
REGULATIONS RELATING TO THE INDUSTRY

The online game industry in the PRC operates under a legal regime that consists of the State Council, which is the highest authority of the executive branch of the PRC central government, and the various ministries and authorities under its leadership. These ministries and authorities include:

- the MII;
- the MOC;
- the GAPP; and
- the NCAC.

The State Council and these ministries and authorities have issued a series of rules that regulate a number of different substantive areas of our business, which are discussed below.

REGULATION OF VALUE-ADDED TELECOMMUNICATION BUSINESS

Internet information services in the PRC are governed by the Telecommunications Regulations (電信條例) issued on 25 September 2000 by the State Council. The Telecommunications Regulations categorise all telecommunications businesses in the PRC as either basic telecommunications businesses or value-added telecommunications businesses. The Catalogue of Classes of Telecommunications Businesses (電信業務分類目錄) (updated on 21 February 2003 and effective as of 1 April 2003) that is attached to the Telecommunications Regulations provides that an Internet information service is a value-added telecommunications business. According to the Telecommunications Regulations, any commercial operator of telecommunications businesses in the PRC must obtain an operating license from MII or provincial-level communications administrative bureaus (“**CAB**”). The Telecommunications Regulations also set forth extensive guidelines with respect to various aspects of telecommunications operations in the PRC.

The Administrative Measures for Telecommunications Business Operating Licenses (電信業務經營許可證管理辦法) (the “**Telecom License Measures**”) were promulgated by MII on 26 December 2001 and became effective as of 1 January 2002. The Telecom License Measures, which are formulated in accordance with the Telecommunications Regulations, set forth the types of licenses required to operate a telecommunications business and the procedures for obtaining such licences. With respect to licenses for value-added telecommunications services, the Telecom License Measures draw a distinction between licenses for business conducted in a single province (which are issued by CAB) and licenses for inter-provincial activities (which are issued by MII).

In addition to the Telecommunications Regulations, Internet information services are also regulated pursuant to the Administrative Measures on Internet Information Services (互聯網信息服務管理辦法) (the “**Internet Measures**”) issued on 25 September 2000 by the State Council. The Internet Measures define “Internet Information Services” as “the service activities which provide information to online players through the Internet”, and are divided into services of a commercial nature and services of a non-commercial nature. “Internet Information Service Providers” (which are commonly referred to as ICPs) that are compensated for their services (i.e., ICPs providing services of a commercial nature) are required to obtain an operation license from MII or the relevant CAB.

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As advised by our PRC legal adviser, Jingtian and Gongcheng, under the provisions of the Catalogue of Classes of Telecommunications Businesses (電信業務分類目錄), information services based on Internet of mobile network is classified as a kind of Class 2 value-added telecommunications services (第二類增值電信業務). The holder of the value-added telecommunications business operation license (class 2) with a service scope of Internet information services will allow the holder to engage in such business. In addition, under the Administrative Measures for Telecommunication Business Operating License (電信業務經營許可證管理辦法), to obtain the value-added telecommunication business license, the applicant shall meet the following conditions - (i) the operator shall be a legally established company; (ii) it shall have funds and specialised personnel commensurate with its proposed business activities; (iii) it shall have the reputation for, or be capable of, providing long-term services to its subscribers; (iv) it shall have RMB1,000,000 of registered capital or above in case it operates within a province, autonomous region or municipality; it shall have RMB10,000,000 of registered capital or above in case it operates by spanning provinces, autonomous regions and municipalities or the whole country; (v) it shall have a feasibility study and technology regarding network formulation; (vi) it shall have the necessary site and resources; (vii) it shall have no record of illegal act which is of grave nature within recently three years. To hold and maintain the said license, the holder shall conduct telecommunication business within the authorised scope, and shall pass annual inspection on a yearly basis. The following are basic license and/or permits necessary for online game operators - (i) ICP license; (ii) network culture operation license; and (iii) business license. NetDragon (Fujian) has obtained business license, ICP license and network culture operation license. For publishing games through Internet, NetDragon (Fujian) is relying on third party for Internet publishing activities. As confirmed by the Directors and the Company's PRC legal adviser, Jingtian and Gongcheng, the Group in compliance with all related requirements.

In addition, the MII Notice requires that ICP license holders or their shareholders directly own the domain names and trademarks used by such ICP license holders in their daily operations. The MII Notice further requires each ICP license holder to have the necessary facilities for its approved business operations and to maintain such facilities in the regions covered by its license. In addition, all the value-added telecommunication service providers are required to maintain network and information security in accordance with the standards set forth under relevant PRC regulations. The MII Notice prohibits ICP license holders from leasing, transferring or selling its telecommunications business operating license to any foreign investors in any form, or providing any resource, sites or facilities to any foreign investors for their illegal operation of telecommunications business in the PRC. Further, the local authorities in charge of telecommunications services were required to ensure that existing ICP license holders conducted a self-assessment of their compliance with the MII Notice and to submit status reports to the MII before November 2006. NetDragon (Fujian), being our ICP license holder, has conducted and filed a self-assessment of its compliance with the MII Notice covering mainly (i) ownership of domain names; (ii) ownership of trademarks; (iii) ownership of operating sites, servers and facilities; and (iv) Internet information safety protection measures in October 2006. As confirmed by our PRC legal adviser, Jingtian and Gongcheng, NetDragon (Fujian), being the ICP license holder, owns the domain names and trademarks used in its daily operation. Details of the domain names and trademarks are set out in "Further information about the business - Intellectual property" to Appendix V of this document. NetDragon (Fujian) also has the necessary facilities for its approved business operations and it has maintained such facilities in the regions covered by its license. The trademarks owned by TQ Digital are trademarks of online game software products which are not the trademarks used by NetDragon (Fujian) for the services under its ICP

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license. In addition, the Structure Contracts do not involve any leasing, transferring or selling NetDragon (Fujian)'s ICP license to TQ Digital or TQ Online in any form, nor provide any resource, sites or facilities to TQ Digital or TQ Online for illegal operation of telecommunications business in the PRC. Accordingly, we and our PRC legal adviser, Jingtian and Gongcheng, confirm that (i) 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; and (ii) the Structure Contracts will not be construed as some form of transfer of the ICP license from NetDragon (Fujian) to TQ Digital or TQ Online or provision of resources or sites or facilities from NetDragon (Fujian) to TQ Digital or TQ Online, thereby contravening the MII Notice. In addition, we rely on an Independent Third Party for the license from the GAPP, which is fundamental to our business, to publish our games. As confirmed by our PRC legal adviser, Jingtian and Gongcheng, the licensing arrangement to publish our games does not involve any leasing, transferring or selling NetDragon (Fujian)'s ICP license to a third party in any form, nor provide any resource, sites or facilities to a third party for illegal operation of telecommunications business in the PRC. Accordingly, we and our PRC legal adviser, Jingtian and Gongcheng, confirm that such arrangement does not constitute a breach of the condition imposed by the MII Notice.

As an ICP operator providing ICP services in multiple provinces, NetDragon (Fujian) is required to hold an ICP license issued by MII to provide Internet information services. NetDragon (Fujian) received on 20 January 2005, an MII-issued ICP license valid until 20 January 2010 to operate throughout the PRC. In addition, as advised by our PRC legal adviser, Jingtian and Gongcheng, NetDragon (Fujian) has passed the 2005 and 2006 annual inspection of its ICP license in June 2006 and August 2007, respectively, which proved that the operation of NetDragon (Fujian) is legally and effectively operating its business under the scope of its ICP license.

FOREIGN OWNERSHIP RESTRICTIONS

Pursuant to the Administrative Provisions on Foreign-invested Telecommunication Enterprises (外商投資電信企業管理規定) issued on 11 December 2001, foreign ownership of companies that provide Internet content services, are limited to 50%. In addition, there are specific qualification requirements for foreign investors to invest in this area. The Company is registered in the Cayman Islands thus classified as a foreign company under PRC law. Due to the restrictions to foreign investment in value-added telecommunication business and other restrictions related to online game operations (as described in other paragraphs of this section), our online game business in the PRC are operated through NetDragon (Fujian).

In the opinion of Jingtian and Gongcheng, our PRC legal adviser, (1) the ownership structures of TQ Digital, TQ Online, NetDragon (Fujian) and NetDragon (Shanghai), all currently and after giving effect to the Introduction, are in compliance with existing PRC laws and regulations, (2) the contractual arrangements between TQ Digital, TQ Online and NetDragon (Fujian) and its equity holders are valid and binding, and will not result in any violation of PRC laws or regulations currently in effect; and (3) the business operations of TQ Digital, TQ Online, NetDragon (Fujian) and NetDragon (Shanghai), as described in this document, are in compliance with existing PRC laws and regulations in all aspects which may affect our business and operation.

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REGULATION OF ONLINE CULTURAL ACTIVITIES

Pursuant to the Internet Culture Regulations, the MOC shall be responsible for making guidelines, policies and planning for the development and administration of Internet culture, supervising the Internet cultural activities nationwide, applying a permit system to operational Internet cultural entities in accordance with the relevant laws, regulations and rules, applying a record system to non-operational Internet cultural entities, overseeing the contents of Internet culture, and punishing the acts in violation of the relevant regulations of the state. The administrative department of culture under the people's government of the province, autonomous region or municipality directly under the central government of the PRC are responsible for, within its own jurisdiction, the daily administration of Internet cultural activities, the preliminary examination of the entities that apply to engage in operational Internet cultural activities, the examination of entities that apply to engage in non-operational Internet cultural activities, and the imposition of punishments on the acts of engaging in Internet cultural activities in violation of the relevant regulations of the state. A commercial operator of online games must, in addition to ICP license, obtain an Internet culture operation license from the appropriate culture administrative authorities for its operation of online games. Foreign invested enterprises are currently not allowed to apply for Internet culture operation license. Furthermore, imported online games are subject to a content review and approval by the MOC while domestic developed online games shall also be filed with the MOC within sixty (60) days after commencement of operation in the PRC. NetDragon (Fujian) is subject to the Internet Culture Regulations when engaging in Internet cultural activities.

On 13 October 2004, NetDragon (Fujian) obtained the Internet culture operation license (網絡文化經營許可證) pursuant to the Internet Culture Regulations. Its scope of operations is operating game products through the Internet. As confirmed by our PRC legal adviser, Jingtian and Gongcheng, NetDragon (Fujian) has filed with the MOC the PRC domestically developed online games in accordance with the relevant PRC laws and regulations.

REGULATION OF INTERNET PUBLISHING

According to the Tentative Measures for Internet Publication Administration (互聯網出版管理暫行規定) issued on 27 June 2002, the provision of online games is deemed to be an Internet publication activity, defined as any act by an Internet information service provider to select, edit and process content or programmes and to make such content or programmes publicly available on the Internet. Therefore, an operator must obtain the approval from the press and publication administrative authorities as an Internet publisher in order to carry on online game publishing businesses in the PRC. Furthermore, the distribution of online game cards are subject to a licensing requirement.

During the Track Record Period, we have engaged an Independent Third Party to publish the online games operated by NetDragon (Fujian) in the Internet. As confirmed by our PRC legal adviser, Jingtian and Gongcheng, that third party is an entity qualified to publish in the Internet. NetDragon (Fujian)'s engagement of that third party to publish its operated online games does not violate any mandatory laws and regulations in the PRC. The agreement entered into between NetDragon (Fujian) and the third party is legal and effective.

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REGULATION OF INTERNET CONTENT

The PRC government has promulgated measures relating to Internet content through a number of ministries and authorities, including the MII, the MOC and the GAPP. These measures specifically prohibit Internet activities, which includes the operation of online games, that result in the publication of any content which is found to, among other things, propagate obscenity, gambling or violence, instigate crimes, undermine public morality or the cultural traditions of the PRC, or compromise State security or secrets.

In 2005, GAPP issued Trial Standards for Development of ‘Anti-addiction System’ (防沉迷系統開發標準(試行)) to promote the development of anti-addiction system which may limit the amount of time that a minor or other user may continuously spend on an online game. On 5 April 2007, eight PRC governmental authorities, including the Ministry of Education (教育部), MII, GAPP and the Ministry of Public Security (公安部) jointly promulgated the Notice Regarding the Implementation of Anti-addiction System on Online Games in Protecting the Physical and Psychological Health of Minors (關於保護未成年人身心健康實施網絡遊戲防沉迷系統的通知). Under this notice, we are required to develop a system for our online games which is aimed to reduce “fatigue time” and “unhealthy time” such that, when a user has been playing an online game for more than three hours, he or she will automatically be sent periodic warnings within the game environment prompting him or her to leave the game and take a break. Such warnings will become more frequent as the user accumulates more playing time. In addition, this system will cause the rate at which the game user can obtain experience points and other virtual assets such as special equipment to decrease to half of normal levels during the “fatigue time” period and to zero during the “unhealthy time” period. If the user goes offline for more than five hours, the available “healthy” playing time will be reset and the user may play the game again normally for an additional three hours before once again entering “fatigue time”. According to the anti-addiction notice, the anti-addiction system shall be put into operation in all online games from 16 July 2007.

We have adopted a system to comply with the Notice Regarding the Implementation of Anti-addiction System on Online Games in Protecting the Physical and Psychological Health of Minors (關於保護未成年人身心健康實施網絡遊戲防沉迷系統的通知). Under this system, if a user has been playing our online game for more than three hours, he or she will automatically be sent periodic warnings prompting him or her to leave the game and take a break. Such warnings will become more frequent as the user accumulates more playing time. In addition, our system will cause the rate at which the game user can obtain experience points and other virtual assets such as special equipment to decrease to half of normal levels during the “fatigue time” period and to zero during the “unhealthy time” period. If the user goes offline for more than five hours, the available “healthy” playing time will be reset and the user may play the game again normally for an additional three hours before once again entering “fatigue time”.

REGULATION OF SOFTWARE DEVELOPMENT ACTIVITIES

The Administrative Measures on Software Products (軟件產品管理辦法) promulgated by MII on 27 October 2000 (the “**Software Measures**”) regulate development and sale of computer software or software embedded in information systems or equipment provided to players and computer software in conjunction with computer information systems integration or application services or other

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technical services (“**software products**”) in the PRC. The Software Measures prohibit the development, production, sale or import of software products that infringe third party intellectual property rights, contain computer viruses, endanger the safety of computer systems, contain content prohibited by the State or do not comply with PRC software standards.

All software products to be sold or operated in the PRC must be tested by an MII approved testing organisation and registered with MII or relevant CAB pursuant to the Software Measures. The registration is valid for a five year period and can be renewed. The Software Measures require software products manufacturers to have a business scope that includes software business, have the conditions and technical strength for software manufacturing, a fixed manufacturing base and the procedures and capability to guarantee product quality.

We have taken all necessary actions to comply with the relevant laws and regulations in operating our software products in the PRC.

REGULATION ON SOFTWARE IMPORT AND EXPORT

We are required to register with the relevant local authority of Ministry of Commerce of the PRC any license agreement with a foreign licensor or licensee that involves an import or export of technologies, including online game software into or outside the PRC. Without that registration, we may not remit licensing fees out of the PRC to any foreign game licensor or collect any licensing fees into the PRC from any foreign licensees. In addition, the MOC requires us to submit for its content review and approval of any online games we want to license from overseas game developers. Furthermore, the NCAC requires us to register copyright license agreements relating to imported software. Without the NCAC registration, we are not allowed to publish or reproduce the imported game software in the PRC.

During the Track Record Period and up to the Latest Practicable Date, we did not encounter any difficulties in making payments out of China or collecting payments into China under any agreements with foreign parties. We further confirm that we will take all necessary actions to comply with the relevant laws and regulations should such obligation arises in the future.

REGULATION ON INTERNET CAFES

Internet cafes are required to obtain a license from the MOC and the SAIC, and are subject to requirements and regulations with respect to location, size, number of computers, age limit of customers and business hours. Although we do not own or operate any Internet cafes, many Internet cafes distribute our pre-paid cards. The PRC government has promulgated several regulations administrating Internet cafes illustrating its intention of intensifying the regulation of Internet cafes, which are currently the primary venue for our players to play online games. The State Council issued the Notice on the Special Regulation against Internet Cafes and Other Internet Access Service Business (國務院辦公廳轉發文化部等部門關於開展網吧等互聯網上網服務營業場所專項整治意見的通知) in February 2004 to overhaul Internet cafes and suspend the issuance of new Internet cafe licenses for a period. In November 2004, the SAIC issued the Circular for Further Strengthening the Special Regulation against Internet Cafes (關於進一步深化網吧專項整治工作的通知) further tightening the restrictions on the establishment of Internet cafes. In February 2007, fourteen PRC

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governmental agencies, including the MOC, MII and GAPP jointly promulgated the Circular for Further Strengthening the Administration of Internet Cafe and Online Games (關於進一步加強網吧及網絡遊戲管理工作的通知) (the “Circular”). According to the Circular, no new Internet cafe should be approved in 2007, and the regulation of existing Internet cafes should be strengthened.

During the Track Record Period and up to the Latest Practicable Date, we did not operate any Internet cafes. However, restrictions on development of Internet Cafes, the major venue for the players to play online games, may negatively affect our business operation. Please see the risk factor set out in “Risk factors - Risks relating to the industry in which we operate - Control or Internet access and the distribution of news, information or other content on Internet in the PRC may adversely affect our business” of this document.

REGULATION ON VIRTUAL CURRENCY

On 15 February 2007, 14 governmental authorities, including the MOC, the MII, the SAIC, and the People’s Bank of China (the “PBOC”), jointly issued the Circular. According to the Circular, the administration of the PBOC on virtual currencies issued by online game operators for the players’ use in online games has been emphasised in order to avoid the potential impact of such virtual currencies on the live financial system. The volume of issuance and purchase of such virtual currencies shall be limited and such virtual currencies shall not be used for purchase of any physical products or refunded with a premium or otherwise illegally traded. As confirmed by our PRC legal adviser, Jingtian and Gongcheng, although the Circular provides that the volume of issuance and purchase of virtual currencies shall be limited, it does not specify expressly the amount of limit thereon. As at the Latest Practicable Date, the PBOC has not issued any further circular, notice or provision which imposes the specific volume restriction on virtual currencies that may be issued by online game operators and purchased by online game players.

During the Track Record Period and up to the Latest Practicable Date, we have been in compliance with the relevant regulation on virtual currency, under which no virtual currencies can be used for purchase of any physical products or refunded with a premium or otherwise illegally traded.

REGULATIONS ON INTERNET SECURITY

The National People’s Congress enacted the Determination in Relation to Protection of the Internet Security (關於維護互聯網安全的決定) in December 2000. The following acts may subject to criminal punishment in the PRC: (i) gain improper entry into a computer or system of strategic importance; (ii) disseminate politically disruptive information or obscenity; (iii) leak state secrets; (iv) spread false commercial information; and (v) infringe intellectual property rights.

The Ministry of Public Security has promulgated measures that prohibit use of the Internet that result in the leakage of state secrets or the spread of socially destabilising content. The Ministry of Public Security has supervision and inspection rights in this regard, and we may be subject to the jurisdiction of the local security bureaus. If an ICP license holder violates these measures, the PRC government may revoke its ICP license and shut down its websites.

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As confirmed by our PRC legal adviser, Jingtian and Gongcheng, we have been in compliance with the regulations on Internet security.

INTELLECTUAL PROPERTY RIGHTS

The State Council and the NCAC have promulgated various regulations and rules relating to protection of software in the PRC. Under these regulations and rules, software owners, licensees and transferees may register their rights in software with the NCAC or its local branches and obtain software copyright registration certificates. Although such registration is not mandatory under PRC law, software owners, licensees and transferees are encouraged to go through the registration process and registered software rights may receive better protections.

Registered trademarks in the PRC are protected under the Trademark Law (商標法) adopted in 1982 and revised in 1993 and 2001. Trademarks can be registered with the Trademark Office of the SAIC for renewable ten-year periods. Trademark license agreements are required to be filed with the Trademark Office of the SAIC.

The MII issued the Administrative Measures on PRC Internet Domain Names (中國互聯網絡域名管理辦法) in the PRC in 2004. The regulation prohibits the registration and use of domain names with the following content that may (i) be in violation of the basic principles set forth in the PRC constitution; (ii) jeopardise state security, disclose any state secret, subvert state power or harm national unification; (iii) damage state honor or interests; (iv) incite ethnic hatred or discrimination or damage ethnical unity; (v) harm state religious policies or advocate heresy or feudal superstition; (vi) disseminate rumors, disrupt social order or sabotage social stability; (vii) disseminate obscenity, pornography or induce gambling, violence, murder, terror or other crimes; (viii) humiliate or slander any other person, or infringe the legal interests of any other person; or (ix) be otherwise prohibited by the PRC laws or administrative regulations.

Domain name disputes are governed by the Measures on Domain Name Dispute Resolution of PRC Internet Network Information Center (中國互聯網絡信息中心域名爭議解決辦法) promulgated by the CNNIC, and amended in February 2006 and becoming effective as of March 2006, under which the CNNIC can authorise domain name dispute resolution institutions to decide such disputes.

In May 2006, the State Council promulgated the Regulations on Protection of the Right of Dissemination through Information Networks (信息網絡傳播權保護條例), which became effective in July 2006. The regulation requires that every organisation or individual who disseminates a third party's work, performance, audio or visual recording products to the public through information networks shall obtain permission from, and pay compensation to, the legitimate copyright owner of such products, unless otherwise provided under relevant laws and regulations. The legitimate copyright owner may take technical measures to protect his or her right of dissemination through information networks and any organisation or individual shall not intentionally avoid, destroy or otherwise assist others in avoiding such protective measures unless permissible under law.

Under the provisions of the Regulations on Protection of Computer Software (計算機軟件保護條例) and the Measures on Registration of Computer Software Copyright (計算機軟件著作權登記辦法), computer software registered under the provisions can be better protected since the registration of computer software under the provisions can be taken as proof to the software copyright ownership in a computer software copyright dispute.

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As at the Latest Practicable Date, we have conducted necessary software products registration and software copyrights registration for our online games necessary for our operation. As confirmed by our PRC legal adviser, Jingtian and Gongcheng, we are in compliance with all the relevant PRC laws and regulations in relation to the intellectual property rights during the Track Record Period and up to the Latest Practicable Date.

PRIVACY PROTECTION

PRC law does not prohibit Internet content providers from collecting and analysing personal information from their users. We require our players to accept a user agreement whereby they agree to provide certain personal information to us. PRC law prohibits Internet content providers from disclosing to any third parties any information transmitted by users through their networks unless otherwise permitted by law. If an Internet content provider violates these regulations, the MII or its local bureaus may impose penalties and the Internet content provider may be liable for damages caused to its users.

During the Track Record Period and up to the Latest Practicable Date, we have not violated the privacy protection law in relation to the personal information we have collected.

REGULATION ON FOREIGN EXCHANGE

The principal regulation governing foreign currency exchange in the PRC is the Foreign Currency Administration Rules (外匯管理條例) which was issued by the State Council in January 1996 and became effective in April 1996 and amended in January 1997. Under these rules, RMB is freely convertible for payments of current account items, including trade and service related foreign exchange transactions and dividend payments, but not for expenses of capital, including direct investment, loan or investment in securities outside the PRC unless the prior approval of the SAFE has been obtained. Under the Foreign Currency Administration Rules (外匯管理條例), foreign-invested enterprises in the PRC may purchase foreign exchange without the approval of SAFE for trade and services-related foreign exchange transactions by providing commercial documents evidencing such transactions. They may also retain foreign exchange (subject to a cap approved by SAFE) to satisfy foreign exchange liabilities or to pay dividends. However, the relevant PRC government authorities, which have significant administrative discretion in implementing the laws, may restrict or eliminate the ability of foreign invested enterprises to purchase and retain foreign currencies in the future. In addition, foreign exchange transactions involving direct investment, loans and investment in securities outside the PRC are subject to limitations and require approvals from SAFE.

Pursuant to the SAFE's Notice on Relevant Issues Concerning Foreign Exchange Administration for PRC Residents to Engage in Financing and Inbound Investment via Overseas Special Purpose Vehicles (關於境內居民通過境外特殊目的公司融資及返程投資外匯管理有關問題的通知) (the "SAFE Circular No. 75"), issued on 21 October 2005, (i) PRC resident, shall register with the local branch of SAFE before it establishes or controls an overseas special purpose vehicle (the "overseas SPV"), for the purpose of overseas equity financing (including convertible debt financing); (ii) when a PRC resident contributes the assets of or its equity interests in a domestic enterprise into an overseas SPV, or engages in overseas financing after contributing assets or equity interests into an overseas

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SPV, such PRC resident shall register his or her interest in the overseas SPV and the change thereof with the local branch of SAFE; and (iii) when the overseas SPV undergoes a material event outside of the PRC, such as a change in share capital or merger and acquisition, the PRC resident shall, within 30 days from the occurrence of such event, register such change with the local branch of SAFE. In May 2007, SAFE issued guidance to its local branches with respect to the procedures for SAFE registration which strengthens the supervision on registrations pursuant to SAFE Circular No.75 and impose obligations on onshore subsidiaries of the overseas SPVs to coordinate and supervise the relevant PRC residents to complete registration.

Under SAFE Circular No. 75, failure to comply with the registration procedures set forth above may result in restrictions on a PRC subsidiary's foreign exchange activities and its ability to distribute dividends to overseas SPV, and penalties.

In accordance with the SAFE Circular No.75, the beneficial owners of the Controlling Shareholders who are PRC residents have conducted the overseas investment registration with Fuzhou Economic and Technical Development Zone Branch of SAFE for their respective overseas investment in us.

As confirmed by our PRC legal adviser, Jingtian and Gongcheng, we have been in compliance with the regulations on foreign currency exchange. Please also refer to "Risk Factors — Risks relating to the operations in the PRC — PRC regulations relating to the establishment of offshore special purpose companies by PRC residents may subject our PRC resident shareholders or us to penalties and otherwise adversely affect us" for the impact of the strengthened regulations on us.

Regulations Relating to Employee Share Options

Pursuant to the Implementation Rules of the Administration Measure for Individual Foreign Exchange (個人外匯管理辦法實施細則) (the "**Individual Foreign Exchange Rule**"), issued on 5 January 2007 by SAFE and relevant guidance issued in March 2007, PRC citizens who are granted shares or share options by an overseas listed company according to its employee share option plan or share incentive plan are required, through the PRC subsidiary of such overseas listed company or any other qualified PRC agent, to register with SAFE and complete certain other procedures related to the share option or other share incentive plan. Foreign exchange income received from the sale of shares or dividends distributed by the overseas listed company may be remitted into a foreign currency account of such PRC citizen or be exchange into RMB. In addition, the overseas listed company or its PRC subsidiary or other qualified PRC agent is required to appoint an asset manager or administrator, appoint a custodian bank and open dedicated foreign currency accounts to handle transactions relating to the share option scheme or other share incentive plan. We and our PRC citizen employees who will be granted share options (including the share options under the Share Option Scheme), or PRC option holders, will be subject to these rules upon the listing of our Shares on the Main Board. Please also refer to "Risk Factors - Risks relating to the operation in the PRC - Failure to comply with PRC regulations in respect of the registration of our PRC citizen employees' share options and restricted share units may subject such employees or us to fines and legal or administrative sanctions" of this document.

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As confirmed by our PRC legal adviser, Jingtian and Gongcheng, the Individual Foreign Exchange Rule does not have any impact to our adoption of the GEM Share Option Scheme and the Proposed Share Option Scheme since no share options under the GEM Share Option Scheme and the Proposed Share Option Scheme have been granted. When such share options are granted to our PRC citizen employees, such employees and we will have to comply with the Individual Foreign Exchange Rule.

The Enterprise Income Tax Law of PRC (中華人民共和國企業所得稅法) and its implementing rules

The Enterprise Income Tax Law of PRC (中華人民共和國企業所得稅法), promulgated by the National People's Congress (the "NPC") on 16 March 2007 and effective as of 1 January 2008, and the Regulations to the Enterprise Income Tax Law of PRC (中華人民共和國企業所得稅法實施條例), promulgated by the State Council on 28 November 2007 and effective as of 1 January 2008, provides that the enterprise income tax ("EIT") rate applicable to all enterprises, resident or non-resident, except individual-invested sole-proprietorship and partnership established under PRC laws and regulations, shall be 25%, generally. Resident enterprises, including but not limited to companies, institutes, associations, and other entities established under PRC laws and regulations, should pay EIT in connection with their income from PRC and abroad; non-resident enterprises with branch(es) within PRC, including but not limited to companies and other entities established under laws of foreign countries / regions, should pay EIT in connection with any income of such branch(es) from PRC, or out of PRC but of substantial connection with such branch(es); non-resident enterprises without any branch in PRC should pay EIT in connection with their income from PRC, at the tax rate of 20%. Hi-tech enterprises highly encouraged and supported by the State should apply to the EIT rate of 15%. Enterprises established before 16 March 2007 and enjoying preferential tax rate under then effective tax laws and regulations, may transit to the tax rate herein pursuant to applicable regulations by the State Council; those entitled to tax reduction and exemption for a fixed term may enjoy such preference until such term expires, provided that, such term which fails to commence because of nonoccurrence of making profit should commence in 2008, pursuant to applicable regulations by the State Council.

During the Track Record Period and up to the Latest Practicable Date, we have been in compliance with the laws and regulations on the enterprise income tax. As confirmed by our PRC legal adviser, Jingtian and Gongcheng, we have not violated any applicable PRC enterprise income tax laws and regulations. Please also refer to "Risk Factors — Risks relating to our business — We cannot assure that we will continue to enjoy preferential tax treatments or financial incentives in the future and changes in the PRC laws or policies may increase the tax burdens of us or our investors" for the impact of the Enterprise Income Tax Law of PRC and its implementing rules on us.

The Labor Contract Law of PRC (中華人民共和國勞動合同法) and The PRC Law for Promotion of Employment (中華人民共和國就業促進法)

The Labor Contract Law of PRC (中華人民共和國勞動合同法), promulgated by NPC Standing Committee on 29 June 2007 and effective as of 1 January 2008, provides that the employer should sign the written labor contract with an employee upon the commencement of such employment, or, at least, within one month thereafter, otherwise the employer should pay the employee twice the salary every

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month. A labor contract may be of a fixed term, indefinite term, or a term until completion of certain work. Unless otherwise stated by the employee, an indefinite labor contract should be established between the employer and the employee i) who has worked for the employer for more than ten consecutive years; ii) who has worked for the employer for more than ten consecutive years and is less than ten years from the statutory retirement age, in case of an employer implementing the labor contract system for the first time or immediately reshuffled from a state-owned enterprises; iii) who has consecutively signed the labor contract of fixed term twice; iv) with whom the employer signs no written contract within one year after commencement of employment. An employer which should sign a labor contract of indefinite term but failed to do so should pay the employee twice the salary every month from the date when the employer should do so. No breach-of-contract damages liable to the employee under a labor contract should be valid unless such damages: i) is stipulated as compensation for expenses on certain technical training in a written agreement under which the employer finances the employee for such training while the employee promises to serve the employer for a particular term; ii) is stipulated in the labor contract or a separated confidentiality agreement under which the employee is obliged to keep confidential the trade secrets and intellectual property-related secrets, and to observe the non-competition clause, while the employer should compensate the employee on a monthly basis within such non-competition period.

The PRC Law for Promotion of Employment (中華人民共和國就業促進法), promulgated by NPC Standing Committee on 30 August 2007 and effective as of 1 January 2008, provides that no employee can be discriminated in employment by reason of ethnic group, race, gender, or religious belief. The employer should neither refuse, nor request higher conditions for, the employment of any woman, merely because of such gender; and no provision limiting any woman employee in marriage and child-bearing is allowed in the labor contract. The employer should not refuse the employment of anybody just because of such person being an infection pathogen carrier, unless otherwise stated by laws and regulations. Additionally, enterprises should allocate the employee education fund intended for occupational training and further education of employees, violation of which may result in punishment imposed by the labor administration.

During the Track Record Period and up to the Latest Practicable Date, we have been in compliance with the laws and regulations on the labor contract and promotion of employment. As confirmed by our PRC legal adviser, Jingtian and Gongcheng, we have not violated any applicable PRC laws and regulations in relation to the labor contract and promotion of employment.

REGULATION ON DIVIDEND DISTRIBUTION

The principal regulations governing distribution of dividends paid by PRC wholly foreign-owned enterprises include (i) PRC Company Law (中華人民共和國公司法); (ii) Wholly Foreign-Owned Enterprise Law (中華人民共和國外資企業法); and (iii) Wholly Foreign-Owned Enterprise Law Implementing Rules (中華人民共和國外資企業法實施細則). Under the above laws and regulations, domestic companies and wholly foreign-owned enterprises in the PRC may pay dividends only from accumulated after-tax profits, if any, determined in accordance with the PRC accounting standards and regulations. In addition, such enterprises are required to set aside at least 10% of their after-tax profits each year, if any, to fund certain reserve funds. These reserves are not distributable as cash dividends. Under the relevant PRC law, no net assets other than the accumulated after-tax profits can be distributed in the form of dividends.

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As confirmed by our PRC legal adviser, Jingtian and Gongcheng, we have been in compliance with the regulations on dividend distribution.

ACQUISITION OF DOMESTIC ENTERPRISES BY FOREIGN INVESTORS

In August 2006, six PRC regulatory agencies promulgated the Rules on Acquisition of Domestic Enterprises by Foreign Investors (關於外國投資者並購境內企業的規定) (the “M&A Rules”) regulating the mergers and acquisitions of domestic enterprises by foreign investors. The M&A Rules became effective in September 2006 and the rules, among other things, purport to require that an offshore special purpose vehicle (“SPV”) formed for listing purposes and controlled directly or indirectly by PRC companies or individuals shall obtain the approval of the CSRC prior to the listing and trading of such SPV’s securities on an overseas stock exchange, especially in the event that the SPV acquires shares of or equity interests in the PRC companies in exchange for the shares of offshore companies. In September 2006, the CSRC published procedures specifying documents and materials required to be submitted for CSRC approval under the M&A Rules. The application of the M&A Rules are subject to interpretation.

Our PRC legal adviser, Jingtian and Gongcheng, advised that the M&A Rules do not require the CSRC approval for the listing of the Company on the Main Board of the Stock Exchange because (i) we have completed the acquisitions of the relevant PRC companies and obtained all necessary approvals from the relevant PRC authorities before 8 September 2006, the date on which the M&A Rules became effective, and (ii) such acquisitions were based on cash consideration and did not involve the exchange of shares of offshore companies.

However, our PRC legal adviser, Jingtian and Gongcheng, cannot rule out the possibility that the CSRC may require, either by interpretation or clarification of the M&A Rules or by any new rules, regulations or directives or in any other ways promulgated after the date of its legal opinion, that overseas listings of all SPVs (or those involving the acquisition of the PRC companies based on cash consideration before September 2006) must obtain the approval from the CSRC. If we are required to obtain CSRC approval, we will make an announcement to the public immediately.

REGULATIONS ON NETDRAGON (USA)

NetDragon (USA) has been in the business of providing support services for our business operation since its inception. Such support services include general administrative, customer services, payment depositing and handling, online promotion and marketing, game master and management services. NetDragon (USA) does not perform any payment and debt collection services and, in addition, when remitting funds to TQ Digital, all the transfers have been carried out through normal banking procedures and do not involve any physical transportation of currency or monetary instruments.

As confirmed by our US legal adviser, Morgan, Lewis & Bockius, LLP, the nature of NetDragon (USA) does not require any permits or licenses specifically related to carrying out such business or contravene any US federal law or regulations.

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INTERNAL COMPLIANCE PROCEDURE

In light of the developing nature of the online game industry and the fact that there have been many regulations introduced recently, including but not limited to the MII Notice and regulations on Internet Cafes, virtual currency and anti-addiction system, and the highly regulatory nature of the industry, we have two departments responsible to ensure our compliance with the relevant PRC laws and regulations. Our legal department constantly checks the publications from the PRC authorities to ensure we have obtained all the licenses and legal documents for our game development and operation. Our legal department coordinates with different governmental departments regarding the regular inspection of our operation as well as application, renewal and filing of our licenses and intellectual property documents. Our legal department is led by Lin Yun. Miss Lin was graduated from Jianlian College of Finance and Economics (建聯財經專科學校) with a major in Accounting. She has been responsible for our public relationship and the legal department since 2002. Miss Lin has been working with various of government departments on our industry regulations for years. Our quality assurance department constantly reviews our game content to ensure compliance with the requirements of the relevant PRC authority. Our quality assurance department is led by Huang Xiaoxi. Mr. Huang graduated from the law department of Hangzhou University of Commerce (杭州商學院). He joined us in June 2006 and has leveraged his legal background to set up the content evaluation criteria for us to comply with the industry regulation. Both our legal department and quality assurance department have been working closely with constant meetings being held to ensure that our online games have met the applicable legal requirements in the PRC. In addition, we have also engaged a law firm in Fujian as our external counsel providing us advice on our operation and legal compliance with the PRC laws and regulations.

As confirmed by our PRC legal adviser, Jingtian and Gongcheng, we have been in compliance with the relevant PRC laws and regulations which would affect our existing operation and business since our establishment. We further confirm that (i) there has not been any breach of applicable laws and regulations in connection with the industry regulations and corporate governance by us which would affect our existing operation and business, and (ii) our management systems and corporate governance practices, our records in protecting Shareholders' interests and our financial resources are in compliance with the applicable laws and regulations.

We have also adopted internal procedure relating to our financial activities. As led by our qualified accountant, Tam Hon Shan, Celia, details of which are set out in the section headed "Directors, senior management and staff" of this document, we have a team of 10 members in the finance department. They are well educated with finance background and related professional experience. We have also established a system for regular reporting of financial information. Quarterly financial information is provided to our Board for discussion with explanations noted for any material variances. Before Tam Hon Shan, Celia joined us in April 2007, our finance team was led by another qualified accountant, Wang Jianguo. Mr. Wang graduated with a tertiary certificate in Industrial Accounting from Fujian Zhonghua Vocational University in 1993 and has over 14 years of experience in financial management. The audit accounts of our group members in the PRC are prepared in accordance with the PRC accounting standards and the Directors have confirmed that there is no non-compliance in this regard since our establishment.