JINCHI BIOTECH LTD

The Manager
National Stock Exchange of Australia Limited
Level 2
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Dear Sir

Risks Associated with Variable Interest Entity (VIE) Structure

Jinchi Biotech Ltd (NSX:JCB) and its subsidiaries and associated companies form a what is commonly known in China as a Variable Interest Structure Entity (VIE) structure. The Company wishes to inform the market about various risks that are associated with a VIE structure.

If the PRC government finds that the agreements that establish the structure for operating our business in China do not comply with its restrictions on foreign investment in development and cultivation of rare and improved breeds, or if these regulations or the interpretation of existing regulations change in the future, we could be subject to severe penalties or be forced to relinquish our economic benefits in the assets and operations of our affiliated PRC entities.

We are a BVI company and as such we are classified as a foreign enterprise under PRC laws. Our PRC subsidiary, Zhangjiajie Divine Spring Enterprise Management and Consulting Co., Ltd., is a wholly owned foreign investment enterprise. Various laws, regulations and rules in China restrict foreign ownership in, and restrict foreign investment enterprises from operating, and the development and cultivation of rare and improved breeds. In light of these restrictions, we conduct our operations in China mainly through a series of contractual arrangements.

We do not have any equity interest in our affiliated PRC entities but through such contractual arrangements we exercise effective control over our affiliated PRC entity. For a description of such contractual arrangements, see Item 2.2 in our Information Memorandum "Summary of Control Agreements". As a result, we are considered the primary beneficiary of our affiliated PRC entity and consolidate the results of operations of our affiliated PRC entity in our financial statements.

Our current ownership structure, the ownership structure of our PRC subsidiary and affiliated PRC entity and the contractual arrangements among our PRC subsidiary, our affiliated PRC entity and their respective shareholders are not in violation of existing PRC laws, rules and regulations and each contract under the contractual arrangements is valid, binding and enforceable under current PRC laws. However, there are substantial uncertainties regarding the interpretation and application of current and future PRC laws and regulations; accordingly, PRC regulatory authorities may ultimately take a view that is contrary to the opinion above.

We rely on contractual arrangements with our affiliated PRC entity and their respective shareholders for the operation of our business, which may not be as effective as direct ownership. If our affiliated PRC entity and their shareholders fail to perform their obligations under these contractual arrangements, we may have to resort to litigation to enforce our rights, which may be time consuming, unpredictable, expensive and damaging to our operations and reputation.

We conduct our business in China mainly through our affiliated PRC entity. The contractual arrangements with our affiliated PRC entity and their respective shareholders provide us with effective control over our affiliated PRC entity. Although each contract under these contractual arrangements is valid, binding and enforceable under current PRC laws, these contractual arrangements may not be as effective as direct ownership in providing us with control over our affiliated PRC entity. For example, our affiliated PRC entity and their shareholders may breach their contractual arrangements with us by, among other things, failing to operate our businesses in an acceptable manner, by refusing to renew these contracts when their initial term expires, or by taking other actions that are detrimental to our interests. If we were the controlling shareholder of our affiliated PRC entity with direct ownership, we would be able to exercise our rights as shareholders, rather than our rights under the powers-of-attorney, to effect changes to its board of directors, which in turn could implement changes at the management and operational level. However, under the current contractual arrangements, as a legal matter, if any of our affiliated PRC entity or its shareholders fails to perform their obligations under these contractual arrangements, we may incur substantial costs to enforce such arrangements and rely on legal remedies under PRC laws, which may not be sufficient or effective. These remedies may include seeking specific performance or injunctive relief and claiming damages, any of which may not be sufficient or effective.

These contractual arrangements are governed by PRC laws. Accordingly, these contracts would be interpreted in accordance with PRC laws and any disputes would be resolved in accordance with PRC legal procedures. The PRC regulatory environment presents inherent uncertainties. Uncertainties presented by the PRC legal system could limit the legal protections available to us and subject us to legal risks, which could have a material adverse effect on our business, financial condition and results of operations. As a result, our rights under the contractual arrangements could not be honoured and our ability to enforce these contracts under the contractual arrangements could be limited. If we are unable to enforce these contractual arrangements, or if we suffer significant delay or other obstacles in the process of enforcing these contractual arrangements, we may not be able to exert effective control over our affiliated PRC entity and their shareholders. As a result, our business and operations could be severely disrupted, which could damage our reputation and materially and adversely affect our business, financial condition, results of operations and prospects.

The contractual arrangements with our affiliated PRC entity may be reviewed by the PRC tax authorities for transfer pricing adjustments, which could increase our overall tax liability.

The PRC Enterprise Income Tax Law, effective on January 1, 2008, or the EIR Law, requires every enterprise in China to submit its annual enterprise income tax return together with a report on transactions with its related parties to the relevant tax authorities. The PRC tax authorities may impose reasonable adjustments on taxation if they have identified any related-party transactions that are inconsistent with arm's-length principles. Zhangjiajie (China) Jinchi Giant Salamander Biological Technology Co., Ltd. and Zhangjiajie Divine Spring Enterprise Management and Consulting Co., Ltd. could face material adverse tax consequences if the PRC tax authorities determined that the contractual arrangements between them were not entered into based on arm's-length negotiations and therefore constitute a favourable transfer pricing arrangement. Although we based our contractual arrangements on those of similar businesses, if the PRC tax authorities determined that these contracts were not entered into on an arm's-length basis, they could request that our affiliated PRC entity adjust their taxable income upward for PRC tax purposes. Such a pricing adjustment could adversely affect us by increasing our affiliated PRC entity tax expenses, and could subject our affiliated PRC entity to late payment fees and other penalties for underpayment of taxes. As a result, our consolidated net income may be adversely affected.