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EXTRAWELL PHARMACEUTICAL HOLDINGS LIMITED

精優藥業控股有限公司*

(incorporated in Bermuda with limited liability)

(Stock Code: 00858)

FULFILLMENT OF ALL RESUMPTION CONDITIONS AND RESUMPTION OF TRADING

FULFILLMENT OF ALL RESUMPTION CONDITIONS

The Board is pleased to announce that the Stock Exchange has issued the Conditional Resumption Letter allowing the resumption of trading in the Shares, subject to the fulfillment of the conditions summarised in this announcement. The Board is pleased to announce that as at the date of this announcement, all the conditions have been fulfilled.

RESUMPTION OF TRADING

At the direction of the Stock Exchange, trading in the Shares on the Stock Exchange was suspended with effect from 10:12 a.m. on 20 September 2007. The Company has made an application to the Stock Exchange for the resumption of trading in the Shares with effect from 9:30 a.m. on 24 December 2009.

INTRODUCTION

Reference is made to the announcements of the Company dated 17 September 2007, 31 October 2007, 16 January 2008, 18 June 2008, 6 November 2008, 3 April 2009, 21 May 2009 and 23 July 2009, and the circular of the Company dated 21 May 2009 respectively. Capitalised terms used in this announcement shall have the same meanings as those defined in the announcement of the Company dated 31 October 2007.

FULFILLMENT OF ALL RESUMPTION CONDITIONS

The Board is pleased to announce that on 27 November 2009, the Stock Exchange issued a letter (“**Conditional Resumption Letter**”) granting its conditional approval for resumption of trading in the Shares, subject to disclosure of the following matters in an announcement:

- (1) actions taken to investigate the 2004 Transaction and the 2007 Transaction;
- (2) findings of the reviews set out in the reports dated 6 March 2008 and 16 December 2008 (each a “**RSM Report**”) and issued by RSM Nelson Wheeler Consulting Limited (“**RSM**”), the independent professional firm engaged by the Company for conducting a general review on the weaknesses and deficiencies in the internal control system of the Group and the internal control measures relating to the 2004 Transaction, the 2007 Transaction and other notifiable transactions entered into by the Group for the four years ended 31 March 2007, as well as actions taken to address the weaknesses identified in these reviews;
- (3) latest intention on the 2007 Transaction;
- (4) verdict of the ICAC court case in relation to the Incident based on public information; and
- (5) actions taken to confirm that 廣東精優惠南醫藥有限公司 (“**Domestic Company**”), as mentioned in the audit qualification made by RSM Nelson Wheeler, Certified Public Accountants (“**RSM CPA**”) in its independent auditor’s report in respect of the Group’s financial statements for the year ended 31 March 2008, is not a related party under Hong Kong Accounting Standard 24 “Related Party Disclosure” (“**HKAS 24**”).

The Company should also update shareholders if there is any development on the recoverability of the Group’s intangible assets and other receivable, or a negative statement.

The Board is pleased to announce that as at the date of this announcement, all the conditions set out above have been fulfilled and the details are set out in this announcement. Despite the Incident, the Group’s business has been operating in its usual and normal manner with its suppliers, customers and business partners, and its financial position has remained solid even under the unprecedented economic downturn resulting from the financial tsunami. The Board is not aware of any disruptions in the trading and production activities of the Group after the Incident.

SCOPE OF REVIEW BY THE INDEPENDENT BOARD

Following the Incident, the Independent Board had been formed to investigate, among others, the 2004 Transaction, 2007 Transaction, and the effectiveness of the Group’s internal control system. In order to assist the Independent Board to conduct such factual findings, the Working Committee then comprising three executive directors, namely Dr. Mao Yu Min, Dr. Xie Yi and Mr. Ho Yu Ling, has also been established. However, Mr. Ho Yu Ling later retired from the Working Committee as he was also charged by the ICAC in relation to the Incident in January 2008. Mr. Ho Yu Ling was later acquitted of such charges.

On 1 November 2007, RSM was engaged by the Company to assist in the review undertaken by the Independent Board.

In May 2009, the Company engaged Baker Tilly Hong Kong Business Services Limited (“**Baker Tilly**”), an independent professional consultancy firm, to conduct an internal control review and risk assessment of the key system control procedures of the Group and the status of implementation of recommendations made by RSM. Based on the first review conducted by Baker Tilly for the period from October 2008 to May 2009 and the second review for the period from May 2009 to August 2009, Baker Tilly concluded that though there was room for improvement, the Company had set up a sound and effective internal control mechanism and had taken appropriate actions and remedies as to the findings made by RSM in accordance with their level of threats to the operations of the Company.

In conducting the review, the Independent Board had taken the following actions:

- (i) in relation to the 2004 Transaction and the 2007 Transaction, the Independent Board reviewed reports prepared by the Group’s management based on discussions and enquiries made with the then management of the Group, accounting records and other documents in relation to the transactions, to evaluate whether there were any irregularities in the 2004 Transaction and 2007 Transaction, the circumstances giving rise to such irregularities and their impact on the Group;
- (ii) analysed the internal control weaknesses of the Group identified by RSM in relation to the 2004 Transaction and 2007 Transaction and the follow up actions taken by the Group’s management;
- (iii) analysed the internal control weaknesses of the Group identified by RSM in relation to other notifiable transactions of the Group during the four years ended 31 March 2007 which had been disclosed by the Company pursuant to the requirements of Chapter 14 of the Listing Rules, as well as the follow up actions taken by the Group’s management;
- (iv) the Independent Board conducted a review on certain other transactions of the Group for the five years ended 31 March 2008 to ascertain whether there were any other transactions entered into by the Group with similar issues as the 2004 Transaction and 2007 Transaction, that is, involving a connected person and subject to the reporting, announcement and/or independent shareholders’ approval requirements under Chapter 14A of the Listing Rules, but in respect of which the Company had failed to comply with the relevant requirements under the Listing Rules;
- (v) analysed the weaknesses and deficiencies identified by RSM in its general internal control review on the Group and follow up actions taken by the Group’s management;
- (vi) reviewed the reports (“**Baker Tilly’s Reports**”) issued by Baker Tilly on 26 June 2009 and 9 September 2009 respectively in relation to the effectiveness of the Group’s internal control system and implementation status of the recommendations made by RSM;
- (vii) made recommendations to the Group in respect of actions that should be taken to address internal control weaknesses identified by the Independent Board, RSM and Baker Tilly; and

(viii) reviewed the procedures for identifying possible and potential connected transactions as set out in the internal control and workflow manual (“**Internal Control and Workflow**”) adopted by the Board on 17 July 2009.

REVIEW OF THE EFFECTIVENESS OF THE GROUP’S INTERNAL CONTROL SYSTEM

(A) The 2004 Transaction and 2007 Transaction

In reviewing the 2004 Transaction and 2007 Transaction, RSM highlighted six deficiencies in the Group’s internal control procedures.

A summary of the observations and recommendations made by RSM, actions taken by the Company, recommendations by the Independent Board and results of the follow-up review conducted by Baker Tilly are set out below:

Observations and recommendations by RSM	Actions taken by the Company and recommendations by the Independent Board	Follow-up review by Baker Tilly
1. No written internal control procedures for identifying connected persons and connected transactions		
— The Company had not formally established written internal control procedures for identifying connected persons and connected transactions except for a list of connected persons maintained by the finance department of the Company which was used to facilitate the identification and timely disclosure of connected and related party transactions.	— The Company adopted the Internal Control and Workflow on 17 July 2009, setting out procedures for identifying possible and potential connected transactions.	— Management has implemented the recommendations made by RSM.
— The Board should establish an internal code (the “ Internal Code ”) describing clearly the necessary procedures for identifying possible and potential connected party relationship and transactions.	— The Independent Board considers that the Internal Control and Workflow is an effective measure for identifying possible and potential connected transactions.	

Observations and recommendations by RSM	Actions taken by the Company and recommendations by the Independent Board	Follow-up review by Baker Tilly
<p>2. Insufficient documentation on discussion of connected persons and connected transactions</p> <ul style="list-style-type: none"> — Discussions among the Directors regarding connected persons and connection transactions in relation to the 2004 Transaction and the 2007 Transaction were documented in the relevant minutes of the Board meetings, but such records were limited. — It should be stated clearly in the Internal Code that the working group (“Working Group”) established for handling the relevant transaction should submit a written report summarizing the identification work for connected persons and connected transactions and its conclusion for discussion and approval by the Board. 	<ul style="list-style-type: none"> — The Internal Control and Workflow has incorporated the recommendations made by RSM. — The Independent Board recommends that the Board minutes should include, where circumstances require, sufficient details of matters discussed at meetings, including contrary views on the relevant resolutions to be passed. The Working Group should also present the results of the internal check under the Internal Control and Workflow in respect of each transaction for the Board’s consideration in the future as and when necessary and in any event on a quarterly basis. 	<ul style="list-style-type: none"> — Management has implemented the recommendations made by RSM.

Observations and recommendations by RSM	Actions taken by the Company and recommendations by the Independent Board	Follow-up review by Baker Tilly
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3. Content of statement of interests (“SOI”) signed by Directors in respect of their interests in the Group’s transactions may not give sufficient attention to the connected persons and connected transactions confirmation

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| <ul style="list-style-type: none"> — The SOI given by each Director in relation to the 2004 Transaction and the 2007 Transaction did not include direct statements requiring the Directors to confirm that he or she is not a connected person with the target companies or companies concerned. — It should be stated clearly in the Internal Code that the Working Group is responsible for reviewing the content of the SOI and confirming with professional parties and the Stock Exchange before arranging for its signing by Directors and senior management. — The SOI should include a direct statement for connected party confirmation. | <ul style="list-style-type: none"> — SOI had been used for each Director to declare the information that are required to be disclosed in the circular and therefore were arranged to be signed after the entering into of the transaction and before the issue of the circular. Pursuant to the Internal Control and Workflow, the SOI, the content of which will be reviewed by the Working Group and will include a direct statement for connected party confirmation, will be signed before the entering into of the transaction by the Group. — The Independent Board also recommends the Company to obtain written independence confirmations from the relevant parties to the transaction at the early stage of negotiation, where practicable. | <ul style="list-style-type: none"> — Management has implemented the recommendations made by RSM. |
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Observations and recommendations by RSM	Actions taken by the Company and recommendations by the Independent Board	Follow-up review by Baker Tilly
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4. The scope of work of legal advisers and financial advisers in relation to identification of connected persons and connected transactions were not clearly defined

<ul style="list-style-type: none"> — The scope of work with legal advisers and financial advisers did not include specifically the work assisting the Board to detect any connected persons and connected transactions which could have been overlooked by the management or the Board. 	<ul style="list-style-type: none"> — The Company will define the scope of work for professional parties in accordance with the Internal Control and Workflow. 	<ul style="list-style-type: none"> — Management has implemented the recommendations made by RSM.
<ul style="list-style-type: none"> — The Board should include in the scope of work of legal advisers and financial advisers the procedures for identifying connected persons for compliance matters. 	<ul style="list-style-type: none"> — Professional parties will perform their duties according to their professional guidelines and industrial practice and will exercise their judgment according to the facts provided by the management and representation of the counterparties. The management considers it more practicable to undertake the action plans under paragraphs 1 and 3 above instead. 	
<ul style="list-style-type: none"> — The procedures should include the review of SOI or alternative declarations. 		

Observations and recommendations by RSM	Actions taken by the Company and recommendations by the Independent Board	Follow-up review by Baker Tilly
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5. Evidence of review and approval of company search performed for due diligence purposes by the Board or the Working Group could not be found

<ul style="list-style-type: none"> — Though company search summary was performed by the Working Group as part of the due diligence work, evidence of review and approval could not be found. 	<ul style="list-style-type: none"> — The Internal Control and Workflow has incorporated the recommendations made by RSM. — The Independent Board concurs with the findings of RSM and accepts the recommendations; and concurs with the management response and action plan. 	<ul style="list-style-type: none"> — Management has implemented the recommendations made by RSM.
<ul style="list-style-type: none"> — It should be stated clearly in the Internal Code that the Working Group should review and ensure that evidence of review and approval for all due diligence reports have been properly documented. 		

Observations and recommendations by RSM

Actions taken by the Company and recommendations by the Independent Board

Follow-up review by Baker Tilly

6. Possible lack of communication on related party issues in the management representation letter

— The Board meeting approving the financial statements and the annual report of the Company for the year ended 31 March 2004 did not document a discussion on the contents of the management representation letter, which specifically addressed particular issue on related party for drawing the management’s attention.

— The Directors should convene a meeting to discuss the management representation letter if it contained particular issues which needed further clarifications before approval. The Directors could in that case circulate the letter to senior management and each Director (including independent non-executive Directors) for advice.

— In relation to the Company’s financial statements for the year ended 31 March 2009, the Company’s auditors had a meeting with the audit committee to discuss audit matters and issued a letter to the audit committee to confirm matters discussed in the meeting.

— In relation to the Company’s financial statements for the year ended 31 March 2009, a management representation letter setting out a list of business parties who had transactions with the Group was provided to Directors to confirm whether they had relationship with such business parties. Minutes of the Board meeting held on 27 July 2009 shows that the Board had discussed, reviewed and approved the management representation letter prior to approving the financial statements.

— Management has implemented the recommendations made by RSM.

In addition to RSM's and Baker Tilly's reviews, the Independent Board has also investigated whether the 2004 Transaction and the 2007 Transaction were transacted on normal commercial terms and on arm's length basis with the Vendors. The Independent Board noted that:

- (a) the board committee formed for handling the 2004 Transaction and the 2007 Transaction comprised members who did not have an interest in the transactions, namely, Dr. Mao Yu Min and Mr. Ho Yu Ling. They handled and negotiated the terms and conditions of the transactions with the Vendors. Mr. Ho had not been involved in the negotiations for the 2004 Transaction and/or the 2007 Transaction;
- (b) the consideration for the 2004 Transaction and 2007 Transaction were determined with reference to the valuation reports on Smart Ascent and its subsidiaries (collectively, the "**Smart Ascent Group**") prepared by an independent professional valuer;
- (c) given the high transparency of the terms and conditions of the transactions disclosed to the public and the involvement of independent professional advisers (that is, the valuers, lawyers and corporate financial advisers) in the process, the Independent Board, in the absence of any evidence to the contrary, concluded that the transactions were transacted at arm's length and that the consideration were fair and reasonable and in the interests of the Company and its shareholders.

Conclusion by the Independent Board on its review on the 2004 Transaction and 2007 Transaction

The Independent Board is of the view that RSM's findings were internal control weaknesses in nature and related to the documentation of the due diligence and review process, rather than irregularities giving rise to the Incident.

To reduce the risk of misrepresentation or misunderstanding arising from miscommunication among the counterparties and the Group's management and Directors, the Independent Board recommends the Company to obtain written confirmations from the counterparties and Directors involved in the transaction at the inception stage of negotiation. While the effectiveness of its recommendations are based on a fundamental assumption that all such representations and confirmations are true and accurate and made by the relevant parties in good faith, and that written representations or confirmations may not be 100% effective against failure or inaccuracy in disclosure arising from willful, reckless or negligent misrepresentation or concealment by Directors, management and/or the counterparties to the transactions, further procedures for identifying possible and potential connected transactions as set out in the Internal Control and Workflow have been adopted by the Company. The Independent Board considers that the adoption of the above recommendations and the procedures set out in the Internal Control and Workflow will have deterrent effect against any such misconduct, and will increase the awareness of Directors and management in handling potential connected transactions.

(B) Other notifiable transactions of the Group during the four years ended 31 March 2007

Apart from the 2004 Transaction and 2007 Transaction, RSM had been engaged by the Company to review other notifiable transactions of the Group during the four years ended 31 March 2007 which have been disclosed by the Company pursuant to the requirements of Chapter 14 of the Listing Rules.

In this connection, a summary of the observations and recommendations made by RSM, actions taken by the Company, recommendations by the Independent Board and results of the follow-up review conducted by Baker Tilly are set out below:

Observations and recommendations by RSM	Actions taken by the Company and recommendations by the Independent Board	Follow-up review by Baker Tilly
1. No written workflow to guide the Working Group on processing of transactions		
— The Company had not maintained a written work flow guiding the members of the Working Group the workflow of processing any transaction.	— A detailed work manual has been set out in the Internal Control and Workflow.	— Management has implemented the recommendations made by RSM.
— The Board should prepare a detailed work manual for processing different kinds of transactions.	— The Independent Board considers that the Internal Control and Workflow is an effective measure for identifying possible and potential connected transactions.	

Observations and recommendations by RSM	Actions taken by the Company and recommendations by the Independent Board	Follow-up review by Baker Tilly
2. Lack of evidence of review and approval of documents	<ul style="list-style-type: none"> — The Internal Control and Workflow has incorporated the recommendations made by RSM. — The Independent Board concurs with the findings of RSM and accepts the recommendations. 	<ul style="list-style-type: none"> — Management has implemented the recommendations made by RSM.
<ul style="list-style-type: none"> — Reviewed works done by Working Group members and the approval thereof were not properly documented. — The Board should implement review and approval procedures for important documents in connection with every transaction. 		
3. Independent non-executive Directors could be more pro-active in giving advice on internal control matters	<ul style="list-style-type: none"> — The Company has engaged external professional consultants to conduct annual review on the Group's internal control system for each of the three years ended 31 March 2009 and intends to continue this practice. — The Independent Board comprises all the independent non-executive Directors, who are also members of the audit committee. The terms of reference of the audit committee have clearly defined its roles, among others, as to review and supervision over the financial reporting process and internal controls of the Group, which have been fully observed and complied by the members. 	<ul style="list-style-type: none"> — Given the size and scale of operations of the Group, the current practice of engaging external professionals to advise on internal control matters is considered adequate and appropriate.
<ul style="list-style-type: none"> — The first internal control review of the Group was performed in 2007 and no formal internal control review had been conducted prior thereto. — Independent non-executive Directors should proactively raise the need for review on all areas related to company's internal control, risk management and compliance matters on a timely basis. 		

**Observations and
recommendations by RSM**

**Actions taken by the
Company and
recommendations by the
Independent Board**

**Follow-up review by
Baker Tilly**

- The Independent Board is of the view that taking into consideration the size and scale of the operations of the Group, RSM's recommendations may not be practicable.
- Notwithstanding the above, the Independent Board has considered that their recommendations would provide a helpful insight to enhance the internal control procedures. The Independent Board considers that independent non-executive Directors should pro-actively review the Group's internal control system, risk management and compliance matters on an on-going basis and discuss with the Board if it identifies any weaknesses.

Observations and recommendations by RSM	Actions taken by the Company and recommendations by the Independent Board	Follow-up review by Baker Tilly
<p>4. Appointment of a connected person as financial controller was not formally approved by the Board</p>		
<ul style="list-style-type: none"> — The son of a former Director had joined the Company as executive Director in 2001. He then resigned and rejoined the Company in 2007 as financial controller. His appointment had not been approved in a formal Board meeting. — The Board should establish the Internal Code for appointment of connected persons as senior management and they should not be involved in any transaction before their appointments are approved by the Board. 	<ul style="list-style-type: none"> — A written guideline as to the appointment of senior management was adopted by the Company pursuant to a Board meeting on 20 December 2007. — The Independent Board concurs with the findings and accepted the recommendation of RSM. 	<ul style="list-style-type: none"> — Management has implemented the recommendations made by RSM.

Observations and recommendations by RSM	Actions taken by the Company and recommendations by the Independent Board	Follow-up review by Baker Tilly
<p>5. No engagement letter signed with legal advisers</p> <ul style="list-style-type: none"> — No engagement letter was signed with the Company’s legal advisers. — The Board should have a written engagement letter signed with legal advisers or agreed fee quotation for each engagement, stating clearly their scope of work, responsibilities and liabilities. 	<ul style="list-style-type: none"> — The Independent Board noted that despite there might not be a written mandate for each transaction, the scope of work of the Company’s legal advisers had been stated in their written quotations for each transaction. The Independent Board also understands that legal advisers owe a general duty of care to their clients irrespective of whether an engagement letter had been signed. — Nonetheless, the Company announced a written guideline in August 2009 requiring the signing of engagement letters with professional services providers, which shall state clearly, among others, the terms and scope of engagement. 	<ul style="list-style-type: none"> — Management has implemented the recommendations made by RSM.

(C) Review of other transactions by the Independent Board

The Independent Board conducted a review on certain other transactions of the Group for the five years ended 31 March 2008 to ascertain whether there were any other transactions entered into by the Group with similar issues as the 2004 Transaction and 2007 Transaction, that is, involving a connected person and subject to the reporting, announcement and/or independent shareholders' approval requirements under Chapter 14A of the Listing Rules, but in respect of which the Company had failed to comply with the relevant requirements under the Listing Rules.

Thresholds for transactions subject to review

In performing the review, the Independent Board has been explained that under Chapters 14 and 14A of the Listing Rules:

- (a) an acquisition of assets by the Group where the consideration includes shares of the Company and all percentage ratios (as defined under Rule 14.06 of the Listing Rules) are less than 5%, or a transaction or a series of transactions by the Group whereby any percentage ratio is 5% or more, shall be categorized as notifiable transaction under the Listing Rules and shall be subject to disclosure and/or shareholders' approval requirements under Chapter 14 of the Listing Rules; and
- (b) apart from the intra-group transactions and other exemptions available under Chapter 14A of the Listing Rules, a connected transaction is subject to announcement, reporting and/or independent shareholders' approval under Chapter 14A of the Listing Rules unless it is on normal commercial terms and (i) each of the percentage ratios (other than the profits ratio) is less than 0.1%; or (ii) each of the percentage ratios (other than the profits ratio) is equal to or more than 0.1% but less than 2.5% and the total consideration is less than HK\$1,000,000.

As the Group engages in a significant amount of transactions in its operations, some of which may involve relatively small monetary amounts, as a matter of practicality, the Independent Board was unable to review every single transaction entered into by the Group. Accordingly, the Independent Board limited its scope of review to "transactions" (falling within the definitions of the Listing Rules) made during the five years ended 31 March 2008, whereby any percentage ratio was 5% or more and could have been subject to disclosure and/or shareholders' approval requirements under Chapter 14 of the Listing Rules, while the de minimis amount of HK\$1,000,000 was used for deciding whether any connected transaction was exempt from the announcement, reporting and/or independent shareholders' approval under Chapter 14A of the Listing Rules.

Methodology of review

The Independent Board adopted the following methodology to investigate transactions falling within its scope of review:

- (a) a review of the notes to the accounts and disclosures made in the consolidated financial statements of the Group;
- (b) a review of the work schedules which comprised consolidation worksheets and working papers/financial data relating to the Company and its subsidiaries prepared for the consolidated financial statements of the Group, as certain transactions may have been aggregated in the published consolidated financial statements;
- (c) a review of the bank ledgers in relation to non-trading receipts and payments with value exceeding HK\$1,000,000;
- (d) a general review on the accounts by considering both quantitative and qualitative factors such as materiality in the context of the consolidated financial statements and the discloseable thresholds, volume of transactions, complexity and susceptibility to involve related parties;
- (e) in ascertaining whether connected parties were involved in the transactions, steps have been taken to:
 - (i) sort out transactions and/or series of transactions with value exceeding HK\$1,000,000;
 - (ii) ascertain the identity of counterparties by referring to the business contacts, financial publications, and other information sources such as their websites;
 - (iii) obtain an understanding of the business purpose of the transaction, considered the reasonableness of the amounts and whether the transaction was made on normal commercial terms, and considered their adequacy of disclosures in the accounts;
 - (iv) examine and review invoices, agreements and other pertinent documents, such as business registration documents; and
 - (v) make further enquiries with the management and obtained confirmations from Directors and substantial Shareholders as to the relationship with the counterparties at the relevant time, as far as possible.

The Independent Board had reviewed the following seven key types of transactions:

- (1) purchases and disposal of properties, plant and equipment;
- (2) purchases and disposal of companies, including subsidiaries, associates and jointly-controlled entities;

- (3) purchases and disposal of intangible assets;
- (4) obtaining borrowings or other financial assistance from persons other than banks and financial institutions;
- (5) redemption of promissory notes;
- (6) current accounts with directors/related companies/minority shareholders; and
- (7) consultancy fees paid/fees payable to third party service providers.

Conclusion by the Independent Board on its review on the other transactions

The Independent Board considered that, save for the transactions between the Group (excluding the Smart Ascent Group) and the Smart Ascent Group as explained below, their review did not reveal any transaction of the Group for the five years ended 31 March 2008 which had similar issues as the 2004 Transaction and 2007 Transaction, that is, involving a connected person and subject to the reporting, announcement and/or independent shareholders' approval requirements under Chapter 14A of the Listing Rules, but in respect of which the Company had failed to comply with the relevant requirements under the Listing Rules.

Transactions between the Smart Ascent Group and the Group (excluding the Smart Ascent Group)

As it had come to the attention of the Board in or around September 2007 that the Vendors of the 2004 Transaction were connected persons of the Company within the meaning of the Listing Rules, any transactions between the Group and the Smart Ascent Group (being non wholly owned subsidiaries of the Company that fall within the definition of "connected person" under Rule 14A.11(5) and (6) of the Listing Rules) might have constituted connected transactions subject to the disclosure and/or independent shareholders' approval requirements under Chapter 14A of the Listing Rules.

During the review by the Independent Board, it noted that during the three years ended 31 March 2007, Extrawell (BVI) Limited ("**Extrawell BVI**"), a wholly owned subsidiary of the Group, had advanced certain sums to Smart Ascent which should have been subject to the reporting and announcement requirements under Chapter 14A of the Listing Rules. The Board (including the independent non-executive Directors) considered the terms and conditions of the advances were fair and reasonable and in the interests of the Company and its shareholders as a whole.

To keep investors informed, the Company considered to issue an announcement in relation to the advances and submitted a draft announcement to the Stock Exchange for vetting in August 2009. The Company was notified by the Stock Exchange of its view that as each of the advances made by Extrawell BVI to Smart Ascent during the five years ended 31 March 2009 and the period from 1 April 2009 to 1 July 2009 had neither been made in the ordinary and usual course of business of the Group nor on normal commercial terms within the meaning of the Listing Rules (or better to

the Group), each of the aforesaid advances constituted a connected transaction which should have been subject to the reporting, announcement and independent shareholders' approval requirements under Chapter 14A of the Listing Rules.

To keep investors informed, the Company issued an announcement on 14 August 2009 to disclose particulars of past advances made by Extrawell BVI to Smart Ascent. The Company confirms that since 14 August 2009, the Group has not made any advances to Smart Ascent.

(D) General internal control review

Review by RSM

In response to the enquiry from the Stock Exchange in respect of the effectiveness of the Group's internal control system, the Company had engaged RSM to conduct an internal control review with respect to the financial, operation, compliance control and risk management functions and to assist the Independent Board to identify any weaknesses and deficiencies in the internal control system of the Group in order to provide an assurance to the Stock Exchange and the investing public that the Group's internal control system is in line with good governance practices.

RSM's review covered the key operations of the Group for the six months ended 30 September 2007, namely (i) operations of the Group's headquarters in Hong Kong ("**EHK**"), (ii) South Asia Pharmaceutical (China) Limited ("**EGZ**"), a subsidiary of the Company and (iii) Changchun Extrawell Pharmaceutical Co. Limited ("**ECC**"), a subsidiary of the Company in the PRC.

A summary of the observations and recommendations made by RSM, actions taken by the Company and recommendations by the Independent Board are set out below:

Observations and recommendations by RSM

Actions taken by the Company and recommendations by the Independent Board

Corporate internal control: control environment

1. Details of discussions on remuneration packages by the remuneration committee were not documented

— The remuneration committee should document the structure of remuneration packages with sufficient details.

— The Independent Board is of the view that it is the generally accepted practice for relevant background information to be set out in documents tabled for discussion and the minutes of the meeting to record resolutions passed at the meeting instead of full details of discussion. The Independent Board recommends the Company Secretary to include, where circumstances require, sufficient details of matters discussed in the minutes.

— Minutes of the remuneration committee meeting held on 20 December 2007 included sufficient details of matters discussed.

Observations and recommendations by RSM

Actions taken by the Company and recommendations by the Independent Board

2. No regular training on regulatory requirements for senior management, for example, the Listing Rules and requirements on connected transactions and continuing obligations

— On-going training should be provided to senior management, in particular those on new regulatory requirements.

— A seminar on directors' duties and responsibilities in a listed company was conducted for Board members by the Company's legal adviser on 7 July 2008. The Independent Board considers that the current training programs of the Company are appropriate for senior management and directors; including: (i) all new senior management members and directors will receive materials concerning their duties and responsibilities in a listed company, (ii) the company secretary will provide regular updates on changes in compliance and regulatory matters, (iii) in-house training courses will be conducted whenever necessary; and recommends external training courses to be arranged if necessary.

3. Certain functions in the Group's PRC subsidiaries operated independently from the Hong Kong headquarter; for instance, there was no centralized human resources function on a Group basis

— The Group should implement centralized human resources functions and business contingency plans to ensure adequate and consistent control in these areas.

— In view of (i) the additional costs for implementing the recommendation and size of the Group's business, compared to the benefits which may be brought by implementation of the recommendation, and (ii) difficulties in implementing a consistent "Group" approach because of the inevitable differences in capabilities and standards among business segments operating in different regions, the Independent Board agreed with the management's decision that it would not be practical to implement the recommendation for the time being.

Observations and recommendations by RSM

Actions taken by the Company and recommendations by the Independent Board

4. Terms and conditions were not clearly stated in agreement and absence of proper documentation

— Pursuant to an agreement between the Group and a PRC party (“**PRC Party**”), the PRC Party provided the Group with a right to carry out the pharmaceutical business in the PRC for a fixed fee, which would be reviewed in 2004. The following issues were noted: (i) although all transactions were recorded in the subsidiary’s books and records, the bank accounts were opened under the trade name of the PRC Party and all invoices were issued under such name. The agreement did not state clearly the detailed rights and responsibilities of the entities involved in the agreement; (ii) no payment had been made since 2004 and no provision on the fee has been made in the accounts. However, there was no written evidence of review or waiver of the fee.

— After reviewing the terms and conditions with the PRC Party, the Company should ensure that all such terms and conditions are included in the agreement to minimize unnecessary legal dispute and risk of inaccuracy on contingent liability.

— A new agreement has been entered into by the relevant parties pursuant to RSM’s recommendation.

Observations and recommendations by RSM

Actions taken by the Company and recommendations by the Independent Board

Corporate internal control: general computer controls

5. Internal control weaknesses in information security

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| <ul style="list-style-type: none">— EHK: The IT vendor, business development manager and assistant product manager shared the same log-in account and knew the password of the “administrator” account for the server maintained in the Hong Kong office. Each administrator should own its dedicated account with unique user identity.
— EHK: No log book was maintained for visits by outsourced IT Vendors. Log book should be maintained to record access to the Company’s computer server and application systems. All visitors must sign the log book.
— EHK: The account of a temporary staff who had left EHK had not been disabled. There should be proper maintenance on user accounts. The user account for resigned staff should be disabled in a timely manner.
— EHK: Each user of the accounting system could view other users’ account passwords. The Company should ensure that a system user does not have access to the passwords of other users.
— ECC: The account supervisor could create/modify a user account for access to the accounting system upon verbal approval by the finance manager. There should be proper documentation for application and approval of access to the accounting system. | <ul style="list-style-type: none">— Management has implemented the recommendations made by RSM. The Independent Board recommends management to closely monitor security and access of management information system as it contains valuable data. |
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Observations and recommendations by RSM

Actions taken by the Company and recommendations by the Independent Board

6. Lack of documented disaster recovery procedures and/or detailed system plans; no drill had been carried out on information system recovery plans
- There should be a properly documented and detailed disaster recovery plan for information system.
 - Drill should be carried out on a periodical basis to ensure that the disaster recovery plan operates properly.
7. Internal control weaknesses in backup maintenance
- EHK: Company should maintain a documented IT backup strategy.
 - EHK: Apart from the daily data backup which is kept for 7 days, the company should retain monthly data backup for accounting software separately.
 - EHK: A copy of the data backup was taken by the IT vendor to their office for safekeeping on an irregular basis, but retention of backup by outsourced IT vendor was not logged and acknowledged and the Group did not know which backup was kept by the outsourced IT vendor at a particular time. Company should maintain regular offsite backup and proper records on offsite backups.
 - ECC: No offsite backup for the accounting system. Company should maintain regular offsite backup and proper records on offsite backups.

Observations and recommendations by RSM

Actions taken by the Company and recommendations by the Independent Board

8. EGZ/ECC: Lack of authenticity documents for certain software installed on the Group's computers (*Note*)
- Management should ensure that there is proper authorization on all the software installed in computers. The management may also consider uninstalling unnecessary software or consider the use of other free application software.
 - Management was unable to confirm the authenticity of certain software installed on the Group's computers as it was unable to locate the relevant responsible persons of the outsourced IT vendors.
 - A software management policy has been implemented by the management to ensure that all new software will be legitimately acquired in the future. Although it is the general practice in the PRC to purchase computer hardware together with the software, to strengthen protection of the Group's interests, the Independent Board recommends management to ensure that details of software purchased are recorded in the relevant invoices.

Financial reporting and disclosure internal control

9. Evidence of review and approval process of consolidated financial statements and annual budgets was not retained
- There should be proper documentation on the review and approval of crucial reports such as financial statements and annual budgets.
 - Management has signed off management reports as evidence of review and approval.
10. Evidence of review of list of connected persons maintained by the Finance Department was not retained
- EHK: The Finance Department maintains a list of connected persons to facilitate the identification and timely disclosure of connected transactions and related party transactions. However, evidence of the review process was not retained. Evidence of review process of the list should be properly maintained.
 - Management has implemented the recommendations made by RSM.

Observations and recommendations by RSM

Actions taken by the Company and recommendations by the Independent Board

Internal control over business processes: revenue

11. EGZ: Terms and conditions stated in the Group's standard sales contract were very brief and vague; and no policy for obtaining legal opinion on terms and conditions stated in customers' form of contract

- The Company should ensure that sales contracts include all essential terms and do not contain unfavourable terms which may lead to inadequate protection of the Company's interest.
- Where practicable, customers should be persuaded to use the Company's standard sales contract. Where the customers' form of contract is used instead of the Group's standard contract, the Group should obtain legal opinion on the terms and conditions.

- The Independent Board is satisfied with measures undertaken by the management including: (i) contract terms have been reviewed by a PRC lawyer and a new contract form is used; (ii) management has endeavored to persuade customers to use the Group's form of contract where practicable; (iii) legal advice will be obtained on contractual terms where customers' forms of contracts are used if the management considers necessary; and (iv) contract terms are reviewed regularly by the management and PRC lawyer to ensure the Company's interests are protected.

12. EGZ: lack of proper record of blank sales contracts given to sales representatives and void contracts; and no register maintained on the use of the company stamp on contracts

- A register should be maintained on sales contracts based on pre-printed sequential numbers. Sales contracts which are void should be marked 'cancelled' and filed accordingly.
- A register should be maintained on the use of company stamp on contracts (with proper evidence on approval of use).

- Management has established a revised policy in accordance with the recommendations made by RSM.

Observations and recommendations by RSM

Actions taken by the Company and recommendations by the Independent Board

13. EGZ/ECC: No policy requirement for setting of customer credit limit, or credit limit was not set in practice in accordance with the policy requirements of the relevant subsidiary
- Credit limit should be assigned to all customers on credit sales.
 - Management has implemented the recommendations made by RSM. The Independent Board also recommends the Company to review credit terms regularly.
14. ECC: No periodic reconciliation of accounts directly carried out by Finance Department with all customers
- The Finance Department should obtain written confirmation and perform reconciliation of accounts receivable directly with all customers on a periodic basis. If it is impractical to perform reconciliation with all customers every month due to the large number of customers, reconciliation of accounts receivable should be performed on all customers on rotation basis. Written evidence of customers' confirmation and reconciliation of accounts receivable should be retained.
 - The Independent Board agrees with the management's view that it is more cost effective to perform reconciliation with major customers at the end of the financial year. The accounts of ECC for the calendar year and the Group's financial year ended 31 March are subject to audit, which management considers to be adequate for internal control purposes. It is also the practice of ECC to perform reconciliation with customers prior to settlement of their accounts receivable in order to ascertain the relevant invoices and the corresponding amount to be paid. It is not practical to obtain customers' written confirmation monthly in China due to the prevailing business practices. The Independent Board concurs with the management's decision not to implement the recommendation for the time being.

Observations and recommendations by RSM

Actions taken by the Company and recommendations by the Independent Board

Internal control over business processes: expenditure

15. ECC: No proper documentary evidence retained for the whole supplier selection process

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| — There should be proper documentation on supplier selection process. | — Management has implemented the recommendations made by RSM. |
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16. ECC: Inadequate documentation on procurement function

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| — Procurement function is performed according to approved purchase requisition forms. However, there is no sequential numbering on the forms. The forms should be sequentially numbered. | — A register has been maintained in addition to indexing the purchase requisition forms. |
| — Procurement/ordering is carried out and confirmed orally with suppliers and there is no proper documentation on the details of procurement activities. There should be proper documentation to record details of each purchase. | — It is the mutually agreed practice with vendors to make verbal purchase orders to reduce administration costs. Letters of intent specifying major trading terms are signed with major vendors once a year and a follow-up register is established to monitor corresponding verbal purchase orders. A new letter of intent will be signed for any variance in the terms of supply. The Independent Board recommends the management to adopt the best practice of issuing written purchase orders as far as possible and evaluate the acceptance of such practice by the vendors from time to time. |

Internal control over business processes: inventory

17. ECC: Goods receipt notes were not always timely issued in accordance with the Group's policy

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| — Goods receipt notes should be timely issued. | — Management has implemented the recommendations made by RSM. |
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Observations and recommendations by RSM

Actions taken by the Company and recommendations by the Independent Board

18. ECC: Inadequate documentation on processing and recording inventory movement

- The quantity stated on goods delivery notes issued by the head of the respective production line sometimes exceeded the quantity stated on the corresponding production order. No written documents were provided to evidence the discrepancy was properly monitored and approved by the supervisor of the head of production line. Management should establish guidance regarding issuance of delivery notes and significant discrepancy between the daily production order and delivery notes should be properly investigated, monitored and approved.
- No sequential numbering was assigned for delivery notes of raw materials, subsidiary materials and packing materials. Delivery notes should be sequentially pre-numbered.
- A register has been maintained in addition to indexing the delivery notes, and discrepancies between the quantity stated on delivery notes and the corresponding production order will be noted on the production order and excessive quantity will be returned to the warehouse. Discrepancies are monitored and approved by the head of production line. The Independent Board considers that the above measures are adequate.

19. ECC: No formal policy on safety stock level to ensure that stock in hand could meet production demand

- Management should establish a formal policy regarding the maintenance of safety stock level. Any significant difference between original purchase requisition and material received should be properly monitored and timely resolved/ reported to the relevant management.
- Management has reviewed stock level critically. Given the nature of the Group's product and perishable nature of raw materials (animal's spleen), production is made according to customers' orders. The Independent Board concurs with the management's view that the current practice of maintaining minimal stock level is appropriate.

Observations and recommendations by RSM

Actions taken by the Company and recommendations by the Independent Board

20. ECC: No insurance coverage for inventory

- The company should establish a policy for inventory insurance coverage and obtain insurance coverage on its inventory. The Finance Department should also closely monitor the adequacy of insurance coverage.
- Management has purchased insurance for its inventory maintained at the plant as recommended, and will maintain adequate inventory insurance coverage in the future.

21. ECC: Internal control weaknesses in stock-taking

- Although the Company has established a stock-taking policy, there was no detailed written instruction or procedure. The Company should set up detailed written instruction and guidance regarding stock-taking.
- No stock-taking policy for stocks maintained by subsidiary sales offices and no stock-take for such stocks. The stock-taking policy should be revised to include stocks kept by subsidiary sales offices and periodical stock-take should include such stocks held by subsidiary sales offices.
- Count sheets for raw materials and packing materials did not contain details of physical count results and explanation on major discrepancies. The Company should revise existing count sheets for raw materials and packing materials.
- No accounting adjustment was made for discrepancy between physical count result and accounting record. Any major discrepancy should be timely investigated and reported to the Finance Department for accounting adjustment upon approval by management.
- The Group's financial controller attended the stock-taking at ECC for the year ended 31 March 2009. In respect of GMP standards, ECC has maintained perpetual inventory control and a control system which records details of receipt, delivery and available balance of each stock item. The Independent Board concurs with the management's view that the existing stock-taking policy, though simple, is adequate for audit purpose.
- Stock-taking at sales offices is carried out in July and December of each year instead of the Group's financial year end at 31 March. The Independent Board recommends management to consider arranging stock-taking for principal sales offices at the Group's financial year end as well.

Observations and recommendations by RSM

Actions taken by the Company and recommendations by the Independent Board

Internal control over business processes: human resources and payroll

22. No employment contract during probation period and documents on background check were not retained

- EGZ: No employment contract was signed with new staff until they passed probation period and became the company's permanent staff. The Company should sign an employment contract with new staff upon employment.
- EGZ/ECC: The company should keep verification documents on background check of candidates.

- Employment contracts would be signed with new staff after probation period to minimize administration costs and workload resulting from high staff turnover rate. Nevertheless, the management has considered to use a standardized document to confirm terms of employment for new staff prior to signing of formal employment contract to balance the cost and dispute concern.
- Evidence of background check is maintained in personal files of newly recruited employees.

23. EGZ/ECC: Calculating payroll for social insurance

- According to the relevant requirements in the PRC, social insurance contributions should be made based on the employee's last year monthly average income. However, the Group had pre-determined fixed base figures in calculating the amount of social insurance premiums.
- Management was advised to revisit the practice and seek necessary legal/professional opinion in making monthly social insurance contributions.

- The Independent Board understands that management has adopted the general prevailing market practice to use the base salary for calculating social insurance premiums as this would significantly reduce the Company's workload. Although the Group would not comply with local regulatory requirements in full, the employees have agreed that the company could compensate them by improved staff benefits. The Independent Board has concurred with the management's view considering the generally acceptable prevailing practices in China. Notwithstanding that, the accounts have already fully provided for the shortfall of any social insurance premium contributed by the Group.

**Observations and recommendations by
RSM**

**Actions taken by the Company and
recommendations by the Independent Board**

Internal control over business processes: fixed assets

24. ECC: Inadequate documentation and policy for acquisitions of fixed assets

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| <ul style="list-style-type: none">— Records of quotations obtained for acquisitions of fixed assets were not retained. Proper documentation should be retained as evidence of comparisons made.
— The practice of obtaining three quotations before an acquisition was not incorporated as a formal requirement in ECC's fixed assets policy. Formal policies and forms should be established, thereby standardizing the requirements for quotation request, criteria for price comparison, principles for negotiation, etc. | <ul style="list-style-type: none">— Management has revised ECC's policy in accordance with the recommendation made by RSM. |
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25. EGZ/ECC: Existing policy on fixed assets did not include a detailed policy and procedure for disposal of fixed assets

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| <ul style="list-style-type: none">— According to ECC's management, there had been no scrapping of fixed assets in the past, and certain fixed assets which were no longer in use may need to be scrapped. Management should include a detailed policy and procedure on handling of scrap and specify frequency of review on the fixed assets value. | <ul style="list-style-type: none">— Management has revised the policy in accordance with the recommendation made by RSM. |
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Observations and recommendations by RSM

Actions taken by the Company and recommendations by the Independent Board

Internal control over business processes: business contingency plan

26. ECC: no business contingency plan

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| — The disaster recovery plans for EHK and EGZ include business contingency planning, but ECC has not established any business contingency plan for its operation. A complete, detailed and feasible business contingency plan should be set up for the operations of ECC. | — Management has revised its disaster recovery plan on a Group basis, while ECC has also prepared its disaster recovery plan for its operations. |
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Note: It is noted in Baker Tilly's follow-up review that the cost of acquiring the relevant software licenses may be high. However, without proper supporting documents to help prove ownership of the software license, the Group may not have access to the necessary technical support in the event of virus attack. Baker Tilly recommended management to review the requirements of the Group's business operations and identified if there was a need to acquire additional licensed software by the business unit. In the future, the Group's business unit should include both hardware cost and software cost in its budget plan when purchasing computers. Management should establish a schedule for replacing old computers which are not compatible with the latest software and lack software licensing documents. The Group should also establish a software management policy to ensure that all software is properly supported by valid software license. Management will implement Baker Tilly's recommendation in the financial year commencing 1 April 2010. The Group's business unit will ensure that all desktop computers purchased in the future should have valid software license for all software installed on the computers.

Follow-up review by Baker Tilly

Based on the follow-up review conducted by Baker Tilly for the period from October 2008 to May 2009 and the second review for the period from May 2009 to August 2009, Baker Tilly concluded that the Company had set up a sound and effective internal control mechanism and had taken appropriate actions and remedies as to the findings made by RSM in accordance with their level of threats to the operations of the Company, with room for improvement on authentication of software license as explained above. Management will implement Baker Tilly's recommendation in the financial year commencing 1 April 2010.

(E) Conclusion

The Independent Board is of the opinion that the overall system of internal controls and business risk management of the Group is adequate for the size and the nature of business of the Group, and has concurred with the view of the audit committee and the Board that the key areas of the

Group's internal control systems are reasonably implemented. The Independent Board is satisfied that circumstances no longer exist to suggest that there may be significant deficiencies in the internal control system of the Group which will pose a risk to investors.

THE INCIDENT

Based on publicly available information, the Company understands that Mr. Ho, a former Director, had pleaded guilty to and had been convicted of the offence of fraud, contrary to section 16A of the Theft Ordinance (Chapter 210 of the Laws of Hong Kong) in relation to the 2004 Transaction. According to publicly available information, it had been admitted by Mr. Ho that he concealed or failed to disclose the relationship between him and the Vendors and that Smart Ascent was controlled by him.

The Company also notes that certain other charges against Mr. Ho, to which Mr. Ho pleaded not guilty, were not proceeded with and the judge of the District Court of Hong Kong ordered these charges to be left on file.

Mr. Ho Yu Ling, another former Director, had also been charged by the ICAC in relation to the 2004 Transaction. Mr. Ho Yu Ling was subsequently acquitted of the charges against him.

The Board confirms that apart from Mr. Ho himself, at all material times when the 2004 Transaction and 2007 Transaction were entered into, none of the Board members were aware of Mr. Ho's interest in those transactions nor that the Vendors were connected persons to the Company.

At the request of the Board, Mr. Ho had refrained from being involved in any management and/or daily operation and administration of the Group since his arrest by the ICAC on 20 September 2007 until his resignation as Director on 12 March 2009. Mr. Ho had over 30 years' business experience in China and other Asian countries and, coupled with his well-established business relationship with Chinese government authorities and business contacts, he had helped the Group build up strategic corporate partners and enhanced the Group's relationship with investors, government authorities and business partners. Mr. Ho's well-established network and extensive knowledge in the PRC pharmaceutical field had also facilitated the Group in drug licensing and registration renewal. His contacts with hospitals had helped the Group keep abreast of relevant product and market information and enhance customer base. To minimise the risk of disruption to the Group's business as a result of his resignation as a Director, as a transitional arrangement, the Group retained Mr. Ho as a consultant during the period from April 2009 to 16 November 2009.

During his engagement as a consultant to the Group, Mr. Ho's role and participation was as follows:

- to give advice on the business development of the Group at the request of the Group's management. As an example, during his engagement as the Group's consultant, Mr. Ho had advised the Group regarding the Group's participation in the national medical insurance program, making analysis as to the pros and cons for the Group to participate in the program; and

- to introduce his business, hospital and government contacts to the Group, with an aim to enhancing the Group's distribution network in light of the pharmaceutical reforms. During the period from April to September 2009, Mr. Ho had introduced his business and government contacts to the Group's management in Beijing and Shanghai.

Mr. Ho Yu Ling had also performed his management roles and duties in the Group until he was charged by the ICAC in January 2008. He retired from the Working Committee immediately after he was charged. From January 2008 until his retirement as Director on 30 September 2008, his daily management functions were undertaken by other executive Directors. The Group had engaged Mr Ho Yu Ling as a consultant to the Group after his retirement as Director to provide assistance to the Board in overseeing the daily administration of the Group's Hong Kong office, and to provide business advice for the Group's business from time to time. His appointment for an initial term of one year from 1 October 2008 has been renewed for a further term of one year with effect from 1 October 2009.

The Board considers that the above appointments enabled the Board and the senior management of the Group to maintain the decision-making and daily operation and management of the Group's business free from interference by Mr. Ho and Mr. Ho Yu Ling pending completion of their respective legal proceedings, and to minimise the disruption to the Group's business by their cessation to act as Directors.

FURTHER INFORMATION

(a) Classification of a PRC Company as unrelated party under HKAS 24

As set out in the Company's annual report for the year ended 31 March 2008, the Group had various transactions with the Domestic Company, a company established in the People's Republic of China, during the year. RSM CPA, the Group's auditor for the financial year ended 31 March 2008, expressed a disclaimer of opinion in its independent auditor's report as to the appropriateness of the classification of the Domestic Company as an unrelated party in accordance with HKAS 24.

The Group has made various arrangements with the Domestic Company to enable it to act as a coordinator for the Group in respect of trading transactions between the Group and its end customers in the PRC on one hand, and for the Group to closely monitor its customer-services to its end customers. Apart from coordinating the Group's trading transactions in the PRC, the Directors note that the Domestic Company has its own businesses and therefore it is not feasible for the Group to exert any control or significant influence over the Domestic Company's financial or operating policies.

To ascertain whether the Domestic Company is an entity independent from the Group, the following actions have been taken:

- (i) the Group has obtained information relating to the shareholders, legal representative and key management personnel of the Domestic Company by conducting independent company searches and collecting other corporate information and documents from the Domestic

Company, to ascertain whether there may be any relationship between the Domestic Company, its legal representative, shareholders or key management personnel with any member of the Group, the Group's directors and key management personnel which may give rise to a related party relationship;

- (ii) in preparing for the Group's 2008 annual results, the Group had reconfirmed the background information with the Domestic Company, including information relating to its shareholders, legal representative and key management personnel, in order to identify any related party relationship;
- (iii) to prepare for the Group's 2009 annual results and to assist the Independent Board in reviewing the Domestic Company's background, an executive Director had visited the Domestic Company again and had obtained oral confirmations from its legal representative and shareholders that none of them or any senior management of the Domestic Company had been a connected person/related party of the Company. The Domestic Company does not have any director;
- (iv) in 2009, the Group had obtained a written confirmation from the Domestic Company signed by its legal representative, confirming that none of its shareholders, legal representative and the senior management had any family or shareholding relationship with the Group's directors and senior management.

As the cooperation arrangements between the Domestic Company and the Company are on a continuing basis, the Group's officers are in contact with the Domestic Company regularly. The Domestic Company is requested to inform the Group of any changes in its shareholding, legal representative and key management personnel. The name of the legal representative of the Domestic Company is also shown on its business license, which is readily available for inspection at its office. The relevant officers of the Group are required to report any relevant changes to the company secretary and Finance Department of the Company, who will alert the Board if necessary.

To the best knowledge of the Directors, (a) the Domestic Company is not a connected person (as defined under the Listing Rules) of the Company and does not have any relationship with connected persons of the Company; (b) neither the Domestic Company nor any of its legal representative, shareholders or the key management personnel has any relationship with any member of the Group, its directors and key management personnel that may otherwise constitute a related party relationship between the Group and the Domestic Company under HKAS 24.

The Company will continue to monitor the Company's transactions in accordance with the procedures for identifying possible and potential connected transactions set forth in the Internal Control and Workflow. For the purpose of complying with the disclosure requirements of HKAS24, the Company will also follow its prescribed procedures to identify and confirm related parties.

(b) Recoverability of intangible assets and other receivable

As disclosed in the Company's annual report for the year ended 31 March 2009, the Group's intangible assets as at 31 March 2009 included a technological know-how ("**Know-how**") with a carrying value of about HK\$284.3 million in relation to an oral insulin product developed by Fosse Bio in collaboration with Tsinghua University and the exclusive right for the commercialization of the Product. In an appraisal conducted by an independent professional valuer, the Know-how was valued at an amount that was no less than HK\$284,260,000 as at 31 March 2009. Notwithstanding the valuation, the recoverability of the carrying value of the Know-how is uncertain as it depends upon the result of the clinical trial and successful launching of the Product.

Pursuant to the 2004 Agreement, the Vendors had jointly and severally undertaken to the Group that they would be responsible to pay in full the outstanding purchase price ("**Outstanding Purchase Price**") of HK\$31.78 million payable by Smart Ascent for its acquisition of 51% interest in Fosse Bio, together with all costs (including legal costs), expenses or other liabilities which any of Smart Ascent or Extrawell BVI may incur in connection with the payment of the Outstanding Purchase Price (collectively, the "**Outstanding Amount**") for and on behalf of Smart Ascent if and when it becomes payable by Smart Ascent. The Receivable represents the Outstanding Purchase Price and is secured by the pledge of Mr. Ong's 49% equity interest in the issued share capital of Smart Ascent in favour of Extrawell BVI. Since the Know-how is the only major asset of Fosse Bio, which in turn is the only investment of Smart Ascent, the value of the pledged 49% equity interest of Smart Ascent is uncertain as it also depends upon the result of the clinical trial and successful launching of the Product.

On 30 April 2008, the State Food and Drug Administration of the PRC ("**SFDA**") granted approval to Fosse Bio and Tsinghua University, Beijing to undertake further clinical trial of the Product. In the said approval, the SFDA imposed more stringent requirements in respect of the next phase clinical trial compared to the phase II clinical trial. As at the date of this announcement, the Group has been deploying resources in consolidating and making adjustments for the best implementation plan having sought consultation and advice from experts and officials of SFDA. The management believes that the revised plan will provide a more solid foundation for clinical trial data, which will enhance and benefit future assessments by the SFDA for granting approval. It is expected that the further clinical trial will commence in March 2010, and that it will be completed and the report thereof will be prepared for approval by the SFDA by end of 2010. However, such further clinical trial is subject to evaluation and queries by SFDA and it is possible that the SFDA may not approve the manufacturing and distribution of the Product.

There is a risk that Fosse Bio may not be able to obtain all licences, certificates and permits from the relevant regulatory authorities in the PRC required for formal production and distribution of the Product.

Should Fosse Bio fail to obtain the necessary approvals from the relevant authorities, it may not be able to commence the production and distribution of the Product in the PRC, which could have material and adverse impact on the business and financial results of Fosse Bio, and in turn the Group's business and financial results. The Group may also have to write-off or suffer impairment on the carrying values of the Know-how and the Receivable.

Pursuant to the 2007 Agreement, the consideration of HK\$768.9 million for the 2007 Transaction shall be paid by Extrawell BVI to Mr Ong in two instalments. The second instalment, representing an amount of HK\$69.201 million, shall be payable only after the Outstanding Amount has been settled in full or Mr Ong has paid to the Group in cash an amount equivalent to the Outstanding Amount for payment of the Outstanding Purchase Price. The Board considers that the aforesaid arrangement would enable the Company to recover the Receivable in the event that it proceeds with the 2007 Transaction.

As disclosed in the Company's annual report for the year ended 31 March 2009, the Group's intangible assets as at 31 March 2009 also comprised a technological know-how of approximately HK\$1.4 million in relation to the manufacture and sales of pharmaceutical products held by a subsidiary of the Company. The Directors conducted an annual assessment on the recoverable amount of the technological know-how and considered that no further provision for impairment was required for the year.

(c) Status of the 2007 Transaction

As disclosed in the circular of the Company dated 21 May 2009 in respect of the ratification actions for 2004 Transaction, completion of the 2007 Agreement is conditional upon the satisfaction or, as the case may be, waiver of the conditions precedent stated therein, on or before 12:00 noon on 31 October 2007 or such later date (the "Long Stop Date") as the Group may agree.

As at the date of this announcement, the Board has not yet decided on whether (i) to extend the Long Stop Date and proceed with the 2007 Acquisition on the same terms and conditions (other than the Long Stop Date) as set out in the 2007 Agreement, or (ii) to re-negotiate with Mr. Ong on an arm's length basis on the terms and conditions for such acquisition.

There is no assurance that the Group will proceed with the 2007 Transaction and, if the 2007 Transaction proceeds, there is no assurance that such acquisition will be on the same terms and conditions as set out in the 2007 Agreement. The Company will make further announcement in respect of the status of such acquisition pursuant to the Listing Rules as and when required. Shareholders and prospective investors should exercise caution when dealing in Shares.

RESUMPTION OF TRADING

At the direction of the Stock Exchange, trading in the Shares on the Stock Exchange was suspended with effect from 10:12 a.m. on 20 September 2007. The Company has made an application to the Stock Exchange for the resumption of trading in the Shares with effect from 9:30 a.m. on 24 December 2009.

By order of the Board
Extrawell Pharmaceutical Holdings Limited
Mao Yu Min
Chairman

Hong Kong, 23 December 2009

As at the date of this announcement, the executive directors are Dr Mao Yu Min, Dr Xie Yi, Dr Lou Yi and Ms Wong Sau Kuen and the independent non-executive directors are Mr Fang Lin Hu, Mr Xue Jing Lun and Ms Jin Song.

* *For identification purpose only*