

**ASIA FASHION HOLDINGS LIMITED**  
(Company Registration No. 41195)  
(Incorporated in Bermuda)

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**QUALIFIED OPINION BY INDEPENDENT AUDITOR ON FINANCIAL STATEMENTS**

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**A. INTRODUCTION**

Pursuant to Rule 704(5) of the Listing Manual of the Singapore Exchange Securities Trading Limited ("**SGX-ST**"), the Board of Directors (the "**Board**") of Asia Fashion Holdings Limited (the "**Company**") wishes to inform its shareholders ("**Shareholders**") that the independent external auditors of the Company, Foo Kon Tan LLP ("**Independent Auditor**"), has, in its Independent Auditor's report dated 8 June 2015 ("**Report**"), included a qualified opinion on the financial statements of the Company and its subsidiaries ("**Group**") for the financial year ended 31 December 2014 ("**FY2014**").

A copy of the Report and the extracts of Note 2(a) (referred to in the Report) to the financial statements of the Group are annexed hereto as "**Annex A**" for shareholders' information.

Shareholders are advised to read the Annual Report for FY2014 of the Company, which will be despatched to Shareholders shortly, for more details.

**B. RESPONSE TO BASIS OF QUALIFICATION**

The Board wishes to respond to the qualified opinion in the Report as follows:

**1. Inability to ascertain the appropriateness of compensation claims and opening balances of the Group**

As stated by the Independent Auditor, these compensation claims ("**Compensation Claims**") relate to the operations of the group comprising Qianfeng International Limited and its subsidiaries (namely, Fujian Qianfeng Textile Technology Company Limited and Fujian Jiamei Textile Company Limited) (collectively the "**Disposed Group**"), which had been disposed by the Group on 3 February 2015 (the "**Disposal**").

The Board is of the view that the Compensation Claims are isolated and non-recurring in nature, relating specifically to the Disposed Group, and that they would not affect the future operations as well as the operating results of the Group from FY2015 onwards for the following reasons:

- (1) In connection with the settlement of these Compensation Claims, the Company had obtained appropriate legal and financial advice. In this regard, as announced by the Company on 14 August 2014, Dacheng Law Offices had issued a legal opinion (the "**Dacheng Legal Opinion**") in respect of the issues identified in respect of the Compensation Claims. A copy of the Dacheng Legal Opinion is attached hereto as "**Annex B**".

- (2) As announced by the Company on 28 March 2014, in connection with arbitration proceedings initiated by the claimants pursuant to the Compensation Claims, the arbitrators had confirmed that the terms of the settlement agreements were valid and enforceable. The final arbitration verdict also confirmed that the settlement amounts are final and that the claimants may not lodge any further compensation claims against the Disposed Group.
- (3) Furthermore, as announced by the Company previously, the Group has enhanced its internal control policies and corporate governance practices, and has taken all necessary and appropriate measures to work towards avoiding the recurrence of similar issues in the current business of the Company as carried on by Rich Circles Enterprise Limited (“**Rich Circles**”) and its subsidiaries, namely China Construction Material (Hong Kong) Limited (“**CCMH**”), Zhongchuang (Xuzhou) Construction Material Co., Ltd. and Xuzhou Zhongwei Tonghao New Board Co., Ltd (“**Xuzhou Zhongwei**”) (collectively, the “**Rich Circles Group**”).
- (4) In connection with the Disposal, under the sale and purchase agreement (“**SPA**”) dated 18 September 2014 and entered into between the Company as vendor, Chengde Industrial Co., Limited as purchaser and Lin Daoqin as obligor (the “**Obligor**”) in relation to the Disposal, the Obligor had undertaken to keep the Company fully and effectively indemnified against any and all losses that the Company may incur or suffer in connection with or arising from (a) any default by the Obligor of any of his obligations under the SPA and/or (b) any proceeding against the Company brought by the purchaser and/or any third party arising out of the SPA or any such breach or default referred to in paragraph (a) above (the “**Obligor Undertaking**”).
- (5) As such, the financial statements of the Group for its financial year ending 31 December 2015 (“**FY2015**”) should no longer be affected by the Compensation Claims as they have no relevance or application to the Group’s current business and the Rich Circles Group, being connected solely with the Disposed Group. Further to the Disposal, the Compensation Claims should not affect the accuracy of the Company’s accounts and its FY2015 financial statements, nor are they expected to have any adverse impact on the financial position of the Group for FY2015.

Therefore, the Board is highly confident that the Compensation Claims are an isolated incident and would not have any impact on the financial performance and operating results of the Group for FY2015.

## **2. Discontinued Operations of the Disposed Group**

As stated by the Independent Auditor and as mentioned in Note 28 to the financial statements, during FY2014, the Company entered into the SPA to sell the Disposed Group for an aggregate consideration of S\$2.4 million (approximately RMB 11 million).

The Board had disposed of the Disposed Group, comprising of financially weak and unprofitable subsidiaries that were not core to the Group’s future, in order to conserve cash for its current profit-making business and to release the Company from tremendous pressure in continuously providing the

Disposed Group with additional working capital to cope with its foreseeable downturn in business and loss making situation. Based on the report by the independent valuer engaged by the Company in connection with the Disposal, the valuation indicated that the Disposed Group carried a negative investment value and that the business goodwill of the Disposed Group had been completely eroded due to the Compensation Claims. The Disposal would enable the Company to obtain cash consideration of S\$2.4 million in return for disposing of a business which is highly likely to continue performing poorly in the future.

However, further to the Disposal and as noted by the Independent Auditor, the Company was initially denied access to the accounting and other records of the Disposal Group by its new owner, Chengde Industrial Co. Limited, and since the effective date of the said Disposal on 3 February 2015, the Independent Auditor was unable to carry out procedures necessary to satisfy itself as to the validity and appropriateness of the carrying values of the assets and liabilities associated with the Disposal Group (which were classified in the balance sheet of the Company as assets and liabilities held-for-sale as at 31 December 2014) and of the net results of the discontinued operations (“**Discontinued Operations**”) of the Disposal Group for the year ended on that date. The Board understands that access to the records of the Disposed Group was initially denied because Chengde Industrial Co. Limited. was in the process of completing its own internal auditing and accounting review. In addition, Management recently understands from Chengde Industrial Co. Limited., that the books and records of certain entities in the Disposal Group were retained by the PRC authorities for their review and examination, and accordingly such books and records could not be made available for audit and review purposes to the Company or to the Independent Auditor. The Independent Auditor was also unable to perform other alternative audit procedures to satisfy itself with respect to these said transactions and balances. As a result of the above, the Independent Auditor was unable to determine the adjustments, if any, and/or disclosures to be made to the FY2014 financial statements.

The Board is of the view that this would not impact the financial statements of the Group for FY2015 as Management had already reported the results of the Discontinued Operations for FY2014 based on the information provided by the Disposed Group when it was still part of the Group. Management had calculated the gain/loss from the Disposal based on this same information. Even though these amounts could not be verified by the Independent Auditor after the Disposal for the reasons stated above, they had been reviewed by the Independent Auditor while the Discontinued Operations were still part of the Group. Management and the Board therefore believe that the truth and fairness of the operating results presented by the Group for FY2014 has not been materially affected by the Independent Auditor’s failure to gain access to the accounting and other records of the Disposal Group.

**3. Inability to be satisfied on the completeness and appropriateness of the provision for compensation to distributors amounting to approximately RMB 8.6 million and provision for minimum guaranteed royalty amounting to approximately RMB 5.3 million as at 31 December 2014**

In the Report, the Independent Auditor indicated that it was not able to obtain independent confirmations or conduct alternative procedures to ascertain if these balances were properly stated as at 31 December 2014.

The Board is of the view that in connection with the Obligor Undertaking, which is binding and legally enforceable, the amount of contingent liabilities had already been fully provided for in the financial statements of the Group for its financial year ended 31 December 2013 and 31 December 2014 respectively. As such, there should be no adverse impact to the Company's operating results for FY2015. On the contrary, as there have been no claims against the Company from these distributors up to the date of this announcement, in light of the Obligor Undertaking, Management is seeking professional advice on the appropriateness and legality of writing back these provisions in the Company's financial results for FY2015.

#### **4. Unverified Transactions Pertaining to the Associated Company**

In the Report, the Independent Auditor indicated that it was not able to gain access to sufficient documentation that will adequately support certain transactions recorded in the accounting books of the Company and the Rich Circles Group. These transactions relate to the appropriateness of the share of results of Rich Circles Group by the Group and the goodwill arising from the acquisition of the entire interest of CCMH and its subsidiaries by Rich Circles on 27 June 2014.

The major transactions in this section relate to the lack of issuance and receipt of local PRC sale and purchases VAT invoices respectively. This is expected to be fully rectified by CCMH and its subsidiaries on or before 30 June 2015 pursuant to an official agreement with the local tax authority. Management is confident that the rectification can be completed as scheduled.

#### **5. Going Concern**

On the basis detailed in Note 2(a) to the financial statements of the Group relating to the going concern assumptions, the Board believes that the Group and the Company have adequate resources to pay their debts as and when they fall due and continue to operate as going concerns within the next twelve months after the end of the reporting period for the following reasons:

- (1) Subsequent to 31 December 2014, the Company has completed two placement exercises and has raised additional capital of approximately S\$6.43 million, thereby substantially reducing the Company's deficit in shareholders' funds from RMB 38.1 million to RMB 8.1 million.
- (2) The Company is exploring the conversion of its convertible bonds into shares in the capital of the Company. This would further enable the Company to maintain a healthy positive capital position.
- (3) In respect of its cash operating fund, the Company has raised a total net proceeds of approximately RMB 42 million through the issuance of new shares and convertible bonds. As a result, the Company has kept a strong and healthy cash position subsequent to FY2014.
- (4) In preparing the financial statements, the Board has taken into account all information currently available to them in relation to these uncertainties. As at the date of this Announcement, the Board strongly believes that there is no significant uncertainty that financial support will continue be available to the Group and the Company.

## 6. Recoverability of Loans

As stated in the Report, the Independent Auditor was unable to ascertain the recoverability of the shareholders' loan made by the Company to Rich Circles of RMB 49 million together with accrued interest thereon, which is repayable on 18 June 2016.

The Company will continually evaluate its financial position and explore alternatives, such as the capitalisation of such shareholders' loans together with Ms. Li Yaxin, the other major shareholder of Rich Circles, who has also granted a loan of RMB 51 Million to Rich Circles under the same terms as the loan extended by the Company. Such capitalization will remove any doubts as to the recoverability of these loans and will strengthen the capital base of Rich Circles .

## C. FURTHER RESPONSE OF THE BOARD ON THE REPORT

The Board refers to the classification by the Independent Auditor of Rich Circles in Note 8 of the Report as an "associated company" instead of a "subsidiary".

As announced by the Company in its circular to Shareholders in relation to the Disposal ("**Circular**") dated 9 January 2015, the Company had in August 2014 engaged in discussions with the Independent Auditor on the accounting treatment of Rich Circles Group. The Independent Auditor advised the Company that pursuant to FRS 110, the Company is required to consolidate the results of the Rich Circles Group into the Group's financial statements if the Company factually has operational control of the Rich Circles Group. As the Company viewed that it had operational control over the Rich Circles Group, for greater disclosure and in accordance with the advice from its Independent Auditor, the Company thereafter consolidated the results of Rich Circles Group into the Group's financial statements for FY2014 and for the first quarter ended 31 March 2015.

However, in the Report, the Independent Auditor disagreed with the Company's view and concluded that the Company did not factually control the Rich Circles Group. In this regard, the Board wishes to respond to the Independent Auditor's conclusions as follows:

### 1. The Company did not have power over the investee

The Independent Auditor concluded in its Report that the Company did not have sufficient voting rights to have power over Rich Circles as it only has 49% of the voting rights. In addition, it has not effectively exercised its rights to direct the relevant activities of Rich Circles.

However, while the Board accepts and respects the fact that the Independent Auditor is entitled to arrive at its own independent views, the Board had arrived at a different conclusion in FY2014 for the following reasons:

- (1) As stated in the Circular, on 5 August 2014, the shareholders of Rich Circles met up to further discuss the value add of the shareholders in respect of the operations and control of the Rich Circles Group. Pursuant to resolutions passed in these meetings, Ms. Li Yaxin expressed that she had visited the Company's other factory in Fujian and was deeply impressed by the management and control system in

place. Ms Li Yaxin expressed appreciation of the efforts of the Company and was confident that the Company could add value to the growth of the Rich Circles Group, and agreed to support the idea that key management personnel of the Rich Circles Group will be appointed by the Company. As such, the shareholders of Rich Circles agreed that the Company would appoint the financial controllers, as well as key management staff, in the Rich Circles Group. Ms Li Yaxin would also leave the daily management and operations of the Rich Circles Group to the Company and will only be involved in the Rich Circles Group as a purely financial investor in Rich Circles.

- (2) In connection with the above, on 7 August 2014, the Company announced a change to the board composition of Rich Circles, CCMH and Xuzhou Zhongwei so as to enable the Company to have majority board control over the operations of Rich Circles, CCMH and Xuzhou Zhongwei as follows:
  - (a) Zhang Xiao Quan and Fang Lu, both being the initial nominees of Ms. Li Yaxin, had on 6 August 2014 retired as directors of Rich Circles. The current directors of Rich Circles are Ms. Li Yaxin, Mr. Yuan Limin and Mr. Neo Chee Beng. Mr. Yuan and Mr. Neo are nominees of the Company.
  - (b) Mr. Yuan Limin and Mr. Neo Chee Beng had on 6 August 2014 been appointed as directors of CCMH. Mr. Huo Weisheng was the sole director of CCMH prior to their appointments and remains a director of CCMH.
  - (c) Mr. Yuan Limin and Mr. Neo Chee Beng had on 6 August 2014 been appointed as directors of Xuzhou Zhongwei. Mr. Huo Weisheng was the sole director of Xuzhou Zhongwei prior to their appointments and remains a director of Xuzhou Zhongwei.
- (3) In return for the Company's commitment to expend additional efforts and resources into the promotion and growth of the Rich Circles Group, and to demonstrate her full support to allow the Company to exercise full and total control over the business operations and corporate decisions of the Rich Circles Group, on 8 August 2014, Ms Li Yaxin executed an irrevocable Power of Attorney ("**POA**") granting Mr. Yuan Limin the authority to represent her in all future shareholders' meetings and resolutions in respect of the Rich Circles Group for a period of 20 months from the date of the POA.
- (4) As stated in the Circular, besides having a majority of directors appointed to the boards of Rich Circles, CCMH and Xuzhou Zhongwei, the Board and the Company have implemented policies whereby all major and material decisions relating to the financial and operational aspects of the Rich Circles Group will be approved by the Board. The Chief Financial Officer of the Company, Mr. Ng Poh Khoon, was also appointed the Chief Financial Officer of the Rich Circles Group on 6 August 2014.
- (5) Mr. Yuan Limin, Mr. Neo Chee Beng and Mr. Ng Poh Khoon have experience in marketing, reviewing, strategic directions and financial control, and had contributed such expertise and strategic direction to the operations of the Rich Circles Group in FY2014.

**2. The Company did not have sufficient ability to use its power over the investee (Rich Circles Group) to affect the amount of the Company's returns**

In the Report, the Independent Auditor noted that the key operating subsidiary of Rich Circles is Xuzhou Zhongwei. However, the Independent Auditor noted that the design and purpose of Xuzhou Zhongwei was such that almost all of the financial and operating activities of Rich Circles were performed by a director of Xuzhou Zhongwei as a principal. As such, the Independent Auditor concluded that the Company did not have the direct decision-making authority or decision-making rights over the relevant activities of Xuzhou Zhongwei.

However, while the Board accepts and respects the fact that the Independent Auditor is entitled to arrive at its own independent views, for the reasons stated in Section (C)(1) above, the Board had concluded that the Company had direct decision-making authority over the Rich Circles Group in FY2014. The Company controlled a clear majority of the boards of the Rich Circles Group and continually monitored their activities and financial performance. Furthermore, in accordance with guidelines established, all major and material decisions relating to the financial and operational aspects of the Rich Circles Group were approved by the Board, including major and material decisions of Xuzhou Zhongwei. The Directors had also played an active role in affecting the amount of the Company's returns by leveraging on its listing status to provide publicity and funding, and providing strategic direction to the Rich Circles Group.

The Board also notes that the controlling director of Xuzhou Zhongwei referred to by the Independent Auditor, Mr Huo Weisheng, has been appointed as the Chief Operating Officer and Executive Director of the Group with effect from 9 February 2015 and 25 May 2015, respectively.

**3. The Company did not have exposure or rights to variable returns from its involvement with the investee.**

The Independent Auditor stated in its Report that apart from the entitlement to dividends as a shareholder of Rich Circles, the Company did not have any exposure or rights to variable returns from Xuzhou Zhongwei. The Company did not hold any other interests in the Rich Circles Group.. The Company did not derive any remuneration from the servicing of Xuzhou Zhongwei's assets and liabilities nor was the Company able to enhance the value of its own other assets through the use of its assets in combination with the assets of Xuzhou Zhongwei.

However, while the Board accepts and respects the fact that the Independent Auditor is entitled to arrive at its own independent views, the Board had arrived at a different conclusion for the following reasons:

- (1) The Company maximises its financial return of the Rich Circles Group through maximisation of the Rich Circles Group's financial performance, instead of through the collection of management fees or service income from the Rich Circles Group.
- (2) For the reasons stated in the above paragraphs, the Company has the authority to exert significant influence and control over the dividend

policy of the Rich Circles Group, and has implemented major sales and marketing strategies which would have affected the variable returns of Xuzhou Zhongwei.

Further to the above, the Board notes that as required by FRS 110 on continuous assessment of control, it should perform a reassessment on whether it controls Rich Circles if facts and circumstances indicate that there are changes to one or more of the above three conditions in subsequent financial years.

Subsequent to FY2014, the Company announced on 27 May 2015 that, with effect from that date, its shareholding in Rich Circles had increased from 49% to 54.46%, or 6,100 shares out of an expanded total number of 11,200 shares. As a result of the above-mentioned changes in management and the composition of the board members of the Rich Circles Group to further strengthen the operating and business control by the Company over the Rich Circles Group, adding the fact that the Company now actually owns a clear majority of 54.46% of the shareholding of the Rich Circles Group, the Independent Auditor had stated in its Report that the Board has strong reasons to treat Rich Circles as the Company's subsidiary instead of an associated company with effect from 27 May 2015 and to prepare its financial statements for FY2015 as a subsidiary and consolidate the accounts of the Rich Circle Group from that date.

#### **D. CONCLUSION**

The Board has responded above to each of the bases for the qualified opinion stated in the Report, and is of the view that none of these bases are expected to have an adverse impact on the financial statements for FY2015.

By Order of the Board

Mak Tin Sang  
Executive Director and Chief Executive Officer  
16 June 2015