



Chongqing Machinery & Electric Co., Ltd.*
重慶機電股份有限公司

(a joint stock limited company incorporated in the People's Republic of China with limited liability)

(Stock Code: 02722)

Terms of Reference of the Audit Committee

Passed at the 2007 second extraordinary meeting of the first session of the Board on 16 August 2007

Amended for the first time at the 2011 twelfth extraordinary meeting of the second session of the Board on 25 November 2011

Amended for the second time at the 2012 fourth extraordinary meeting of the second session of the Board on 11 July 2012

Article 1 Definitions

For the purpose of these terms of reference (the **"Terms of Reference"**):

"Board" means the board of Directors of the Company.

"Company" or **"the Company"** means Chongqing Machinery & Electric Co., Ltd.*

"Secretary of the Board" means the secretary to the Board of the Company

"Director(s)" means members of the Board.

"Group" means the Company and its subsidiaries

and associated companies at the relevant time or, where the context so requires, in respect of the period before the Company became the holding company of its current subsidiaries and associated companies, the current subsidiaries and associated companies of the Company or the businesses operated by its current subsidiaries and associated companies or (as the case may be) its predecessor.

“Listing Rules” or “Rules” means the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, as amended from time to time.

“Articles of Association” means the articles of association of Chongqing Machinery & Electric Co., Ltd.*, as amended from time to time.

“Audit Committee” means the audit committee established by the Board according to the resolution which was approved under the Terms of Reference.

"Shareholder(s)" means the person(s) or corporation(s) who holds shares of the Company

Article 2 Constitution

The Board hereby resolves to establish a committee of the Board to be known as the Audit Committee.

Article 3 Composition and Membership of the Audit Committee

The Audit Committee shall comprise at least three non-executive Directors, a majority of whom should be independent non-executive Directors ("INEDs"). The Board may adjust the size of the Audit Committee according to the needs of the Company, provided that such adjustment is in compliance with relevant regulatory requirements. The Audit Committee shall have one chairman elected from the committee members who are INEDs, to take charge of its work.

At least one of the members must be an INED with appropriate accounting or related financial management expertise as required under the Listing Rules and

- (1) have no significant connected relationship with the Company.

- (2) fulfill the requirement of independence as stipulated by relevant regulatory rules.
- (3) A former partner of the Company's external independent auditor ("Auditor") shall not be appointed as a member of the Audit Committee within one year after the date of his ceasing to be a partner of the Auditor or to share any financial interest of the Auditor, whichever is the later.

Article 4 Term of Office of the Audit Committee

The term of office of the Audit Committee shall be the same as that of the Board, and its members may be eligible for re-election upon the expiry of their term of office. Any member who, during his term of office, ceases to be a non-executive Director shall automatically lose his membership on the Audit Committee and a replacement shall be appointed by the Board to fill the vacancy in accordance with relevant requirements of the Company.

Any change of the committee members shall be, if involving change of directors, subject to the approval of a general meeting in accordance with the procedure for change of directors stipulated in the Articles of Association as well as announcement as required by regulatory requirements.

Article 5 Resignation of Members

- (1) Should any member resign during his term of office, such

member shall submit to the Board through the Secretary to the Board a resignation letter one month in advance, in which detailed explanations should be given.

(2) In the event that the number of the Audit Committee is less than the quorum required due to the resignation of member(s), such resignation shall not take effect until the replacement member(s) elected by the Company take office.

(3) For any member who automatically loses his membership due to his resignation as a non-executive Director, there is no need to apply the resignation procedure for members of the Audit Committee. Such member shall automatically lose his membership on the date when he officially resigns from his position as a non-executive Director in accordance with the procedure for resignation of non-executive Directors of the Company. In the event that such automatic loss of membership may result in the number of the Audit Committee falling below the quorum, paragraph (2) of this Article shall apply as to when such loss of membership shall take effect.

Article 6 Meetings

(1) The Audit Committee should hold at least two regular meetings every year (before annual and interim results announcements, respectively).

(2) An extraordinary meeting of the Audit Committee may be

convened when the Auditor of the Company deems it necessary or two-thirds of the members propose to do so.

An Audit Committee meeting may not be held unless more than half of the members are present. It may be held by telephone conferencing or video conferencing or other means.

Article 7 Meetings by Way of Written Proposals

The Audit Committee may adopt written proposals and pass resolutions by way of circulation of written resolutions instead of holding a physical meeting. A written resolution shall be effective when the meeting materials are delivered to all members and the number of members who sign their consent reaches the quorum for passing such resolution.

Article 8 Convening and Chairing of Meetings

The meetings of the Audit Committee shall be convened by its chairman with assistance from the Secretary to the Board who may authorize the office of the Board to help deal with the convening, preparation and meeting affairs, etc.

Notice of an Audit Committee meeting should be delivered to every member at least ten days in advance. The meeting agenda and relevant documents should be delivered to every member at least five days in advance.

The meeting shall be presided over by the chairman.

Article 9 Resolutions of Meeting

Any resolution of an Audit Committee meeting shall be subject to the approval of two-thirds or more of all members, with each member having one vote.

Voting at an Audit Committee meeting may be taken by ballot or show of hands. Voting at an extraordinary Audit Committee meeting may be taken via telecommunications.

Any resolution of an Audit Committee meeting shall be in writing form and signed by each member present.

Article 10 Meeting Minutes

Each Audit Committee meeting shall keep complete and true meeting minutes. The office of the Board shall be in charge of taking the minutes of the Audit Committee meetings. The draft versions of the minutes shall be delivered to all members for review and confirmation within a week from the close of the meeting. The original minutes shall be kept by the Secretary to the Board.

Article 11 Non-voting Attendance

When it deems necessary, the Audit Committee may invite the Company's Management and other Directors to attend its meeting

as observers. Such attendees have no voting rights.

Article 12 Supporting Offices of the Audit Committee

The audit department and the office of the Board shall provide coordination and support for the routine operation of the Audit Committee.

Article 13 Terms of Reference of the Audit Committee

The primary duties of the Audit Committee are to assist the Board in supervising the following:

1. Management of relationship with the Company's Auditor
 - (1) to be primarily responsible for making recommendation to the Board on the appointment, reappointment and removal of the Company's Auditor, and to approve the remuneration and terms of engagement of the Auditor, and to take care of any issues concerning resignation or dismissal of that Auditor. Comments from the management and internal audit body of the Company should be given due consideration when the Audit Committee assesses the work of the Auditor;
 - (2) to review and monitor the Auditor's independence

and objectivity and the effectiveness of the audit process in accordance with applicable standards. The Audit Committee shall discuss with the Auditor the nature and scope of the audit and relevant reporting obligations before the audit commences;

- (3) to develop and implement policies on the engagement of the Auditor to supply non-audit services, including but not limited to providing recommendations for business development, industry study and internal controls of the Company. For this purpose, the Auditor shall include any entity that is under common control, ownership or management with the audit firm or any entity that a reasonable and informed third party having knowledge of all relevant information would reasonably conclude as part of the audit firm nationally or internationally. The Audit Committee should report to the Board, identifying any matters in respect of which it considers that action or improvement is needed and making recommendations as to the steps to be taken;
- (4) to oversee the work of the Auditor and to hear and consider any written report required to be submitted by the Auditor according to law;
- (5) to resolve the disagreement between the management of the Company and the Auditor on

the financial statements.

- (6) to oversee other activities as required by regulatory requirements.

2. Review of the financial information of the Company

- (1) to monitor the integrity of the Company's financial statements, annual report and accounts, half-year report and, if prepared for publication, quarterly reports, and to review the significant financial reporting judgements contained in them. In this regard, in reviewing the Company's annual report and accounts, half-year report and, if prepared for publication, quarterly reports before submission to the Board, the Audit Committee should focus particularly on:

- (i) any changes in accounting policies and practices;
- (ii) major judgmental areas;
- (iii) significant adjustments resulting from audit;
- (iv) the going concern assumptions and any qualifications;
- (v) compliance with accounting standards; and
- (vi) compliance with the Listing Rules and other legal requirements in relation to financial reporting.

- (2) In regard to (1) above:

- (i) members of the Audit Committee must liaise with the Board, management of the Company and qualified accountants. The Audit Committee must meet, at least twice a year, with the Auditor; and
- (ii) the Audit Committee should consider any significant or unusual items that are, or may need to be, reflected in such reports and accounts and must give due consideration to any matters that have been raised by the Company's financial controller, qualified accountants (if any), officer in charge of internal audit or the Auditor.

3. Oversight of the Company's financial reporting system and internal control procedures

- (1) to review the Company's financial control, internal control and risk management systems and to monitor the implementation thereof;
- (2) to discuss with the management the system of internal control and ensure that the management has discharged its duty to have an effective internal control system in place, including considering the adequacy of resources, qualifications and experience of staff of the issuer's accounting and financial reporting function, and their training programmes and budget;

- (3) to consider and analyse any findings of major investigations of internal control matters and managements' response as delegated by the board or on its own initiative;
- (4) to review the Company's financial and accounting policies and practices;
- (5) to review the Auditor's *Letter of Audit Fact* submitted to the management, any material queries raised by the Auditor to the management in respect of the accounting records, financial accounts or control systems and the management's response;
- (6) to ensure that the Board will provide a timely response to the issues raised in the Auditor's *Letter of Audit Fact* submitted to the management;
- (7) to report to the Board on the matters set out in this provision; and
- (8) to consider other topics, as defined by the Board.

4. Supervision of the internal audit matters of the Company

- (1) to co-ordinate the work of the internal audit body and the Auditor within the internal audit function of

the Company, and to ensure that the internal audit function is in full and effective operation and has appropriate standing within the Company, and to review and monitor the effectiveness of the internal audit function;

- (2) to maintain timely and effective communications with the management and internal audit body of the Company in regard to internal audit matters.

5. Other terms of reference of the Audit Committee

- (1) to set up the tip-offs mailbox and tip-offs phone line 63075735 in the audit department of the Company to deal with complaints and tip-offs about possible improprieties in financial reporting, internal controls or other matters, and ensure that proper arrangements are established for the fair and independent investigation of and appropriate follow-up action of the Company.
- (2) to act as the key representative body for overseeing the Company's relation with the Auditor. At least twice a year the Audit Committee shall meet with the Auditor.
- (3) to review at least once a year the management's annual report on execution of connected transactions and give review comments.

Article 14 Rights of the Audit Committee

1. To make inquiries with the general manager and the financial controller of the Company about the following issues:

- (1) whether there is any significant deficiency in the design or operation of internal controls which may affect the Company's ability to record, process, summarize, and report financial data;
- (2) any weakness in internal controls;
- (3) any fraud acts, whether or not material, that involves the management or other employees who have a significant role in the Company's internal controls;
- (4) any significant change in internal controls; and
- (5) other matters as required by regulatory policies, laws and regulations.

2. To engage professional advisers

For the purpose of carrying out its duties, the Audit Committee is entitled to engage independent legal advisors, certified accountants or other professional advisers with regard to such issues as recognizing potential conflict of interests, assessing

disclosure and other law and regulatory compliance matters and conducting independent investigation of financial statements and compliance with securities regulations, etc.

Article 15 Preparation of the Committee Report

The Audit Committee shall prepare and present its report to the Board, and disclose the same in the relevant report of the Company (if applicable) as required by regulatory requirements.

Article 16 Establishment of the Whistle-Blowing Mechanism

The Audit Committee shall accept and deal with complaints or tip-offs regarding finance, internal controls and audit of the Company and shall treat as confidential the confidential or anonymous tip-offs and relevant materials about suspected accounting or auditing irregularities.

Article 17 Obligations of the Committee Members

The obligations of Audit Committee members shall, as required by regulatory requirements and provisions hereof, include but not limited to the following:

- (1) to faithfully perform their duties, reasonably safeguard the best interests of the Company and fairly protect the interests of all Shareholders;

- (2) to attend meetings of the Audit Committee in person and on time, or, when failing to attend, appoint another member to attend on his behalf by power of attorney which shall state the scope of authorization;
- (3) to carefully review and consider all documents and topics presented to them;
- (4) to maintain adequate and effective communications with the management and internal audit body of the Company and the Auditor;
- (5) to ensure the time and energy devoted to the work of the Audit Committee. The Audit Committee members shall not take the same position in more than three domestic or overseas listed companies, unless otherwise approved by the Board.

Article 18 Remuneration of the Committee Members

The remuneration of the members of the Audit Committee shall be determined and approved by the Board. Payment may be made in the form of cash, shares or options. The members shall not receive, whether directly or indirectly, any consulting fees, advisory fees or other compensation from the Company other than the following:

- (1) remuneration received as a Director (including any

allowances and other benefits paid to all Directors) or as an employee representative.

- (2) remuneration for a position in any committee of the Board.
- (3) pension or other deferred compensation for the services that have been rendered as a Director (provided that such compensation is not contingent upon the provision of any other services by such Director in the future).

Article 19 Funds of the Audit Committee

The Audit Committee shall have funds and other resources necessary for the performance of its duties, including:

- (1) compensations payable to the Auditor for audit, review or attestation services;
- (2) all expenses for engagement of any external professional advisors; and
- (3) all necessary or appropriate administrative expenses for the Committee to perform its duties.

Article 20 Failure to Reach a Consensus on Engagement of External Auditor

When the Board disagrees with the recommendations made by the Audit Committee in respect of selection or appointment of the external auditor or resignation or removal of the Auditor, the Audit Committee shall present a statement explaining such recommendations to the Company which shall incorporate such statement in its corporate governance report in accordance with the Listing Rules.

Article 21 Availability of Terms of Reference

The Terms of Reference shall be made available upon request and published on the website of the Company by the Audit Committee so as to expound its duties and powers authorized by the Board.

Article 22 Amendment to and Termination of Terms of Reference

Any amendment hereto or the termination hereof is subject to the approval by the Board through resolutions.

(If there is any inconsistency or ambiguity between the English and Chinese versions of the Terms of Reference, the Chinese version shall prevail.)