LAWS, REGULATIONS AND POLICIES RELATED TO THE TEXTILE INDUSTRY

There are currently no specific laws or regulations governing the production and distribution of textile industry in the PRC. Foreign-invested enterprises engaging in such businesses are subject to the requirements prescribed in various legislations applicable to textile products.

According to the *Catalogue of Industries for Guiding Foreign Investment (Revised 2007)* (外商投資產業指導目錄(2007年修訂)) issued by the *Ministry of Commerce of the PRC* (中華人民共和國商務部) ("MOFCOM") and the *National Development and Reform Commission of the PRC* (中華人民共和國國家發展和改革委員會) ("NDRC") on 31 October 2007, which became effective on 1 December 2007, the production of textile products belongs to the "encouraged category".

On 19 November 2008, the PRC Government declared six measures below to promote the healthy development of light textile industry:

Fiscal Subsidies to Stimulate Domestic Consumption

The PRC Government will introduce fiscal subsidies with the key objective to stimulate domestic consumption and promote production in the PRC for domestic consumption. These include offering fiscal subsidies to peasants for buying domestic appliances, and increasing financial support to the quake-stricken areas and frontier ethnic minority regions.

Setting Aside Special Funds to Support Small and Medium Textile Enterprises

The PRC Government will set aside special funds to support small and medium textile enterprises with the key objective of creating job opportunities, economic and social efficiency and also to attract more investment in the light textile industry.

Reducing Tax Burden and Increasing Export Tax Rebate

The PRC Government plans to reduce the tax burden on small and medium textile enterprises so as to ease cost pressure. It will also continue to increase export tax rebate on textiles, clothing and light industrial products.

The export tax rebate for certain textile products, garments and home furnishing products such as curtains and bed linens has been increased from 11% to 13% commencing from 1 August 2008, then to 14% with effect from 1 November 2008, to 15% with effect from 1 February 2009, to 16% with effect from 1 April 2009 and is now expected to be increased to 17%.

Strong Support for Enterprises to Develop International Markets and Trade Development Fund to Support Merger and Acquisitions, Research and Development and Marketing Activities

To strengthen the light textile industry, the PRC Government has expressed strong support for small and medium enterprises in the light textile industry to develop international markets. Further, a trade development fund will be set up to support merger and acquisition, research and development and marketing activities in the industry.

Encouraging Bank Support

The PRC Government encourages and will guide financial institutions to enhance the financial support for small and medium enterprises in the PRC. This will include measures such as advocating financial institutions to provide more lending and simplify approval process, and developing the export credit insurance business to small and medium textile enterprises.

Funds Set Aside to Promote Technological Transformation

The PRC Government will emphasise on the technological transformation of light textile industry and promote industrial upgrading. Small and medium textile enterprises are encouraged to strengthen their research and development capability and improve market competitiveness. A central budget fund will be set aside for this purpose.

SUMMARY OF RELEVANT LAWS AND REGULATIONS ON IMPORTS OF COTTON AND EXPORTS OF TEXTILE PRODUCTS

Relevant Regulations on Imports of Cotton

According to the *Regulation on the Administration of Import and Export of Goods of the PRC* (中華人民共和國貨物進出口管理條例) promulgated by the *State Council of the PRC* ("State Council") on 10 December 2001, enterprise that import goods which are subject to tariff and quotas should apply for quotas with quotas administration department to obtain certificates for tariff and quotas.

In order to fulfil *the commitments to reduce tariff made by the PRC* (中國入世關稅減讓承諾表) when entering into the *World Trade Organisation* ("WTO") and *Bangkok Agreement* (曼谷協定), on 21 December 2001, the *Customs Tariff Commission of the State Council* ("Customs Tariff Commission") issued the *Notice of the Customs Tariff Commission of the State Council on the Implementation of the Customs Tariff of 2002* (國務院關稅稅則委員會關於2002年關稅實施方案的通知), pursuant to the Notice, starting from 1 January 2002, imported cotton will subject to tariff quotas management, and corresponding in-quota rates and out-of-quota rates were also came into effect. Imported cotton within tariff quotas were subject to applicable 1% tax rate, while the imported cotton that out of the tariff quotas were subject to applicable 54.4% Most Favoured Nation rate and 125% general tax rate.

According to the *Interim Measures for the Administration of Import Tariff Quotas of Agricultural Products* (農產品進口關稅配額管理暫行辦法) ("Interim Measures") promulgated by MOFCOM and NDRC on 27 September 2003, cotton is one of the agricultural products that subject to import tariff quota. Except for foreign products that went to bonded warehouses, bonded areas and export processing zones can be waived to obtain the *Certificates of Import Tariff Quotas for Agricultural Products* (農產品進口關稅配額證), enterprises that import cotton for normal trade, process trade, barter trade, small scale border trade, subsidy, donation, etc. should apply for import tariff quotas for agricultural products with the organisations authorised by NDRC and obtain the Certificates of Import Tariff Quotas for Agricultural Products (effective for one calendar year).

Pursuant to the above interim measures, the organisations authorised by NDRC will allocate the import tariff quotas of agricultural products according to the application amounts and the historical import record, productivity, other related business standard of the applicants or using the first-come-first-serve method.

If end-users holding the import tariff quotas for agricultural products could not fully use up the quotas they applied in that year, they should return the unused quotas to the original issue organisations.

On 26 April 2005, the *Customs Tariff Commission issued Notice on the Problem Using Limited Interim Tariffs to Import Cotton that Exceeds Tariff Quotas 2005* (關於2005年在關稅配額外以有數量限制的暫定關稅方式進口棉花問題的通知). According to the notice, from 1 May 2005 to 31 December 2005, imported cotton which declared as out-of tariff quota will subject to import tariff based on the "limited interim tariff rate" (有數量限制的暫定關稅稅率), the interim tariff rate will be determined using sliding duties method, the tax rate slid range from 5% to 40%.

Relevant Regulations on Exports of Textile Products

According to the *Regulations on the Administration of Import and Export of Goods of the PRC* (中華人民共和國貨物進出口管理條例) promulgated by the State Council on 10 December 2001, export quotas and export licences system had been implemented on goods that subject to export control. While exporting restricted export goods that subject to export quotas and export licences, exporters should apply for quota certificates and export licences.

According to the *Measures on the Administration of Passive Quotas for Textile Products* (紡織品被動配額管理辦法) ("Measures") promulgated by the *Ministry of Foreign Trade and Economic Cooperation of the PRC* on 20 December 2001, export quotas and export licences system were implemented on textile products that export to countries which has imposed restrictions, such as the European Union and the United States. The systems are subject to the supervision of the Customs and under the examination of the entry-exit inspection and quarantine authorities according to relevant requirements. Exporting companies may acquire the export quotas through various means such as tendering, self-applications and allocation by performance. Exporting companies should return any unused export quota to the original issue authority. Quotas acquired through tendering, self- applications and allocation by performance may be transferred in accordance with the above Measures and relevant provisions.

According to the *2004 Announcement No. 82 of MOFCOM* and *General Administration of Customs*, under the relevant provisions stipulated in the *Agreement on Textile Products and Clothing* (紡織品與服裝協定) of the WTO in respect of the integration of textile products quotas and *China's World Trade Organisation Accession Protocol* (中國加入世界貿易組織議定書), countries previously imposing restrictions on textiles export from China, such as the European Union and the United States, had lifted the export quota imposed on China since 1 January 2005.

On 18 September 2006, MOFCOM promulgated the *Measures for the Administration of the Export of Textiles (Provisional)* (紡織品出口管理辦法(暫行)) ("Provisional Measures"). According to the Provisional Measures, interim export control had been implemented on textiles products listed in the *Catalogue of Textile Exports Subject to Provisional Administration* (紡織品出口臨時管理商品目錄) ("Exports Catalogue"). While exporting textile products listed in the Exports Catalogue, foreign trade companies should apply to the local commerce authorities for a *Provisional Export Licence for Textile Products*. As for commodities that subject to the provisional export licence administration, foreign trade companies should apply to the organisations authorised by the *General Administration of Quality Supervision, Inspection and Quarantine* ("General Administration of Quality Supervision") for the certificate of country of origin for the products after acquiring the *Provisional Export Licence for Textile Products* (紡織品臨時出口許可證).

Provisional export quotas on textile products is assigned to foreign trade companies by commerce authorities through various means such as allocation by performance and tendering agreement. Provisional export quotas for textile products are allowed to transfer through the transfer platform of provisional export quotas. Should the provisional export quotas were not fully used up within the valid period of the provisional export quota, foreign trade companies should return the remaining provisional quotas to the commerce authorities.

On 14 December 2006, MOFCOM, *General Administration of Customs and General Administration of Quality Supervision* issued the 2006 Announcement No. 106, announcing a new *Catalogue of Textile Exports to the United States Subject to Provisional Administration* (輸美紡織品出口臨時管理商品目錄) and *Catalogue of Textile Exports to the European Union Subject to Provisional Administration* (輸歐盟紡織品出口臨時管理商品目錄) to replace the above Export Catalogue. The United States and the European Union imposed import restrictions on textiles from China to reduce the impact of an influx of Chinese textiles imports according to the relevant provisions of the special safeguards on importing textiles from China stipulated under the paragraph 242 of the *Report of the Working Party on the Accession of China to the WTO* (中國加入世貿組織工作組報告書). To settle the trade disputes with both the United States and European Union, the PRC Government entered into memoranda of understanding with the United States and European Union respectively in 2005 which prescribed annual quotas and caps on annual increases of quotas on 21 categories and 10 categories of Chinese textiles imports into the United States and European Union.

According to the memoranda of understanding entered into between the European Union and China, management over the export quantity of 10 categories of textile products exported to European Union will be lifted as from 1 January 2008 and export licence management over 8 categories of textile products exported to European Union members shall be carried out as from 1 January 2008, and shall be ended as from 31 December 2008.

On 31 December 2008, the memoranda of understanding entered into between the European Union and China, and the United States and China expired. Since 1 January 2009, MOFCOM no longer imposed administration on the export amount and quota licence on the 21 categories of textile products exported to the United State and the 8 categories of textile products under bilateral control exported to the European Union.

ENVIRONMENTAL PROTECTION REGULATIONS

In accordance with the *Environmental Protection Law* (環境保護法) adopted by the *Standing Committee of the National People's Congress* on 26 December 1989, the *Administration Supervisory Department of Environmental Protection* sets the national guidelines for the discharge of pollutants. The provincial and municipal governments of provinces, autonomous regions and municipalities may also set their own guidelines for the discharge of pollutants within their own provinces or districts in the event that the national guidelines are inadequate.

A company or an enterprise which causes environmental pollution and discharges other polluting materials which endanger the public should implement environmental protection methods and procedures into their business operations. This may be achieved by setting up a system of accountability within the company's business structure for environmental protection; adopting effective procedures to prevent environmental hazards such as waste gases, water and residues, dust powder, radioactive materials and noise arising from production, construction and other activities from polluting and endangering the environment. The environmental protection system and procedures should be implemented simultaneously with the commencement of and during the operation of construction, production and other activities undertaken by the company. Any company or enterprise which discharges environmental

pollutants should report and register such discharge with the *Administration Supervisory Department of Environmental Protection* and pay any fine imposed for the discharge. A fee may also be imposed on the company for the cost of any work required to restore the environment to its original state. Companies which have caused severe pollution to the environment are required to restore the environment or remedy the effects of the pollution within a prescribed time limit. If a company fails to report and/or register the environmental pollution caused by it, it will receive a warning or be penalised. Companies which fail to restore the environment or remedy the effects of the pollution within the prescribed time will be penalised or have their business licences terminated. Companies or enterprises which have polluted and endangered the environment must bear the responsibility for remedying the danger and effects of the pollution, as well as to compensate for any loss or damages suffered as a result of such environmental pollution.

On 29 November 1998, the State Council promulgated the *Regulations on the Administration of Construction Project Environmental Protection* (建設項目環境保護管理條例). On 28 October 2002 the Standing Committee approved the *Law of the People's Republic of China on Appraising of Environment Impacts* (中華人民共和國環境影響評價法) which became effective on 1 September 2003. According to the aforesaid laws, the PRC Government has set up a system to appraise the environmental impact from construction projects, and classify and administer the environmental impact appraisals in accordance with the degree of the environmental impact. If the construction project may result in a material impact on the environment, a thorough environmental impact report on the potential environmental impact is required; if the construction project may result in a slight impact on the environment, an environmental impact statement of analysing or special evaluation will be required; and if the construction project may only result in very little impact on the environment, an environmental impact appraisal is not required but an registration form of environmental impact is needed to be filed. The construction units responsible for the construction projects must submit the aforesaid environmental impact appraisal documents to the relevant administrative departments of environmental protection for examination and approval. If the construction units fail to submit the aforesaid environmental impact appraisal documents according to the applicable PRC laws and regulations or if the documents are not approved after examination by the relevant administrative departments, the departments responsible for examination and approving the relevant construction projects shall not approve such projects and the construction units shall not commence the construction.

Under the *Prevention and Control of Water Pollution Law* (水污染防治法), companies which discharge pollutants directly or indirectly into bodies of water must register with the environmental protection department of the local government at county level or above in the area where they are situated. Such companies must provide information on their facilities which discharge such pollutants, their treatment plants, the type, amount and concentration of the pollutants discharged under normal business operations, in accordance with regulations set by the *Administration Supervisory Department of Environmental Protection*. If there are significant changes to the type, amount or concentration of pollutants being discharged, such changes must be reported immediately. The dismantling or non-usage of pollution treatment plants also require the approval of the environmental protection department of the local government at county level or above.

Under the *Prevention and Control of Atmospheric Pollution Law* (大氣污染防治法), companies which discharge pollutants into the atmosphere must provide details of the discharge to the environmental protection department of the local government. Such details must include the facilities which discharge such pollutants, their treatment plants, the type, amount and concentration of the pollutants discharged under normal business operations, in accordance with regulations made by the *Administration Supervisory Department of Environmental Protection*. If there are significant changes to the type, amount or concentration of pollutants being discharged, such changes must be reported immediately. The dismantling or non-usage of pollution treatment plants also requires the approval of the environmental protection department of the local government.

Under the *Prevention and Control of Solid Waste Pollution Law* (固體廢物污染環境防治法), companies which discharge solid waste pollution shall be responsible for their pollution. Companies must register with the local relevant authority for their solid waste pollution, and must provide information in relation to the type, amount, discharge and treatment of such pollution, in accordance with regulations made by the *Administration Supervisory Department of Environmental Protection*. If there are significant changes to the type, amount or concentration of pollutants being discharged, such changes must be reported immediately. The dismantling or non-usage of pollution treatment plants also requires the approval of the environmental protection department of the local government.

TAXATION

The applicable income tax laws, regulations, notices and decisions (collectively referred to as "Applicable FIEs Tax Law") related to FIEs and their investors include the following:

- the EIT Law promulgated by the State Council on 16 March 2007 which came into effect on 1 January 2008;
- *Implementing Rules of the Enterprise Income Tax Law of PRC* (中華人民共和國企業所得稅法實施條例) promulgated by the State Council on 6 December 2007 which came into effect on 1 January 2008;
- *Notice on the Implementation of the Transitional Preferential Policies in respect of Enterprise Income Tax* (國務院關於實施企業所得稅過渡優惠政策的通知) ("Notice") promulgated by the State Council on 26 December 2007 which came into effect on the same date;
- *Notice relating to Taxes Applicable to Foreign Investment Enterprises/Foreign Enterprises and Foreign Nationals in Relation to Dividends and Gains obtained from Holding and Transferring of Shares* (國家稅務總局關於外商投資企業、外國企業和外籍個人取得股票(股權)轉讓收益和股息所得稅收問題的通知) promulgated by the *State Tax Bureau* on 21 July 1993;
- *Income Tax Law Applicable to Individuals of PRC* (中華人民共和國個人所得稅法) promulgated by the *Standing Committee of the NPC* on 10 September 1980 and last amended on 29 December 2007 and its latest Implementation Regulations promulgated on 18 February 2008; and
- *Notice on Relevant Policies Concerning Individual Income Tax* (關於個人所得稅若干政策問題的通知) issued by the *Ministry of Finance* and the *State Tax Bureau* on 13 May 1994.

Taxpayer

The taxpayer of income tax of foreign invested enterprises refers to Sino-foreign equity joint ventures, Sino-foreign contractual joint ventures and foreign-capital enterprises that are established in the PRC.

Tax Rate

In accordance with the EIT Law, a unified EIT rate of 25% and unified tax deduction standards will be applied equally to both domestic-invested enterprises and foreign-invested enterprises. In accordance with the Notice, the EIT rate applicable to foreign-invested enterprises which are currently subject to a deducted rate will be gradually increased up to 25% within five years commencing from 1 January 2008.

Losses Incurred in a Tax Year May Be Carried Forward for Not More Than Five Years

Losses incurred in a tax year by any enterprise with foreign investment and by an establishment or a place set up in the PRC by a foreign enterprise to engage in production or business operations may be made up by the income of the following tax years. Should the income of the following tax year be insufficient to make up for the said losses, the balance may be made up by its income of the further subsequent year, and so on, over a period not exceeding five years.

Any enterprise with foreign investment shall be allowed, when filing a consolidated income tax return, to deduct from the amount of tax payable the foreign income tax already paid abroad in respect of the income derived from sources outside the PRC. The deductible amount shall, however, not exceed the amount of income tax otherwise payable under the EIT Law in respect of the income derived from sources outside the PRC.

Pursuant to the EIT Law, the *Income Tax Law of the PRC for Enterprises with Foreign Investment and Foreign Enterprises* (中華人民共和國外商投資企業和外國企業所得稅法) and its Implementing Rules shall be abolished, and the rate of EIT applicable to all resident enterprises, including foreign invested enterprises and domestic companies in the PRC shall be at a uniform rate of 25% in five years. According to the EIT Law, any enterprise established prior to the promulgation of the EIT Law and is currently enjoying tax incentives, shall be entitled to continue to enjoy such incentives till the date of expiry. In the case of an enterprise that had been established before the EIT Law, but had not declared its first profitable year, the term of any entitlement to tax incentives shall commence from 1 January 2008 for a transition period of five years.

According to the Notice which was promulgated and came into effect on 26 December 2007, commencing from 1 January 2008, enterprises that previously enjoy the preferential policies of low tax rates shall be gradually transited to enjoy the statutory tax rate within 5 years after the implementation of the EIT Law. Among them, the enterprises that enjoy the EIT rate of 15% shall be subject to the EIT rate of 18% in 2008, 20% in 2009, 22% in 2010, 24% in 2011 and 25% in 2012. The enterprises that previously enjoy the tax rate of 24% shall be subject to the tax rate of 25% commencing from 2008. As of 1 January 2008, enterprises that previously enjoy "2-year exemption and 3-year half payment", "5-year exemption and 5-year half payment" of the enterprise income tax and other preferential treatments in the form of periodic tax deductions and exemptions may, after the implementation of the EIT Law, continue to enjoy the relevant preferential treatments under the preferential measures and the time period prescribed in the former tax law, administrative regulations and relevant documents until the expiration of the said time period. However, if such an enterprise has not enjoyed the preferential treatments yet because of its failure to make profits, its preferential time period shall be calculated from 2008. The expression "enterprises enjoying the preferential policies" as mentioned above refers to the enterprises established and registered in the industrial and commercial administrative department and in other registration administrative departments prior to 16 March 2007.

Value-Added Tax

The *Provisional Regulations Concerning Value-Added Tax of the PRC* (中華人民共和國增值稅暫行條例) promulgated by the State Council and amended on 5 November 2008 came into effect on 1 January 2009. Under these regulations and the *Implementing Rules of the Provisional Regulations Concerning Value-Added Tax of the PRC* (中華人民共和國增值稅暫行條例實施細則), value-added tax is imposed on goods sold in or imported into the PRC and on processing, repair and replacement services provided within the PRC.

The value-added tax rates shall be as follows:

(a) The tax rate for goods sold or imported by taxpayers other than the goods set forth in Items 2 and 3 below shall be 17%.

(b) The tax rate for sale or import of the following goods by taxpayers shall be 13%:

(i) grain, edible vegetable oil;

(ii) tap water, heating, air-conditioning, hot water, coal gas, liquid petroleum gas;

(iii) natural gas, methane, and coal products for use by residents;

(iv) books, newspapers, magazines;

(v) feed, chemical fertiliser, agrochemicals, agricultural equipment and machinery, agricultural film; and

(vi) other goods specified by the State Council.

(c) The tax rate for goods exported by taxpayers shall be zero, except where otherwise determined by the State Council.

(d) The tax rate for processing and repair and replacement services provided by taxpayers shall be 17%. The value-added tax rates for small scale taxpayer shall be 3%.

Business Tax

With effect from 1 January 2009, businesses that provide services (including entertainment business), assign intangible assets or sell immovable property are liable to business tax at a rate ranging from 3% to 20%, of the charges of the services provided, intangible assets assigned or immovable property sold, as the case may be.

The formula for calculation of the amount of tax payable is set forth below:

Amount of tax payable = amount of business × tax rate

The amount of tax payable shall be calculated in RMB. Taxpayers that settle their amounts of business income in foreign exchange shall convert the amounts into RMB at the foreign exchange market rate.

PRC Customs Duties

According to the *Customs Law of the PRC* (中華人民共和國海關法), the consignee of the imports, the consignor of exports and the owner of the imports and the exports are the persons obligated to pay customs duties (generally speaking, exports are not subject to customs duties). The PRC Customs is the authorities in charge of the collection of customs duties.

The customs duties in the PRC mainly fall under ad valorem duties, namely the price of import/export commodities is the basis for the calculation of the duties. When calculating the customs duties, import/export commodities shall be classified under appropriate tax items in accordance with the category provisions of the *Customs Import and Export Tariff* and shall be subject to tax levies pursuant to relevant tax rates.

Under the laws of the PRC, raw materials, supplementary materials, parts, components, accessories and packing materials imported for processing and assembling finished products for foreign parties or for manufacturing products for export shall be exempt from import duties pursuant to the actual amount of goods processed for export; or import duties may be levied upfront on import materials and parts and subsequently refunded pursuant to the actual amount of goods processed for export.

To encourage the introduction of foreign investment, commencing from 1992, the PRC exercised exemption and reduction of customs duties on the import of equipment, machinery, parts and other materials within the total investment of foreign investment companies. But after the adjustment of policies as of 1 April 1996, such exemption and reduction has been terminated, while the foreign investment companies incorporated before then can still continue to enjoy such preferential treatment within the grace period.

As from 1 January 1998, according to the *Notice of the State Council regarding the Adjustment of Taxation Policy of Import Equipment* (國務院關於調整進口設備稅收政策的通知), in respect of the foreign investment projects that fall under *Encouraging Category and Restricted B Category of the Industrial Guidance Catalogue of Foreign Investment* (外商投資產業指導目錄鼓勵類和限制乙類) and also involve the transfer of technology, the equipment imported for its own use within the total investment can be exempt from the customs duties, except for the commodities listed in the *Catalogue of the Non-tax Exemption Import Commodity of Foreign Investment Projects* (外商投資項目不予免稅的進口商品目錄).

Tax on Dividends from PRC Enterprise with Foreign Investment

According to the Applicable FIEs Tax Law, income such as dividends and profits distribution from the PRC derived from a foreign enterprise which has no establishment in the PRC is subject to a 20% withholding tax, subject to reduction as provided by any applicable double taxation treaty, unless the relevant income is specifically exempted from tax under the Applicable FIEs Tax Law. The profit derived by a foreign investor from a PRC enterprise with foreign investment is exempted from PRC tax according to the Applicable FIEs Tax Law. However, following the enforcement of the EITL from 1 January 2008, dividends of the year 2008 and the years afterwards distributed from foreign investment enterprises to foreign investors shall be subject to the Enterprise Income Tax. Profits accumulated by foreign investment enterprises before 1 January 2008 but distributed to foreign investors after 1 January 2008 are exempted from the Enterprise Income Tax.

Apart from the above, the Applicable FIEs Tax Law provides that:

(a) pursuant to the *Implementing Rules of the Enterprise Income Tax Law of PRC* (中華人民共和國企業所得稅實施條例) promulgated by the State Council commencing on 1 January 2008, 10% income tax is applicable to dividends payable from a foreign enterprise which has no establishment in the PRC to investors that are "non-resident enterprises" (and that do not have an establishment or place of business in the PRC, or that have such establishment or place of business but the relevant income is not effectively connected with the establishment or place of business); and

(b) pursuant to the *Notice concerning Tax Rates for Dividends Declared* (關於下發協定股息稅率情況一覽表的通知) issued by the State Administration of Taxation, 5% withholding tax is applicable to dividends payable from the PRC subsidiary to its Hong Kong holding company, pursuant to an arrangement for the avoidance of double taxation between Mainland China and Hong Kong which provides for a withholding tax at a rate of 5% for dividend payments the Hong Kong holding company receives from the PRC entities in which it holds an interest of 25% or more, to the extent such dividends have their source within the PRC.

In addition, the Applicable FIEs Tax Law also provides that dividends received by a qualified PRC tax resident from another PRC tax resident are exempted from withholding tax.

LABOUR LAWS AND SAFETY MATTERS

Relevant labour and safety laws and regulations in the PRC include the *PRC Labour Law* (中華人民共和國勞動法), the *PRC Labour Contract Law* (中華人民共和國勞動合同法), the *Decision of the State Council on Establishing the Unified Basic Pension Insurance System for the Employees of Enterprises* (國務院關於建立統一的企業職工基本養老保險制度的決定), the *Decision of the State Council on Establishing the Basic Medical Insurance System for the Urban Employees* (國務院關於建立城鎮職工基本醫療保險制度的決定), the *Regulation on Work-related Injury Insurance* (工傷保險條例), the *Regulation on Unemployment Insurance* (失業保險條例), the *Provisional Insurance Measures for Maternity of Employees* (企業職工生育保險試行辦法), the *Interim Provisions on Registration of Social Insurance* (社會保險登記管理暫行辦法), the *Interim Regulation on the Collection and Payment of Social Insurance Premiums* (社會保險費徵繳暫行條例) and other related regulations, rules and provisions issued by the relevant governmental authorities from time to time are applicable to our operations in the PRC.

According to the *Social Insurance Law of the PRC* (中華人民共和國社會保險法), which was promulgated on 28 October 2010 and became effective from 1 July 2011, employers are obliged to make contributions to, and employees including migrant workers from rural areas are required to participate in, all social insurance schemes, which include basic pension insurance, basic medical insurance, unemployment insurance, work-related injury insurance and maternity insurance schemes. Basic pension insurance, and basic medical insurance and unemployment insurance contributions shall be paid by both employers and employees. Employees shall participate in work-related injury insurance and maternity insurance schemes. Work-related injury insurance and maternity insurance contributions shall be paid by employers rather than employees.

Pursuant to the *Social Insurance Law of the PRC*, if an employer fails to pay work-related injury insurance contributions in accordance with the law, it shall pay work-related injury insurance benefits in the case of a work-related injury accident. If the employer fails to make such payment, the benefits shall first be reimbursed by the work-related injury insurance fund. Work-related injury insurance benefits reimbursed by the work-related injury insurance fund shall be repaid by the employer. If the employer fails to make repayment, social insurance agencies may recover such benefits from the employer in accordance with the law.

Furthermore, as to unemployment insurance, employers shall provide unemployed individuals with certification of expiry or termination of their employment in a timely manner, and within 15 days of such expiry or termination, inform social insurance agencies of the list of the unemployed individuals. Unemployed individuals shall undertake the procedures for unemployment registration with the designated public employment service institutions in a timely manner by producing the certification of expiry or termination of their employment issued by their former employers. The period for receiving unemployment insurance benefits shall be calculated from the date of unemployment registration.

An employer shall register with the local social insurance agency in accordance with the provisions of the *Social Insurance Law of the PRC*. Moreover, an employer shall declare and make social insurance contributions in full and on time. Except for mandatory exceptions such as force majeure, social insurance may not be paid late, reduced or be exempted. If an employer fails to report the social insurance premium payable in accordance with the relevant regulations, the social insurance agency shall provisionally set the amount payable at 110% of the premium paid in the previous month. Once the employer has retroactively undertaken the reporting procedures, the social insurance agency shall settle

the amount in accordance with the relevant regulations. Where an employer fails to make social insurance contributions in full and on time, the social insurance agency may order rectification within a specified time limit. If the employer fails to rectify within the specified time limit, the social insurance agency may enquire with the relevant banks and financial institutions in which the employer has an account in, and may apply with the relevant administrative department above county level to allocate and transfer the unpaid social insurance contributions and notify the relevant banks or other financial institutions in writing to allocate and transfer the unpaid social insurance contributions. Where the balance in the employer's bank account is less than the overdue social insurance contributions, the social insurance agency may request the employer to provide a guarantee and sign a social insurance payment agreement for the delayed payment. If the employer does not make the social insurance contributions within the specified time limit and fail to provide a guarantee with respect to the same, the social insurance agency may request the people's court to seize the property of the employer (equivalent in value to the unpaid overdue social insurance contributions), and collect the overdue social insurance contributions from the proceeds obtained from the auction of such property.

According to the *PRC Labour Law* (中華人民共和國勞動法) and the *PRC Labour Contract Law* (中華人民共和國勞動合同法), labour contracts in written form shall be executed to establish labour relationships between employees and employers. The employers must provide wages which are no lower than local minimum wage standards to the employees from time to time. The employers are required to establish a system for labour safety and sanitation, strictly abide by State rules and standards and provide relevant education to the employees. The employers are also required to provide the employees with labour safety and sanitation conditions meeting State rules and standards and carry out regular health examinations of the employees engaged in hazardous occupations.

As required under the *Decision of the State Council on Establishing the Unified Basic Pension Insurance System for the Employees of Enterprises*, the *Decision of the State Council on Establishing the Basic Medical Insurance System for the Urban Employees*, the *Regulation on Work-related Injury Insurance*, the *Provisional Insurance Measures for Maternity of Employees*, the *Interim Regulation on the Collection and Payment of Social Insurance Premiums* and the *Interim Provisions on Registration of Social Insurance*, the employers are obliged to provide the employees in the PRC with welfare schemes covering basic pension insurance, unemployment insurance, maternity insurance, injury insurance and basic medical insurance.

The *PRC Production Safety Law* (中華人民共和國安全生產法) requires that the employers maintain safe production conditions as required by the *PRC Production Safety Law* and other relevant laws, administrative regulations, national standards and industrial standards. It further provides that any entity that is not sufficiently equipped to ensure safe production may not engage in production and business operation activities, and that companies must provide production safety education and training programmes to employees. The design, manufacture, installation, use, checking and maintenance of the safety equipment are required to conform to applicable national or industrial standards. In addition, it is required that labour protection equipment must meet the national or industrial standards and that companies must supervise and educate their employees to wear or use such equipment according to the prescribed rules.

Relevant Regulations on Housing Fund

Pursuant to the *Regulations on the Administration of Housing Fund* (《住房公積金管理條例》) effective in 1999, as amended in 2002, PRC companies shall register with the competent housing fund management centre and establish a special housing fund account in an entrusted bank. Both PRC companies and their employees are required to contribute to the housing fund and their respective deposits shall not be less than 5% of an individual employee's monthly average wage during the

preceding year. If an employer fails to make housing fund contributions for its employees, the housing fund management centre may order rectification, and a fine of between RMB10,000 and RMB50,000 may be imposed. In practise, local policy and regulations on the implementation of the housing fund may vary from place to place in PRC.

WHOLLY FOREIGN-OWNED ENTERPRISE ("WFOE")

The establishment, operation and management of corporate entities in China are governed by the *Company Law of the PRC* (中華人民共和國公司法) ("Company Law"), which was adopted by the Standing Committee on 29 December 1993 and became effective on 1 July 1994. It was latest amended on 27 October 2005 and became effective from 1 January 2006. Under the Company Law, the companies are generally classified into two categories: limited liability companies and limited companies by shares. The Company Law also applies to foreign-invested limited liability companies. According to the Company Law, where laws on foreign investment have different stipulations, such stipulations shall prevail. According to the *Implementing Opinion on Several Issues Concerning the Application of Law in the Administration of the Examination, Approval and Registration of Foreign-invested Companies* (關於外商投資的公司審批登記管理適用法律若干問題的執行意見) issued jointly by the *State Administration for Industry and Commerce*, MOFCOM, the *General Administration of Customs and the State Administration of Foreign Exchange* on 24 April 2006 and became effective on the same day, the organisation structure of limited liability companies in the form of a foreign equity joint venture, wholly foreign-owned limited liability company or foreign-invested stockholding limited company shall comply with the provisions of the Company Law and the articles of associations. Furthermore, where a foreign-invested company increases its registered capital, the shareholders of a limited liability company (including one-person limited company), or the stock holding limited company established by way of promotion shall pay no less than 20% of the registered capital to be increased when the company applies for modifying the registration of registered capital. The time of capital contribution of the remaining portion shall meet the provisions of the Company Law, the laws on foreign investment and *Regulations on the Administration of Company Registration*. If other laws or administrative regulations provide otherwise, such provisions shall prevail.

A WFOE is governed by the *Law of the PRC on Wholly Foreign-owned Enterprises* (中華人民共和國外資企業法), which was promulgated on 12 April 1986 and revised on 31 October 2000, and its Implementation Regulations promulgated on 12 December 1990 and revised on 12 April 2001 ("WFOE Law").

Procedures for Establishment of a WFOE

The establishment of a WFOE must be approved by the MOFCOM. If two or more foreign investors jointly apply for the establishment of a WFOE, a copy of the contract between the parties must also be submitted to the MOFCOM (or its delegated authorities) for its record. A WFOE must also obtain a business licence from the relevant local Administration for Industry and Commerce before it can commence business operation.

Nature of WFOE

A WFOE is a limited liability company under the WFOE Law. A WFOE is a legal person who is entitled to independently assume civil obligations, enjoy civil rights and own, use and dispose of property. It is required to have a registered capital contributed by the foreign investor(s). The liability of the foreign investor(s) is limited to the amount of registered capital it subscribed to contribute. A foreign investor is permitted to make its contributions by instalments and the registered capital shall be contributed within the required time period as approved by the MOFCOM (or its delegated authorities) in accordance with relevant PRC laws and regulations.

Profit Distribution

The WFOE Law provides that a WFOE shall withdraw reserve fund and employee bonus and benefit fund from the after-tax profit. The allocation ratio for the employee bonus and welfare fund shall be determined by the enterprise. However, at least 10% of the after-tax profits must be allocated to the reserve fund. If the cumulative total of allocated reserve funds reaches 50% of the enterprise's registered capital, the enterprise will not be required to make any additional contribution. The enterprise is prohibited from distributing dividends unless the losses (if any) of previous years have been made up.

FOREIGN EXCHANGE CONTROL

Prior to 31 December 1993, enterprises in the PRC requiring foreign currency were required to obtain approval from the *State Planning Committee* and the *China Ministry of Foreign Trade and Economic Cooperation* before it could convert Renminbi into foreign currency, and such conversion had to be effected at the official rate prescribed by SAFE. Renminbi reserved by foreign investment enterprises could also be converted into foreign currency at swap centres with the prior examination and verification by SAFE. The exchange rates used by swap centres were largely determined by the supply of and demand for foreign currencies and Renminbi.

On 28 December 1993, the PBOC announced that the dual exchange rate system for Renminbi against foreign currencies would be abolished with effect from 1 January 1994 and be replaced by the unified exchange rate system. Under the new system, the PBOC publishes the Renminbi exchange rate against the US dollar daily. The daily exchange rate is set by reference to the Renminbi/US dollar trading price on the previous day on the "inter-bank foreign exchange market".

On 1 April 1996, the *Foreign Exchange Control Regulations of the PRC* (中華人民共和國外匯管理條例) by the State Council (as amended on 14 January 1997 and 1 August 2008) came into effect. On 20 June 1996, the PBOC issued the *Announcement on the Implementation of Sale and Purchase of Foreign Exchange for the Foreign Investment Enterprises* (中國人民銀行關於對外商投資企業實行銀行結售匯的公告) which allows foreign-invested enterprises ("FIEs") to settle their foreign exchange related transactions at designated banks or at swap centres from 1 July 1996. This Announcement was abolished on 1 December 2002 by the *Interim Measures for the Administration of Foreign Exchange Settlement and Sales Operations by Designed Foreign Exchange Banks* (外匯指定銀行辦理結匯、售匯業務管理暫行辦法). On 20 June 1996, the *Regulations on Settlement and Sales of and Payment in Foreign Exchange* (結匯、售匯及付匯管理規定) was promulgated by the PBOC and came into effect on 1 July 1996.

On 25 October 1998, the *PBOC* and *SAFE* issued the *Joint Announcement on Abolishment of Foreign Exchange Swap Business* (中國人民銀行、國家外匯管理局關於停辦外匯調劑業務的通知) which stated that from 1 December 1998, foreign exchange transactions for FIEs may only be conducted at designated banks. In addition, some of the swap centres would be abolished, while the others which are already linked up with the *China Foreign Exchange Trading Centre* (the "CFETC") by the computerised network will be merged with the CFETC and sub-centres to the CFETC.

On 21 July 2005, the PBOC issued the public announcement regarding reforming the Renminbi exchange rate regime. With effect from 21 July 2005:

(a) The PRC will reform the exchange rate regime by moving into a managed floating exchange rate regime based on market supply and demand with reference to a basket of currencies and the Renminbi will no longer be pegged to the US dollar;

(b) The PBOC will announce the closing price of foreign currencies including but not limited to the US dollar traded against Renminbi in the inter-bank foreign exchange market after the closing of the market on each working day, and will make it the central price for the trading against Renminbi on the following day;

(c) The exchange rate of the US dollar against the RMB will be adjusted to 8.11 RMB per US dollar at the time of 19: 00 hours of 21 July 2005, which will be made as the central price for the trading against the RMB on the following working day. The foreign exchange designated banks may since then adjust quotations of foreign currencies to their customers; and

(d) The daily trading price of the US dollar against the RMB in the inter-bank foreign exchange market will continue to be allowed to float within a band of ±0.3% around the central parity published by the PBOC, while the trading prices of the non-US$ currencies against the RMB will be allowed to move within a certain band announced by the PBOC.

In the future, the PBOC will make adjustment of the RMB exchange rate band when necessary according to market development as well as the economic and financial situation.

The *Foreign Exchange Control Regulations of China* was amended on 1 August 2008. Pursuant to this amendment: (1) the compulsory requirements for PRC enterprises to transfer their foreign exchange income back into PRC territory is abolished; (2) control and inspection over cross-border capital flow are further strengthened; and (3) the foreign exchange approval over direct investment overseas is simplified.

In summary, the present position under PRC laws relating to foreign exchange control, taking into account the promulgation of the recent new regulations and the extent the existing provisions stipulated in previous regulations do not contradict these new regulations, are as follows:

(a) The previous dual exchange rate system for RMB was abolished and a managed floating exchange rate regime based on market supply and demand with reference to a basket of currencies was introduced. The PBOC will announce the closing price of foreign currencies including but not limited to the US dollar traded against the RMB in the inter-bank foreign exchange market after the closing of the market on each working day, and will make it the central parity for the trading against the RMB on the following working day.

(b) Foreign exchange receipts and payments shall be based on true and lawful transactions. PRC enterprises may retain or sell their foreign exchange earnings to financial institutions which are allowed to conduct foreign exchange businesses and use their own retained foreign exchange or purchase foreign exchange at financial institutions which are allowed to conduct foreign exchange businesses for current account transactions.

(c) Capital foreign exchange receipts of PRC enterprises, upon SAFE approval (unless no approvals required), may be retained or sold to financial institutions which are allowed to conduct foreign exchange businesses. PRC enterprises may use their retained foreign exchange or purchase foreign exchange at financial institutions which are allowed to conduct foreign exchange businesses for capital account transactions.

(d) Despite the relaxation of foreign exchange control over current account transactions, the approval of SAFE is still required before an enterprise may receive a foreign currency loan, provide a foreign exchange guarantee, make an investment outside the PRC or enter into any other capital account transaction that involves the purchase of foreign exchange.

(e) FIEs which require foreign exchange for their ordinary trading activities such as trade services and payment of interest on foreign debts may purchase foreign exchange from designated foreign exchange banks if the application is supported by proper payment notices or supporting documents.

(f) FIEs may require foreign exchange for the payment of dividends that are payable in foreign currencies under applicable regulations, such as distributing profits to their foreign investors. They can withdraw funds in their foreign exchange bank accounts kept with designated foreign exchange banks, subject to the due payment of tax on such dividends. Where the amount of the funds in foreign exchange is insufficient, the enterprise may, upon the presentation of the resolutions of the directors on the profit distribution plan of the particular enterprise, purchase foreign exchange from designated exchange banks.

(g) FIEs may apply to designated foreign exchange banks to remit the profits out of the PRC to the foreign parties to equity or cooperative joint ventures or the foreign investors in wholly foreign-owned enterprises if the requirements provided by PRC laws, rules and regulations are met.

Pursuant to the *Circular of the SAFE on Relevant Issues concerning Foreign Exchange Administration of Financing and Return Investments Undertaken by Domestic Residents through Overseas Special Purpose Vehicles* (《關於境內居民通過境外特殊目的公司融資及返程投資外匯管理有關問題的通知》, "SAFE Circular No. 75"), promulgated on 21 October 2005 and effective on 1 November 2005,

(a) a PRC citizen or enterprises, or a PRC resident, must register with the local SAFE branch before he, she or it establishes or controls an overseas special purpose vehicle (SPV), for the purpose of obtaining overseas equity financing using the assets of or equity interests in a domestic enterprise;

(b) when a PRC resident contributes the assets of or its equity interests in a domestic enterprise to an overseas SPV, or engages in overseas financing after contributing assets or equity interests in a domestic enterprise to an overseas SPV, such PRC resident must register his or her interest in the overseas SPV or any change to his or her interest in the overseas SPV with the local SAFE branch;

(c) when the overseas SPV undergoes a material event outside the PRC, such as a change in share capital or merger and acquisition, the PRC resident must, within 30 days after the occurrence of such event, register such change with the local SAFE branch.

Pursuant to SAFE Circular No. 75, failure to comply with these registration procedures may result in penalties, including the imposition of restrictions on a PRC subsidiary's foreign exchange activities and its ability to distribute any dividends to the overseas SPV.

Our PRC legal adviser, Commerce & Finance, opined that since our Shareholders, Mr. Zheng, Mr. Sze, Mr. Lin and Ms. Chow, had become Hong Kong residents prior to the announcement of the SAFE Circular No. 75 and Jiangxi Jinyuan was established as a foreign investment enterprise in 2005 directly by Mr. Zheng and Mr. Sze and no overseas SPV was involved, no registration under the SAFE Circular No. 75 was required at the time of its establishment. In addition, the Corporate Reorganisation does not fall within the scope of the SAFE Circular No. 75 and no registration is required.

M&A Rules

On 8 August 2006, six PRC governmental and regulatory agencies, including the MOFCAM and the CSRC, promulgated *the Regulation on the Acquisitions of Domestic Enterprises by Foreign Investors* (關於外國投資者併購境內企業的規定) ("M&A Rules") which became effective on 8 September 2006 and was revised on 22 June 2009. Pursuant to the M&A Rules, merger or acquisition of a domestic enterprise by a foreign investor means (i) that a foreign investor purchases equity interest owned by shareholders in a domestic enterprise other than a foreign-invested enterprise or subscribes to the increased capital of a domestic company, whereby to convert such domestic company into a foreign-invested company, or (ii) that a foreign investor establishes a foreign-invested enterprise through which assets of a domestic enterprise are subsequently acquired by agreement and operated, or (iii) that a foreign investor acquires the assets of a domestic enterprise by agreement and subsequently establishes a foreign-invested enterprise with such assets and then operate such assets.

Under such M&A Rules, establishment of a foreign-invested enterprise by foreign investors through merger with and acquisition of a domestic entity shall be subject to approval by the approval authority, and to completion of new registration, or amendment to existing registration, with the registration administrative authority.

Our PRC legal adviser, Commerce & Finance, advised that approval by the CSRC under the M&A Rules for the Corporate Reorganisation is not required for the following reasons: (a) Jiangxi Jinyuan was established as a wholly foreign-owned enterprise by Mr. Zheng and Mr. Sze before the effective date of the M&A Rules; and (b) no merger and acquisition as defined in the M&A Rules occurred in connection with the Corporate Reorganisation of Jiangxi Jinyuan.

THE REGULATION ON ADJUSTMENT IN THE STRUCTURE OF INDUSTRIES

On 27 March 2011, the NDRC promulgated the *Guiding Catalog for Adjustment in the Structure of Industries* (產業結構調整指導目錄) ("Guiding Catalog"), which became effective on 1 June 2011. Pursuant to the *Guiding Catalog,* certain categories of outdated products or projects are subject to restriction or obsolescence.

As advised by our PRC legal adviser, Commerce & Finance, since Jinyuan is and will not engage in such products or projects in the specified category under the Guiding Catalog, the Guiding Catalog will not have material adverse financial and operational impacts on us.