# Report of the PRC Auditors

**TO THE SHAREHOLDERS OF NORTHEAST ELECTRICAL TRANSMISSION & TRANSFORMATION MACHINERY MANUFACTURING COMPANY LIMITED**

We have accepted the appointment by the shareholders of the Company to audit the balance sheet of the Company and the consolidated balance sheet of the Company and its subsidiaries (the "Group") as at 31 December 2000, profit and loss account and profit appropriation statement of the Company and the Group and the cash flow of the Company and the Group for the year then ended. These financial statements are the responsibility of the Company. Our responsibility is to express an audit opinion on the financial statements. Our audit was conducted in accordance with China Certified Public Accountants Independent Auditing Standards and consequently included such auditing procedures as were considered necessary and appropriate to the Company's circumstances, including examination, on a test basis, of the Company's transactions and accounting records.

As at 31 December 2000, the net assets of the Group included amounts receivable from the holding company, Northeast Electrical Transmission and Transformation Equipment Group Corporation ("NET") and other related companies of Rmb217,341,565.82. As more fully explained in note V(5) to the financial statements, during the year NET has reached another debt settlement agreement after the asset transfer of Kingdom Hotel. The unsettled outstanding remaining balance stipulated that NET may settle the indebtedness by way of other asset transfers. Up to the date of approval of the financial statements, no repayment was received from NET to settle the outstanding remaining balance and the plan to partially settle the indebtedness by way of other asset transfers is still in progress. In view of NET's failure to meet the terms of the debt settlement agreement in full so far, in our opinion, a provision should have been made. However, it is not practicable to estimate the amount of provision required.

As at 31 December 2000, the net assets of the Group included loans to a third party company of Rmb96,000,000. As more fully explained in note IV(2)to the financial statements, the loans were originally repayable on 15 September 1999. Although both parties had agreed to extend the loan repayment date to 31 December 2000 and certain property and shareholding interests have been pledged as security, no repayment of loans has been made as agreed up to the date of approval of the financial statements. We are also unable to confirm whether the securities can be realised easily and to quantify the realisable amounts. In view of the above, in our opinion, a provision should have been made. However, it is not practicable to estimate the amount of provision required.

For the years ended 31 December 1999 and 2000, the Group incurred significant losses of Rmb166,836,722 and Rmb363,597,324.39 respectively. Principally as a result of the loss, at 31 December 2000, the Company is not in compliance with certain financial covenants in respect of a syndicated bank loan of US$ 40,000,000 (equivalent to Rmb331,124,000). Moreover, pursuant to the original loan agreement a principal amount of US$13,333,333.33 (equivalent to Rmb110,374,666.67) will be due on 4 May 2001. However, up to the date of approval of the financial statements, there is no indication that the Company is able to make the required repayment. As more fully explained in note II(1) to the financial statements, the financial statements have been prepared on a going concern basis. The validity of the going concern basis of preparation depends on the assumptions made by the directors that the Company will be successful in obtaining a waiver from the syndicate and in extending the maturity date of the original loan agreement; an improvement in financial performance of the Group; and the success of the asset transfer arrangement (as explained in note V(5) to the financial statements) with NET. However, in the absence of sufficient documentary evidence, we have been unable to ascertain whether the above assumptions made by the directors can be supported. Therefore we have been unable to satisfy ourselves that the going concern basis is appropriate. Had the going concern basis not been used, adjustments would need to be made to reclassify non-current assets as current assets, to reclassify long term liabilities as current liabilities, to reduce the value of assets to their net realisable amounts and to provide for any further liabilities which might arise.

Because of the significance of the matters referred to in the above paragraphs, we are unable to form an opinion as to whether the financial statements present fairly, in all material aspects, the financial position of the Company and the Group as at 31 December 2000 and the results and cash flow of the Company and the Group for the year then ended in accordance with Accounting Standards for Enterprises and Accounting Regulations for Joint Stock Enterprises of the PRC.

Hualun Certified Public Accountants
PRC
Beijing

Hu Pi Hua
Certified Public Accountant

Li Chen
Certified Public Accountant

Dated : 20 April 2001