

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

**UPDATE ON RECOMMENDATIONS IN INTERNAL AUDIT REPORT AND CONTROLS
IMPLEMENTED**

A. Introduction

The Board of Directors (“**Board**”) of Asia Fashion Holdings Limited (the “**Company**”) refers to the announcements by the Company dated 27 May 2014, 30 May 2014 and 14 August 2014 (“**Announcements**”), where the Company had, *inter alia*, announced additional controls and measures implemented and had annexed the report dated 11 August 2014 (the “**HLB Report**”) issued by HLB Atrede LLP (“**HLB**”) in respect of its findings on its assessment of the effectiveness of the internal controls systems of the Company and its subsidiaries (the “**Group**”).

B. Implementation of Recommendations in the Internal Audit Report

Further to the Announcements, the Company wishes to announce that that it has implemented the following measures recommended in the HLB Report:

(a) Legal claims from customers

HLB had noted certain discrepancies between finance department’s monthly consolidated records and the delivery orders issued to Haining Hanchen Textile Co., Ltd and Fuzhou Fule Shoe Material Co., Ltd, and had recommended that Fujian Qianfeng Textile Technology Co. Ltd (“**Qianfeng**”) should update its records to determine the correct quantities fulfilled to-date. Any differences should immediately be investigated and adjusted.

Ng Poh Khoon, the Chief Financial Officer of the Company, has investigated the discrepancies highlighted in the HLB Report and noted that these resulted due to samples sent to two customers which the finance department treated as billed items. The differences have been resolved with the two customers, and the monthly consolidated records have been amended to reflect the quantities in the delivery orders issued.

Mr Ng Poh Khoon has reviewed the reconciliations for June 2014 to August 2014, and confirms that Qianfeng’s finance department has also been performing daily reconciliation of delivery orders issued against stock records, to enable the Company to follow up immediately if there is discrepancy found during reconciliation and to rectify any error. The Company will continue to monitor and audit the finance department of Qianfeng to ensure that no such discrepancies occur in the future, and have put in place policies and procedures for the finance department to follow.

(b) Production and Delivery

(i) HLB notes that the policy and procedures manual of the Company provides that all final products checking records must be authorised by the warehouse manager and quality control manager. However, HLB understands that this document is no longer in use as the products were checked before they are transferred to and stored in the warehouse (pending delivery to customers).

HLB had recommended that Management should review their policies and procedures to determine if a final inspection should be carried out before the products are delivered to the customers. If such procedure is not considered necessary, HLB has recommended that Management should then revise the policy and procedures manual.

Management has since reviewed the policies and procedures, taking into account HLB's concern that there may be a risk that products may be damaged while they are stored in the warehouse, and that failure to perform a final inspection before delivery may result in rejection of goods delivered. Management has revised the policy and procedures manual by implementing additional control policies to ensure that all final products checking records must be authorised by the sales, quality control and the warehouse departments.

Ng Poh Khoon has reviewed delivery records in the month of August 2014 and has confirmed that the above policies have been adhered to.

- (ii) HLB had noted that the policy and procedures manual of the Company provides that all delivery orders must be acknowledged by the sales department and checked and signed by the security department before the products are loaded to the transport vehicle. Of the 30 random samples selected by HLB, one delivery order had not been acknowledged by the security department and four delivery orders have not been acknowledged by the sales department.

HLB had recommended that Management should ensure that the policies and procedures stipulated in the manual are adhered to.

For all goods delivered, the Company has taken measures to ensure that the security department will check and endorse the delivery notes, and has incorporated a new requirement that the customers' acknowledged copies of delivery orders shall be included as part of the accounting records. The technical director, Mr Zhang Maoliang, has been tasked to review the delivery orders on a daily basis and to endorse these.

Ng Poh Khoon has also reviewed delivery records in the month of August 2014 and has confirmed that such delivery orders have Mr Zhang's endorsement, and have been acknowledged by the sales department and checked and signed by the security department before the products are loaded to the transport vehicle.

The Company will continue to monitor and audit Fujian Jiamei Textile Co., Ltd. and Qianfeng (the "**Key Subsidiaries**") to ensure that the policies and procedures stipulated in the manual have been adhered to.

(c) Payment Authorisation Limit

- (i) HLB noted that the payment control policy provided by the Key Subsidiaries differs from the procedure approved by the Board, and had recommended that the Key Subsidiaries align the payment control policy with those approved by the Board.

The Company reiterates that the Board's payment control policy has been followed by the Key Subsidiaries notwithstanding the old policy manual, and has revised the policy manuals of its Key Subsidiaries in early August 2014 to incorporate the procedures approved by the Board, clearly specifying the level of authorisation required for the specific payments. Following the amendments, the Company confirms that the payment control policies of the Key Subsidiaries are in line with the procedure approved by the Board and that there are no further inconsistencies.

- (ii) HLB noted that certain supporting documents in respect of two payments made to two vendors in April 2014 were misplaced by previous accountants, and had recommended that the Key Subsidiaries should exercise more care in the handling of all documents.

The Company has implemented measures for the proper handling of documents by incorporating proper handing-over and checking policies between individuals in the same department should there be a change of responsibilities, which shall be supervised by the finance manager. Ng Poh Khoon has reviewed the policy kept by the finance department, and has interviewed the finance manager and cashier, and noted adherence to the above controls.

(d) Company Seal Usage

HLB noted that Management had implemented a logbook to record the usage of the Official Company Seal and Finance Seal, but that the logbook was not implemented for the other relevant seals (including the Legal Representative Seal).

HLB had recommended that a logbook be kept for each seal so that a proper audit trail can be kept for the usage of each seal.

The Company has since implemented a logbook for all seals, including the Legal Representative Seal, since early August 2014. Ng Poh Khoon has reviewed the logbook usage entries for the Legal Representative Seal for the month of August 2014 and confirms that the entries are in order.

The Company will continue to test and audit the entries in these logbooks.

C. Further Clarifications and Updates

The Company wishes to provide the following clarifications and/or updates to its Shareholders as follows:

(a) Legal Representatives and Seals of Key Subsidiaries

(i) Amendments to the Constitution of the Key Subsidiaries

The Company had on 27 May 2014 announced that it had on 20 May 2014 appointed Dacheng Law Offices (“**Dacheng**”) to advise them on the amendments to the Constitution of the Key Subsidiaries to facilitate the change of legal representatives. The Company has since been working closely with Dacheng on the amendments to the constitution of the Key Subsidiaries to facilitate the change of legal representatives. Dacheng has advised the Company that these changes will have to be approved by PRC government authorities (the “**Governmental Authorities**”) in the following sequence:

1. Foreign Trade and Economic Cooperation Bureau (福清市对外贸易经济合作局)
2. Fuzhou Foreign Trade and Economic Cooperation Bureau (福州市对外贸易经济合作局)
3. Fuqing Municipal Administration of Industry and Commerce. (福清市工商管理局)
4. Administration of Quality and Technology Supervision of Fuqing (福清市质量技术监督局)
5. Fuqing Municipal Bureau of state taxation (福清市国税局)
6. Local Taxation Bureau of Fuqing (福清市地税局)

The Company had on 18 June 2014 submitted applications to the Foreign Trade and Economic Cooperation Bureau for the approvals for these changes, and is currently awaiting its approval. Based on Dacheng's advice, it is estimated that the standard timeframe to obtain the approval of all the Governmental Authorities should take at least an additional three to six months.

Dacheng has confirmed that the process of obtaining the approvals of the Governmental Authorities is merely a procedural requirement, and that the relevant approvals of all Governmental Authorities should be granted as a matter of course in due time. The Company is working to expedite this process and will provide updates to its shareholders on the status of the approvals as and when these are available.

(ii) Current Legal Representatives of the Key Subsidiaries

The current legal representative of the Key Subsidiaries is Lin Xiu Jin. The Company will be changing the legal representatives of the Key Subsidiaries to Ng Poh Khoon to ensure proper oversight over compliance, as soon as the Constitutions of the Key Subsidiaries have been amended.

(iii) Current Physical Location of the Seals

The Finance Seal and the Official Company Seal are currently controlled and held by Ng Poh Khoon. The Legal Representative Seal is currently controlled and held by Lin Xiu Jin, the current legal representative.

(iv) Views of Internal Auditors on Controls on the Legal Representative and Use of Seals

HLB were informed of items (C)(a)(i)-(iii) above as part of their internal audit process and understand that the changes are in the process of being implemented. HLB had considered these items when they proposed the recommendations and findings in the HLB Report. HLB understands that the Company has taken all necessary steps to address the above.

Section 3 of the Executive Summary of the HLB Report provides that based on the samples selected and the work performed (which would include the evaluation of the above issues), HLB is not aware of any material weakness in the internal controls of the Company.

(b) Additional Measures

The Company had on 27 May 2014 announced that it had implemented the following additional control measures, which HLB has evaluated as follows:

(i) Improved Quality Control Procedures

HLB has assessed the detailed quality control procedures of the Company, through on-site observations of the procedures and random samples selected.

(ii) Purchase Orders and Delivery Orders

HLB had done sampling tests to confirm that the purchase orders and the delivery orders issued upon the delivery of the products provide that the customers of the Key Subsidiaries shall acknowledge that they shall examine the goods and shall promptly inform the supplier of any defects identified.

(iii) Standard Procedures for Significant Compensation Claims

As announced on 27 May 2014, the Board has implemented policies and procedures to address significant compensation claims of RMB500,000 and above, and is confident that these will be effective to address such claims in the future. HLB has reviewed these relevant procedures and procedures during their internal audit process.

The Company has also implemented a new form for the reporting of customers' complaints, if any. The level of reporting is in line with the Board's payment control policy.

Ng Poh Khoon has also interviewed sales representatives on the above and noted their understanding on the procedures implemented.

(iv) Views of Internal Auditors on Controls on the Legal Representative and Use of Seals

HLB had reviewed items (C)(b)(i)-(iii) above as part of their internal audit process, and had considered these items when they proposed the recommendations and findings in the HLB Report.

Section 3 of the Executive Summary of the HLB Report provides that based on the samples selected and the work performed (which would include the evaluation of the above issues), HLB is not aware of any material weakness in the internal controls of the Company.

(c) Views of the Board

The Board has carefully considered the various control measures undertaken by the Group, and is of the opinion that the updated system of internal controls addressing financial, operational and compliance risks maintained by the Group are adequate, and that there are no material weaknesses in the internal control systems of the Group.

D. Conclusion

The Board will release further announcements as and when there are any developments on the above.

By Order of the Board

Neo Chee Beng
Executive Chairman
1 September 2014