

CORPORATE GOVERNANCE

1. There has been a deviation between the actual corporate governance implemented by the Company and the rules and requirements of corporate governance required to be observed by listed companies. In order to ensure compliance, the Company will further amend its rules for general meetings, set up different committees in addition to its audit committee (the "Audit Committee"), for example a remuneration committee, a selection committee and a development strategy committee under the Board of Directors. Further the Company would formulate and implement rules in respect of its independent non-executive directors.
2. Independent non-executive directors

The Company has appointed three independent non-executive directors. Pursuant to the Rules governing the listing of securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules"), the Audit Committee, comprising the three independent non-executive directors was established.

By reference to "A Guide for the Formation of an Audit Committee" published by the Hong Kong Society of Accountants, written terms of reference, which describe the authority and duties of the Audit Committee, were prepared and adopted by the Board of Directors. The Audit Committee is mainly responsible for reviewing the financial reports of the Company. Through the various analyses, the Audit Committee aims to locate any existing financial risks and make suggestions to the Board of Directors in their resolutions. The Audit Committee also reviews the provision for diminution in value of assets and treatment of related loss.

The independent non-executive directors would review whether or not the connected transactions entered into by the Company are on normal commercial terms and in the ordinary and usual course of the Company's business, as well as review whether the connected transactions are detrimental to the interests of the Company's shareholders. The independent non-executive directors are responsible to all of the shareholders of the Company.

3. The Company is independent of its controlling shareholder in respect of its business, assets, management, institutions and financial team. The Company has complete and independent production and operations capabilities.
- (i) The Company is mainly engaged into the business of development, manufacture and

sale of bulk pharmaceuticals, preparations and chemical products. Regarded as the controlling shareholder of the Company, SXPGC undertakes not to engage in any business directly or indirectly in competition with the businesses of the Company.

- (ii) The Company has its own independent production and supplementary production system and vital auxiliary equipment. Apart from the seven patented technologies and the "Xinhua" label, which are owned by the controlling shareholder, the Company owns all of the other industrial property rights and know-hows used by the Company. The Company also has an independent procurement and sales network.
- (iii) The Company is independent of its controlling shareholder in the respect of its management of its workforce and their salaries. The Senior Officers including the general manager and the deputy general managers of the Company are paid by the Company and, except Ms. Guo Qin who is also a director of SXPGC, the other Senior Officers do not hold any position within SXPGC.
- (iv) The Company holds its own shareholders' general meetings, and has its own board of directors, supervisory committee, company secretaries and management, which are responsible for the different areas and functions of the Company. The Company is also independent of its controlling shareholder in terms of its office and production space.
- (v) The Company has an independent financial department with an independent accounting and financial management system. The Company also maintains its own independent accounts with banks.

4. Incentive for and retention mechanisms of Senior Officers

The Company selects its Senior Officers on the basis of talent and work ability. Prior to selecting and appointing the Senior Officers, the Board of Directors would follow a strict set of selection criteria, which include the assessment of each of the candidates' individual character and ability to work in coordination with others. Once appointed, the Board of Directors would supervise the Senior Officers' work multimensionally, particularly in respect of their achievements and their execution of resolutions passed by the Board of Directors.

By analysing the duties of each of the Senior Officer, the Company would establish an incentive and retention mechanisms to draw distinction between the Senior Officers' work responsibilities, relative rewards and punishments. The Company is planning to implement a reward system of annual remuneration package and a share options scheme for its Senior

Officers.