue Recognition

Revenue from sales of surveillance and safety products and systems are recognized in accordance with Staff Accounting Bulletin (SAB) No. 104: *Revenue Recognition* and related interpretations. Revenues are recognized when the following criteria are met:

(i) Persuasive evidence of an arrangement exists The Company requires evidence of an agreement with a customer specifying the terms and conditions of the products to be delivered typically in the form of a signed contract or purchase order;

(ii) Delivery has occurred For product sales, delivery generally takes place when titles to the products are shipped to or accepted by the customer;

(iii) The fee is fixed or determinable   Fees are fixed or determinable based on the contract or purchase order terms; and

(iv) Collection is probable   The Company performs a credit review of all customers with significant transactions to determine whether a customer is creditworthy and collection is probable.

All revenues are recognized net of any taxes collected from customers and subsequently remitted to governmental authorities.

Product sales contracts generally provide a one-to-three-year product warranty to customers from the date of purchase. The Company estimates the costs of satisfying warranty claims based on an analysis of past experience and provides for future claims in the period the revenue is recognized. As of March 31, 2011 and December 31, 2010, no material product warranty reserve was accrued. Warranty costs incurred by the Company have not been material.

CHINA SECURITY & SURVEILLANCE TECHNOLOGY, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
Expressed in thousands of U.S. dollars
(Except for share and per share amounts)

2. SUMMARY OF SELECTED SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(h) Revenue Recognition - continued

The Company derives a significant portion of its revenue from the supply and installation of surveillance and safety equipment in its Installation Segment; the two deliverables do not meet the separation criteria under ASC 605-25 *Multiple-Element Arrangements.* Installation segment contracts vary in terms of contract amount and period of performance. The performance period for short-term contracts is usually between three and six months. The period of performance for long-term contracts is typically between a year and 36 months. Long-term contracts generally are entered into with municipalities, provinces, or their affiliates located in China. These long-term contracts are further defined by agreed-upon detail specifications that outline defined stages. Completion of a defined stage represents basic service and products delivered, such as the installation of specified surveillance and safety systems in defined locations within the project area. Stages are typically planned to be completed over defined three to six-month periods. Each stage represents a discreet, defined phase of the total contract, for which completion can be readily determined. At the completion of a stage, and upon customer inspection, verification and acceptance of the work performed, the Company recognizes the fixed price per stage as revenue. At the time of stage completion, the Company considers the title to work performed passing to the customer. Other than a warranty reserve, discussed below, the Company has no further obligations to the customer for a completed stage.

The use of contract accounting requires significant judgment in estimating total contract pricing and costs, including assumptions relative to the length of time to complete the contract, the nature and complexity of the work to be performed, anticipated increases in wages and prices for subcontractor services and materials, and the availability of subcontractor services and materials. The Company's estimates are based upon the professional knowledge and experience of its engineers, program managers and other personnel, who review each long-term contract continually to assess the contract's schedule, performance, technical matters and estimated cost at completion. The risk to the Company on fixed-price contracts is that if estimates to complete the contract change from one period to the next, profit levels will vary from period to period.

Approximately 1% of contract installation revenue is deferred for repair work during the one-year warranty period. The Company monitors the warranty work requested by its customers, and has determined that minimal warranty work has historically been requested to be performed. Deferred income balances as of March 31, 2011 and December 31, 2010 were $2,768 and $3,201, respectively, and represented amounts invoiced but deferred as revenue as an estimated warranty reserve. Management believes that this 1% warranty reserve is adequate as of March 31, 2011 and December 31, 2010.

Repairs and maintenance service revenue is recognized when the service is performed.

The Company derives a portion of its revenue from one-year software upgrades. These services are typical post-contract service (PCS) arrangements according to ASC 985-605-25 *Revenue Recognition* . Under this guidance, PCS revenue may be recognized together with the initial licensing fee on delivery of the software if all of the following conditions are met:

(i) The PCS fee is included with the initial licensing fee;

(ii) The PCS included with the initial license is for one year or less;

(iii) The estimated cost of providing PCS during the arrangement is insignificant; and

(iv) Unspecified upgrades/enhancements offered during PCS arrangements historically have been and are expected to continue to be minimal and infrequent.

Revenue from surveillance and safety system with one-year software upgrades is recognized when delivery occurs and the risk of ownership passes to the customers, as the Company believes it meets the conditions above related to its PCS arrangements and is therefore in compliance with applicable accounting guidance.

During the three months ended March 31, 2011and 2010, one individual customer accounted for approximately 47% and 21% of the Company s revenue, respectively. There was no other individual customer who accounted for greater than 10% of the Company s revenue in either period.

CHINA SECURITY & SURVEILLANCE TECHNOLOGY, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
Expressed in thousands of U.S. dollars
(Except for share and per share amounts)

2. SUMMARY OF SELECTED SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(i) Research and Development Costs

Research and development costs are expensed as incurred. Research and development costs included in general and administrative expenses for the three months ended March 31, 2011 and 2010 amounted to $649 and $633, respectively.

(j) Advertising Costs

The Company expenses advertising costs as incurred or the first time advertising takes place. During the three months ended March 31, 2011 and 2010, the Company incurred advertising costs of approximately $1,134 and $649, respectively.

(k) Retirement Benefits

Retirement benefits in the form of contributions under defined contribution retirement plans to the relevant authorities are charged to the consolidated statements of income as incurred. Retirement benefit expense for the three months ended March 31, 2011 and 2010 were $447 and $290, respectively, and are included in both selling and marketing expenses and general and administrative expenses.

(l) Income Taxes

The Company accounts for income taxes using the asset and liability method prescribed by ASC 740 *Income Taxes* . Under this method, deferred tax assets and liabilities are determined based on the difference between the financial reporting and tax bases of assets and liabilities using enacted tax rates that will be in effect in the year in which the differences are expected to reverse. The Company records a valuation allowance to offset deferred tax assets if based on the weight of available evidence, it is more-likely-than-not that some portion, or all, of the deferred tax assets will not be realized. The effect on deferred taxes of a change in tax rates is recognized as income or loss in the period that includes the enactment date.

The Company does not have any material unrecognized tax benefits.

The Company files income tax returns with the relevant government authorities in the U.S. and the PRC. The Company is not subject to U.S. federal tax examinations for years before 2007. The Company does not believe there will be any material changes in its unrecognized tax positions over the next 12 months.

The Company s policy is to recognize interest and penalties accrued on any unrecognized tax benefits as a component of income tax expense. The Company does not have any accrued interest or penalties associated with any unrecognized tax benefits, nor was any interest expense recognized during the three months ended March 31, 2011 and 2010. The Company s effective tax rate differs from the federal statutory rate primarily due to non-deductible expenses, preferential tax treatment, subsidiary tax rates different from the effective tax rate, and changes in the deferred tax valuation allowance.

(m) Earnings Per Share

ASC 260 *Earnings Per Share*, requires dual presentation of basic and diluted earnings per share (EPS) with a reconciliation of the numerator and denominator of the basic EPS computation to the numerator and denominator of the diluted EPS computation. Basic EPS excludes dilution. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the entity.

Earning per basic share of common stock is based on the weighted average number of shares of common stock outstanding during each respective period. Earnings per diluted share of common stock adds to basic weighted shares the weighted average number of shares issuable under convertible securities, contingent issuances, and warrants outstanding during each respective period, using the if-converted or treasury-stock methods.

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2. SUMMARY OF SELECTED SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(m) Earnings Per Share continued

Unvested restricted shares issued under the Equity Incentive Plan are not included in basic weighted average number of shares but are considered to be outstanding as of the grant date for purpose of computing diluted EPS even though the shares are subject to vesting requirements.

The calculation of diluted EPS also considers the dilutive effect of outstanding warrants for the three months ended March 31, 2011 and 2010. With respect to outstanding warrants, the dilutive impact on the weighted average number of shares as calculated under the if-converted method was 0 and 11,000 for the three months ended March 31, 2011 and 2010, respectively. Warrants which were outstanding to acquire 157,373 and 3,498,296 shares of common stock were not included in the dilutive calculation for the three months ended March 31, 2011 and 2010, as the effect would be anti-dilutive.

Basic and diluted earnings per share for the three months ended March 31, 2011 and 2010, were calculated as follows:

		2011		2010
Net income attributable to the Company	$	1,679	$	3,277
Weighted average number of common shares:				
Basic		84,310,000		63,961,000
Effect of dilutive securities:				
Warrants		--		11,000
Employee share-based compensation		5,386,000		4,397,000
Diluted		89,696,000		68,369,000
Earnings per share attributable to the Company				
Basic	$	0.02	$	0.05
Diluted	$	0.02	$	0.05

(n) Recently Issued and Adopted Accounting Pronouncements

Business Combinations

(Included in ASC 805 Business Combination, previously SFAS No. 141(R))

In December 2010, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2010-29, *Business Combinations* (Topic 805): *Disclosure of Supplementary Pro Forma Information for Business Combinations.* This ASU specifies that when financial statements are presented, the revenue and earnings of the combined entity should be disclosed as though the business combination that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only. ASU 2010-29 is effective for business combinations with acquisition dates on or after January 1, 2011. The adoption of this update did not have an impact on the Company's consolidated financial statements.

Goodwill

(Included in ASC 350 "Intangibles-Goodwill and Other)

In December 2010, the FASB issued ASU No. 2010-28, *Intangibles-Goodwill and Other* (Topic 350): *When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts.* This ASU requires that reporting units with zero or negative carrying amounts perform Step 2 of the goodwill impairment test if it is more likely than not that a goodwill impairment exists. ASU 2010-28 is effective for the Company beginning with this interim period. The adoption of this update did not have an impact on the Company s financial condition or results of operations.

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2. SUMMARY OF SELECTED SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(n) Recently Issued and Adopted Accounting Pronouncements - continued

Multiple Deliverable Revenue Arrangements

(Accounting Standards Updates 2009-13 and 2009-14)

In October 2009, the FASB issued a new accounting standard which provides guidance for arrangements with multiple deliverables. Specifically, the new standard requires an entity to allocate consideration at the inception of an arrangement to all of its deliverables based on their relative selling prices. In the absence of the vendor-specific objective evidence or third-party evidence of the selling prices, consideration must be allocated to the deliverables based on management s best estimate of the selling prices. In addition, the new standard eliminates the use of the residual method of allocation. In October 2009, the FASB also issued a new accounting standard which changes revenue recognition for tangible products containing software and hardware elements. Specifically, tangible products containing software and hardware that function together to deliver the tangible products essential functionality are scoped out of the existing software revenue recognition guidance and will be accounted for under the multiple-element arrangements revenue recognition guidance discussed above. Both standards were effective for the Company beginning on January 1, 2011. The adoption of this standard did not have a material impact on the Company s consolidated financial statements.

3. ACCOUNTS AND OTHER RECEIVABLES

The Company provides an allowance for doubtful accounts receivable. The receivables and allowance balances at March 31, 2011 and December 31, 2010 are as follows:

		March 31, 2011		December 31, 2010
Accounts receivable	$	420,704	$	436,700
Less: allowance for doubtful accounts		(2,738)		(2,714)
Accounts receivable, net	$	417,966	$	433,986

Other receivables primarily represent unsecured, short-term advances that the Company makes from time-to-time to third-party entities. These advances are due on demand.

4. INVENTORIES

Inventories consist of the following as of March 31, 2011 and December 31, 2010:

		March 31, 2011		December 31, 2010
Raw materials	$	13,330	$	12,449
Work in progress		3,161		2,713
Finished goods		15,158		13,465
Installations in process		13,606		32,953
Total		45,255		61,580

Less: allowance for obsolete inventories		(2,229)		(2,212)
Inventories, net	$	43,026	$	59,368

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5. PREPAYMENTS AND DEPOSITS

Prepayments and deposits consist of the following as of March 31, 2011 and December 31, 2010:

Current assets		March 31, 2011		December 31, 2010
Prepaid expenses	$	3,426	$	3,392
Installation contract deposits		53,383		52,849
	$	56,809	$	56,241
Non-current assets				
Deposits paid for business acquisitions	$	47,770	$	42,888
Deposits paid for acquisition of land use rights, properties and intangible assets		105,887		103,355
	$	153,657	$	146,243

Installation contract deposits are made from time-to-time by the Company to demonstrate capital and resources in connection with bidding on certain projects. Such amounts are refundable upon the grant of the contract.

Non-current deposits are refundable on demand, and there are no binding commitments to acquire these assets.

6. ADVANCES TO SUPPLIERS AND SUBCONTRACTORS

The Company has made advances to third-party suppliers in advance of receiving inventory parts. These advances are generally made to expedite the delivery of required inventory when needed and to help to ensure priority and preferential pricing on such inventory. The amounts advanced to suppliers are fully refundable on demand and totaled $81,509 and $48,977 as of March 31, 2011 and December 31, 2010, respectively. The Company has also made advances to third-party subcontractors for work to be performed on certain projects, as work is performed by sub-contractors, such costs are allocated to installations in process (a component of inventories). Any unused amounts of such advances are refundable to the Company on demand. Advances to subcontractors were $22,192 and $39,383 at March 31, 2011 and December 31, 2010.

7. PLANT AND EQUIPMENT

Plant and equipment consists of the following as of March 31, 2011 and December 31, 2010:

		March 31, 2011		December 31, 2010
Buildings	$	64,942	$	64,029
Leasehold improvements		4,517		4,362
Plant and equipment		8,513		8,687
Electronic equipment		10,029		9,872
Motor vehicles		5,439		5,327
		93,440		92,277
Less: accumulated depreciation		(18,304)		(16,983)
Plant and equipment, net	$	75,136	$	75,294

Depreciation expense for the three months ended March 31, 2011 and 2010, was $1,439 and $1,209, respectively.

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8. LAND USE RIGHTS

Land use rights consist of the following as of March 31, 2011 and December 31, 2010:

		March 31, 2011		December 31, 2010
Cost of land use rights	$	8,877	$	8,791
Less: accumulated amortization		(920)		(895)
Land use rights, net	$	7,957	$	7,896

Amortization expense for the three months ended March 31, 2011 and 2010 was $96 and $42, respectively.

Estimated amortization expense for the next five years and thereafter is as follows:

2011 (remaining nine months)	$	133
2012		177
2013		177
2014		177
2015		177
2016		177
Thereafter		6,939
Total	$	7,957

9. INTANGIBLE ASSETS

Intangible assets consist of the following as of March 31, 2011 and December 31, 2010:

		March 31, 2011		December 31, 2010
Trademarks (life of 11 to 25 years)	$	17,222	$	17,222
Exclusive cooperation agreements (life of 20 years)		13,632		13,632
Customer base (life of 5 to 10 years)		10,448		10,448
Patents (life of 10 years)		4,542		4,542
Technical know-how (life of 9 to 10 years)		17,085		17,072
Non-compete agreements (life of 5 years)		1,303		1,303
Contracts in progress (life of 2 to 9 months)		410		410
Surveillance software (life of 5 years)		11,581		11,219
Surveillance recording system (life of 5 years)		500		500
		76,723		76,348
Less: accumulated amortization		(29,377)		(27,656)
Intangible assets, net	$	47,346	$	48,692

Amortization expense for the three months ended March 31, 2011 and 2010 was $1,692 and $1,983, respectively.

Estimated amortization expense for the next five years and thereafter is as follows:

2011 (remaining nine months)	$	5,237
2012		6,216
2013		5,635
2014		5,295
2015		3,998

2016		3,553
Thereafter		17,412
Total	$	47,346

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10. NOTES PAYABLE

The following is a summary of the Company s short-term and long-term notes payable as of March 31, 2011 and December 31, 2010:

	March 31, 2011	December 31, 2010
Bank loans	$ 482,560	$ 256,899
Less: current portion	(182,657)	(196,329)
Long-term portion	$ 299,903	$ 60,570

As of March 31, 2011, notes payable are due as follows:

	Long-term notes	Short-term notes	Total
2011(remaining nine months)	$ 1,783	$ 138,920	$ 140,703
2012	23,717	41,340	65,057
2013	152,686	--	152,686
2014	102,867	--	102,867
2015	3,060	--	3,060
2016	3,265	--	3,265
Thereafter	14,922	--	14,922
Total	$ 302,300	$ 180,260	$ 482,560

On March 1, 2011, the Company entered into a term loan facility agreement with the China Development Bank Corporation Hong Kong Branch (CDB), pursuant to which CDB agreed to make available to the Company a term loan facility in an aggregate principal amount of up to $200,000, subject to terms and conditions of the agreement. The Company borrowed $200,000 from this facility on March 1, 2011. The loan carries an annual interest rate of 3% per annum over the applicable six-month London Inter Bank Offered Rate (3.46% as of March 31, 2011). Approximately $800 of other costs directly associated with the facility were recorded as deferred financing costs in the balance sheet on March 1, 2011. The Company is amortizing these financing costs over the term of the loan. The loan under the facility will mature on the third anniversary of the first date when the facility is utilized by the Company with 50% of the principal due in August 2013 and the remaining 50% due in February 2014. Pursuant to the term loan facility agreement, if the Company s chairman and chief executive officer, Mr. Guoshen Tu, (the CEO or Mr. Tu) ceases to be the beneficial owner of at least 10% of the Company s outstanding capital stock, the facility may be cancelled and all outstanding amounts under the facility may become immediately due and payable with no less than 30 days notice. As of March 31, 2011, this condition was satisfied, and management believes the Company is in compliance with all terms and conditions of the term loan facility agreement.

In October 2010, the Company entered into a term loan facility agreement with CDB, pursuant to which CDB agreed to make available to the Company a term loan facility in an aggregate principal amount of up to $50,000, subject to terms and conditions of the agreement. The Company borrowed a total of $50,000 on October 29, 2010 under the facility. The loan carries an annual interest rate of 3% per annum over the applicable six-month London Inter Bank Offered Rate (3.46% as of March 31, 2011). Approximately $1,000 of other costs directly associated with the facility were recorded as deferred financing costs in the balance sheet on October 29, 2010. The Company is amortizing these financing costs over the term of the loan. The loan under the facility is due in October 2013. Pursuant to the term loan facility agreement, if Mr. Tu ceases to be the beneficial owner of at least 10% of the Company s outstanding capital stock, the facility may be cancelled and all outstanding amounts due under the facility may become immediately due and payable with no less than 30 days notice. As of March 31, 2011, this condition was satisfied, and management believes the Company is in compliance with all terms and conditions of the term loan facility agreement.

On March 24, 2011, the Company entered into a loan agreement with China Merchants Bank. The Company borrowed RMB31,500 (approximately $4,804) with an annual interest rate equal to the 1 to 6 month s benchmark lending rate of the People s Bank of China (5.60% as of March 31, 2011), with interest payable on the 20th of each month. The loan is due in September 2011. The loan is guaranteed by a subsidiary of the Company.

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10. NOTES PAYABLE (CONTINUED)

On March 21, 2011, the Company entered into a loan agreement with China Construction Bank. The Company borrowed RMB50,000 (approximately $7,626) with an annual interest rate equal to 7.20%, with interest payable on the 20th of each month. The loan is due in March 2012. The loan is guaranteed by the CEO and two subsidiaries of the Company, and is collateralized by the property of a subsidiary.

On March 16, 2011, the Company entered into a loan agreement with Guangdong Development Bank. The Company borrowed RMB121,000 (approximately $18,455) with an annual interest rate equal to 105% of the 1 to 6 month s benchmark lending rate of the People s Bank of China (5.88% as of March 31, 2011), with interest payable on the 20th of each month. The loan is due in March 2012. The loan is collateralized by a restricted cash amount of $20,000 of a subsidiary of the Company.

On February 9, 2011, the Company entered into a loan agreement with Societe Generale. The Company borrowed RMB27,000 (approximately $4,118) with an annual interest rate equal to 9.10%, with interest payable on the due date of the loan. The loan was due and repaid in March 2011. The loan was guaranteed by a subsidiary of the Company.

On February 1, 2011, the Company entered into a loan agreement with China Merchants Bank. The Company borrowed RMB59,000 (approximately $8,999) with an annual interest rate equal to 105% of the 1 to 3 year s benchmark lending rate of the People s Bank of China (6.41% as of March 31, 2011), with interest payable on the 20th of each month. The loan is due in November 2012. The loan is guaranteed by the CEO, his wife and a subsidiary of the Company, and is collateralized by the property and land use rights of a subsidiary.

On January 31, 2011, the Company entered into a loan agreement with the Industrial and Commercial Bank of China. The Company borrowed RMB100,040 (approximately $15,259) with an annual interest rate equal to 95% of the 12 month s benchmark lending rate of the People s Bank of China (5.76% as of March 31, 2011), with interest payable on the 20th of each month. The loan is due in January 2012. The loan is guaranteed by four subsidiaries of the Company.

On January 12, 2011, the Company entered into a loan agreement with China Zheshang Bank. The Company borrowed RMB20,000 (approximately $3,050) with an annual interest rate equal to 120% of the 6 to 12 month s benchmark lending rate of the People s Bank of China (7.27% as of March 31, 2011), with interest payable on the 20th of each month. The loan is due in August 2011. The loan is guaranteed by the CEO and two subsidiaries of the Company.

On January 10, 2011, the Company entered into a loan agreement with China Merchants Bank. The Company borrowed RMB40,000 (approximately $6,101) on January 10, 2011, and RMB169,340 (approximately $25,829) on February 9, 2011 with an annual interest rate equal to 105% of the 5 to 10 year s benchmark lending rate of the People s Bank of China (6.93% as of March 31, 2011), with principal and interest payable in each quarter. In March 2011, the Company repaid principal of the loan in the amount of RMB5,439 (approximately $830) in accordance with the terms of the loan. The loan matures in January 2021. The loan is guaranteed by Shenzhen Zhonghe Industrial Limited, an independent third party, and is secured by the rights of properties currently under construction and which will be acquired by the Company upon their completion.

On January 4, 2011, the Company entered into a loan agreement with China Merchants Bank. The Company borrowed RMB10,000 (approximately $1,525) with an annual interest rate equal to 105% of the 1 to 3 year s benchmark lending rate of the People s Bank of China (6.41% as of March 31, 2011), with interest payable on the 20th of each month. The loan is due in November 2012. The loan is guaranteed by the CEO, his wife and a subsidiary of the Company, and is collateralized by the property and land use rights of a subsidiary.

On December 29, 2010, the Company entered into a loan agreement with Bank of China. The Company borrowed RMB71,100 (approximately $10,844) with an annual interest rate equal to 5.15%, with interest payable on the 20th of each month. The loan is due in December 2011. The loan is guaranteed by the CEO and a subsidiary of the Company, and is collateralized by the property and land use rights of a subsidiary.

On December 24, 2010, the Company entered into a loan agreement with Bank of China. The Company borrowed RMB71,100 (approximately $10,844) with an annual interest rate equal to 5.15%, with interest payable on the 20th of each month. The loan is due in December 2011. The loan is guaranteed by the CEO and a subsidiary of the Company, and collateralized by the property and land use rights of a subsidiary.

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10. NOTES PAYABLE (CONTINUED)

On December 10, 2010, the Company entered into a loan agreement with Shanghai Pudong Development Bank. The Company borrowed RMB66,000 (approximately $10,066) with an annual interest rate equal to the 6 month s benchmark lending rate of the People s Bank of China (5.60% as of March 31, 2011), with interest payable on the 20th of each month. The loan is due in June 2011. The loan is collateralized by a cash deposit of Whitehorse Technology Limited, a company wholly-owned by the CEO of the Company. The Company repaid RMB6,650 (approximately $1,014) and RMB6,600 (approximately $1,007) in January and March 2011, respectively.

On December 2, 2010, the Company entered into a loan agreement with China Merchants Bank. The Company borrowed RMB70,000 (approximately $10,676) with an annual interest rate equal to 105% of the 1 to 3 year s benchmark lending rate of the People's Bank of China (6.14% as of March 31, 2011), with interest payable on the 20th of each month. The loan is due in November 2012. The loan is guaranteed by the CEO, his wife and a subsidiary of the Company, and is collateralized by the property and land use rights of a subsidiary.

On November 19, 2010, the Company entered into a loan agreement with Industrial and Commercial Bank of China. The Company borrowed RMB30,000 (approximately $4,576) on December 21, 2010, RMB30,000 (approximately $4,576) on December 29, 2010 and RMB40,000 (approximately $6,101) on January 31, 2011 with an annual interest equal to 95% of the 12 month's benchmark lending rate of the People s Bank of China (5.76% as of March 31, 2011), with interest payable on the 20th of each month. The loan is due in December 2011. The loan is guaranteed by three subsidiaries of the Company and is collateralized by the property of a subsidiary.

On November 17, 2010, the Company entered into a loan agreement with Bank of China. The Company borrowed RMB48,600 (approximately $7,413) with an annual interest rate equal to 5.15%, with interest payable on the 20th of each month. The loan is due in May 2011. The loan is guaranteed by the CEO of the Company and a subsidiary of the Company, and was collateralized by the property and land use rights of a subsidiary.

On October 29, 2010, the Company entered into a loan agreement with the Industrial and Commercial Bank of China. The Company borrowed RMB51,000 (approximately $7,779) with an annual interest rate equal to 95% of the 12 month's benchmark lending rate of the People s Bank of China (5.76% as of March 31, 2011), with interest payable on the 20th of each month. The loan is due in November 2011. The loan is guaranteed by three subsidiaries of the Company, and is collateralized by the property of a subsidiary.

On October 18, 2010, the Company entered into a loan agreement with China Merchants Bank. The Company borrowed RMB25,000 (approximately $3,813) with an annual interest equal to 110% of the 12 month's benchmark lending rate of the People s Bank of China (6.67% as of March 31, 2011), with interest payable on the 20th of each month. The loan is due in October 2011. The loan is guaranteed by the Chief Operating Officer of the company, the CEO of the Company and his wife.

On August 18, 2010, the Company entered into a loan agreement with Shenzhen Development Bank. The Company borrowed RMB40,000 (approximately $6,101) with an annual interest rate equal to 6.06%, with interest payable on the 20th of each month. The loan is due in August 2011. The loan is guaranteed by the CEO of the Company and two subsidiaries of the Company, and is collateralized by the property of a subsidiary.

On August 9, 2010, the Company entered into a loan agreement with Societe Generale. The Company borrowed RMB27,000 (approximately $4,118) with an annual interest rate equal to 5.35%, with interest payable on the due date of the loan. The loan was due and repaid in February 2011. The loan was guaranteed by a subsidiary of the Company.

On July 26, 2010, the Company entered into a loan agreement with China Everbright Bank Co., Ltd. The Company borrowed RMB40,000 (approximately $6,101) with an annual interest rate equal to 5.31%, with interest payable on the 20th of each month. The loan is due in July 2011. The loan is guaranteed by the CEO of the Company, a subsidiary of the Company and Chuang Guan.

On July 21, 2010, the Company entered into a loan agreement with the Industrial and Commercial Bank of China. The Company borrowed RMB54,600 (approximately $8,328) with an annual interest rate equal to 6.06%, with interest payable on the 20th of each month. The loan is due in July 2011. The loan is guaranteed by three subsidiaries of the Company and is collateralized by the property of a subsidiary.

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10. NOTES PAYABLE (CONTINUED)

On July 15, 2010, the Company entered into a loan agreement with China Construction Bank. The Company borrowed RMB30,000 (approximately $4,576) with an annual interest rate equal to 6.67%, with interest payable on the 20th of each month. The loan is due in July 2011 and is collateralized by the property of a subsidiary.

On July 1, 2010, the Company entered into a loan agreement with Guangdong Development Bank. The Company borrowed RMB49,600 (approximately $7,565) with an annual interest rate equal to 6.67%, with interest payable on the 20th of each month. The loan is due in June 2011. The loan is guaranteed by the CEO and a subsidiary of the Company.

On June 18, 2010, the Company entered into a loan agreement with Industrial and Commercial Bank of China (Asia) Limited. The Company borrowed $8,000 and $2,000 on July 15, 2010 and August 12, 2010, respectively, with an effective interest rate at 3% per annum over the applicable one year London Inter Bank Offered Rate (3.78% at March 31, 2011), with interest payable on the due date of the loan. Interest payable is calculated on the basis of the actual number of days elapsed and a 360-day year. The loan is due in July 2011. The loan is guaranteed by the CEO of the Company and is collateralized by fixed assets of a subsidiary and the shares of a subsidiary.

On April 16, 2010, the Company entered into a loan agreement with Shanghai Pudong Development Bank. The Company borrowed RMB80,000 (approximately $12,202) with an annual interest rate equal to 6.06%, with interest payable on the 20th of each month. The loan was due and repaid in April 2011. The loan was guaranteed by the CEO of the Company and a subsidiary of the Company, and was collateralized by the properties and land use rights of a subsidiary.

On April 15, 2010, the Company entered into a loan agreement with Shanghai Pudong Development Bank. The Company borrowed RMB80,000 (approximately $12,202) with an annual interest rate equal to 6.06%, with interest payable on the 20th of each month. The loan was due and repaid in April 2011. The loan was guaranteed by the CEO of the Company, and was collateralized by the properties and land use rights of a subsidiary.

On March 31, 2010, the Company entered into a loan agreement with China Merchants Bank. The Company borrowed RMB50,000 (approximately $7,626) with an annual interest rate equal to 5.81%, with interest payable on the 20th of each month. The loan was due and repaid in March 2011. The loan was guaranteed by the CEO of the Company, his wife and a subsidiary of the Company, and was collateralized by the property and land use rights of a subsidiary.

On March 25, 2010, the Company entered into a loan agreement with China Citic Bank. The Company borrowed RMB90,000 (approximately $13,727) with an annual interest rate equal to 5.81%, with interest payable on the 20th of each month. The loan was due and repaid in March 2011. The loan was guaranteed by the CEO of the Company, his wife and a subsidiary of the Company, and was collateralized by the properties of two subsidiaries of the Company.

On March 24, 2010, the Company entered into a loan agreement with China Citic Bank. The Company borrowed RMB60,000 (approximately $9,151) with an annual interest rate equal to 5.81%, with interest payable on the 20th of each month. The loan was due and repaid in March 2011. The loan was guaranteed by the CEO of the Company, his wife and a subsidiary of the Company, and was collateralized by the properties of two subsidiaries of the Company.

On March 4, 2010, the Company entered into a loan agreement with the Industrial and Commercial Bank of China. The Company borrowed RMB31,000 (approximately $4,728) with an annual interest rate equal to 5.23%, with interest payable on the 20th of each month. The loan was due in March 2011, but repaid in February 2011. The loan was guaranteed by three subsidiaries of the Company, and was collateralized by the property of a subsidiary.

On March 4, 2010, the Company entered into a loan agreement with the Industrial and Commercial Bank of China. The Company borrowed RMB39,000 (approximately $5,948) with an annual interest rate equal to 5.23%, with interest payable on the 20th of each month. The loan was due in March 2011, but repaid in January 2011. The loan was guaranteed by three subsidiaries of the Company, and was collateralized by the property of a subsidiary.

On March 3, 2010, the Company entered into a loan agreement with China Construction Bank. The Company borrowed RMB50,000 (approximately $7,626) with an annual interest rate equal to 6.10%, with interest payable on the 20th of each month. The loan was due and repaid in March 2011. The loan was guaranteed by the CEO of the Company and a subsidiary of the Company, and was collateralized by the property of a subsidiary.

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10. NOTES PAYABLE (CONTINUED)

On March 2, 2010, the Company entered into a loan agreement with China Merchants Bank. The Company borrowed RMB41,000 (approximately $6,253) with an annual interest rate equal to 5.81%, with interest payable on the 20th of each month. The loan was due and repaid in March 2011. The loan was guaranteed by the CEO of the Company, his wife and a subsidiary of the Company, and was collateralized by the property and land use rights of a subsidiary.

On February 3, 2010, the Company entered into a loan agreement with China Merchants Bank. The Company borrowed RMB59,000 (approximately $8,999) with an annual interest rate equal to 5.81%, with interest payable on the 20th of each month. The loan was due and repaid in February 2011. The loan was guaranteed by the CEO of the Company, his wife and a subsidiary of the Company, and was collateralized by the property and land use rights of a subsidiary.

On January 26, 2010, the Company entered into a loan agreement with the Industrial and Commercial Bank of China. The Company borrowed RMB100,000 (approximately $15,252) with an annual interest rate equal to 4.78%, with interest payable on the 20th of each month. The loan was due in January 2011. The Company repaid RMB80,000 (approximately $12,202) and RMB 20,000 (approximately $3,050) in June 2010 and January 2011, respectively. The loan was guaranteed by the CEO of the Company.

11. OBLIGATIONS UNDER PRODUCT FINANCING ARRANGEMENTS

In June 2010, the Company entered into product financing agreements with a financial institution. Under the terms of the agreements, the Company agreed to pay an annual interest rate of 8.23% on inventory financings. The Company borrowed RMB50,000 (approximately $7,626). The loans expire in June 2013, and payments of principal and interest are due at the end of each quarter.

In September 2009, the Company entered into product financing agreements with a financial institution. Under the terms of the agreements, the Company agreed to pay an annual interest rate of 8.46% on inventory financings. The Company borrowed RMB50,000 (approximately $7,626). The loans expire in September 2012, and payments of principal and interest are due at the end of each quarter.

In February 2009, the Company entered into product financing agreements with a financial institution. Under the terms of the agreements, the Company agreed to pay an annual interest rate of 10.5% on inventory financings. The Company borrowed RMB 7,114 (approximately $1,085). The loans expire in September 2013, and payments of principal and interest are due at the end of each quarter.

In July 2008, the Company entered into product financing agreements with a financial institution. Under the terms of the agreements, the Company agreed to pay an annual interest rate of 10% on inventory financings. The Company borrowed RMB53,492 (approximately $8,158). The loans expire in July 2011, and payments of principal and interest are due at the end of each quarter.

The Company incurred $287 and $271 during the three months ended March 31, 2011 and 2010, of interest expense on the product financing arrangements, respectively.

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11. OBLIGATIONS UNDER PRODUCT FINANCING ARRANGEMENTS (CONTINUED)

The following is a summary of the Company s obligations under product financing arrangements as of March 31, 2011 and December 31, 2010:

		March 31, 2011		December 31, 2010
Obligations under product financing arrangements	$	11,274	$	13,161
Less: current portion		(6,110)		(6,687)
Long-term portion	$	5,164	$	6,474

Estimated repayments for the terms of the arrangements are as follows:

2011 (remaining nine months)	$	5,341
2012		5,300
2013		1,629
Total		12,270
Less: amount representing interest		(996)
Net	$	11,274

Approximately $1,590 and $1,863 of other costs directly associated with the product financing agreements are recorded as deferred financing costs in the balance sheets as of March 31, 2011 and December 31, 2010, respectively. The Company is amortizing these financing costs over the terms of the respective obligations. This amortization is recorded as interest expense.

12. GUARANTEED SENIOR UNSECURED NOTES PAYABLE

As of March 31, 2011, the Company has outstanding Tranche B Zero Coupon Guaranteed Senior Unsecured Notes (the Tranche B Notes). The Tranche B Notes had an original principal amount of $84,000, zero coupon interest and a fair value of $78,440, resulting in a debt discount of $5,560 and an effective interest rate of approximately 5%. The notes mature on September 2, 2012. The Company is to repay the principal amount in six consecutive semi-annual installments, which began on March 2, 2010, with 46%, 46% and 8% of the principal amount to be repaid in the first, second and third year, respectively. The Tranche B Notes are not convertible. The Company is entitled to redeem the Tranche B Notes at any time with no premium or penalty at a redemption price equal to 100% of the principal amount of the Tranche B Notes to be redeemed, plus default interest, if any. The Tranche B Notes are guaranteed by the Company's significant subsidiaries to the extent permitted under the applicable laws. The Company repaid $19,320 of principal on the Tranche B Notes in both March 2011 and March 2010.

The Company has recorded $524 and $950 of debt discount amortization for the three months ended March 31, 2011 and 2010, respectively, related to the Tranche B Notes. This amount is included in interest expense.

Approximately $300 of legal fees and other costs directly associated with the issuance of the Tranche B Notes is recorded as deferred financing costs in the balance sheet at March 31, 2011. The Company is amortizing these financing costs over the term of the Tranche B Notes.

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12. GUARANTEED SENIOR UNSECURED NOTES PAYABLE (CONTINUED)

The following is a summary of the Company s guaranteed senior unsecured notes payable as of March 31, 2011 and December 31, 2010:

		March 31, 2011		December 31, 2010
Total	$	25,192	$	43,988
Less: current portion		(21,907)		(37,408)
Long-term portion	$	3,285	$	6,580

Repayments under the terms of the notes are as follows:

2011 (remaining nine months)	$	19,320
2012		6,720
Total		26,040
Less: amount representing unamortized discount		(848)
Net	$	25,192

13. WARRANTS

A summary of the status of the Company's warrants and the changes during the three months ended March 31, 2011 and 2010, is presented below:

	2011			2010		
	Shares		Weighted Exercise Prices	Shares		Weighted Exercise Prices
Outstanding at January 1	157,373	$	18.05	3,528,302	$	8.72
Granted	--		--	--		--
Exercised	--		--	--		--
Outstanding at March 31	157,373	$	18.05	3,528,302	$	8.72
Warrants exercisable at March 31	157,373	$	18.05	3,528,302	$	8.72

14. EQUITY INCENTIVE PLAN

On February 7, 2007, the Company adopted the 2007 Equity Incentive Plan (the Plan), which was amended in February 2010. The plan, as amended, has a ten-year term and provides for grants of stock options, stock appreciation rights, performance units, restricted stock units and performance shares. The total number of shares which may be issued under the plan is 12,000,000. These restricted stock awards represent share-based payments subject to the provisions of ASC 718 *Stock Compensation* . The fair value of these restricted stock awards are equal to the fair value of the Company's stock on the date of grant. Such restricted stock is subject to the risk of forfeiture upon the occurrence of certain events.

During the three months ended March 31, 2011 and 2010, the Company granted 200,908 and 686,705 shares of restricted stock, respectively. During the three months ended March 31, 2011 and 2010, 0 and 59,165 shares of restricted stock were forfeited and retired, respectively. The shares that have been issued vest over a four to five-year period, and at issuance, resulted in total deferred compensation of $102,423 and $101,554 as of March 31, 2011 and December 31, 2010, respectively. The fair value of these restricted stock awards are equal to the fair value of the

Company's stock on the date of grant, after taking into account certain discounts. Such restricted stock is subject to the risk of forfeiture upon the occurrence of certain events. During the three months ended March 31, 2011 and 2010, the Company recognized $5,547 and $8,326, respectively, of compensation expense under the plan. As of March 31, 2011 and December 31, 2010, there was $36,216 and $40,895, respectively, of unrecognized compensation expense related to the nonvested restricted stock. This cost is expected to be recognized over a four to five-year period. During the three months ended March 31, 2011 and 2010, the Company has not recognized any tax benefits for the compensation expense under the Plan.

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14. EQUITY INCENTIVE PLAN (CONTINUED)

The following table summarizes the status of the Company's nonvested restricted stock awards during the three months ended March 31, 2011 and 2010:

	Nonvested Restricted Stock and Stock Unit Awards 2011		Nonvested Restricted Stock and Stock Unit Awards 2010	
	Number of Shares	Weighted Average Grant Date Fair Values	Number of Shares	Weighted Average Grant Date Fair Values
Outstanding at January 1	6,485,008	$ 6.42	4,713,983	$ 9.47
Granted	200,908	4.32	686,705	7.78
Vested	(694,228)	(7.99)	(857,055)	(9.71)
Forfeited	--	--	(59,165)	(13.79)
Outstanding at March 31	5,991,688	$ 6.16		