

Kunming Dianchi Water Treatment Co., Ltd.

Implementation Rules for Audit Committee of the Board

Chapter I General Provisions

- Article 1** In order to strengthen the decision making function of the board of Directors of Kunming Dianchi Water Treatment Co., Ltd. (the “**Company**”), achieve audit in advance and professional audit, ensure the Board’s effective surveillance of the management and further improve the corporate governance structure, the Company established the audit committee (the “**Audit Committee**”) of the Board and formulated these Implementation Rules for the Audit Committee in accordance with the Company Law of the People’s Republic of China, the Code of Corporate Governance for Listed Companies in China (promulgated by China Securities Regulatory Commission), the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “**Hong Kong Listing Rules**”), the Articles of Association of the Company and other relevant provisions.
- Article 2** The Audit Committee is a special working committee established by the Board as a professional committee under it. The Audit Committee reports and is accountable to the Board. In fulfilling its responsibilities, the Audit Committee shall abide by applicable laws and regulations, the Articles of Association and these Rules. By virtue of legislative requirements, the Articles of Association shall be subject to the supervision by the general meeting of shareholders and the Supervisory Committee of the Company. Its main responsibilities include supervision and examination of the internal and external audits and the internal control systems of the Company.

Chapter II Composition

- Article 3** The Audit Committee shall comprise three Directors (including two independent Directors). The members shall include at least one independent Director who shall be a professional accountant with qualifications stipulated under Rule 3.10(2) of the Hong Kong Listing Rules.
- Article 4** The members of the Audit Committee shall be nominated by the Chairman of the Board or more than one-half of independent Directors or one-third of all Directors and shall be elected by the Board.
- Article 5** The Audit Committee shall have one chairman, who shall be an independent Director, and shall be responsible for directing the works of the Audit Committee. The Chairman of the Audit Committee shall be voted and chosen from the members and shall be submitted to the Board for consideration and approval.
- Article 6** The term of office of the Audit Committee shall be in congruence with the term of the Board, and its members may be re-selected upon the expiry of the current term of office. If any member ceases to be a Director of the Company during his/her term of office, he/she shall automatically be disqualified as a member, and the vacancy shall be filled by the Audit Committee in accordance with the provisions of Articles 3 to 5 above.

Article 7 The Audit Department is an internal audit body of the Company and shall be responsible for the internal audit works under the guidance and supervision of the Audit Committee.

Article 8 The former partner of the existing external auditor of the Company shall not act as a member of the Audit Committee within one year from the following dates (whichever is the latter):

- (1) the date of his/her ceasing to be a partner of this auditor; or
- (2) the date where he/she no longer has any financial interest in this auditor.

Chapter III Terms of References

Article 9 The major terms of references of the Audit Committee include:

- (1) to make recommendations to the Board on the appointment, reappointment or removal of the external auditor, and approve the remuneration and terms of engagement of the external auditor, and any question about its resignation or dismissal;
- (2) to review and monitor the external auditor's independence and objectivity and the effectiveness of the audit process in accordance with applicable standards. The Audit Committee shall discuss with the external auditor about the nature and scope of the audit and related reporting obligations before the audit commences;
- (3) to guide and supervise the establishment and implementation of non-audit service system for internal and external audits of the Company;
- (4) to act as the key representative body between the Company and the external auditors, which shall be responsible for the internal audit and the communications between the Company and the external auditors (such as the accounting firms and Auditing Institutions of the People's Republic of China), and ensure a smooth coordination between the internal and external audits;

- (5) to review and monitor integrity of the Company's financial information (including its annual reports, half-year reports and quarterly reports (if prepared for publication)) and the disclosures thereof, and review significant financial reporting judgments contained therein; and to give due consideration to any matters raised by the Company's staff responsible for accounting and financial reporting function, compliance officers or auditors when considering any significant or unusual items that are reflected in the above financial information;
- (6) to organize and conduct various special audit tasks;
- (7) to review the financial and accounting policies and practices of the Company;
- (8) to review and examine the financial control, internal control and risk management systems of the Company, establish the Company's internal control systems, organize internal examinations and discuss with its management about the internal control systems;
- (9) to evaluate major investigation findings on internal control matters and management's response to these findings, as delegated by the Board or on its own initiative;
- (10) to review the letter from the external auditor to the management concerning the explanation of audit situation, any material queries raised by the external auditor to the management about accounting records, financial accounts or systems of control and management's relevant response;
- (11) to ensure that the Board will provide a timely response to the issues raised in the letter from the external auditor to the management concerning the explanation of audit situation;
- (12) to make a list of connected persons of the Company in a timely manner and submit to the Board and the Supervisory Committee in time;
- (13) to advice on the following in relation to purchase of assets from connected person by the Company at a premium, including but not limited to:
 1. the reasons supporting its opinion and the factors considered;
 2. whether the consideration of the transaction is fair and reasonable and in the interests of the Company and its shareholders as a whole;
 3. to make recommendation to the non-connected Directors and non-connected shareholders on agreeing or disagreeing such connected transaction.

- (14) to convene at least one meeting every quarter to consider the work plans and reports submitted by the internal audit department;
- (15) to report the decisions and proposals of the Audit Committee in writing to the Board and report regularly to the Board on the following matters:
 - 1. to promptly inform the Board on major matters which might affect the financial status and business operation of the Company;
 - 2. a self-appraisal of the Audit Committee and each member on the fulfillment of their duties.

To report to the Board at least once every quarter on matters including but not limited to progress and quality of internal audit and major problems identified. In reviewing these statements and reports before submitting them to the Board, the Audit Committee shall focus particularly on:

- 1) any changes in accounting policies and practices;
- 2) major judgmental area;
- 3) significant adjustments resulting from audit;
- 4) the going concern assumptions and any qualifications;
- 5) compliance with accounting standards or not;
- 6) compliance with the Hong Kong Listing Rules and legal requirements in relation to financial reporting or not;

- (16) to meet the external auditor at least twice a year;
- (17) to review relevant arrangements of the Company, under which the employees of the Company can in confidence raise concerns about possible improprieties in financial reporting, internal control or other matters and to ensure that proper arrangements are in place for fair and independent investigation of these matters and for appropriate follow-up action of the Company;
- (18) other issues authorized by the Board of the Company.

Article 9 The Audit Committee shall be accountable to the Board, and its proposals shall be submitted to the Board for approval. The Audit Committee shall assist the Supervisory Committee with the audit supervision.

The internal audit department shall report any material weakness or risk in the internal control systems identified in the process of audit to the Audit Committee in a timely manner. In the event that the Audit Committee deems the internal control systems of the Company have any material weakness or risk, the Board shall report to any relevant stock exchange promptly and make relevant disclosure. The Company shall publish an announcement to disclose any material weakness or risk in the internal control systems, any consequences that have occurred or may occur and any actions taken or to be taken.

Chapter IV Decision-making Procedures

Article 10 The audit working group shall be responsible for the pre-work of the Audit Committee in its decision making, and providing relevant materials to the Company in writing:

- (1) relevant financial reports of the Company;
- (2) internal and external auditors' working reports;
- (3) external audit contracts and relevant working reports;
- (4) information disclosed to the public by the Company;
- (5) audit report on material connected transactions of the Company;
- (6) other related matters of the Company.

Article 11 The Audit Committee meeting shall assess the report submitted by the audit department, and then submit relevant resolutions to the Board in writing:

- (1) evaluating the external auditor's work, recruiting or changing of the external auditor;
- (2) whether the Company's internal audit policies have been effectively implemented, and whether its financial report is complete and true;
- (3) whether the information disclosed to the public by the Company (including the financial report) is objective and true, and the material connected transactions are in compliance with the relevant laws and rules;
- (4) evaluation of the performance of the financial department and audit department of the Company and their responsible persons;
- (5) other relevant matters.

Chapter V Rules of Procedure

Article 12 The meetings of the Audit Committee shall consist of regular meetings and interim meetings. The regular meeting shall be held at least four times a year and one meeting shall be held in each quarter, and the interim meeting shall be held when it is proposed by members of the Audit Committee. Notice shall be given to all members seven days in advance. The meeting shall be chaired by chairman of the Audit Committee. Where the chairman is unable to attend the meeting, he/she may delegate another member (independent Director) to preside over the meeting. In case of emergency where an interim meeting of the Audit Committee needs to be convened as soon as practicable, the notice of meeting may at any time be given through telephone, fax or email, provided that an explanation shall be made by the convener at the meeting.

Article 13 The meeting of the Audit Committee shall not be held unless over two-thirds of the members attend the meeting. Each member shall have one vote and the resolutions made by the meeting must be approved by over half of all members.

Article 14 Voting at the meeting of the Audit Committee shall be taken by a show of hands or by voting and a meeting may also be convened in the form of communication in case of emergency.

Article 15 The Directors, supervisors and other senior management of the Company may be invited to attend meetings of the Audit Committee, if necessary.

- Article 16** The Audit Committee may retain an intermediary institution to provide professional advice on its decision when necessary. The expenses incurred shall be borne by the Company.
- Article 17** The convening procedures and voting methods of meetings of the Audit Committee as well as the resolutions passed at such meetings shall comply with relevant laws, regulations, the Articles of Association and these Rules.
- Article 18** The Audit Committee shall keep minutes of its meetings. The minutes shall be signed by committee members attending the meeting and minutes shall be kept by the secretary of the Board. Draft and final versions of minutes of each Audit Committee meeting shall be sent to all members of the Audit Committee for their comments and records, respectively, in both cases within a reasonable time after such meeting.
- Article 19** The resolutions passed and voting results of a meeting of the Audit Committee shall be submitted to the Board in writing.
- Article 20** All members of the committee present at the meeting shall keep confidential all matters discussed at the meeting and shall not disclose without approval.

Chapter VI Supplementary Provisions

- Article 21** These Rules shall come into effect on the date of the listing of the overseas-listed foreign shares (the H shares) of the Company on The Stock Exchange of Hong Kong Limited upon approval at a general meeting.
- Article 22** Any matters not covered by these Rules shall be implemented in accordance with relevant laws and regulations of the People's Republic of China, Hong Kong Listing Rules and the Articles of Association. In the event that the these Rules contravene any future laws and regulations of the People's Republic of China to be promulgated or the Articles of Association amended through valid procedures or the Hong Kong Listing Rules, the relevant laws and regulations of the People's Republic of China, the Hong Kong Listing Rules, and the Articles of Association shall prevail and these Rules shall be revised immediately and then reported to the Board for consideration and approval.
- Article 23** The right to interpret these Rules shall reside in the Board of the Company.