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## STRUCTURE CONTRACTS

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The existing PRC laws and regulations restrict foreign investment in businesses providing Internet content and information services in the PRC. Our wholly-owned subsidiary, TQ Digital, being a foreign owned enterprise, does not have the requisite licenses to provide Internet content and information services in the PRC.

Prior to 1 January 2007, we operated pursuant to a cooperation arrangement between TQ Digital and NetDragon (Fujian). Under such cooperation arrangement, TQ Digital was responsible for game software development and provision of the relevant technical services while NetDragon (Fujian) was responsible for the overall operation of the relevant games. In addition, each of TQ Digital and NetDragon (Fujian) was entitled to use the trademarks, copyrights and other intellectual property rights of the other party. Revenue generated from the operation of the games was collected by TQ Digital on behalf of NetDragon (Fujian). Pursuant to the cooperation arrangement, TQ Digital would then return 30% of the total revenue received to NetDragon (Fujian), representing the revenue attributable to the operation of the games, and retain the remaining 70% of the total revenue, representing the games license fee.

Our PRC legal adviser, Dacheng Law Offices, has confirmed that, as TQ Digital has the technical capability to develop game software and NetDragon (Fujian), which holds the ICP license, may operate the relevant games according to the Telecommunications Regulations (電信條例), the Administrative Measures for Telecommunications Business Operating Licenses (電信業務經營許可證管理辦法) and other applicable laws and regulations, details of which are set out in “Regulations relating to the industry - Regulation of value-added telecommunication business” of this prospectus, both TQ Digital and NetDragon (Fujian) had the respective capacity to enter into the cooperation arrangement prior to 1 January 2007. Such cooperation arrangement manifests the intents of TQ Digital and NetDragon (Fujian). Further, neither any laws published by the National People’s Congress of the PRC or its Standing Committee, nor any administrative regulations issued by the State Council of the PRC, nor any ministerial rules issued by all ministries and commissions under the State Council of the PRC impose any restrictive or prohibitory provision against such cooperation arrangement as a whole. Therefore, the cooperation arrangement prior to 1 January 2007 did not violate any law or public interest. Pursuant to the MII Notice, details of which are set out in “Regulations relating to the industry - Regulation of value-added telecommunication business” of this prospectus, an ICP license holder is required to have its own domain names, registered trademarks and operating facilities. NetDragon (Fujian) had its own domain names, registered trademarks and operating facilities at all material times while the cooperation arrangement was in place prior to 1 January 2007.

Based on the above, our PRC legal adviser, Dacheng Law Offices, confirmed that NetDragon (Fujian) has been in compliance with the MII Notice and that the cooperation arrangement prior to 1 January 2007 was legal, effective and was in compliance with relevant laws and regulations in the PRC.

In preparation for the Listing and with a view to offer further protection to the interests of the Company and the Shareholders as a whole by means of contractual arrangements, TQ Digital and NetDragon (Fujian) and its equity holders entered into the Structure Contracts, which superseded the cooperation arrangements between TQ Digital and NetDragon (Fujian) effective from 1 January 2007. Under the Structure Contracts, NetDragon (Fujian) is responsible to collect the revenue generated

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from the operation of the games. The bank accounts of NetDragon (Fujian) are operated through its company seal and the personal seal of Liu Dejian, an executive Director. The company seal is kept by Zheng Hui, an executive Director. The Management Committee currently determines the service fees to NetDragon (Fujian) quarterly and NetDragon (Fujian) is billed monthly. NetDragon (Fujian) is required to settle the service fees within 10 days of the billing date. Through the Structure Contracts, we are able to recognise and receive the economic benefits of the business and operations of NetDragon (Fujian). The Structure Contracts enable TQ Digital to control over and to acquire the equity interests in and/or assets of NetDragon (Fujian) when permitted by the relevant PRC laws and regulations. The following sets out a summary of the arrangements under the Structure Contracts:

- TQ Digital will receive service fees from NetDragon (Fujian), the total amount of which shall be determined by the Management Committee with reference to the amount of expenditure incurred by NetDragon (Fujian) in the conduct of its business and operations and its working capital requirements under the guiding principles that (i) NetDragon (Fujian) shall pay the maximum amount of fees to TQ Digital without incurring any loss for each financial year; (ii) the net asset value of NetDragon (Fujian) shall not exceed its net asset value as at 31 December 2006, being approximately RMB15,000,000. The Directors confirm that this arrangement ensures that substantially all economic benefits generated from the operation of NetDragon (Fujian) will be enjoyed by TQ Digital;
- TQ Digital has the right to acquire any or all the shares and/or assets of NetDragon (Fujian) when permitted by the relevant PRC laws and regulations with a nominal amount of consideration or the lowest price permitted by the relevant laws and regulations;
- the equity holders of NetDragon (Fujian) has granted to TQ Digital a pledge over the entire equity interests in the registered capital of NetDragon (Fujian), for the purpose of securing the performance of the contractual obligations by NetDragon (Fujian) and its equity holders under the Structure Contracts; and
- to ensure that TQ Digital retains control over NetDragon (Fujian), under the Structure Contracts, the equity interests of NetDragon (Fujian) may not be transferred or otherwise disposed of by any of the equity holders of NetDragon (Fujian) without the consent of TQ Digital, furthermore, as a succession arrangement, the obligations of the equity holders of NetDragon (Fujian) under the Structure Contracts (including the irrevocable undertaking to authorise TQ Digital or its nominee to exercise their voting rights in NetDragon (Fujian)) will bind all of their respective successors.

The Structure Contracts, taken as a whole, permit the financial results of NetDragon (Fujian) to be consolidated with the Company as if it were a subsidiary of the Company and the economic benefit of its businesses to flow to the Company and TQ Digital. The Structure Contracts could also prevent any possible leakages of assets and values to NetDragon (Fujian)'s equity holders.

As a result of the Structure Contracts, TQ Digital is able to control NetDragon (Fujian) and NetDragon (Shanghai) and accordingly, they are regarded as our subsidiaries and their results are to be consolidated into our financial statements. Since NetDragon (Fujian) and NetDragon (Shanghai) were under the common control of the same group of persons before and after our formation, the

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results and financial positions of NetDragon (Fujian) and NetDragon (Shanghai) are combined into our financial statements using merger accounting as if NetDragon (Fujian) and NetDragon (Shanghai) were part of us since their respective date of establishment or since the date when they first came under the common control. As confirmed by our reporting accountants, these are in compliance with the relevant accounting standards.

In addition, TQ Digital and NetDragon (Fujian) have the right to all our intellectual properties. In order to secure that TQ Digital is able to process the right to the intellectual properties held by NetDragon (Fujian), TQ Digital and all the equity holders of NetDragon (Fujian) entered into the Exclusive Acquisition Rights Agreement, details of which are set out in “Structure Contracts - Agreement for the Exclusive Right to Acquire Equity Interest and Assets” of this prospectus. Pursuant to the Exclusive Acquisition Rights Agreement, TQ Digital, among others, has the right to acquire part or all of the assets of NetDragon (Fujian), including but not limited to its intellectual properties, from the equity holders of NetDragon (Fujian) as and when permitted by the relevant PRC laws and regulations.

### **Management Committee**

The Structure Contracts establish the Management Committee to oversee the business and operations of NetDragon (Fujian). Through its control over NetDragon (Fujian), the Management Committee is also able to oversee the business and operations of NetDragon (Shanghai), being the subsidiary of NetDragon (Fujian). The Management Committee comprises four members, of which each of TQ Digital and NetDragon (Fujian) is entitled to appoint two members from its respective board of directors. Other than by reason of retirement, resignation, incapability or death, a member of the Management Committee may only be removed by the party who originally appointed such member. As a general requirement, the members appointed by NetDragon (Fujian) must also be the equity holders of NetDragon (Fujian) as well as directors of TQ Digital. In the case where the number of members who concurrently act as a director of both TQ Digital and NetDragon (Fujian) is less than two, TQ Digital is entitled to appoint an additional member of the Management Committee. As such, under the Structure Contracts, the Management Committee is allowed to have a maximum of five members.

Currently, the Management Committee comprises Liu Dejian and Liu Luyuan who were appointed by NetDragon (Fujian), and Zheng Hui and Chen Hongzhan who were appointed by TQ Digital. The directors of NetDragon (Fujian) comprise Liu Dejian, Liu Luyuan, Zheng Hui, being executive Directors, Wu Jialiang, being a member of our senior management, and Lin Lizhi, being our general manager. Zheng Hui, an executive Director, is the only director of NetDragon (Shanghai). Further details of the above members are set out in the section headed “Directors, Senior Management and Staff” in this prospectus.

Save for the respective directors’ service fees receivable from TQ Digital and NetDragon (Fujian) (as applicable), the members of the Management Committee do not receive any remuneration for their involvement in the affairs of the Management Committee.

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### *Meetings of the Management Committee*

Meetings of the Management Committee are held regularly on a monthly basis. The quorum for a meeting of the Management Committee is three (including at least one member appointed by each of TQ Digital and NetDragon (Fujian)).

The Management Committee adopts decisions by simple majority resolution of its members. If there is an equal number of votes for and against a decision, TQ Digital and NetDragon (Fujian) shall each appoint an independent third person to decide the matter, failing which the matter shall be decided by the common ultimate individual equity holders of TQ Digital and NetDragon (Fujian), whose decision shall be final and binding on members of the Management Committee.

The Management Committee will hold meeting quarterly to determine the service fees payable by NetDragon (Fujian) to TQ Digital. To facilitate such determination, accounts of NetDragon (Fujian) as at the end of the relevant period have to be submitted to the Management Committee for review and discussion. As a result, the Management Committee will take the figures into consideration to determine the service fees payable by NetDragon (Fujian) to TQ Digital. The service fees are paid by NetDragon (Fujian) to TQ Digital from time to time in accordance with the decisions of the Management Committee. The Management Committee will also review the net asset value of NetDragon (Fujian) at least every three months and make necessary adjustment to the net asset value to a level not exceeding RMB15 million.

The Management Committee will also consider the future benefits and effects while determining the amount to be charged by TQ Digital to NetDragon (Fujian). According to the business model, the revenue received by NetDragon (Fujian) is duly generated from the online games licensed from TQ Digital. The Management Committee is eligible to determine and set the license fees at the highest possible amount.

Through its control over the Management Committee by the above arrangement, TQ Digital is able to monitor, supervise and effectively control NetDragon (Fujian)'s business and operations so as to ensure and facilitate the implementation of the Structure Contracts, particularly the abovementioned guiding principles laid down thereunder. Amongst its various functions, the Management Committee is responsible for determining and adjusting the amount and pricing basis of the various license and service fees payable by NetDragon (Fujian) to TQ Digital with reference to the amount of expenditure incurred by NetDragon (Fujian) in the conduct of its business and operations and its working capital requirements.

Any amendments to the Structure Contracts may be made subject to resolution of members of the Management Committee and approval of our Shareholders in general meeting. No amendments to the Structure Contracts can be made unless it is required under the GEM Listing Rules or is consented by us in writing in advance.

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Our PRC legal adviser, Dacheng Law Offices, after taking all possible actions or steps to enable it to reach its legal conclusions, is of the opinion that:

- each of our PRC entities has been duly incorporated and is validly existing under the relevant PRC laws and regulations;
- the cooperation arrangements between TQ Digital and NetDragon (Fujian) prior to 1 January 2007 was legal, effective and in compliance with the relevant laws and regulations in the PRC;
- each of the Structure Contracts has been duly authorised, executed and delivered by the parties to the Structure Contracts and such contracts are legal, valid, admissible as evidence and binding under the relevant PRC laws and regulations, enforceable against the parties to Structure Contracts in accordance with the terms and conditions in the Structure Contracts and under the relevant PRC laws and regulations;
- the execution, delivery and performance of the Structure Contracts do not violate or result in a breach of or default under any PRC laws, regulations, rules or government policies or their respective articles of association or material contracts which any of them is a party;
- none of the terms and conditions in each of the Structure Contracts (taken individually or together as a whole) nor our legal structure described in this section contravenes any applicable laws, regulations, rules or government policies of the PRC;
- NetDragon (Fujian) complies with all the provisions in the MII Notice, including but not limited to the requirements on NetDragon (Fujian) relating to its ownership of domain names, trademarks and operating facilities;
- the Structure Contracts will not be construed as some form of transfer of the ICP license, leasing or selling any telecommunications business operating license from NetDragon (Fujian) to TQ Digital or provision of resources or sites or facilities from NetDragon (Fujian) to TQ Digital, thereby contravening the MII Notice;
- the MII Notice does not have any impacts on the operation, legality and validity of any of the Structure Contracts; and
- all necessary filings, consents, approvals, permits, authorisations, certificates and licenses of all PRC national, provincial or local government authorities, or any subdivision or department of any such authority, that are required in relation to the execution, delivery, effectiveness and enforceability of each of the Structure Contracts have been made or obtained and remain in full force and effect.

To reach its legal conclusions, our PRC legal adviser, Dacheng Law Offices, has conducted due diligence works on our interests in the PRC, studied relevant PRC legal issues, and consulted the market management department under the information management bureau of MII which is responsible for supervising and administrating the telecommunication business market in the

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PRC. Our PRC legal adviser, Dacheng Law Offices, has further confirmed that there has been no objection from PRC regulatory authority against the contractual arrangements as described in this prospectus. Based on the above, the Joint Sponsors are of the view that there is no reasonable doubt as to the conclusion that our PRC legal adviser, Dacheng Law Offices, has taken appropriate actions or steps to enable it to reach its legal conclusion regarding the Structure Contracts.

Set out below is a brief summary of the terms of the Structure Contracts:

### **(1) Cooperation Framework Agreement**

On 15 October 2007, TQ Digital and NetDragon (Fujian) entered into a cooperation framework agreement (the “Cooperation Framework Agreement”) pursuant to which TQ Digital and NetDragon (Fujian) agreed to cooperate in the provision of services relating to the online game development for and the operation of the online game business of NetDragon (Fujian). The Cooperation Framework Agreement and the terms of reference of the Management Committee laid down the principles that the Management Committee shall have right to determine the amount of license and service fees payable by NetDragon (Fujian) with reference to the amount of expenditure incurred by NetDragon (Fujian) in the conduct of its business and operations and its working capital requirements, including the guiding principles that (i) NetDragon (Fujian) shall pay the maximum amount of fees to TQ Digital without incurring any loss for each financial year; and (ii) the net asset value of NetDragon (Fujian) shall not exceed its net asset value as at 31 December 2006, being approximately RMB15,000,000. This principle will ensure that all of the net profit after tax of NetDragon (Fujian) in each financial year shall be paid to TQ Digital as service or license fees, and will give flexibility to the Management Committee to implement the Structure Contracts and its underlying principles more effectively in response to constantly changing PRC laws and regulations.

The Structure Contracts empower the Management Committee to monitor the expenses of NetDragon (Fujian) which are subject to annual review by the independent non-executive Directors. The Structure Contracts also impose restrictions on certain activities which can only be carried on by NetDragon (Fujian) subject to approval of the Management Committee or otherwise carried on in accordance with the instructions or business plans adopted by the Management Committee from time to time, which include, amongst others, entering into agreements with or making payments or advances to any third parties outside the ordinary course of business; disposal or acquisition of any assets or rights; creating security interests over its assets or intellectual property rights in favour of any third parties; and entering into any connected transactions save for transactions with us.

Pursuant to the Cooperation Framework Agreement and the terms of reference of the Management Committee, the Management Committee was set up to, amongst other things:

- (a) assist NetDragon (Fujian) in arranging the operation of its online game business and oversee the day-to-day operations of its online games business in the PRC and formulate and adjust the scope of authority granted to NetDragon (Fujian) in relation to its operations;

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- (b) monitor, supervise and give advice in relation to the provision by TQ Digital to NetDragon (Fujian) of (i) licenses for the use of software developed by TQ Digital; (ii) software development consultancy services; and (iii) technical support services;
- (c) determine and adjust the amount of license and service fees payable by NetDragon (Fujian) to TQ Digital with reference to the amount of expenditure incurred by NetDragon (Fujian) in the conduct of its business and operations and its working capital requirements, under the guiding principle that NetDragon (Fujian) shall pay the maximum amount of fees to TQ Digital without incurring any loss for each financial year;
- (d) supervise the expenditure of NetDragon (Fujian) to maintain it at a level sufficient for its basic day-to-day operations;
- (e) monitor the net asset value of NetDragon (Fujian), to be reviewed by NetDragon (Fujian) every three months, such that it shall not exceed its net asset value as at 31 December 2006, being approximately RMB15,000,000;
- (f) coordinate the allocation of manpower and supervise the appointment or replacement of senior management members of NetDragon (Fujian);
- (g) supervise the recruitment and training of staff for online games development and online games business operations;
- (h) supervise the implementation of the Structure Contracts;
- (i) make recommendations and decisions in respect of material issues which arise in the cooperation between TQ Digital and NetDragon (Fujian);
- (j) supervise and direct the financial, accounting and the settlement of service and license fees payable under the Structure Contracts;
- (k) assist in the formulation of the business plan of NetDragon (Fujian) and providing guidance and recommendations to NetDragon (Fujian) in respect of its strategic development; and
- (l) monitor the activities of NetDragon (Fujian) such that it would not, amongst other things, (i) enter into agreements with or making payments or advances to any third parties outside the ordinary course of business; (ii) dispose of or acquire any assets or rights; (iii) create security interests over its assets or intellectual property rights in favour of any third party; (iv) agree or allow any third party to infringe in any way the intellectual property rights owned by TQ Digital; (v) give any form of guarantees in favour of any third party; (vi) enter into any connected transactions save for transactions with us; or (vii) enter into any cooperation arrangements with any third party which are similar to those provided under the Structure Contracts.

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Attached to the Cooperation Framework Agreement are forms of 1) cooperation and license agreements in respect of online games; 2) online games software development service agreements; and 3) technical support service agreement, to be entered into by TQ Digital and NetDragon (Fujian), for the purpose of license, development of online games and provision of technical services from TQ Digital to NetDragon (Fujian) and determining the service fees, license fees and commission to be paid from NetDragon (Fujian) to TQ Digital.

The term of the Cooperation Framework Agreement is 10 years commenced from 1 January 2007 and ending on 31 December 2016, and automatically renewable for successive 10-year terms provided that TQ Digital does not issue any notice of termination one month before the termination date.

### **(2) Agreement for Cooperation and Licence in respect of Online Games**

On 15 October 2007, TQ Digital and NetDragon (Fujian) entered into eight agreements for cooperation and license in respect of online games (the “Cooperation and License Agreements”) for each of Eudemons Online, Conquer Online, Zero Online, Monster & Me, Era of Faith, Happiness Q, Piao Miao Online and Heroes of Might and Magic Online, respectively, pursuant to which TQ Digital will license the said online game softwares to NetDragon (Fujian) for use in the PRC in consideration for an initial license fee and a per annum license fee determined as a percentage of NetDragon (Fujian)’s annual gross revenues (which may be adjusted by the Management Committee from time to time pursuant to the Cooperation Framework Agreement).

The scope of activities licensed by TQ Digital to NetDragon (Fujian) under each of Cooperation and License Agreements includes the sales and maintenance of online games developed by TQ Digital, allocation of servers, marketing and distribution of pre-paid cards, and provision of maintenance and technical support services to customers in the PRC. The geographical restriction imposed under the Cooperation and License Agreements is aimed at restricting the activities actively carried on by NetDragon (Fujian), rather than the geographical location of the players accessing the online games operated by NetDragon (Fujian) through the Internet.

Each of the Cooperation and License Agreements is for a term of ten years commenced from 1 January 2007 and ending on 31 December 2016, and automatically renewable for successive ten year terms provided that TQ Digital does not issue any notice of termination one month before the termination date.

### **(3) Online Game Software Development Service Agreement**

On 15 October 2007, TQ Digital and NetDragon (Fujian) entered into an online game software development service agreement (the “Software Development Agreement”) pursuant to which TQ Digital will provide online software development service to NetDragon (Fujian) in consideration of a service fee, the amount of which to be determined by the Management Committee.

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The Software Development Agreement is for a term of 10 years commenced from 1 January 2007 and ending on 31 December 2016, and automatically renewable for successive 10-year terms provided that TQ Digital does not issue any notice of termination one month before the termination date.

### **(4) Technical Support Service Agreement**

On 15 October 2007, TQ Digital and NetDragon (Fujian) entered into a technical support service agreement (the “Technical Support Agreement”) pursuant to which TQ Digital would provide technical support services to NetDragon (Fujian) in consideration of a per annum services fee determined as a percentage of NetDragon (Fujian)’s annual gross revenues (which may be adjusted by the Management Committee from time to time pursuant to the Cooperation Framework Agreement).

The Technical Support Agreement is for a term of 10 years commenced from 1 January 2007 and ending on 31 December 2016, and automatically renewable for successive 10-year terms provided that TQ Digital does not issue any notice of termination one month before the termination date.

### **(5) Equity Interest Pledge Agreement**

On 28 September 2007, TQ Digital, NetDragon (Fujian) and all equity holders of NetDragon (Fujian) entered into an equity interest pledge agreement (the “Pledge Agreement”), pursuant to which all such equity holders granted to TQ Digital a continuing first priority security interests over their respective equity interests in the registered capital of NetDragon (Fujian) (the “Pledged Securities”), representing all of the equity interest in its registered capital, for the purpose of securing the performance of the contractual obligations by NetDragon (Fujian)’s equity holders under the Structure Contracts.

Under the Pledge Agreement, TQ Digital is entitled to exercise its right to purchase the Pledged Securities at an agreed price or sell the Pledged Securities through an auction or private sale or dispose of the Pledged Securities in any other manner permitted by applicable laws and regulations, on the occurrence of any of the following:

- any of the equity holders of NetDragon (Fujian) is in breach of any of his or her obligations under the Pledge Agreement, the Exclusive Acquisition Rights Agreement and the Proxy Agreement;
- NetDragon (Fujian) is in breach of any of its material obligation under the Structure Contracts;
- the representations, undertakings given by NetDragon (Fujian) or its equity holders become untrue or misleading in material aspect; and
- any term of the Structure Contracts becomes unenforceable as a result of change in the relevant law and regulations of the PRC or by any other reasons.

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The Pledge Agreement is for a term commenced from 28 September 2007 and ending on the date of discharge of all obligations under the Pledge Agreement or all secured obligations, whichever is the earlier.

In March 2007, the Real Rights Law of the PRC 《中華人民共和國物權法》 promulgated the requirement that pledge agreements which are entered into on or after 1 October 2007 would only become effective upon registration at the relevant PRC authority. As confirmed by our PRC legal adviser, Dacheng Law Offices, the Pledge Agreement was entered into on 28 September 2007 while the registration requirement under the Real Rights Law of the PRC 《中華人民共和國物權法》 only requires registration of pledge agreements which are entered into on or after 1 October 2007. Accordingly, the effectiveness of the Pledge Agreement does not require registration at the relevant PRC authority and the registration requirement under 《中華人民共和國物權法》 does not have any retrospective impact on the Pledge Agreement.

### **(6) Agreement for the Exclusive Right to Acquire Equity Interest and Assets**

On 15 October 2007, TQ Digital, NetDragon (Fujian) and all of the equity holders of NetDragon (Fujian) entered into an agreement for the exclusive right to acquire equity interest and assets (the “Exclusive Acquisition Rights Agreement”), pursuant to which NetDragon (Fujian) and all its equity holders granted to TQ Digital or its designee (a) a right to acquire part or all of the equity interest in the registered capital of NetDragon (Fujian); and (b) a right to acquire part or all of the assets of NetDragon (Fujian) from the equity holders of NetDragon (Fujian) as and when permitted by the relevant PRC laws and regulations. The amount of consideration payable by TQ Digital to the equity holders of NetDragon (Fujian) shall be a nominal amount or the lowest possible amount permissible under the applicable PRC law. If the minimum amount of consideration stipulated under the relevant PRC laws and regulations is higher than the nominal amount at the time of exercise of the acquisition right, Liu Dejian, Liu Luyuan and Zheng Hui had jointly, severally and irrevocably undertaken to reimburse the Company or its subsidiaries of any amount in excess of the nominal amount.

The Exclusive Acquisition Rights Agreement contains specific covenants given by NetDragon (Fujian) and its equity holders with respect to the governance of NetDragon (Fujian) and the conduct of the business of NetDragon (Fujian). Among these covenants, the equity holders of NetDragon (Fujian) have agreed not to transfer or encumber their equity interests in NetDragon (Fujian) without the consent of TQ Digital. NetDragon (Fujian) has agreed, among others,

- not to sell or encumber any of NetDragon (Fujian)’s assets without TQ Digital’s prior written consent or as permitted under the Equity Interest Pledge Agreement;
- not to change its registered capital structure without TQ Digital’s prior written consent;
- not to distribute profits of NetDragon (Fujian) to its equity holders;

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- to conduct the business of NetDragon (Fujian) in accordance with the Cooperation Framework Agreement and Management Committee's directions from time to time; and
- not to liquidate or dissolve NetDragon (Fujian) without TQ Digital's prior written consent.

The terms of the Exclusive Acquisition Rights Agreement commenced on 1 January 2007 and shall expire upon the end of the term of incorporation of NetDragon (Fujian), or the date on which the entire ownership interest of the assets or registered capital of NetDragon (Fujian) is purchased by TQ Digital or its designee, whichever is the earlier.

### **(7) Equity Holders' Voting Rights Proxy Agreement**

On 15 October 2007, all equity holders of NetDragon (Fujian) entered into an equity holders' voting rights proxy agreement (the "Proxy Agreement") with TQ Digital and NetDragon (Fujian), pursuant to which all equity holders of NetDragon (Fujian) have irrevocably authorised TQ Digital or a nominee designated by TQ Digital (which will likely be a director of TQ Digital) to exercise all their voting rights in NetDragon (Fujian). The term of the Proxy Agreement shall continue indefinitely for so long as NetDragon (Fujian) subsists in order to secure our control over NetDragon (Fujian).

In July 2007, to ensure the continuity of the Structure Contracts, NetDragon (Shanghai), being a subsidiary of NetDragon (Fujian), has applied for an ICP license to operate the online games in addition to NetDragon (Fujian) and NetDragon (Shanghai) has undertaken to enter into contracts substantially the same as the Structure Contracts with TQ Digital to ensure the continuity of the Structure Contracts. NetDragon (Shanghai) will apply for a revision of its business scope in its business license to include the operation of online games upon obtaining its ICP license.

In addition to the Structure Contracts, a service agreement which took effect on 1 July 2007 has been entered into between NetDragon (USA) and NetDragon (Shanghai). Although such service agreement does not form part of the Structure Contracts, a specific waiver will be sought from the Stock Exchange in respect of such agreement. Further details of the above service agreement are set out in the section headed "Waivers from the Stock Exchange" below.

### **Waivers from the Stock Exchange**

The Company conducts internet content and information services through NetDragon (Fujian) and NetDragon (Shanghai) under the suite of Structure Contracts entered into between TQ Digital (an indirect wholly-owned subsidiary of the Company) and NetDragon (Fujian). As Liu Dejian, Liu Luyuan and Zheng Hui, being the executive Directors and the Controlling Shareholders, are interested in an aggregate of 98.9% in NetDragon (Fujian), NetDragon (Fujian) and NetDragon (Shanghai), being a subsidiary of NetDragon (Fujian), are technically associates of Liu Dejian, Liu Luyuan and Zheng Hui, and therefore connected persons of the Company. Transactions between the Company, NetDragon (BVI), TQ Digital, NetDragon (HK) or NetDragon (USA) (all being wholly-owned

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subsidiaries of the Company) on one hand and NetDragon (Fujian) or NetDragon (Shanghai) on the other hand, including the Structure Contracts, would technically be connected transactions and, unless an exemption is available under the GEM Listing Rules, must comply with the applicable disclosure, reporting and shareholders' approval requirements under Chapter 20 of the GEM Listing Rules.

The Directors (including the independent non-executive Directors) are of the view that the Structure Contracts are fundamental to the legal structure and the business operations of the Group and are on terms that are fair and reasonable so far as the Company is concerned and in the interests of the Shareholders as a whole. The Company also believes that the unique nature of the Group's structure whereby the results and financial condition of NetDragon (Fujian) is consolidated with our financial statements as if it is a subsidiary of the Company, and the economic benefit of their business flows to the Group, places the Group in a unique position in relation to the connected transaction rules. Accordingly, notwithstanding that the Structure Contracts technically constitute continuing connected transactions for the purposes of Chapter 20 of the GEM Listing Rules, the Directors consider that it would not be appropriate for the Structure Contracts to be subject to, amongst other things, the periodic approval of the independent Shareholders.

Therefore, the Company hereby applies to the Stock Exchange for a specific waiver in respect of the Structure Contracts and the Other Contracts with conditions as follows:

***Specific waiver***

(a) *Waiver for the Structure Contracts and the Other Contracts from strict compliance with Chapter 20 of the GEM Listing Rules*

The Structure Contracts will be exempt from strict compliance with the announcement, reporting and independent Shareholders' approval requirements under Chapter 20 of the GEM Listing Rules. According to rule 20.35(1) of the GEM Listing Rules, the agreement must set out the basis of calculation of the payments to be made and the period for the agreement must be fixed and reflect normal commercial terms and, except in special circumstances, must not exceed three years. As the Directors are of the view that the Structure Contracts and the Other Contracts , with durations of over three years, are fundamental to the legal structure and business operations of the Group, and that flexibility has to be given to the Management Committee to determine the fees payable under each of the Structure Contracts in response to constantly changing PRC laws and regulations and other aspects of operations of the Group, the Structure Contracts and the Other Contracts will be exempt from strict compliance with rule 20.35(1) and rule 20.35(2) of the GEM Listing Rules.

(b) *No change without Shareholders' approval*

Save as described below, no changes to the Structure Contracts will be made without the approval of the Shareholders by ordinary resolution. Once Shareholders' approval of any change has been obtained, no further periodic or other approvals will be required under Chapter 20 of the GEM Listing Rules unless and until further changes are proposed.

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## STRUCTURE CONTRACTS

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(c) *“Economic benefits” flexibility*

The structure under the Structure Contracts has been designed to enable TQ Digital through the Management Committee to implement the terms of the Structure Contracts relating to fees so as to allow the economic benefits generated by NetDragon (Fujian) to be flowed to TQ Digital, having regard to changes in the quantum of NetDragon (Fujian)'s and NetDragon (Shanghai)'s earnings and applicable PRC laws and regulations (including taxation), without requiring the approval of the Shareholders. The Structure Contracts also enable TQ Digital to receive the economic benefits derived by NetDragon (Fujian) and NetDragon (Shanghai) through the right to acquire NetDragon (Fujian)'s and NetDragon (Shanghai)'s equity interests and/or assets for a consideration fixed by the parties under the Structure Contracts and confirmed by the Management Committee in accordance with the relevant PRC laws and regulations without requiring the approval of the Shareholders.

(d) *Renewal and cloning*

On the basis that the Structure Contracts provide an acceptable framework for the relationship between the Company, NetDragon (BVI), TQ Digital, NetDragon (HK) and NetDragon (USA) on one hand and NetDragon (Fujian) and NetDragon (Shanghai), on the other, framework may be renewed and/or “cloned” upon the expiry of the existing arrangements or in relation to any existing or new wholly foreign-owned enterprise, operating company or FITE (as defined below) that the Company might wish to establish, without obtaining the approval of the Shareholders on terms that the protections for the Shareholders described in this paragraph will apply.

(e) *Foreign-invested Telecommunication Enterprise (“FITE”) or Wholly Foreign-owned Enterprise (“WFOE”)*

Whenever the existing legal restrictions prohibiting foreign investment in business providing Internet content and information services in the PRC be abolished or relaxed, the Company intends to apply for the establishment of a FITE or a WFOE or acquire NetDragon (Fujian) and NetDragon (Shanghai) by exercising the right to acquire equity interest and asset under the Structure Contracts (collectively, the “Reorganization of Structure Contracts Arrangement”). This may require the Structure Contracts to be amended or terminated as the case may be. The Company shall be able to carry out the Reorganization of Structure Contracts Arrangement without Shareholders’ approval.

***Conditions***

The Company is prepared to accept conditions to be imposed by the Stock Exchange in respect of the above specific waiver as follows:

- (a) The Company will disclose the Structure Contracts and the Other Contracts in place during each financial period in our annual report and accounts in accordance with the relevant provisions of Rule 20.45 of the GEM Listing Rules;

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## STRUCTURE CONTRACTS

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- (b) The Company's independent non-executive Directors will review the Structure Contracts and the Other Contracts annually and confirm in its annual report and accounts for the relevant year that the transactions carried out during such year have been entered into in accordance with the relevant provisions of the Structure Contracts and the Other Contracts, have been operated so as to allow the economic interest generated by NetDragon (Fujian) and NetDragon (Shanghai) to be flowed to TQ Digital and any new Structure Contracts and the Other Contracts entered into, renewed and/or cloned during the relevant financial period are fair and reasonable so far as the Company is concerned and in the interests of the Company's Shareholders as a whole;
- (c) The Company's auditors will carry out review procedures annually on the transactions carried out pursuant to the Structure Contracts and the Other Contracts and will provide a letter to the board of Directors, with a copy to the Stock Exchange, at least 10 business days before the Company bulk print its annual report, confirming that the economic interest generated by NetDragon (Fujian) and NetDragon (Shanghai) is flowed to TQ Digital are in accordance with the criteria and principles set out in the Structure Contracts and the Other Contracts and are properly approved by the Management Committee, that the net asset value of NetDragon (Fujian) at end of the year does not exceed its net asset value as at 31 December 2006, being approximately RMB15,000,000, and that no dividends or other distributions have been made by NetDragon (Fujian) or NetDragon (Shanghai) (save as to NetDragon (Fujian)) to the holders of its equity interests;
- (d) For the purpose of Chapter 20 of the GEM Listing Rules, and in particular the definition of "connected person", each of NetDragon (Fujian), NetDragon (Shanghai) and any other newly established operating company, will be treated as a subsidiary of the Company, but at the same time, the directors, chief executive, substantial shareholders or management shareholders of NetDragon (Fujian), NetDragon (Shanghai) and any other newly established operating company, and their respective associates will be treated as "connected persons" of the Group (including NetDragon (Fujian), NetDragon (Shanghai) and any other newly established operating company) and transactions (excluding the Structure Contracts and the Other Contracts) between these connected persons and the Group (including NetDragon (Fujian), NetDragon (Shanghai) and any other newly established operating company), shall comply with Chapter 20 of the GEM Listing Rules; and
- (e) NetDragon (Fujian) and NetDragon (Shanghai) will provide to the Company an undertaking that, for so long as the Shares are listed on the Stock Exchange, NetDragon (Fujian) and NetDragon (Shanghai) will allow the Company and its auditors to have full access to relevant records of NetDragon (Fujian) and NetDragon (Shanghai) for the purpose of the Company's auditors' review of the transactions referred to above.

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## STRUCTURE CONTRACTS

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In addition to the Structure Contracts, a service agreement which took effect on 1 July, 2007, has been entered into by and between NetDragon (USA) and NetDragon (Shanghai) pursuant to which NetDragon (Shanghai) will provide various services to NetDragon (USA) in exchange for a flat fee calculated based on the number of servers running certain non-Chinese language games. Pursuant to this service agreement, NetDragon (Shanghai) will: (1) provide email correspondence to answer inquiries from customers including payment and password related issues; (2) handle customer complaints regarding hacked accounts and assist such customers in resolving their concerns; and (3) monitor the status of certain servers and perform server maintenance when needed. The term of such service agreement is five years. Other than the above, we expect that there may be other contracts to be entered from time to time (together with the service agreement between NetDragon (USA) and NetDragon (Shanghai), the “Other Contracts”) between the Company and its subsidiaries on the one hand and NetDragon (Fujian) or NetDragon (Shanghai) on the other. So far as are foreseeable by the Directors, the Other Contracts to be entered into from time to time between the Company and its subsidiaries on the one hand and NetDragon (Fujian) or NetDragon (Shanghai) on the other will include other service agreements and/or cooperation and license agreements between TQ Digital and NetDragon (Shanghai) after NetDragon (Shanghai) has obtained the requisite licenses for providing internet content and operating online games. Given that the results of NetDragon (Fujian) and NetDragon (Shanghai) are consolidated into the Group’s accounts, and given the relationship between the various companies within the Group (including NetDragon (Fujian) and NetDragon (Shanghai)) created by the Structure Contracts, the Directors also consider that it would not be appropriate for the Other Contracts to be subject to, amongst other things, the periodic approval of the independent Shareholders.

### **Joint Sponsors’ View**

The Joint Sponsors are of the view that the Structure Contracts taken as a whole is fair and reasonable and in the interests of our Shareholders as a whole.