

Fuwei Films (Holdings), Co. Ltd.  
Form 20-F  
April 11, 2014

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 20-F**

(Mark One)

**REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934**

**OR**

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the fiscal year ended December 31, 2013**

**OR**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**OR**

**SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**OR**

Date of event requiring this shell company report \_\_\_\_\_

**Commission file number: 001-33176**

Fuwei Films (Holdings) Co., Ltd.

(Exact name of Registrant as specified in its charter)

(Translation of Registrant's name into English)

Cayman Islands

(Jurisdiction of incorporation or organization)

No. 387 Dongming Road

Weifang Shandong

People's Republic of China, Postal Code: 261061

(Address of principal executive offices)

Yong Jiang

Tel: +86133 615 59266

fuweiir@fuweifilms.com

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(Name, Telephone, E-mail and/or Facsimile number and Address of Company Contact Person)

Securities registered or to be registered pursuant to Section 12(b) of the Act.

Title of each class Name of each exchange on which registered

Ordinary Shares NASDAQ Global Market

Securities registered or to be registered pursuant to Section 12(g) of the Act. None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act. None

As of December 31, 2013, there were 13,062,500 ordinary shares outstanding.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes  No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

Yes  No

Note - Checking the box will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 from their obligations under those Sections.

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

International Financial Reporting Standards as issued by  
U.S. GAAP  Other   
the International Accounting Standards Board

If "Other" has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow:

Item 17  Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

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## SPECIAL NOTE ON FORWARD-LOOKING STATEMENTS

This Annual Report contains many statements that are “forward-looking” and uses forward-looking terminology such as “anticipate,” “believe,” “expect,” “estimate,” “future,” “intend,” “may,” “ought to,” “plan,” “should,” “will,” negatives of such similar statements. You should not place undue reliance on any forward-looking statement due to its inherent risk and uncertainties, both general and specific. Although we believe the assumptions on which the forward-looking statements are based are reasonable and within the bounds of our knowledge of our business and operations as of the date of this annual report, any or all of those assumptions could prove to be inaccurate. As a result, the forward-looking statements based on those assumptions could also be incorrect. The forward-looking statements in this Annual Report include, without limitation, statements relating to:

- our goals and strategies;
- our future business development, results of operations and financial condition;
- our ability to protect our intellectual property rights;
- expected growth of and changes in the PRC BOPET film industry and in the demand for BOPET film products;
- projected revenues, profits, earnings and other estimated financial information;
- our ability to maintain and strengthen our position as a leading provider of BOPET film products in China;
- our ability to maintain strong relationships with our customers and suppliers;
- our planned use of proceeds;
- effect of competition in China and demand for and price of our products and services; and
- PRC governmental policies regarding our industry.

The forward-looking statements included in this Annual Report are subject to risks, uncertainties and assumptions about our businesses and business environments. These statements reflect our current views with respect to future events and are not a guarantee of our future performance. Actual results of our operations may differ materially from information contained in the forward-looking statements as a result of risk factors some of which are described under “Risk Factors” and elsewhere in this Annual Report. Risks, uncertainties and assumptions include, among other things:

- competition in the BOPET film industry;
- growth of, and risks inherent in, the BOPET film industry in China;
- unpredictable impact on the company’s revenue by price movements of crude oil in recent years;
- uncertainty in our export due to trade protectionism around the world;
- uncertainty as to future profitability and our ability to obtain adequate financing for our planned capital expenditure requirements;
- uncertainty in our ability to develop and manufacture high value-added products for the new production line (thick film) to win in the competition;
- uncertainty as to our ability to continuously develop new BOPET film products and keep up with changes in BOPET film technology;
- risks associated with possible defects and errors in our products;
- uncertainty as to our ability to protect and enforce our intellectual property rights;
- uncertainty as to our ability to attract and retain qualified executives and personnel;

- uncertainty as to our ability to attract and retain experienced financial reporting staff familiar with U.S. GAAP;
- uncertainty in acquiring raw materials on time and on acceptable terms;
- adverse effect on our business caused by adjustment of economic structure regulations of the Chinese government;
- adverse effect on our business caused by the uncertainty in economic recovery of major developed countries; and
- adverse effect on our business caused by extreme climate changes.

These risks, uncertainties and assumptions are not exhaustive. Other sections of this Annual Report include additional factors which could adversely impact our business and financial performance. The forward-looking statements contained in this Annual Report speak only as of the date of this annual report or, if obtained from third-party studies or reports, the date of the corresponding study or report, and are expressly qualified in their entirety by the cautionary statements in this Annual Report. Since we operate in an emerging and evolving environment and new risk factors and uncertainties emerge from time to time, you should not rely upon forward-looking statements as predictions of future events. Except as otherwise required by the securities laws of the United States, we undertake no obligation to update or revise any forward-looking statements to reflect events or circumstances after the date of this Annual Report or to reflect the occurrence of unanticipated events.



## INTRODUCTION

This annual report on Form 20-F includes our audited consolidated financial statements as of December 31, 2013 and 2012 and for the years ended December 31, 2013, 2012 and 2011.

Our ordinary shares are listed on the Nasdaq Global Market, or NASDAQ, under the symbol “FFHL”.

Except as otherwise required and for purposes of this Annual Report only:

- “Fuwei”, “Company”, “us”, “our” or “we” refer to Fuwei Films (Holding) Co., Ltd. The term “you” refers to holders of our ordinary shares.
- “China” or “PRC” and the “Chinese government” refer to the People’s Republic of China and its government. All references to “Renminbi,” or “RMB” are to the legal currency of China, all references to “U.S. dollars,” “dollars,” “\$” or “US” are to the legal currency of the United States and all references to “Hong Kong dollars” or “HK\$” are to the legal currency of Hong Kong. Any discrepancies in any table between totals and sums of the amounts listed are due to rounding.
- “BOPET” refers to the Biaxially Oriented Polyester Film.

## CURRENCIES AND EXCHANGE RATES

We publish our financial statements in Chinese Yuan (“Renminbi” or “RMB”). In this annual report on Form 20-F, references to “U.S. dollars” or “\$” are to the currency of the United States and references to “RMB” are to the currency of China.

Solely for your convenience, certain RMB amounts in this annual report have been translated into U.S. dollars. The rate of translation is based on the noon buying rate for Chinese Yuan in New York City as certified for custom purposes by the Federal Reserve Bank of New York on the various dates specified where the translations are set forth in this annual report. References to the “noon buying rate” in this annual report refer to this rate. These translations should not be taken as assurances that the RMB amounts actually represent these U.S. dollar amounts or that they were or could have been converted in U.S. dollars at the rate indicated or at any other rate. The noon buying rate was US \$1.00 = RMB6.0537 on December 31, 2013.

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The following table sets forth various information concerning exchange rates between the Renminbi and the U.S. dollar for the periods indicated. These rates are provided solely for your convenience and are not necessarily the exchange rates that we used in this Annual Report or will use in the preparation of our other periodic reports or any other information to be provided to you. The source of these rates is the Federal Reserve Bank of New York.

|                               | Average | High   | Low    | Period-end |
|-------------------------------|---------|--------|--------|------------|
| 2009 <sup>(1)</sup>           | 6.8311  | 6.8368 | 6.8242 | 6.8270     |
| 2010 <sup>(1)</sup>           | 6.7788  | 6.8336 | 6.5820 | 6.6118     |
| 2011 <sup>(1)</sup>           | 6.4630  | 6.6364 | 6.2939 | 6.2939     |
| 2012 <sup>(1)</sup>           | 6.3088  | 6.3879 | 6.2221 | 6.2301     |
| 2013 <sup>(1)</sup>           | 6.1478  | 6.2438 | 6.0537 | 6.0537     |
| November 2013 <sup>(2)</sup>  | 6.0929  | 6.0993 | 6.0903 | 6.0922     |
| December 2013 <sup>(2)</sup>  | 6.0738  | 6.0927 | 6.0537 | 6.0537     |
| January 2014 <sup>(2)</sup>   | 6.0509  | 6.0600 | 6.0402 | 6.0590     |
| February 2014 <sup>(2)</sup>  | 6.0816  | 6.1448 | 6.0591 | 6.1448     |
| March 2014 <sup>(2)</sup>     | 6.1729  | 6.2273 | 6.1183 | 6.2164     |
| April 2014 <sup>(2) (3)</sup> | 6.2085  | 6.2118 | 6.2064 | 6.2118     |

(1) Annual averages are calculated by averaging the rates on the last business day of each month during the relevant period.

(2) Monthly average is calculated by averaging the daily rates during the relevant period.

(3) As of April 4, 2014, the exchange rate was 6.2188.

## **PART I**

### **Item 1. Identity of Directors, Senior Management and Advisers**

Not applicable.

**Item 2. Offer Statistics and Expected Timetable**

Not applicable.

**Item 3. Key Information****A. Selected financial data.**

The following selected financial data should be read in conjunction with Item 5 - the “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and the Financial Statements and Notes thereto included elsewhere in this Annual Report.

The following selected historical statement of income data for the years ended December 31, 2013, 2012 and 2011 and the selected historical balance sheet data as of December 31, 2013 and 2012 have been derived from the Company’s audited consolidated financial statements included in this Annual Report beginning on page F-1. The following selected historical statement of income data for the years ended December 31, 2010 and 2009, and the selected historical balance sheet data as of December 31, 2011, 2010 and 2009 have been derived from the Company’s audited financial statements not included in this Annual Report. The audited financial statements are prepared and presented in accordance with United States generally accepted accounting principles, or U.S. GAAP.

Certain factors that affect the comparability of the information set forth in the following table are described in the “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” and the Financial Statements and related notes thereto included elsewhere in this Annual Report.

|                                       | For the year ended December 31, |           |           |           |          |           |
|---------------------------------------|---------------------------------|-----------|-----------|-----------|----------|-----------|
|                                       | 2013                            |           | 2012      | 2011      | 2010     | 2009      |
| (in thousands, except per share data) | RMB                             | US\$      | RMB       | RMB       | RMB      | RMB       |
| Statement of Operations Data:         |                                 |           |           |           |          |           |
| Revenues                              | 304,950                         | 50,374    | 372,866   | 537,645   | 501,458  | 320,731   |
| Gross (loss) profit                   | (15,425 )                       | (2,548 )  | (3,107 )  | 85,472    | 130,553  | 24,612    |
| Operating (loss) income               | (64,394 )                       | (10,637 ) | (63,984 ) | 30,736    | 59,630   | (16,547 ) |
| Interest expense                      | (10,094 )                       | (1,667 )  | -         | (10,227 ) | (8,846 ) | (6,540 )  |

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|  |            |            |            |            |            |            |
|--|------------|------------|------------|------------|------------|------------|
| (Loss) Income before income taxes                          | (68,959 )  | (11,391 )  | (62,164 )  | 24,993     | 50,754     | (23,024 )  |
| Net (loss) income attributable to the Company              | (58,971 )  | (9,741 )   | (54,427 )  | 21,081     | 40,783     | (18,963 )  |
| (Loss) Earnings per share                                  |            |            |            |            |            |            |
| Basic  | (4.51 )    | (0.74 )    | (4.17 )    | 1.61       | 3.12       | (1.45 )    |
| Diluted  | (4.51 )    | (0.74 )    | (4.17 )    | 1.61       | 3.12       | (1.45 )    |
| Weighted average number ordinary shares, Basic and diluted |            |            |            |            |            |            |
| Basic  | 13,062,500 | 13,062,500 | 13,062,500 | 13,062,500 | 13,062,500 | 13,062,500 |
| Diluted  | 13,062,500 | 13,062,500 | 13,062,500 | 13,062,500 | 13,062,500 | 13,062,500 |

| (in thousands)                     | Year Ended<br>December 31, |         | 2012<br>RMB | 2011<br>RMB | 2010<br>RMB | 2009<br>RMB |
|------------------------------------|----------------------------|---------|-------------|-------------|-------------|-------------|
|                                    | 2013<br>RMB                | US\$    |             |             |             |             |
| Balance Sheet Data:                |                            |         |             |             |             |             |
| Cash and cash equivalents          | 11,578                     | 1,913   | 5,006       | 44,172      | 171,227     | 26,804      |
| Accounts and bills receivable, net | 8,373                      | 1,383   | 21,587      | 52,457      | 25,482      | 28,785      |
| Inventories                        | 38,454                     | 6,352   | 34,291      | 41,774      | 52,577      | 45,039      |
| Total current assets               | 134,613                    | 22,237  | 123,915     | 281,904     | 263,458     | 119,282     |
| Property, plant and equipment, net | 524,777                    | 86,687  | 233,335     | 277,119     | 284,891     | 318,600     |
| Total assets                       | 732,047                    | 120,926 | 747,550     | 790,174     | 798,152     | 735,509     |
| Short-term bank loans              | 105,000                    | 17,345  | 110,000     | 168,501     | 142,000     | 153,179     |
| Total current liabilities          | 250,200                    | 41,329  | 201,922     | 205,492     | 214,580     | 198,666     |
| Total shareholders' equity         | 460,307                    | 76,038  | 519,234     | 573,669     | 552,544     | 511,567     |

Shandong Fuwei was entitled to preferential tax treatment at an EIT rate of 15% for the years ended December 31, 2010, 2011, 2012 and 2013 due to its status as a High-and-New Tech Enterprise since December 2009. If Shandong Fuwei was no longer designated as such, it would have been subject to a standard enterprise income tax at a rate of 25%. Net income and basic and diluted earnings per share would be reduced by the following amounts, if Shandong Fuwei was not entitled to a reduced EIT rate for the years 2013, 2012, 2011, 2010, and 2009:

| (In thousands, except per share data) | Year Ended December 31, |             |             |             |             |
|---------------------------------------|-------------------------|-------------|-------------|-------------|-------------|
|                                       | 2013<br>RMB             | 2012<br>RMB | 2011<br>RMB | 2010<br>RMB | 2009<br>RMB |
| Net income                            | -                       | -           | (2,499)     | (5,075)     | -           |
| Earnings per share                    |                         |             |             |             |             |
| - basic                               | -                       | -           | (0.19 )     | (0.39 )     | -           |
| - diluted                             | -                       | -           | (0.19 )     | (0.39 )     | -           |

The 2013 RMB amounts included in the above selected financial data have been translated into U.S. dollars at the rate of US \$1.00 = RMB6.0537, which was the noon buying rate for U.S. dollars in effect on December 31, 2013 in the City of New York for cable transfer in RMB per U.S. dollar as certified for custom purposes by the Federal Reserve Bank. No representation is made that the RMB amounts could have been, or could be, converted into U.S. dollars at that rate or at any other certain rate on December 31, 2013, or on any other date.

### Exchange Rate Information

On July 21, 2005 the Chinese government changed its policy of pegging the value of the Renminbi to the U.S. dollar. This revaluation of the Renminbi was based on a conversion of Renminbi into United States dollars at an exchange rate of US\$1.00=RMB8.11. Under the new policy, the Renminbi will be permitted to fluctuate within a band against a basket of certain foreign currencies. On December 31, 2013, this change in policy resulted in an approximately 25.36% appreciation in the value of the Renminbi against the U.S. dollar compared to 2005. Although the Company generates its revenue in the PRC in Renminbi which has become more valuable in U.S. dollars, the Company's overseas sales and U.S. dollars cash deposits are subject to foreign currency translations which will impact net income (loss).

**B. Capitalization and indebtedness.**

Not applicable.

**C. Reasons for the offer and use of proceeds.**

Not applicable.

**D. Risk factors.**

The following matters and other additional risks not presently known to us or that we deem immaterial, may have a material adverse effect on our business, financial condition, liquidity, results of operations or prospects or otherwise. Reference to a cautionary statement in the context of a forward-looking statement or statements shall be deemed to be a statement that any one or more of the following factors may cause actual results to differ materially from those in such forward-looking statement or statements.

**(a) Risks Associated with Our Business**

*Our business may be adversely affected by the continued appreciation of RMB against US dollar and trade protection measures in place by several countries against exports of BOPET films from China.*

Our business operation may be adversely affected due to continued appreciation of RMB against US dollar, and more stringent trade protection measures in place such as antidumping investigations conducted by several countries against exports of BOPET films originated from China.

*A sharp fluctuation in the demand for raw materials may have a negative impact on our operations if we are unable to pass on all increases in cost of raw materials to our customers on a timely basis.*

The total cost of raw materials made up approximately 71.4%, 73.0% and 78.3% of our production cost in 2013, 2012 and 2011, respectively. The main raw materials used in our production of BOPET film are polyethylene terephthalate (or PET) resin and additives, which respectively made up approximately 86.7% and 13.3% of our total cost of raw materials in the past three years on average.

The prices of PET resin and additives are, to a certain extent, affected by the price movement of crude oil. Currently the PET resin is mainly used as a raw material in China's textile industry. Therefore, the market prices of PET resin will fluctuate due to changes in supply and demand conditions in that industry. Any sudden shortage of supply or significant increase in demand of PET resin and additives may result in higher market prices and thereby increase our cost of sales.

In 2014, it is expected that there will be a continued capacity expansion within China, and we may not be able to pass on the increase in costs of raw materials to our customers on a timely basis, which may have an adverse impact on the results of our operations. Our ability to hedge against these fluctuations by either entering into long-term supply contracts or offsetting our exposure to these commodity price variations has been significantly limited. Currently, we have no hedging transactions in place with respect to PET resin or any other petroleum product.

*Rising Competition caused by soaring capacity of BOPET films may materially affect our operations and financial conditions.*

We operate in a highly competitive and rapidly evolving field, and new developments are expected to continue at a rapid pace. Competitors may succeed by expanding their capacity or succeed in developing products that are more efficient, easier to use or less expensive than those which have been or are being developed by us or that would render our technology and products obsolete and non-competitive. Any of these actions by our competitors could adversely affect our sales.

In addition, several companies are developing similar and substitute products to address the same packaging field that we are targeting. These competitors may have greater financial and technical resources, productivity, marketing capabilities and facilities, cost-efficiency and human resources, or they may have a better quality of products, service, and shorter lead time. The competition from these competitors may adversely affect our business.

An increase in competition could result in slow increase in demand, selling price reductions or loss of our market share, which could have an adverse material impact on our operations and financial condition, or result in substantial losses to the Company.

The existing manufacturers and new entrants have been expanding their production capacity of the BOPET films since the second half of 2010, which have resulted in substantial increase in production of BOPET films from 2011 to 2013. As a result, the market supply in 2014 will increase more than demand. This will have an adverse impact on our sales and operation. In the event that we are unable to compete successfully or retain effective control over the pricing of our products, our profit margins might decrease.

In addition, China has gradually lowered import tariffs after its entry into the World Trade Organization in December 2001. Aiming at the huge market for high value-added films in China, manufacturers from developed countries, including Japan and South Korea started investing in China and some of these facilities had been put into production. This may lead to increased competition from foreign companies in our industry, some of which are significantly larger and financially stronger than us. If we fail to compete effectively with these companies in the future, our current business and future growth potential would be adversely affected.

***We maybe subject to inventory risks that would negatively impact our operating results.***

The possible price decline of the inventory may adversely affect the Company's operation. The fluctuation of the market prices of our raw material inventory and end product inventory will also adversely affect the value of our inventory.

***A significant portion of our revenue is derived from the flexible packaging industry in the PRC; our revenue might be adversely impacted if the flexible packaging industry is adversely affected.***



A significant portion of our revenue is currently derived from the production and sale of BOPET films. Our BOPET films are mainly used in the flexible packaging industry for consumer products such as tobacco packaging, alcoholic beverages, food, cosmetics and so on. The demand for our BOPET films is therefore affected by the demand for flexible packaging.

Since the second half of 2011, the sales and prices of our products has been declining significantly as a result of increased supply over demand in China and declined demand from overseas market. If such situation continues in the future, such as the continued slowdown of the market demand or the increase of the demand continues to be less than that of the supply, it could continue to have an adverse impact on our financial condition and operation of our business.

***We rely on key managerial and technical personnel and failure to attract or retain such personnel may compromise our ability to perform our strategies and then to develop new products and to effectively carry on our research and development and other efforts.***

Our success to date has been largely attributable to the contributions of key management and experienced personnel, with whom we have entered into service agreements. The loss of their services might impede the achievements of our strategies and development objectives and might damage the close business relationship we currently enjoy with some of our major customers. Our continued success is dependent, to a large extent, on our ability to attract or retain the services of these key personnel. Except for Mr. Xiaohan He, we do not currently maintain any other life insurance for our directors or officers. Our future success will also depend on our continued ability to attract and retain highly motivated and qualified personnel. The rapid growth of the economy in China has caused intense competition to attract and retain qualified personnel. Considering deficiency in legal environment in China, we cannot assure you that we will be able to retain our key personnel or that we will be able to attract, train or retain qualified personnel in the future.

If our R&D team cannot effectively develop new products, promote the market process, or we are unable to afford to continue to maintain this team or are not able to hire eligible and talented personnel, our ability to research and development, operation results and market competitiveness may be adversely affected.

***Marketability of any of our new products is uncertain and low acceptance levels of any of our new products will adversely affect our revenue and profitability.***

The development of our products is based on complex technology, and requires significant time and expertise in order to meet industry standards and customers' specifications. Although we have developed some products that meet customers' requirements in the past, there is no assurance that any of our research and development efforts will necessarily lead to any new or enhanced products or generate expected market share to justify commercialization. We must continually improve our current products and develop competitive new products to address the requirements of our customers. If our new products are unable to gain market acceptance, we would not be able to generate future revenue from our investment in research and development. In such event, we would be unable to increase our market share and achieve and sustain profitability. Our failure to further refine our technology and develop and introduce new products attractive to the market could cause our products to become uncompetitive or obsolete, which could reduce our market share and cause our sales to decline.

***It is difficult to anticipate whether and when the new production line can develop and manufacture high value-added films; this may have an adverse impact on us and we may not be able to reduce our losses.***

The total investment of the new production line is estimated to be US\$51 million. We have commenced the R&D of the high value-added products (such as films for TFT-LCD screens) to be manufactured by this line, however, we are uncertain as to whether the products can be developed as scheduled or recognized by customers.

The new production line has been approved to produce common thick films ranging from thickness of 38 $\mu$ m to 250 $\mu$ m, however, it is difficult to anticipate when the new production line can develop high-value-added films. In addition, the sales prices of our commodity thick films are far less than our costs due to more supply than demand in such a tough market. As a result, the new production line may not be profitable in the short term and may be faced with more loss.

***The circumstances under which we acquired ownership of our main productive assets may jeopardize our ability to continue as an operating business.***

On September 24, 2004, the People's Court of Weifang declared Shandong Neo-Luck bankrupt due to its financial difficulties. Shandong Neo-Luck pledged its main assets for the operation of the DMT production line to Weifang Commercial Bank before its bankruptcy.

The pledged DMT production line was auctioned on October 22, 2004 by the Shandong Neo-Luck Clearance Committee. DMT subsequently sought monetary damages from Shandong Neo-Luck for approximately US \$1.25 million plus interest relating to a claim of partial non-payment for the DMT production line by way of application of the ICC arbitration and the hearing was held in Geneva in November 2007. Fuwei Shandong joined these discussions later as an interested party and in order to support a resolution of the pending dispute and to achieve resolution of certain outstanding service and spare part issues. All parties entered into a Settlement Agreement in March 2008 and the arbitration was withdrawn by the ICC. Under the Service Agreement entered into in connection with the Settlement Agreement, Shandong Fuwei would pay an amount of US\$180,000 in two installments with respect to service and spare parts. The Company made its first payment in April 2008. As of December 31, 2013, Shandong Fuwei had paid US\$135,000 and still has US\$45,000 left unpaid.

Under the Settlement Agreement, the Neoluck Group was obligated to pay an amount equal to US\$900,000 in RMB by delivery of a bank draft to DMT. In April 2008, the Neoluck Group had not performed its obligation under the Settlement Agreement, and, the Neoluck Group and DMT entered into a Supplemental Agreement pursuant to which the Neoluck Group would pay the amount owed to DMT in two installments. The Neoluck Group paid the first installment equal to US\$450,000 in April 2008. As agreed between Neoluck Group and DMT, the remaining US\$450,000 was to be paid in installments by the end of December 2008. As of December 31, 2013, Neoluck Group had paid US\$320,000 and still had US\$130,000 outstanding to DMT.

Substantially all of our operating assets were acquired through two auction proceedings under relevant PRC law. We acquired the Brückner production line in 2003 as a result of a foreclosure proceeding enforcing an effective court judgment and the DMT production in 2004 as a result of a commercial auction from a consigner who obtained such assets through a bankruptcy proceeding. In the opinion of our PRC counsel, Concord & Partners, these proceedings are both valid under Chinese auction and bankruptcy law based on certain factual assumptions. Our PRC counsel's opinion solely relates to the legal procedure of the auctions and is based upon certain factual assumptions, our written representations and written reports of the auction company and other related parties. There can be no assurance that relevant authorities or creditors of the predecessor owner of these assets will not challenge the effectiveness of these asset transfers based upon the facts and circumstances of these transfers, despite the existence of independent appraisals, and other facts and circumstances of the auctions that cannot be verified by our PRC counsel. Taking into consideration the facts known by our PRC counsel related to the auction of the Brückner production line and the significant difference in the price paid for the DMT production line at the two bankruptcy auctions involved in our purchase of that asset and, assuming the representations and reports received by our PRC counsel are true and correct in all material respects, our PRC counsel is of the opinion that the auctions of the Brückner and DMT production lines were valid under PRC law and the possibility of the creditors of Shandong Neo-Luck successfully exercising recourse or claiming repayment with respect to our assets purchased in the bankruptcy proceeding should be remote. However, should any such challenge be brought in China (or elsewhere) and prevail, we may incur substantial liabilities and be required to pay substantial damages as a result of acquiring these assets and this could materially affect our ability to continue our operation.

***We have, in the past, experienced and may, from time to time, experience negative working capital. We also face risks associated with debt financing (including exposure to variation in interest rates).***

Our total short-term loan as of December 31, 2013 was RMB105.0 million (US\$17.3 million), which excludes RMB10.0 million (US\$1.7 million) of long-term loans. We have pledged property, plant and equipment and lease prepayments as security for indebtedness of RMB 105.0 million (US\$17.3 million) of bank loans and credit line amounting to RMB50.0 million (US\$8.3 million) granted by SPD bank. In the event that we default on all expired indebtedness, our lenders could foreclose on our assets. In the event that our assets are foreclosed upon, we will not be able to continue to operate our business.

Our obligations under our existing loans have been mainly met through the cash flow from our operations and our financing activities. We are subject to risks normally associated with debt financing, including the risk of significant

increases in interest rates and the risk that our cash flow will be insufficient to meet required payment of principal and interest. In the past, cash flows from operations have been sufficient to meet payment obligations. There is, however, no assurance that we will be able to continue to do so in the future. We may also underestimate our capital requirements and other expenditures or overestimate our future cash flows. In such event, we may consider additional bank loans, issuing bonds, or other forms of financing to satisfy our capital requirements. If any of the aforesaid events occur and we are unable for any reason to raise additional capital, debt or other financing to meet our working capital requirements, our business, operating results, liquidity and financial position will be adversely affected. For example, if we fail to get appropriate ongoing funds especially enough working capital, it will negatively impact the investment in the continued operation of our new production line. In addition, if we do not obtain financing or have negative working capital, there is a possibility that we may not be able to perform our contracts with our suppliers as a result of our inability to pay them back. The foregoing factors may have an adverse effect on our operation.

***We may lose our competitive advantage and our operations may suffer if we fail to prevent the loss or misappropriation of, or disputes over, our intellectual property.***

As of December 31, 2013, we have received 21 patents from, and have 12 patent applications pending with the PRC authorities. All these patents are related to our products and production processes. We may not be able to successfully obtain the approvals of the PRC authorities for the pending patent applications. In addition to the patents, proprietary techniques including processes, ingredients and technologies are important to our business as they enable us to maintain our competitive advantage over our competitors. Furthermore, third parties may assert claims to our proprietary processes, ingredients and technologies.

Our ability to compete in our markets and to achieve future revenue growth will depend, in significant measure, on our ability to protect our proprietary technology and operate without infringing upon the intellectual property rights of others. The legal regime in China for the protection of intellectual property rights is still at its early stage of development. Intellectual property protection became a national effort in China in 1979 when China adopted its first statute on the protection of trademarks. Since then, China has adopted its Patent Law, Trademark Law and Copyright Law and promulgated related regulations, such as the Regulation on Computer Software Protection, Regulation on the Protection of Layout Designs of Integrated Circuits and Regulation on Internet Domain Names. China has also acceded to various international treaties and conventions in this area, such as the Paris Convention for the Protection of Industrial Property, Patent Cooperation Treaty, Madrid Agreement and its Protocol Concerning the International Registration of Marks. In addition, when China became a party to the World Trade Organization in 2001, China amended many of its laws and regulations to comply with the Agreement on Trade-Related Aspects of Intellectual Property Rights. Despite many laws and regulations promulgated and other efforts made by China over the years with a view to tightening up its regulation and protection of intellectual property rights, the enforcement of such laws and regulations in China has not achieved the level in developed countries. Both the administrative agencies and the court system in China are not well-equipped to deal with violations or handle the nuances and complexities between compliant technological innovation and non-compliant infringement.

We rely on trade secrets and registered patents and trademarks to protect our intellectual property. We have also entered into confidentiality agreements with our management and employees relating to our confidential proprietary information. However, the protection of our intellectual properties may be compromised as a result of:

- departure of any of our management member(s) or employee(s) in possession of our confidential proprietary information;
- breach by such resigned management member(s) or employee(s) of his or her confidentiality and non-disclosure undertaking to us;
- expiration of the protection period of our registered patents or trademarks;
- infringement by others of our proprietary technology and intellectual property rights; or
- refusal by relevant regulatory authorities to approve our patent or trademark applications.

Any of these events or occurrences may reduce or eliminate any competitive advantage we have developed, causing us to lose sales or otherwise harm our business. There is no assurance that the measures that we have put into place to protect our intellectual property rights will be sufficient. As the number of patents, trademarks, copyrights and other intellectual property rights in our industry increases, and as the coverage of these rights and the functionality of the products in the market further overlaps, we believe that business entities in our industry may face more frequent infringement claims. Litigation to enforce our intellectual property rights could result in substantial costs and may not be successful. If we are not able to successfully defend our intellectual property rights, we might lose the rights to technology that we need to conduct and develop our business. This may seriously harm our business, operating results and financial condition, and enable our competitors to use our intellectual property to compete against us.

Furthermore, if third parties claim that our products infringe their patents or other intellectual property rights, we might be required to devote substantial resources to defend against such claims. If we fail to defend against such infringement claims, we may be required to pay damages, modify our products or suspend the production and sale of such products. We cannot guarantee that we will be able to modify our products on commercially reasonable terms.

***We may incur capital expenditures in the future in connection with our growth plans and therefore may require additional financing.***

To expand our business, we will need to increase our products mix and capacity, which will require substantial capital expenditures especially enough working capital for the continued operation of our new production line. Such expenditures are likely to be incurred in advance of any increase in sales. We cannot assure you that our revenue will increase after such capital expenditures are incurred. Any failure to increase our revenue after incurring capital expenditures to expand production capacity will reduce our profitability.

In addition, we may need to obtain additional debt or equity financing to fund our capital expenditures. Additional equity financing may result in dilution to existing shareholders' return. Additional debt financing may be required which, if obtained, may:

- limit our ability to pay dividends or require us to seek consents for the payment of dividends;
- increase our vulnerability to general adverse economic and industry conditions;
- limit our ability to pursue our growth plan;  
require us to dedicate a substantial portion of our cash flow from operations to payment for our debt, thereby
- reducing availability of our cash flow to fund capital expenditures, working capital and other general corporate purposes;
- limit our flexibility in planning for, or reacting to, changes in our business and our industry; and/or
- not assure that we will be able to obtain the additional financing on terms that are acceptable to us, if at all.

***A disruption in the supply of utilities, fire or other calamity at our manufacturing plant would disrupt production of our products and adversely affect our sales.***

Our BOPET films are manufactured solely at our production facilities located in Weifang City in the PRC. Any disruption in the supply of utilities, in particular, electricity, water or gas supply or any outbreak of fire, flood or other calamity resulting in significant damage at our facilities would severely affect our production of BOPET film and, as a result, we could incur substantial loss of equipment and properties.

While we maintain insurance policies covering losses in respect of damage to our properties, machinery and inventories of raw materials and products, we cannot assure you that our insurance would be sufficient to cover all of our potential losses.

***We have limited experience in operating outside mainland China, and failure to achieve our overseas expansion strategy may have an adverse effect on our business growth in the future.***

Our future growth depends, to a considerable extent, on our ability to develop both the domestic and overseas markets. We are currently exploring new business opportunities outside mainland China for our BOPET film products. Our primary overseas customers are from Europe, Asia and North America. However, we have limited experience in operating outside mainland China, and limited experience with foreign regulatory environments and market practices. As a result, we cannot guarantee that we will be able to penetrate any overseas market. Failure in the development of overseas market may have an adverse effect on our business growth in the future.

***We have encountered anti-dumping investigations in South Korea and the United States, and our overseas expansion strategy in our future business growth may be adversely affected.***

Since 2007, the manufacturers in China, India and other countries have encountered anti-dumping investigations conducted by South Korea and the United States.

The Korean Trading Committee (KTC) announced the final results for anti-dumping investigations for enterprises in China and India on August 27, 2008. We finally received the anti-dumping duties (ADD) rate of 5.67% which is much lower than the average rate of 23.60% for other enterprises in China. On June 22, 2011, Ministry of Strategy and Finance, Republic of Korea, initiated a sunset review concerning the continued imposition of an anti-dumping duty on imports of the BOPET Films originating from China and India. The rate for Shandong Fuwei, the subsidiary of Fuwei Films was set at 11.72%, higher than one of its counterparts at 5.87%. Punitive duties of 25.32% will be imposed on the PET films manufactured by six Chinese firms. The rate for the remaining Chinese manufacturers was set at 23.61%. The anti-dumping duties imposed on the Company's exported biaxially oriented polyethylene-terephthalate (BOPET) films to South Korea will be extended for three more years beginning on May 25, 2012.

The US Department of Commerce conducted the anti-dumping investigation in October 2007 covering exporters in China, Brazil, Thailand and the United Arab Emirates. 41 exporters in China were under investigation. In October 2008, the anti-dumping judgments were announced. Although we received the lowest ADD rate of 3.49% among five exporters that received a duty, our export to the United States, to a certain extent, was still adversely affected by paying the ADD.



On January 23, 2010, the US Department of Commerce (“USDOC”) began a first round annual review of Chinese BOPET exporters. Fuwei received the lowest anti-dumping duty (ADD) rate of 30.91% in this administrative review conducted by the USDOC, while the ADD rate of other four Chinese companies reviewed by the USDOC is more than 36.93%. In accordance with relevant laws and regulations in the US, the ADD rate of final results will retroactively apply to those US companies which imported Chinese-exported BOPET films, including Fuwei Films USA, LLC, during the period of first review, so these US importers are obligated to pay a supplementary antidumping duty at this ADD rate. In March 2011, we submitted comments to the USDOC regarding perceived ministerial errors made in calculating the ADD applicable to us. As a result of a Court challenge brought by Fuwei, in January 2013, the USDOC found that Fuwei did not dump goods in the United States market for the period from November 6, 2008 to October 31, 2009. The USDOC, after recalculating the rate, found that the level of dumping was “de minimis.” A rate which is de minimis is treated by the USDOC as a finding of zero. The final results of the second round annual review were announced in March 2012, according to which, an ADD rate of 8.48% was imposed on Fuwei Films which is slightly higher than the lowest antidumping duty rate of 8.42% of all the Chinese exporters being reviewed.

On December 30, 2011, USDOC commenced its third routine annual review of BOPET films originated from China. In order to gain an opportunity to continue exporting to the United States, Fuwei Films, although not a mandatory respondent, will actively respond to the review to the extent permitted by law and will continue to seek the low rate which should properly apply to its exports to the United States. In June 2013, the final results of the third round annual review were issued and an ADD rate of 12.80% was imposed on Fuwei Films. The preliminary results of the fourth round annual review were announced in December 2013, according to which, an ADD rate of 31.77% was imposed on Fuwei Films. The exports value to the United States accounted for less than 0.01% for the year of 2013.

In addition, if other countries or regions, such as the European Union, take trade protection measures against China's BOPET film or downstream industries, our business may be adversely affected.

***Changes in Applicable PRC Taxes may be adversely affect the Company.***

On October 18, 2010, the State Council issued a notice that the city maintenance and construction tax as well as educational surcharges shall be extended from Chinese companies to foreign-funded enterprises and citizens. Beginning December 1, 2010, Interim Regulations on City Maintenance and Construction Tax of the People's Republic of China and Decision of the State Council on Amending the Interim Provisions on the Collection of Educational Surcharges shall be applicable to foreign-funded enterprises, foreign enterprises and foreign citizens, which mean they will no longer exempt from such taxes. In accordance with the regulations, since December 1, 2010, our subsidiary - Shandong Fuwei became a taxpayer of city maintenance and construction tax as well as educational surcharges which shall be based on value-added tax, the consumption tax and business tax which currently stands at 12%. In July 2011, according to the new rules promulgated by the local government in China, Shandong Fuwei shall contribute to a fund for local water conservation projects since July 1, 2011 which is based on the actual value-added tax, consumption tax and business tax with a rate of 1%. The new policy incurs additional tax expense. If the Chinese government changes its tax policies or adds new types of taxes in the future, our business may be adversely affected.

***China's actions to save energy and reduce emissions may adversely affect our business, by subjecting us to significant new costs and restrictions on our operations.***

Recently the Chinese government has tightened its control over energy saving and emission reduction. The Chinese government intends to reduce energy consumption for gross domestic products and water consumption for industrial added value. Certain of our manufacturing plants that use significant amounts of energy, including electricity and gas, are likely to be affected by this plan. Therefore, our operation might be influenced by the energy saving and emission reduction measures of the Chinese government. Regulations for restricting greenhouse gas emission may increase the prices of the electricity we purchase, increase costs for our use of natural gas, potentially restrict access to or the use of natural gas, require us to purchase allowances to offset our emissions or result in an overall increase in our costs of raw materials, any of which could increase costs and negatively affect our business operations or financial results.

***The current labor law changes in the PRC may have an adverse impact on our business and profitability.***

The Company is of the view that the amended Labor Law of the People's Republic of China (the "PRC"), which took effect on January 1, 2008 and contains certain heightened requirements with respect to employment law, does not constitute a material risk to the Company. The amended Labor Law contains new provisions which protect the interests of the employees, including provisions which stipulate that an employer shall enter into labor contracts with its employees and pay social welfare insurance which may increase our human resources costs. In addition, the amended Labor Law also states that upon expiry of the labor contract, under some circumstances, an employer shall compensate an employee of the employer who does not renew the labor contract, which may increase our operating expenses. However, to the best of the Company's knowledge, Shandong Fuwei constantly abides by the Labor Law of PRC, as amended, and therefore we does not believe the labor law provisions and any changes will have any material

impact on its business or profitability. However, the Labor Law changes in the PRC in the future may have an adverse impact on our business and profitability.

***Our primary source of funds for dividends and other distributions from our operating subsidiary in China is subject to various legal and contractual restrictions and uncertainties, and our ability to pay dividends or make other distributions to our shareholders are negatively affected by those restrictions and uncertainties.***

We are a holding company established in the Cayman Islands and conduct our core business operations through our principal operating subsidiary, Shandong Fuwei, in China. As a result, our profits available for distribution to our shareholders are dependent on the profits available for distribution from Shandong Fuwei. If Shandong Fuwei incurs debt on its own behalf, the debt instruments may restrict its ability to pay dividends or make other distributions, which in turn would limit our ability to pay dividends of our ordinary shares. Under the current PRC laws, because we are incorporated in the Cayman Islands, our PRC subsidiary, Shandong Fuwei, is regarded as a wholly foreign-owned enterprise in China. For dividends paid by foreign invested enterprises, the PRC laws permit payment of dividends only out of net income as determined in accordance with PRC accounting standards and regulations. Determination of net income under PRC accounting standards and regulations may differ from determination under U.S. GAAP in significant respects, such as the use of different principles for recognition of revenues and expenses. In addition, distribution of additional equity interests by our PRC subsidiary, Shandong Fuwei, to us (which is credited as fully paid through capitalizing its undistributed profits) requires additional approval of the PRC government. Under the PRC laws, Shandong Fuwei, a wholly foreign-owned enterprise, is required to set aside a portion of its net income each year to fund designated statutory reserve funds. These reserves are not distributable as cash dividends. As a result, our primary internal source of funds of dividend payments from Shandong Fuwei is subject to these and other legal and contractual restrictions and uncertainties, which in turn may limit or impair our ability to pay dividends to our shareholders. Moreover, any allotment of funds from us to Shandong Fuwei, either as a shareholder loan or as an increase in registered capital, is subject to registration with or approval by PRC governmental authorities. These limitations on the flow of funds between us and Shandong Fuwei could restrict our ability to act in response to changing market conditions.

***Investor confidence and the market price of our shares may be adversely impacted if we are unable to issue an unqualified opinion on the adequacy of our internal controls over our financial reporting beginning as of December 31, 2013, as required by Section 404 of the U.S. Sarbanes-Oxley Act of 2002.***

As a public company, we are required by section 404 of the Sarbanes-Oxley Act 2002 to include a report by management on our internal controls over financial reporting that contains our management's assessment of the effectiveness of our internal controls in our annual report on Form 20-F. Based on our evaluation, our principal executive officer and principal financial officer previously concluded as of December 31, 2010, our internal controls over financial reporting were effective as of such date. However, in connection with the review of our Annual Report on Form 20-F by the Securities and Exchange Commission and subsequent reconsideration of the conclusion regarding effectiveness originally expressed therein, our principal executive officer and principal financial officer have now revised their conclusions and believe that as of the Evaluation Date, our internal controls over financial reporting were ineffective as of December 31, 2010 and that such internal controls exhibited a "material weakness," or a deficiency, or combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis. The material weaknesses identified resulted from inadequate technical accounting staff with knowledge of and experience with US generally accepted accounting principles, pursuant to which we prepare our consolidated financial statements, to support stand-alone external financial reporting under public company or SEC requirements. The report of management contained in this Annual Report on Form 20-F also reflects the determination of the reviewing officers that as of December 31, 2011, 2012 and 2013, we continued to have a material weakness in our internal controls over financial reporting.

We are in the process of developing and implementing a remedial plan to address the deficiencies in the areas of personnel with knowledge of and experience with US generally accepted accounting principles, including recruiting a full-time reporting manager with U.S. GAAP experience and conducting training in U.S. GAAP principles for all the financial reporting staff of the Company. However, additional measures may be necessary, and the measures we expect to take to improve our internal controls may not be sufficient to address the issues identified, to ensure that our internal controls are effective or to ensure that such material weakness or other material weaknesses would not result in a material misstatement of our annual or interim financial statements. In addition, other material weaknesses or significant deficiencies may be identified in the future. If we are unable to correct deficiencies in internal controls in a timely manner, our ability to record, process, summarize and report financial information accurately and within the time periods specified in the rules and forms of the SEC will be adversely affected. This failure could negatively affect the market price and trading liquidity of our common stock, cause investors to lose confidence in our reported financial information, subject us to civil and criminal investigations and penalties, and generally materially and adversely impact our business and financial condition.

**(b) Risks Relating to Business Operations in China**

***A Chinese entity has substantial influence over our company and its interest may not be aligned with the interests of other holders of our ordinary shares.***

Shandong SNTON Optical Materials Technology Co., Ltd., a PRC entity (“Shandong Optical”), beneficially owns approximately 52.90% of our outstanding share capital. On March 25, 2014, beneficial ownership of 6,912,503 ordinary shares of the Company previously owned by Weifang State-Owned Assets Operation Administration Company (the “Administration Company”), a wholly-owned subsidiary of Weifang State-Owned Asset Management and Supervision Committee (the “Weifang Committee”) through Apex Glory Holdings Limited, a British Virgin Islands corporation, was transferred to Shandong SNTON Optical Materials Technology Co., Ltd., a PRC entity (“Shandong Optical”) through a public auction. The transfer process is expected to be completed by the end of April 2014. As a result, this major shareholder has substantial influence over our business, including decisions regarding mergers, consolidations and the sale of all or substantially all of our assets, election of directors and other significant corporate actions. This concentration of ownership may discourage, delay or prevent a change in control of our company, which could deprive our shareholders of an opportunity to receive a premium for their shares as part of a sale of our company and might reduce the price of our ordinary shares. Alternatively, our controlling shareholder may cause a merger, consolidation or change of control transaction even if it is opposed by other shareholders.

In addition, as a new entrant into the BOPET industry, the main business of Shandong Optical and its two BOPET production lines that are currently under construction, may overlap with our business operations. Majority of our products, customers and market orientation may be the same and as a result, the marketing strategy of Shandong Optical may conflict with the interests of other holders of our ordinary shares.

*The discontinuation of any preferential tax treatments or other incentives currently available to us in the PRC could materially and adversely affect our business, financial condition and results of operations.*

Our subsidiary, Shandong Fuwei, was converted into a wholly foreign owned enterprise in January 2005 and could enjoy certain special or preferential tax treatments regarding enterprise income tax in accordance with the “Income Tax Law of the PRC for Enterprises with Foreign Investment and Foreign Enterprises” at that time. Accordingly, at that time, it was entitled to tax concessions whereby the profit for the first two financial years beginning with the first profit-making year (after setting off tax losses carried forward from prior years) was exempt from income tax in the PRC and the profit for each of the subsequent three financial years was taxed at 50% of the prevailing tax rates set by the relevant tax authorities. Shandong Fuwei was designated as a High-and-New Tech Enterprise in December 2008 and was recertified in October 2011 and enjoys a favorable enterprise income tax rate of 15%. If there are any future changes in PRC tax laws, rules and regulations or Shandong Fuwei will not be designated as a High-and-New Tech Enterprise, Shandong Fuwei will no longer enjoy the preferential tax treatment. If that were to occur, Shandong Fuwei would be subject to a 25% standard enterprise income tax rate which would significantly increase our effective tax rate and materially adversely affect our operating results.

On March 16, 2007, the National People’s Congress of the PRC passed the Enterprise Income Tax Law of the People’s Republic of China, which took effect on January 1, 2008. In accordance with the law, a unified enterprise income tax rate of 25% and unified tax deduction standards were applied equally to both domestic-invested enterprises and foreign-invested enterprises. Enterprises established prior to March 16, 2007 eligible for preferential tax treatment in accordance with the currently prevailing tax laws and administrative regulations would, under the regulations of the State Council, gradually become subject to the new tax rate over a five-year transition period starting from the date of effectiveness of the law. We expect details of the transitional arrangement for the five-year period from January 1, 2008 to December 31, 2012 applicable to enterprises established prior to March 16, 2007, such as Shandong Fuwei, to be set out in more detailed implementing rules to be adopted in the future. In addition, certain qualifying “High Technology Enterprises” may still benefit from a preferential tax rate of 15% under the new tax law if they meet the definition of “Government Advocated High Technology Enterprise” to be set forth in the more detailed implementing rules when they become adopted. Shandong Fuwei was designated as a High-and-New Tech Enterprise in December 2008 and will retain its status as a high-tech enterprise for three years commencing from 2011 enjoying a favorable corporate tax rate during the term from January 1, 2011 to December 31, 2013 pursuant to the income law Enterprise Income Tax Law.

In accordance with a notice issued by the PRC government in October, 2010, since December 1, 2010, Shandong Fuwei, our subsidiary, will become a taxpayer of city maintenance and construction tax as well as educational surcharges which shall be based on value-added tax, the consumption tax and business tax which currently stand at 12%. In July 2011, according to the new rules promulgated by the local government in China, Shandong Fuwei shall contribute to a fund for local water conservation projects since July 1, 2011 which is based on the actual value-added tax, consumption tax and business tax with a rate of 1%. The policy changes may have an adverse impact on our net profit.

***We are subject to environmental laws and regulations in the PRC.***

We are subject to environmental laws and regulations in the PRC. Any failure by us to comply fully with such laws and regulations will result in us being subject to penalties and fines or being required to pay damages. Any change in the regulations may require us to acquire equipment or incur additional capital expenditure or costs in order to comply with such regulations. Our profits will be adversely affected if we are unable to pass on such additional costs to our customers.

In recent years, there have been many newly-built residential buildings in close proximity to our factory. The complaints from nearby residents about the noise caused by our production may require us to take measures to lower noise, which will lead to additional cost to us. In the event that we are forced to suspend our production to take improvement measures, our operations and earnings may be adversely affected.

***Changes in foreign exchange regulations in China may affect our ability to pay dividends in foreign currencies.***

We currently receive most of our operating revenues in Renminbi. Currently, Renminbi is not a freely convertible currency and the restrictions on currency exchanges in China may limit our ability to use revenues generated in Renminbi to fund our business activities outside China or to make dividends or other payments in U.S. dollars. The PRC government strictly regulates conversion of Renminbi into foreign currencies. Over the years, the PRC government has significantly reduced its control over routine foreign exchange transactions under current accounts, including trade- and service-related foreign exchange transactions, foreign debt service and payment of dividends. In accordance with the existing foreign exchange regulations in China, our PRC subsidiary, Shandong Fuwei, is able to pay dividends in foreign currencies, without prior approval from the PRC State Administration of Foreign Exchange, or SAFE, by complying with certain procedural requirements. The PRC government may, however, at its discretion, restrict access in the future to foreign currencies for current account transactions and prohibit us from converting our Renminbi-denominated earnings into foreign currencies. If this occurs, our PRC subsidiary may not be able to pay us dividends in foreign currency without prior approval from SAFE. In addition, conversion of Renminbi for most capital account items, including direct investments, is still subject to government approval in China and companies are required to open and maintain separate foreign exchange accounts for capital account items. This restriction may limit our ability to invest earnings of Shandong Fuwei.

***Fluctuation in the value of Renminbi could adversely affect our overseas sales and import of raw materials and the value of, and dividends payable on, our shares in foreign currency terms.***

The value of Renminbi is subject to various factors and depends to a large extent on China's domestic and international economic, financial and political developments, as well as the currency's supply and demand in the local market. From 1994, the conversion of Renminbi into foreign currencies, including the U.S. dollar, was based on exchange rates set and published daily by the People's Bank of China, the PRC central bank, based on the previous day's interbank foreign exchange market rates in China and exchange rates on the world financial markets. The official exchange rate for the conversion of Renminbi into U.S. dollars remained stable until Renminbi was revalued in July 2005 and allowed to fluctuate by reference to a basket of foreign currencies, including the U.S. dollar. Under the new policy, Renminbi is permitted to fluctuate within a band against a basket of foreign currencies. This change in policy resulted initially in an approximately 2.0% appreciation in the value of Renminbi against the U.S. dollar. The Chinese government may adopt a substantially more liberalized currency policy, which could result in a further and more significant appreciation in the value of Renminbi against the U.S. dollar. Since our income and profits are denominated in Renminbi, fluctuation in the value of Renminbi could adversely affect our overseas sales and import of raw materials and further negatively affect our revenue and net income. Any appreciation of Renminbi would increase the value of, and any dividends payable on, our shares in foreign currency terms. Conversely, any depreciation of Renminbi would decrease the value of, and any dividends payable on, our shares in foreign currency terms.

***The uncertain legal environment in China could limit the legal protections available to you.***

The PRC legal system is a civil law system based on written statutes. Unlike the common law system, the civil law system is a system in which decided legal cases have little precedential value. In the late 1970s, the PRC government began to promulgate a comprehensive system of laws and regulations to provide general guidance on economic and business practices in China and to regulate foreign investment. Our PRC subsidiary, Shandong Fuwei, is a wholly foreign-owned enterprise and is subject to laws and regulations applicable to foreign investment in China in general and laws and regulations applicable to wholly foreign-owned enterprises in particular. China has made significant progress in the promulgation of laws and regulations dealing with economic matters such as corporate organization and governance, foreign investment, commerce, taxation and trade. However, the promulgation of new laws, changes of existing laws and abrogation of local regulations by national laws may have a negative impact on our business and prospects. In addition, as these laws, regulations and legal requirements are relatively recent and because of the limited volume of published cases and their non-binding nature, the interpretation and enforcement of these laws, regulations and legal requirements involve significant uncertainties. These uncertainties could limit the legal protections available to foreign investors, including you. For example, it is not clear if a PRC court would enforce in China a foreign court decision brought by you against us in shareholders' derivative actions. Moreover, the enforceability of contracts in China, especially with the government, is relatively uncertain. If counterparties repudiated our contracts or defaulted on their obligations, we may not have adequate remedies. Such uncertainties or inability to enforce our contracts could materially and adversely affect our revenues and earnings.



***Outbreak of viruses such as SARS, H1N1 or other epidemics could materially and adversely affect our overall operations and results of operations.***

From March to July 2003, mainland China, Hong Kong, Taiwan and some other areas in Asia experienced an outbreak of a new and contagious form of atypical pneumonia known as severe acute respiratory syndrome, or SARS. A recurrent outbreak, or an outbreak of a similarly contagious disease, such as the H1N1 avian flu, could potentially disrupt our operations to the extent that any one of our employees is suspected of having the infection or that any of our facilities is identified as a possible source of spreading the virus or disease. We may be required to quarantine employees who are suspected of having an infection. We may also be required to disinfect our facilities and therefore suffer a suspension of production of indefinite duration. Any quarantine or suspension of production at any of our facilities will adversely affect our overall operations. In addition, any such outbreak will likely restrict the level of economic activities in the affected areas, which could lead to a substantial decrease in our revenues accompanied by an increase in our costs.

***Regulations relating to offshore investment activities by PRC residents may limit our ability to acquire PRC companies and adversely affect our business and prospects.***

The Chinese State Administration of Foreign Exchange (“SAFE”) has promulgated several regulations, including the Notice on Relevant Issues Concerning Foreign Exchange Administration for Domestic Residents’ Financing and Roundtrip Investment Through Offshore Special Purpose Vehicles, or Circular 75, effective on November 1, 2005 and its implementation rules. These regulations require PRC residents and PRC corporate entities to register with local branches of SAFE in connection with their direct or indirect offshore investment activities. These regulations are applicable to our shareholders who are PRC corporate entities and may be applicable to any offshore acquisitions that we make in the future. Under these foreign exchange regulations, PRC residents who make, or have prior to the implementation of these foreign exchange regulations made, direct or indirect investments in offshore special purpose vehicles, or SPVs, will be required to register such investments with SAFE or its local branches. In addition, any PRC corporate entities who is a direct or indirect shareholder of an SPV, is required to update its filed registration with the local branch of SAFE with respect to that SPV, to reflect any material change.

Circular of the State Administration of Foreign Exchange on Printing and Distributing on the Operating Rules for the Administration of Foreign Exchange with Respect to the Financing and Round-tripping Investment of Domestic Residents via Overseas Special Purpose Companies (“Circular 19”) was promulgated by SAFE on May 20, 2011 and came into effect on July 1, 2011. Circular 19 further clarifies the administration principles of Circular 75 and the relevant issues in its application and simplifies operating procedures. To a certain extent, Circular 19 will benefit the offshore investment and round-tripping investment.

Provisions on the Merger and Acquisition of Domestic Enterprises by Foreign Investors (Revised in 2009) (“Circular 6”) was promulgated by Ministry of Commerce and came into effect on June 22, 2009. According to Circular 6, where a domestic company sets up a company with special purpose abroad, it shall apply to the Ministry of Commerce for going through the examination and approval formalities. When merging or acquiring related domestic companies in the name of the companies in foreign countries legally established or controlled by them, the domestic companies, enterprises or natural persons shall report to the Ministry of Commerce for approval.

#### **Item 4. Information on the Company**

##### **Overview**

We were formed as a Cayman Islands corporation in August 2004 under the name “Neo-Luck Plastic Holdings Co., Ltd.” and changed our name to “Fuwei Films (Holdings) Co., Ltd.” in April 2005. Our corporate headquarters, principal place of business, production and ancillary facilities occupy an area of approximately 74,251 square meters at No. 387 Dongming Road, Weifang Shandong 261061, People’s Republic of China. Our agent for service in the United States is CT Corporation System located at 111 Eighth Avenue, NY, NY 10011.

We develop, manufacture and distribute high quality plastic film using the biaxially- oriented stretch technique, otherwise known as BOPET film (biaxially-oriented polyethylene terephthalate). The film is light-weight, non-toxic, odorless, transparent, glossy, temperature and moisture-resistant, making it suitable for many forms of flexible packaging, printing, laminating, aluminum-plating and other applications. In addition, it retains high dielectric strength and volume resistance even at high temperatures, which are essential qualities for electrical and electronic uses. Our BOPET film is widely used in consumer based packaging (such as food, pharmaceutical, cosmetics, tobacco and alcohol industries), imaging (such as printing plates and microfilms), electronics and electrical industries (such as wire and cable wrap, capacitors and motor insulation), as well as in magnetic products (such as audio and video tapes). We market our products under our brand name of “Fuwei Films”. Our main products are as below:

· Printing base film used in printing and lamination;

- Stamping foil base film and transfer base films used for packaging of luxury items of cigarettes and alcohol to increase the aesthetic presentation of the item and improving environmental performance ;
- Metallized film or aluminum plating base film used for vacuum aluminum plating for flexible plastic lamination;
- High-gloss film used for aesthetically enhanced packaging purposes;
- Heat-sealable film used for construction, printing and making heat sealable bags;
- Laser holographic base film used as anti-counterfeit film for food, medicine, cosmetics, cigarettes and alcohol packaging;
- Dry film is generally used in circuit boards (PCB & FPC) production, and sometimes used for nameplate and crafts etching;
  - Heat shrinkable film is widely used for special-shaped packaging for beverage and cosmetics; and
- Chemically treated film used to enhance properties including barrier resistance, printing properties and electrostatic resistance.

Since our establishment, a significant portion of our revenues has been derived from the sales of BOPET film, particularly our printing film, stamping film, transfer film and chemical pretreated film, high-gloss film, heat sealable film, dry film, and heat shrinkable film and so on.

We operate three production lines and have had one trial production line as of December 31, 2013. The first line is a Brückner 6.3 m (in width) production line with an annual design capacity of 13,000 metric tons of BOPET film. The second line is a DMT production line which is three-layer co-extruded with 6.7 m (in width), and has an annual design capacity of 16,100 metric tons of BOPET film. We also have a Mitsubishi trial production line which has an annual design capacity of 1,500 metric tons. The new production line has been put into trial operation at the end of January 2013. The commissioning of this production line was delayed due to the former major shareholders' ownership transfer in early 2011. This production line will manufacture high-performance electric insulation film, base film for solar backsheet and TFT-LCD optical film with an annual design capacity of 23,000 metric tons and thickness between 38 and 250 $\mu$ m. As of September 2013, our third production line has been approved and a sample diffusion film (a type of TFT-LCD optical film) has been delivered to clients for testing. This type of diffusion films will be produced in small batches if the test is well received. As of December 31, 2013, our manufacturing operations had a total annual design capacity of 53,600 metric tons based upon 7,200 production hours per annum.

Our top five customers in the year ended December 31, 2013 were Eternal Electronic Material (Guangzhou) Co., Ltd., Eternal Photo Electronic Materials (Guangzhou) Co., Ltd., Dongguan Guangqun Laser Technology Co., Ltd., Itochu Shanghai Co., Ltd., Huizhou Baobo Packing Co., Ltd.. None of our customers accounted for more than 10% of our total revenues in any such year. We sell most of our BOPET film products to customers in the flexible packaging industry in the PRC in the coastal region of China. In addition, we expect to continue to expand our product portfolio to exploit opportunities in different market sectors, such as electronics industries. In 2013, 2012 and 2011, our sales to our overseas customers constituted approximately 13.7%, 18.9% and 27.1% of our total revenue, respectively.

On April 23, 2009, Fuwei Films USA, LLC was set up in South Carolina and co-invested by Fuwei Films (Holdings) Co., Ltd. and Newell Finance Management Co., Ltd.. Fuwei Films USA, LLC has a registered capital of US\$10,000 and total investment amount of US\$100,000. Fuwei Films (Holdings) Co., Ltd. and Newell Finance Management Co., Ltd. own 60% and 40% of the total shares of Fuwei Films USA, LLC, respectively. For the year ended December 31, 2013, the sale revenue of the Fuwei Films USA, LLC was US\$0.

### **Competitive Strengths**

We believe that our competitive strengths have enabled us over the years to meet the needs of our customers and become a leading provider of BOPET film products in China. We also believe that our strengths will continue to help us grow in the BOPET film industry in both China and internationally. Our principal strengths include the following:

***We have the capability to expand our product range and markets by introducing new products required by customers.***

We believe that our experience in the industry and personnel will enable us to continue to provide new BOPET film products required by customers, and we have already developed a series of new products. Our R&D team comprises of 7 full-time research personnel in total.

***We have an established brand name and are recognized for our product quality in the PRC.***

Our products are marketed under our brand name, “Fuwei Films”. We believe that this brand name is well known in the BOPET film market in the PRC and, although our selling prices sometimes exceed those of our competitors, our products have achieved significant market acceptance because of its high quality and our superior customer service. In January 2011, Fuwei Films was recognized as “Shandong Famous Brand”. In January, 2014, Fuwei Films was awarded once more as “Shandong Famous Brand” for an additional five years after being reviewed.

*We manufacture high quality products that can be customized for our clients.*

We implement and enforce stringent quality controls on our production process and products. As part of our production process, we formulate different blends of PET resins and additives to produce film with specific properties for our customers based on their requirements. In addition, we have developed a special production process and we believe using these formulas will produce products that will meet our customers' requirements in quality.

*We have an experienced management team with extensive industry experience.*

Our management team is led by our Chairman and Chief Executive Officer, Mr. Xiaohan He who has more than ten years of related experience in the plastics and packaging industries. He has been instrumental in our operations and strategies, contributing his knowledge and experience in the industry. Our management team has extensive management experience and most of them have many years of experience in the R&D, manufacturing and marketing of BOPET films.

*We can continually renovate or update our production lines according to the market trends and our R&D facilities are advanced in the PRC.*

Our first production line was German made and manufactured by Brückner and the second was made by DMT in France. The third production line was made by Lindner Dornier GmbH in Germany. We continually renovate or update these production lines according to the market trends to enable these lines to produce competitive and premium products. We have a trial production line for R&D, which enables our R&D capability to take lead in the industry.

### **Awards and Certifications**

Our subsidiary, Shandong Fuwei, has received the following awards and certificates, each of which, we believe, is an indication of our achievements, the quality of our products and makes us more attractive to our potential customers and therefore a more competitive company both in the local and international markets:

| <b>Date</b>                      | <b>Award/Certificate</b>  | <b>Issuing Authority</b>   |
|----------------------------------|---|--|
| September 2004 <sup>(1)</sup>    | ISO 9001:2000 Certificate   | China Certification Center for Quality Mark  |
| July 2006 <sup>(2)</sup>         | ISO 14001 Certificate   | SGS  |
| December 2007 <sup>(3)</sup>     | Key High-Tech Enterprise of the National Torch Program                          | Ministry of Science and Technology   |
| December 2008 <sup>(4)</sup>     | · High-and-New Tech Enterprise  | Shandong Department of Science and Technology, National and Local Taxation Bureau of Shandong Province, and Shandong Province Financial Bureau |
| May 2009                         | · “Advanced Enterprise of Chinese plastic industry”                             | China Plastic and Packaging Association  |
| August 2009                      | · Technological Innovation Award  | Shandong Province enterprise technological innovation promotion association  |
| June 2010 <sup>(5)</sup>         | · A-Category taxpayer   | The National Taxation Bureau and the Local Taxation Bureau of Shandong Province  |
| October 2010 <sup>(6)</sup>      | · Shandong Engineering Technology Research Center                               | Department of Science & Technology of Shandong Province  |
| January 2011 <sup>(7), (8)</sup> | · Award for Cooperative and Innovative Manufacturing, Study and Research of SME | SME Productivity Promotion Center of Shandong Province   |
| January 2011                     | · First Award of Private SME Innovation of Shandong Province                    | SME Innovative Committee of Technological Promotion of Shandong Province   |
| January 2011                     | · Award of Tax Contribution of the Year of 2010                                 | Weifang Municipal Finance Bureau   |
| January 2011 <sup>(9)</sup>      | · “Fuwei Films” was awarded as Famous Shandong Brand                            | Shandong Provincial Quality Supervision Bureau   |
| February 2011 <sup>(10)</sup>    | · Scientific Innovative Enterprise of Shandong Province                         | Department of Science & Technology of Shandong Province  |
| October 2011                     | · Creditable Private Enterprise of Weifang 2011                                 | Weifang SME Advocacy Office  |

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|                                |  |  |
|--------------------------------|--|--|
| October 2011 <sup>(3)</sup>    | · Key High-Tech Enterprise of the National Torch Program   | Ministry of Science and Technology   |
| October 2011 <sup>(4)</sup>    | · High-and-New Tech Enterprise   | Shandong Department of Science and Technology, National and Local Taxation Bureau of Shandong Province, and Shandong Province Financial Bureau |
| December 2011                  | · Award for Enhanced Productivity  | SME Productivity Promotion Center of Shandong Province   |
| December 2011 <sup>(11)</sup>  | · Famous Brand   | SME Productivity Promotion Center of Shandong Province   |
| February 2012 <sup>(11)</sup>  | · Outstanding Brand of Plastic Packaging Industry in China in 2011 and 2012                        | China Packaging Federation   |
| June 2012 <sup>(12)</sup>      | · OHSAS 18001:2007 Occupational Health and Safety Management Systems                               | SGS  |
| December 2012                  | · Reliable Enterprise of Weifang   | Weifang Administration for Industry & Commerce   |
| December 2012                  | · Best Employer of Weifang   | Weifang Enterprise Confederation   |
| March 2013 <sup>(11)</sup>     | Private Economy Famous Brand of Shandong Province  | Private Economy Brand Promotion Center of Shandong Province, SME Productivity Promotion Center of Shandong Province                            |
| March 2013                     | Award for Enhanced Productivity in 2012  | SME Technology Innovation Promotion Association of Shandong Province, SME Productivity Promotion Center of Shandong Province                   |
| March 2013 <sup>(7), (8)</sup> | Award for Cooperative and Innovative Manufacturing, Study and Research of SME for the Year of 2012 | SME Technology Innovation Promotion Association of Shandong Province, SME Productivity Promotion Center of Shandong Province                   |
| March 2013                     | First Award of Private SME Innovation of Shandong Province for the Year of 2012                    | SME Technology Innovation Promotion Association of Shandong Province, SME Productivity Promotion Center of Shandong Province                   |
| April 2013                     | 2012 Human Resources and Social Security Credibility Demonstration Enterprise                      | Weifang Municipal Human Resources and Social Security Bureau   |
| May 2013 <sup>(5)</sup>        | AA-Category taxpayer   | The National Taxation Bureau and the Local Taxation Bureau of Shandong Province  |
| July 2013 <sup>(11)</sup>      |  |  |

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the Most Competitive Brand in the Market of Shandong Province      Shandong Province Economic and Information Technology Committee

August 2013<sup>(13)</sup>      The Third Award of Patent for BOPET and Manufacturing in Weifang City      Weifang Municipal Government



|                              |   |  |
|------------------------------|---|--|
| October 2013                 | The Most Significant Innovation Awarded for Dry Film Resist | Weifang Enterprises Confederation, Weifang Enterprisers Association. |
| December 2013 <sup>(9)</sup> | “Fuwei Films” was awarded as Famous Shandong Brand          | Shandong Provincial Quality Supervision Bureau                       |

(1) ISO 9000 certification has become an international reference for quality management requirements in business-to-business dealings. This certification enables us to compete on many more markets around the world and provides our customers with assurances about our quality, safety and reliability.

(2) After strict examination and approval by SGS, Fuwei Films (Shandong) Co., Ltd. has successfully passed the ISO14001 Environmental Administration System in July 2006.

(3) Fuwei Films (Shandong) Co., Ltd. was awarded as Key High-Tech Enterprise of the National Torch Program in December 2007 and October 2011. This title is recertified every two years.

(4) In December 2008 and October 2011, Fuwei Films was awarded as High-and-New Tech Enterprises by Shandong Department of Science and Technology, National and Local Taxation Bureau of Shandong Province, as well as from the Shandong Province Finance Bureau.

(5) The A-Category is the top of the four ratings for corporate taxpayers in China. Candidates eligible for the category are reviewed and designated by the authorities every two years.

(6) This center is mainly engaged in the research and development of polyester new materials and high-tech products. Currently, it has made more than ten R&D achievements and plays a positive leading role in the development of BOPET industry.

(7) Fuwei Films starts technological cooperation with Chinese colleges and hires South Korean experts to research and develop new products, techniques and process.

(8) Fuwei Films has already developed and applied more than ten kinds of new products, including laser anti-counterfeit film, chemical pretreated film, heat-sealable film, dry film and heat shrinkable film. All these have been widely used in production.

(9) The brand of “Fuwei Films” has been honored as famous brand resulting in visibility, credibility, reputation and continued growth.

(10) Under the fierce competition, Fuwei Films is encouraged by the government to develop new products.

(11) All these awards show that our established brand name “Fuwei Films” are recognized for our product quality in the PRC.

(12) OHSAS 18001 is an internationally recognized assessment specification for occupational health and safety management systems. OHSAS promotes a safe and healthy working environment by providing a framework that allows organizations to reduce the potential for accidents and improve overall performance. We believe this distinction will not only insure a safe environment for our workers, it will also be attractive to global companies looking for BOPET suppliers in China.

(13) We have been focusing on R&D as a key differentiator to enable us a competitive advantage in the market.

### **Business Prospects**

In 2013, we continued to be adversely affected by enhanced competition and increased supply over demand in China’s BOPET market as well as the oversea market. In addition, anti-dumping measures taken by USA and South Korea caused a decrease in orders from international markets. The foregoing factors have contributed to significant decrease in sales volumes, which resulted in reduced total revenue compared with the revenue of 2012.

We have identified BOPET thick film, which is mainly used in the electronics, electrical, solar energy and other industries, as a key market segment for potential growth. The thick film rapidly grows with the development of the above-mentioned industry. Currently, giants including Mitsubishi Plastics, Inc., SKC, Inc. and China Lucky Film Corporation invested in and built production lines in China, which will bring fiercer competition to us.

### ***Business Development Strategies***

As a primary part of our business strategy, we will speed up the R&D of high value-added products for the new production line for thick films. We believe that we have the ability to increase our sales and expand our markets. We will continue to improve our products by developing new functions and applications of the BOPET films and enhancing our products mix. Meanwhile, we will continue to secure opportunities to develop new domestic and overseas customers. We believe that expanding the overseas business is a key part of our business strategy. So we will continue to focus on the development of the BOPET industry and look for the opportunities for merger and acquisition.

***Our future plans include: Accelerating the R&D of high value-added products for the new production line for thick films***

We have completed the construction of a new production line capable of producing BOPET film that is between 38 to 250 $\mu$ m in our current premises in Weifang City, PRC. The BOPET film production using this new production line is targeted at industrial use, including TFT-LCD screen films. We expect to penetrate into the electrical, electronics, solar energy and other industries with this new BOPET film. Such industries for high-end and special usage currently rely on expensive imports. The total investment of the new production line is estimated to be US\$51 million. The third production line has been put into trial operation at the end of January 2013. As of September 2013, our third production line has been approved and a sample diffusion film (a type of TFT-LCD optical film) has been delivered to clients for testing. This type of diffusion films will be produced in small batches if the test is well received. In addition, we have started the R&D for our thick films to be manufactured by this production line including high-performance electric insulation film, base film for solar backsheet and TFT-LCD optical film. However, due to the intense competition in the market, we believe that upon commencing production, the third production line may not be profitable in a short term, or bring about losses.

### ***Expansion into overseas markets***

We believe that the overseas markets hold significant potential for future growth. We believe that our venture into the overseas markets which began in 2004 has been successful. Although we are not focused on any particular overseas market, we have identified Europe, Asia and North America as our primary overseas markets.

Our overseas sales were significantly affected by the anti-dumping investigations conducted by South Korea and the United States against BOPET manufacturers originated from China, India and other countries and the appreciation of Renminbi. However, we still believe there is a great potential in overseas BOPET market. Therefore, we will continue to carry out the marketing in the overseas market to attract new clients and sell our specialty films.

### ***Investment in research and development***

As one of our key strategies, we continue to invest substantially in R&D area. We have constructed a trial production line for research and development of new products, which also saves experimental cost. We also intend to expand our R&D team by hiring more senior research personnel from both China and foreign countries. We attach great importance to intellectual property. To date, 21 patents have been granted and 12 patents are pending.

### ***Our Products and Services***

We are principally engaged in the manufacture and distribution of BOPET film. As of December 31, 2013, we produced BOPET films from the three production lines and one trial production line, with an aggregate annual design capacity of 53,600 metric tons with thicknesses varying between 6 - 250 $\mu$ m.

BOPET is a high quality plastic film manufactured using the biaxially-oriented stretch (transverse and machine direction) technique. Our advanced production process improves the physical properties of the plastic film such as its tensile strength, resistance to impact, resistance to tearing and malleability. The high dimensional stability of the film over a wide range of humidity and temperature fulfills the basic requirements for flexible packaging. The film is light-weight, non-toxic, odorless, transparent, glossy, moisture-resistant, and retains high barrier resistance, making it suitable for many forms of flexible packaging, printing, laminating, aluminum-plating and other processes. In addition, it retains high dielectric strength and volume resistance even at high temperatures, which are essential qualities for electrical and electronic uses. The three-layer co-extruded structure enables us to develop high-quality BOPET products.

BOPET film has been widely used in the flexible packaging (such as food, pharmaceutical, cosmetics, cigarettes, alcohol), imaging (such as printing plates and microfilms), and electronics and electrical (such as wire and cable wrap, capacitors and motor insulation). Due to its unique qualities, it has become a popular choice as a flexible packaging material in these industries in recent years.

We market our products under our brand name “Fuwei Films”. Our operations are based primarily in Shandong Province, PRC, where we manufacture our products for sale to customers engaged in flexible packaging businesses and electronics industry in the PRC, in particular the coastal region. We also export our products to end-users and distributors mainly in Europe, Asia and North America.

Our BOPET film is mainly used in the flexible packaging industry for consumer products such as those relating to processed foods, pharmaceutical products, cosmetics, tobacco and alcohol. Our products may be sub-divided into five main categories constituting the following percentages of our total revenue for each of the twelve months ended 2013, 2012 and 2011:

| Category                         | 2013  | 2012  | 2011  |
|----------------------------------|-------|-------|-------|
| Stamping and transfer film       | 46.7% | 54.2% | 54.6% |
| Printing film                    | 9.1 % | 11.3% | 10.3% |
| Metallized film                  | 5.8 % | 5.1 % | 5.3 % |
| Specialty film                   | 29.3% | 24.8% | 26.1% |
| Base film for other applications | 9.1 % | 4.6 % | 3.7 % |

The above categorizes BOPET film products by application.

***Stamping and transfer film***

This is a film that displays excellent thermal stability and tensile strength and is used in metallized film and laser stamping foil and transfer.

***Printing film***

This is a high transparency film that is corona treated on one side to provide excellent adhesion to ink. This is primarily used in printing and lamination.

***Metallized film***

This is an aluminum plating base film that displays good thermal stability and tensile strength and provides good adhesion between film and aluminum layer. This is applied to flexible plastic lamination.

***Specialty film***

We mainly produce the following types of specialty film:

High-gloss film: Film with high levels of reflection approaching a mirror-like surface, used for aesthetically-enhanced packaging purposes.

Heat-sealable film: Film with a three layer structure. The heat-sealable film is primarily used in construction, printing and making heat sealable bags.

Dry film: Generally used in circuit boards (PCB & FPC) production, and sometimes used for nameplate and crafts etching.

Heat shrinkable film is widely used for special-shaped packaging for beverage and cosmetics; and

Chemically treated film used to enhance properties including barrier resistance, printing properties and electrostatic resistance.

***Base film for other applications***

Base films for other application are ordinary commodity polyester films with applications other than for the usages mentioned above.

## **Production**

As of December 31, 2013, we operate three production lines and have had one trial production line. The first line is a Brückner 6.3 m (in width) production line with an annual design capacity of 13,000 metric tons of BOPET film. The second line is a DMT production line which is three-layer co-extruded with 6.7 m (in width), and has an annual design capacity of 16,100 metric tons of BOPET film. We also have a Mitsubishi trial production line which has an annual design capacity of 1,500 metric tons. The third production line has been put into trial operation at the end of January 2013. This production line will manufacture high-performance electric insulation film, base film for solar backsheet and TFT-LCD optical film with an annual design capacity of 23,000 metric tons and thickness between 38 and 250 $\mu$ m. In September 2013, our third production line was approved and a sample diffusion film (a type of TFT-LCD optical film) has been delivered to clients for testing. This type of diffusion films will be produced in small batches if the test is well received. As of December 31, 2013, our manufacturing operations had a total annual design capacity of 53,600 metric tons based upon 7,200 production hours per annum.

BOPET film is manufactured from polyethylene terephthalate (PET) resin. BOPET film is produced by melting the granulated PET resin and extruding it into a flat sheet. This sheet is stretched to 3.0 to 3.6 times its original length, and then horizontally from 3.0 to 3.6 times its width, before being heat-set and finally wound into reels. The orientation process (stretching during the application of heat) gives the film its mechanical strength, barrier and optical properties (clarity and gloss). The main steps of our manufacturing process involve:

### ***Dosing and Mixing***

PET resin is dosed and mixed with relevant additives to give it its desired characteristics. In the case of the production three-layer co-extruded BOPET film, the materials are dosed and mixed separately for each of the core and outer layers.

### ***Extrusion/Co-extrusion***

The mixed material is melted and plasticized to achieve the required homogenous state with the requisite characteristics and then it is filtered and transported to the die unit. Our DMT production line has one main extruder and two auxiliary extruders to allow us to produce multiple-layer co-extruded BOPET film.





### ***Die Casting***

The respective mixed materials are extruded from the die unit which produces a flat layered cast sheet and casted on the chill roll which is cooled by the pinning system.

### ***Machine Direction Orientation (vertical stretching)***

The cast sheet is then heated and stretched by machine direction before annealing the cast sheet, which is a process of heat-setting so as to control the shrinkage of the sheet after the vertical stretching.

### ***Transversal Direction Orientation (horizontal stretching)***

After the machine direction stretching, the cast sheet is horizontally stretched before annealing again.

### ***Pull Roll Station***

The stretched sheet is trimmed and measured for thickness. For the production of base film for printing, the surface is treated by corona treatment. Corona treatment is the process which enables the BOPET film to become receptive to printing. At the pull roll station, continuous feedback on the thickness of the BOPET film is also relayed back to the die unit which therefore ensures consistency in the thickness of the BOPET film.

### ***Winder***

The final BOPET film is then wound up into metal rolls in the mill roll by the winder.

### ***Slitter***

The wound BOPET film is then unwound from the metal rolls, divided to the requisite width and length, and wound again into paper or plastic core for delivery to customers.

### ***Inventory Management***

Our warehousing facilities are located in the Shandong Province, PRC. Our warehouses are guarded by security personnel and loss of our inventory is covered under our insurance policies. As of December 31, 2013, our total inventories amounted to approximately RMB38.5 million and our raw materials, work-in-progress, finished goods and spare parts(including consumables) made up approximately 21.7%, 8.9%, 56.9% and 12.5% of our inventories, respectively.

To ensure an accurate inventory record and to monitor our inventory aging, we conduct monthly stock counts. We usually maintain raw materials which can be used for one or two weeks of production. Typically, we start manufacturing such goods upon our receipt of orders from our customers.

Our inventory turnover periods (in days) for 2013, 2012 and 2011 were 43.8, 35.8 and 38.1, respectively. Inventory turnover is calculated as 365 days times inventory at period/year end date divided by cost of sales in respect of the financial period/year.

In 2013, there were no provisions for inventory obsolescence and inventory written off. As of December 31, 2013, we accrued RMB6.1 million for inventory falling price reserves.

### **Manufacturing Facilities and Utilization Rates**

As of December 31, 2013, the following production lines are in operation:

| <b>Production Line</b>   | <b>Design Capacity</b> | <b>Estimated Remaining Life Span</b> |
|--------------------------|------------------------|--------------------------------------|
| Brückner Production Line | 13,000 tons per annum  | Approximately 0years                 |
| DMT Production Line      | 16,100 tons per annum  | Approximately 5years                 |
| Dornier Production Line  | 23,000 tons per annum  | Approximately 15years                |
| Trial Production Line    | 1,500 tons per annum   | Approximately 6years                 |

The design capacity as given by the manufacturer is determined based on the assumption of the production of a specific mix of BOPET films of varying thicknesses. Our Brückner, DMT and Dornier production lines and the trial

production line have been in use since 2003, 2004, 2013 and 2009, respectively. The production lines are depreciated on the straight-line method over their respective estimated useful lives.

Our approximate annual production volumes and the average annual utilization rates for our facilities for 2013, 2012 and 2011, based on our estimated operational production capacities were as follows.

| Production Line          | Approximate Annual Production Volume |        |        | Average Annual Utilization Rate |        |        |  |  |  |
|--------------------------|--------------------------------------|--------|--------|---------------------------------|--------|--------|--|--|--|
|                          | (tons)                               |        |        | (%)                             |        |        |  |  |  |
|                          | 2013                                 | 2012   | 2011   | 2013                            | 2012   | 2011   |  |  |  |
| Brückner Production Line | 9,854                                | 12,076 | 12,369 | 75.8 %                          | 92.9 % | 95.1 % |  |  |  |
| DMT Production Line      | 13,229                               | 15,166 | 15,350 | 82.2 %                          | 94.2 % | 95.3 % |  |  |  |
| Dornier Production Line  | 423                                  | -      | -      | 10.5 %                          | -      | -      |  |  |  |
| Trial Production Line    | 547                                  | 698    | 1,240  | 36.5 %                          | 46.5 % | 82.7 % |  |  |  |

There are currently no regulatory requirements that may materially affect the utilization rates of our property, plant and equipment. However, certain of the fixed assets relating to our production lines have been mortgaged in respect of certain of our bank loans as described under “Properties” for further details.

## Quality Control

The quality and reliability of our products are essential for our continued success. We adopt strict measures for quality control in the entire production process of all our products, from the purchase and selection of raw materials, to each stage of the manufacturing processes and to the final inspection of end products. Our quality control procedures were certified for ISO 9001:2000 compliance in September 2004 and the review of it is conducted every three years.

As of December 31, 2013, our product inspection and quality control department comprised of 22 employees. We have one manager, 18 quality inspectors, 1 procurement inspector and 2 after-sale personnel. Members of our quality control departments have had relevant training in the area of quality control in accordance with ISO 9001:2000 procedures. Our product inspection and quality control department ensure that our production process, raw materials and end products are of the quality to our customers’ satisfaction.

## Raw Materials

We adopt and adhere to a set of quality inspection procedures and internal controls for the procurement, selection and quality checks of raw materials. Different types of checks are utilized for different categories of raw materials. Our suppliers are also required to meet our internal qualification criteria such as the quality and pricing of their suppliers, their ability to meet our requirements and timely delivery. We conduct batch inspections for raw materials delivered to

us before they are accepted and stored in our warehouses. Defective materials are returned to our suppliers for necessary corrective action to ensure that no defected materials are used for production.

### ***Production Process***

We have established standard operational procedures and implementation rules for each stage of the production process to ensure that our products comply with and adhere to our stringent quality control standards and that our productivity is optimized. We only permit employees who have undergone and completed the relevant training to work on our production lines. At each stage of the production process, our inspectors check and ensure that our production process complies with our quality standards, while our quality control department monitors and ensures that our products-in-process and final products comply with our internal and international standards of quality control by carrying out random sampling of the products.

### ***Finished Products***

To ensure that our products fulfill our quality criteria established by our product inspection and quality control department, our products undergo final quality inspection upon production, labeling and packaging. Our product inspection and quality control department continues to monitor and ensure that our products are properly handled and stored in our warehouses. Prior to delivery to our customers, our products are inspected one final time to ensure that they are in good condition and not damaged.

### ***Maintenance***

Our maintenance engineers regularly maintain and repair our machinery and equipment to ensure that they are in good working order and functioning properly. We also conduct periodic maintenance of all our machinery on a rotation basis. On an average basis, we replace our filter disks every 20-30days and this replacement process takes about six to eight hours during which we will conduct routine maintenance. And each year we will conduct one comprehensive maintenance project for each production line which will cost five to ten days varying according to different maintenance projects. We believe that due to our stringent maintenance policies, our equipment is still in good condition. Our average downtime for 2013 (primarily for maintenance) was 5.2% of our overall production time.

***New Products***

Through years of R&D endeavors, we have introduced a variety of BOPET film products. The following are some of the new products for which commercial production has begun:

| <b>Product</b>                   | <b>Achievement</b>   |
|----------------------------------|--|
| Laser holographic base film      | Our laser holographic base film is a directly embossable BOPET film, ideal for holographic applications. This film eliminates the need to coat and prepare substrates for holographic embossing, thus reducing costs for our customers. It can be used for anti-counterfeit purposes and in packaging to help enhance the aesthetic perception of food, medicine, cosmetics, cigarettes and alcohol.   |
| Single/double surface matte film | Our matte film is mainly used for aesthetically-enhanced packaging purposes. Our ability to produce single-sided matte films offers significant cost savings for our customers as the non-matte side of the film may be used for other applications without further processing.  |
| Anti-counterfeit film            | Our anti-counterfeit film changes color under ultraviolet rays. Accordingly, it is used for packaging branded products for anti-counterfeit purposes.  |
| Chemical pretreated film         | Our film is pretreated in-line and coated, which results in a strong adhesion to ink and aluminum.   |
| Heat-sealable film               | Heat-sealable film is a three layers co-extruded Biaxially oriented polyester film with an amorphous polyester heat seal layer. Available with corona treatment on the non-seal side to give improved adhesion to typical packaging inks and metallizing. It cannot only provide permanent seals to itself for package bag, but also to APET, CPET, PETG and others. Heat-sealable film can be aluminized, printed and composite with other films. It is applied to packaging for food, construction and other applications. |
| Heat sealable film for steel     | To improve the heat-sealable strength between the film and steel and adjust the stretchable capability so as to be more suitable for steel's heat sealing. Mainly used for protection and decoration of colorful armor plate for home appliances.  |

|                                 |   |
|---------------------------------|---|
| High-gloss film                 | By using special raw chips and process, provides very high gloss, uniform thickness, good mechanical properties, and surface smoothness. It can be used under -70~200°C for packaging food, cigarettes, alcohol and laser embossing, holographic anti-fake and metallic yarn and others.                  |
| White film                      | To be used for print, composite, coating and others, such as advertising lamp house, release film and reflector film.   |
| DFR base film                   | Generally used in circuit boards (PCB & FPC) production, sometimes used for nameplate and crafts etching.   |
| Heat shrinkable film            | To change the heat shrinkage rate by enlarging the draw ratio. It is mainly used for PET beverage bottle shrinkable tags. Heat shrinkable film uses PET structure which is the substitute of PVC shrinkable tags, which is also in line with the requirements of environmental protection and recyclable. |
| Smooth heat sealable film       | Excellent smoothness widely used in packaging of mosquito-repellent incense.  |
| Anti-static film                | Featuring low static electricity with surface resistance below $10^{10}$ /sqm applied to printing and packaging which require films with excellent anti-static properties.  |
| Reinforced coated printing film | Excellent adhesion to UV ink and UV gloss oil suitable for high-end printing.   |

### **New Product Development**

We have also begun working on the following projects which are currently in the test production phase:

| <b>Product</b>                                     | <b>Objectives and Applications</b>   | <b>Commercialization Date Expected</b> |
|--|--|--|
| Metal-adhesion improved film                       | To improve the peel strength after metallized sealing. Mainly used for liquid packages.  | June 2014                              |
| Base film for solar backsheet                      | Used in solar backsheet due to its excellent gas and water permability, UV wear resistance and stability of size with additives.   | September 2014                         |
| Functional protective film for optical application | Coated films for different functions suitable for protection of LCD, LED and other industries.   | March 2014                             |
| Base film for diffusion and prism film             | Coated film made by PET resin for optical purposes featuring outstanding optical characteristics and adhesion used as base film for diffusion and prism films in LCD and LED | September 2014                         |

Our expenditure on research and development in 2013, 2012 and 2011 were as follows (in thousands):

|                                   | Year Ended<br>December 31,<br>2013<br>RMB |     | Year Ended<br>December 31,<br>2012<br>RMB |     | Year Ended<br>December 31,<br>2011<br>RMB |     |
|-----------------------------------|---|-----|---|-----|---|-----|
| Research and Development Expenses | 10,906                                    | (1) | 9,617                                     | (2) | 10,159                                    | (3) |

(1)&(2)&(3) In addition to the above-mentioned expenses in 2013, 2012 and 2011 of RMB10,906, RMB9,617 and RMB10,159, respectively, the R&D capital expenditure was RMB1,084, RMB4,928 and RMB10,014, respectively.

We view research and development as an essential part of our business. We believe that higher investment in the equipment of our R&D center and in the development of new products and upgrading of existing products will enhance our ability to compete.

### **Sales, Marketing and Key Customers**

As of December 31, 2013, our sales department comprised of 12 employees in the domestic sales division, 3 employees in the overseas sales division and 2 for sales support. Our sales department is responsible for market penetration such as cultivating new customers and businesses, and market development such as developing existing accounts through better service support and customer relationship. Our marketing department is responsible for



market research, development and promotion. Our management is actively involved in overseeing and supervising our sales and marketing activities and often visits our clients together with the sales personnel. They have established and maintained close business relationship with our key customers.

### *Customers and Markets*

Over the past years, we have established good working relationships with our customers in the flexible packaging industry. Our products are mainly used in the packaging of consumer products such as those relating to processed foods, pharmaceutical products, cosmetics, tobacco and alcohol. In addition, we entered into dry films market and maintain good relationship with major dry films customers in Mainland China.

The majority of our domestic customers are located in the coastal region of the PRC. Our overseas customers are mostly based in Europe, Asia, North America and others. In 2013, sales from our domestic and overseas customers constituted approximately 86.3% and 13.7%, of our annual revenue, respectively.

The following are our top five customers and their respective percentages of contribution to our total revenue for each of the years ended December 31, 2013, 2012 and 2011:

|  | Percentage of Total Revenue (%) |      |      |
|--|---------------------------------|------|------|
|  | 2013                            | 2012 | 2011 |
| Eternal Electronic Material (Guangzhou) Co., Ltd.        | 6.5                             | 7.6  | 3.1  |
| Eternal Photo Electronic Materials (Guangzhou) Co., Ltd. | 3.5                             | 2.8  | -    |
| Dongguan Guangqun Laser Technology Co., Ltd.             | 3.4                             | 2.6  | 3.0  |
| Itochu Shanghai Co., Ltd.                                | 3.0                             | -    | -    |
| Huizhou Baobo Packing Co., Ltd.                          | 2.7                             | 2.5  | -    |

None of our customers accounted for more than 10% of our total revenue in any of the previous three years.

None of our directors or principal shareholders or any of their affiliates has any interest, direct or indirect, in any of our customers listed above.

### ***Sales***

Because of our broad range of product offerings and customers, our sales and marketing efforts are generally specific to particular types of product, customer or geographic region. Most of our products are sold by our own direct sales force. These salespeople, including our management, maintain close relationships with our customers by paying visits to our customers from time to time to understand their needs, and to obtain their feedback and suggestions. Our sales personnel provide technical support to our customers when required. We also regularly invite our existing and potential customers to our manufacturing facilities for visits as we believe that such visits enable our customers to better understand our production processes and operations and also enhance our customers' confidence in us.

We adopt a risk assessment model to our customer credit management system, and we offer different credit terms to our customers based on criteria such as working relationship, payment history, creditworthiness and their financial position. We offer our domestic customers credit terms of up to 30 - 45 days. Our international sales are settled through telegraphic transfer and letters of credit, which generally have payment terms of between 30 and 60 days. However, in 2013, more than 50% of transactions were paid by cash in delivery.

We offer a basic salary and commission package for our sales personnel. The scale for the commission payable is dependent on a number of factors such as sales targets completion, debt collection and marketing cost allocation.

### ***Customer Service***

We place great emphasis on good, fast and effective pre-sales and after-sales customer support services. As such, all our sales personnel have undergone stringent training and have sufficient knowledge and understanding of our products. Our sales personnel are responsible for coordinating and providing after-sales services which include following through with our customers' orders, maintaining relationships with our customers, handling complaints effectively, ensuring that our customers' needs are met and understanding the future needs of our customers. Our quality department gives support to our customer service, and is responsible for explaining questions related to our products usage from customers. If there are complaints as to our product quality, they are responsible for receiving and settling complaints on our customers' site.

We accept returned defective products from customers or compensate our customers for the losses incurred from our defective products. For 2013, our losses due to returned products from our customers were approximately 1.0% of our total sales.

### *Marketing*

We have the following marketing channels:

we regularly attend trade fairs and exhibitions as we believe that they serve as a good platform for us to exhibit our new products and expand our sales network. In addition, participation in seminars, fairs and exhibitions provides us with opportunities to network with our potential and existing customers and allows us to obtain up-to-date information on new products, market trends and consumer demand;

·referrals from existing customers as well as business associates to generate sales opportunities; and

·promotion through our corporate website. Information on our products and services are also found on our corporate website which allows us to reach out to potential domestic and overseas customers.

Our marketing personnel also conduct PRC domestic and overseas market surveys and research. The statistics, findings and information obtained from such surveys and research are then passed on to our management and production department for their analysis on the demand for and supply of our products, which allows them to make adjustments to our production and sales targets as well as our marketing strategies.

## Suppliers and Raw Materials

### *Suppliers*

We purchase raw materials according to the relevant technical specifications and production requirements. We select our suppliers based on the following considerations and/or methods:

- the consistency of the quality of raw materials supplied and any relevant certifications;
- our inspection of the supplier's quality control system;
- positive feedback from the supplier's other customers;
- pricing of raw materials;
- timely delivery of raw materials;
- the supplier's financial position and viability;
- the service provided by the supplier;
- qualifying suppliers by sample testing and batch purchasing of their raw materials; and
- annual evaluation and review of our suppliers.

The following are the suppliers that supplied 10% or more of our purchases of raw materials and supplies for each of the years ended December 31, 2013, 2012 and 2011:

|  | Supply                 | Percentage of total purchases (%) |      |      |
|--|------------------------|-----------------------------------|------|------|
|  |                        | 2013                              | 2012 | 2011 |
| Sinopec Yizheng Chemical Fibre Company Limited | PET resin and Additive | 56.7                              | 36.4 | 43.8 |

We purchase the majority of our PET resin from Sinopec Yizheng as the quality of its supply of PET resin consistently meets our requirements. We currently have an annual supply agreement with Sinopec Yizheng pursuant to which Sinopec Yizheng has agreed to supply us fixed quantities of PET resin monthly at the prevailing market prices. Such supply agreement is renewable annually. We have not entered into any long-term supply contracts with any other supplier. Our purchases of raw materials are on a cash basis. There are a number of suppliers of PET resin at home and abroad that can consistently meet our quality and quantity requirements on a timely basis.

None of our directors or principal shareholders or any of their affiliates has any interest, direct or indirect, in any of our major suppliers mentioned above.

### ***Raw Materials***

The main raw materials that we purchase from our suppliers are as follows:

| Main Raw Material | Percentage of each category within main raw material purchases (%) |      |      | Country       |
|-------------------|--|------|------|---------------|
|                   | 2013   | 2012 | 2011 |               |
| PET resin         | 88.2   | 90.7 | 85.1 | PRC,Korea,BVI |
| Additives         | 11.8   | 9.3  | 14.9 | PRC           |

The market prices of PET resin and additives may fluctuate due to changes in supply and demand conditions. Any sudden shortage of supply or significant increase in demand of PET resin and additives may result in higher market prices and thereby increase our costs of sales. The prices of PET resin and additives are, to a certain extent, affected by the price movement of crude oil. The average price for PET resin in 2013 decrease by 3.0% compared to that in 2012.

As we are unable to predict the price movements of such raw materials and to minimize the impact of such price fluctuations on our cost, we generally purchase such raw materials in quantities sufficient for our production process for approximately one or two weeks. Based on orders from our customers, we may increase or reduce the inventory of our raw materials.

## Competition

We face intense competition in the PRC plastic film industry. We believe that there are currently many plastic film manufacturers in the PRC and we expect further entrants into this market in the future. Among the flexible packaging industries, in particular those involving packaging of processed food and pharmaceutical products, the primary types of plastic films in the packaging products include BOPET, Biaxially oriented polyester (BOPP); and Biaxially oriented polyamide (BOPA).

The following table gives a general comparison of the key differences in the technical specifications and usage of the above types of plastic films.

### Comparison of BOPP Film, BOPET Film and BOPA Film<sup>(1)</sup>

| <b>Features</b>             | <b>BOPP</b> | <b>BOPET</b> | <b>BOPA</b>   |
|-----------------------------|-------------|--------------|---------------|
| Water vapor barrier         | Excellent   | Fair         | Poor          |
| Gas barrier properties      | Poor        | Excellent    | Excellent     |
| Break down voltage          | Poor        | Excellent    | Excellent     |
| Machine-ability             | Fair        | Excellent    | Excellent     |
| Print-ability               | Fair        | Excellent    | Fair          |
| Suitability for Metallizing | Poor        | Excellent    | Fair          |
| Density (gm/cc)             | Low (0.91)  | High (1.39)  | Medium (1.15) |
| Tensile strength            | Poor        | Excellent    | Excellent     |

This comparison is based on the book of Biaxially Oriented Plastics Film, edited by Yanping Yin and published by (1)China Chemical Press in August 1999. The Company did not notice updated technical specifications subsequently as of December 31, 2012.

We believe that we are one of the few BOPET film manufacturers in the PRC with research and development capabilities.

We believe that the major competitive factors in our industry include:

- research and development capability;
- quality and reliability of products;
- technical/manufacturing capability;
- industrial reputation; and
- production cost and sales prices.

We believe that our major competitors in BOPET manufacturing are currently:

- Dupont Hongji Films Foshan Co., Ltd.;
- Yihua Toray Polyester Film Co., Ltd.; and
- Ningbo Shunsu Film Co., Ltd.

We believe that we have established a good reputation and management track record as a manufacturer of BOPET film and are able to offer quality products.

**C. Organizational structure.**

The following table set forth the details of our subsidiaries as at the date of this Annual Report:

| <b>Name</b>                      | <b>Country of Incorporation</b> | <b>Ownerships Interests</b>        | <b>Direct Parent</b>             |
|----------------------------------|---------------------------------|------------------------------------|----------------------------------|
| Fuwei Films (Shandong) Co., Ltd. | Weifang Shandong, China         | 100% wholly owned by Direct Parent | Fuwei Films (BVI) Co., Ltd.      |
| Fuwei Films (BVI) Co., Ltd.      | British Virgin Islands          | 100% wholly owned by Direct Parent | Fuwei Films (Holdings) Co., Ltd. |
| Fuwei Films USA, LLC             | South Carolina, USA             | 60% owned by Direct Parent         | Fuwei Films (Holdings) Co., Ltd. |

***D. Property, plant and equipment.***

Our corporate headquarters and production and ancillary facilities occupy an area of approximately 74,251 square meters in Weifang City, Shandong Province. The land at our facilities is covered by land use rights held by us. The land use rights for the land upon which our buildings and facilities are located have terms of 50 years, the earliest of which expires in November 2050. All of our research and development, manufacturing, warehousing and administrative functions are conducted at our corporate headquarters. The total gross floor area of production and other facilities owned by us is approximately 46,196 square meters. We own all the buildings and facilities on the premises. Most of our land use rights, office buildings and three facilities in operation have been mortgaged to two banks in the PRC.

**Item 4A. Unresolved Staff Comments**

None.

**Item 5. Operating and Financial Review and Prospects**



## **MANAGEMENT'S DISCUSSION AND**

## **ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

You should read the following discussion and analysis of our financial condition and results of operations in conjunction with our consolidated financial statements included in this Annual Report beginning on page F-1. The consolidated financial statements have been prepared in accordance with U.S. GAAP. The following discussion and analysis contain forward-looking statements that involve risks and uncertainties.

### **Overview**

We develop, manufacture and distribute high quality plastic film using the biaxially oriented stretch technique, otherwise known as BOPET film. Since the establishment of the Company, a substantial portion of our revenues has been derived from the sales of BOPET film. We sell majority of our BOPET film products to domestic customers in China with minority of them sold to Europe, Asia, North America and other overseas markets.

### **Our Corporate Structure and Operating History**

The diagram below illustrates our corporate structure:

Shandong Fuwei, our PRC operating subsidiary, was formed on January 28, 2003, as a Sino-foreign equity joint venture under the name Weifang Fuwei Plastic Co., Ltd. In July 2003, this company began production of BOPET film, initially renting the necessary fixed assets from Shandong Neo-Luck, a company involved in BOPET film production in which Mr. Xiaoming Wang, our current executive officer, served as executive officer at the time.

Shandong Fuwei subsequently acquired these fixed assets through two auction proceedings, the first in October of 2003 and the second in December 2004. At the first auction proceeding in October 2003, Shandong Fuwei acquired assets related to the Brückner production line that it had been renting from Shandong Neo-Luck. This line had been previously mortgaged by Shandong Neo-Luck to Bank of China, Weifang city branch as security for several loans extended to Shandong Neo-Luck's affiliates. When these loans went into default, Bank of China brought a series of legal actions in Weifang Municipal People's Court that resulted in the assets securing the loans being sold at a public auction. Following its successful bid at an auction on October 9, 2003, Shandong Fuwei acquired the Brückner production line and facilities (with an appraised value of approximately RMB169 million) for RMB156 million.

In November 2003, Shandong Fuwei's shares were sold to Shenghong Group Co., Ltd. ("Shenghong Group") and Shandong Baorui for an aggregate consideration of RMB98.2 million. Tongju Zhou, a former director of the Company, and Duo Wang each indirectly own 50% of Easebright Investments Limited ("Easebright"), one of our principal shareholders, and are both officers and directors of Shandong Baorui. Jun Yin and Duo Wang own 17.5% and 4.6%, respectively, of Shandong Baorui. In 2004, Messrs. Zhou and Wang, along with Jun Yin established several offshore holding companies in the British Virgin Islands and the Cayman Islands to acquire and hold these shares. In October 2004, Fuwei (BVI) entered into a sale and purchase agreement with Shenghong Group and Shandong Baorui pursuant to which Fuwei (BVI) acquired the respective equity interest of Shenghong Group and Shandong Baorui in Shandong Fuwei for an aggregate consideration of RMB91 million. Shandong Fuwei thereafter became a wholly-owned subsidiary of Fuwei (BVI) and was converted into a wholly-foreign owned enterprise pursuant to PRC law.

As a result of its ongoing financial difficulties, Shandong Neo-Luck was declared bankrupt by the Weifang Municipal People's Court in the PRC on September 24, 2004. Prior to the bankruptcy, Shandong Neo-Luck's then major operating asset, the DMT production line, had been pledged by Shandong Neo-Luck to Weifang City Commercial Bank. When Shandong Neo-Luck was declared bankrupt, the Shandong Branch of Bank of China seized the production line by order of the Qingdao Intermediate People's Court and the Qingdao Southern District People's Court while the Weifang Branch of Bank of Communications did so through Weifang Intermediate People's Court. As such, the effectiveness of the pledge in favor of Weifang City Commercial Bank was under dispute. Subsequently, pursuant to the decision from Weifang Intermediate People's Court, Weifang City Commercial Bank ranked senior in terms of the right of claims.

The pledged DMT production line was put up for public auction by the Shandong Neo-Luck Liquidation committee on October 22, 2004. In view of the above complexities, the auction was deemed to be tremendously risky at that time, and therefore, our PRC operating subsidiary did not directly participate in the first auction, which began with a bid price of approximately RMB53 million by reference to an independent valuation performed on a forced sale basis. However, due to the potential tremendous risk involved, the auction had been withdrawn twice and the starting bid price had been further reduced to approximately RMB34 million and was finally purchased by Beijing Baorui, a company indirectly controlled by Shandong Baorui. When the DMT production line was put for public auction by Beijing Baorui three months later, our PRC operating subsidiary purchased it for approximately RMB119 million, which was supported by an independent valuation performed on a going concern basis. We understood that acquiring the DMT production line from Beijing Baorui through the first auction would be an effective way to minimize the risk associated with the uncertainties arising from the bankruptcy of Shandong Neo-Luck. The price difference of approximately RMB85 million represented a risk premium paid to Beijing Baorui, which bore the ultimate risks of

recourse from creditors of Shandong Neo-Luck.

Subsequent to the auction for several years, the PRC government conducted an investigation into the conduct of certain individuals in connection with such transactions. In March 2009, Messrs. Yin, Wang and Zhou committed the crime of corruption by verdict of the Jinan Intermediate People's Court in the city of Jinan, Shandong Province. In November 2009, the Company became aware of the final verdict issued by the Supreme People's Court of Shandong Province. The Supreme People's Court upheld the initial verdict issued by the Intermediate court in March 2009. The March 2009 initial verdict sentenced Mr. Yin to death, with a stay of execution for two years, and the other two defendants, Mr. Zhou and Mr. Wang, each received life imprisonment. All of the personal property of the three individuals will be confiscated.

At the time of the Company's initial public offering, we had obtained an opinion of PRC counsel with respect to the validity of the auction proceedings under PRC law, although you should read the description of the opinion and the subsequent development in March 2009 described under the title "*Risk Factors — The circumstances under which we acquired ownership of our main productive assets may jeopardize our ability to continue as an operating business*". Certain of the assumptions relied upon in providing that opinion have been called into question by the verdict referred to above.

On May 9, 2011, the Company received a notification from the Weifang State-owned Assets Operation Administration Company, a wholly-owned subsidiary of Weifang State-owned Asset Management and Supervision Committee (the "Administration Company") regarding the transfer of the ownership of controlling shareholders.

According to the notification, the former controlling shareholders of the Company, Messrs. Jun Yin, Duo Wang and Tong Ju Zhou, had transferred their entire ownership in several intermediate holding companies to the Administration Company, Ms. Qing Liu and Mr. Zhixin Han. As a result of the transfers, and based on the information provided by the Administration Company, 52.90% of its outstanding ordinary shares are controlled indirectly by the Administration Company and 12.55% of its outstanding ordinary shares are jointly controlled indirectly by Ms. Liu and Mr. Han.

The Company received a second notification dated May 17, 2011 (the “Second Notification”) from the Administration Company regarding the transfer of ownership of Fuwei stock previously controlled by the Company’s major shareholders.

As discussed in the Second Notification, Ms. Qing Liu and Mr. Zhixin Han have transferred their entire ownership in the intermediate holding company, Easebright Investments Limited, to the Administration Company. As a result of the transfer, and based on the information provided by the Administration Company, 65.45% of its outstanding ordinary shares are controlled indirectly by the Administration Company and the sole director of each of the intermediate holding companies, Mr. Zheng Min.

On August 14, 2013, the Company announced that it had received the first notice from the its controlling shareholder, the Weifang State-owned Assets Operation Administration Company, a wholly-owned subsidiary of Weifang State-owned Asset Management and Supervision Committee (collectively, the “Administration Company”) indicating that the Administration Company had determined to place control over 6,912,503 (or 52.9%) of its outstanding ordinary shares up for sale at a public auction to be held in China. Four public auctions were held in Jinan, Shandong Province, China, The Company learned that they failed due to lack of bidders registered for the auction. On March 25, 2014, the fifth public auction was held in Jinan, Shandong Province, China and the Company became aware that the fifth public auction has resulted in the acceptance of a successful bid. The beneficial ownership of 6,912,503 ordinary shares of the Company previously owned by the Administration Company through Apex Glory Holdings Limited, a British Virgin Islands corporation, was transferred to Shandong SNTON Optical Materials Technology Co., Ltd. (“Shandong SNTON”) through the public auction. Shandong SNTON received control over 6,912,503 (or 52.9%) of the Company’s outstanding ordinary shares at a price of RMB101, 800,000 (approximately US\$16,572,787) or approximately US\$2.40 per ordinary share. The transfer process is expected to be completed by the end of April 2014.

## **Key Factors Affecting Our Results of Operation**

The following are key factors that affect our financial condition and results of operations and we believe them to be important to the understanding of our business:

### ***Raw Material Prices***

For the years ended 2013, 2012 and 2011, the total cost of raw materials made up approximately 71.4%, 73.0% and 78.3% of production cost, respectively. The primary raw materials used in our production of BOPET film are polyethylene terephthalate (or PET) resin and additives, which made up approximately 88.2% and 11.8%, respectively, of our total cost of raw materials in 2013. PET resin trades as a commodity and its market price is influenced significantly by global energy prices, including the price of crude oil. In addition, PET resin is mainly used

in textile industry and accordingly the demand from that industry will also affect the price of PET resin.

Although we try to pass on all increases in our raw material costs to our customers, we can only pass on a portion of the increase to our customers due to the increased supply than demand in the market. We obtain a significant amount of the PET resin used at our facilities from one supplier, who has agreed to supply us fixed quantities of PET resin monthly at the prevailing market price. We have not engaged in any hedging transactions to limit our exposure to fluctuations in the market prices of these raw materials or their components.

### ***Prices of Our Products***

Our BOPET film products generally fall into two categories: commodity products and specialty products. The price of commodity products, such as printing films, stamping and transfer films and metallized films, is typically driven by supply and demand conditions in the market. We have more control over pricing for our specialty products, such as dry films.

As selling prices are generally higher for those types of BOPET film products which require higher technical expertise, our revenue will be affected, to certain extent, by our product mix. Our product mix is dependent on, among other things, our production facilities, R&D abilities and new product commercialization.

### ***Demand for Our Products***

We have been able to expand our product range and markets by introducing new products required by customers. We believe that our technical expertise is important in introducing products that are in demand.

Our BOPET film products are mostly sold to customers in the flexible packaging industry for consumer products such as food, pharmaceutical products, cosmetics, tobacco, alcohol and beverage. Recently, the sales of the light-resistant dry film which is used in printed circuit board also significantly increased. In the fiscal years ended December 31, 2013, 2012 and 2011, approximately 86.3%, 81.1% and 72.9%, respectively, of our total revenue was derived from the PRC. The demand for our products is therefore, to a large extent, affected by the general economic conditions in the PRC. A significant improvement in the economic environment in the PRC will likely improve consumer spending and increase the demand for our products. However, the economic downturn of the PRC market will impact our customers' demand and will decrease the demand for our products.

### ***Production Capacity and Utilization Rates***

Our sales volume is limited by our operational annual production capacity.

As we grow our business in the future, our ability to fulfill more and larger orders will be dependent on our ability to increase our production capacity. As our business is capital-intensive, our ability to expand our production capacity will depend on, *inter alia*, the availability of capital to meet our needs of expansion or upgrading of production lines.

### ***Competition***

We believe that we are currently one of the few producers of BOPET films in the PRC with research and development capability. Our past financial performance is attributable to our market position in the industry. Over time, there may be new investors into our industry, and the current BOPET film manufacturers may expand their production capacity. We believe that currently our major competitors in the BOPET manufacturing market in the PRC include Dupont Hongji Films Foshan Co., Ltd., Yihua Toray Polyester Film Co., Ltd., and Ningbo Shunsu Film Co., Ltd.

Our ability to enhance existing products, introduce new products to meet customers' demand, deliver quality products to our customers and maintain our established industry reputation will affect our competitiveness and market position.

Our ability to compete against new and existing competitors to maintain or improve our market position and secure orders will affect our revenue and financial performance.

### **Description of Certain Statements of Income Line Items**

#### ***Revenues***

Revenue from the sale of our domestic BOPET film products is recognized when significant risks and rewards of ownership have been transferred to the buyer. No revenue is recognized if there are significant uncertainties regarding recovery of the consideration due, associated costs or the possible return of goods, or when the amount of revenue and costs incurred or to be incurred in respect of the transaction cannot be measured reliably. In respect of our overseas

sales, we ship directly to the destinations of our overseas customers and our revenue is recognized at the time when we receive customs clearance of our exports. Most of our overseas sales are conducted on a Cost, Insurance and Freight (or “CIF”) basis, meaning that we pay the costs and freight necessary to get the products to the port of destination, and the risk of loss is transferred from us to the buyer when the goods pass the ship’s rail at the port of destination. In addition, we have to procure marine insurance against the buyer’s risk of loss of damage to the goods during the carriage. Most of our sales invoices are denominated in the Chinese Yuan(Renminbi), although certain of our overseas sales are denominated in US dollars.

### ***Cost of Goods Sold***

Our cost of goods sold comprises mainly of materials costs, energy expenses, factory overheads, packaging materials and direct labor. The breakdown of our cost of goods sold in percentage is as follows:

|                     | Year Ended<br>December 31, 2013 |   | Year Ended<br>December 31, 2012 |   | Year Ended<br>December 31, 2011 |   |
|---------------------|---------------------------------|---|---------------------------------|---|---------------------------------|---|
| Materials costs     | 71.4                            | % | 73.0                            | % | 78.3                            | % |
| Energy expense      | 9.0                             | % | 8.3                             | % | 6.9                             | % |
| Factory overhead    | 14.6                            | % | 13.9                            | % | 10.7                            | % |
| Packaging materials | 2.7                             | % | 3.0                             | % | 2.7                             | % |
| Direct labor        | 2.3                             | % | 1.8                             | % | 1.4                             | % |

### ***Material Costs***

As noted above, the raw materials used in our BOPET film production are PET resin and additives, which made up approximately 88.2% and 11.8%, respectively of our total materials costs in 2013.

### ***Energy expense***

Energy expense includes electricity, gas and water costs, in which electricity is the main energy consumed.

### ***Factory Overhead***

Factory overhead comprises primarily of depreciation, electricity and water charges, and repair and maintenance of our machinery and equipment, etc. In 2013, the depreciation expense and repair and maintenance expenditure accounted for 78.5% and 15.4% of factory overhead, respectively.

### ***Packaging Materials***

Our packaging materials mainly comprise of, among other things, packaging pallets and carton cores, used for the packaging of our BOPET film products for delivery to customers. Generally, our unit cost of packaging materials does not fluctuate significantly and our total costs for packaging materials typically vary in line with our sales volume.

### ***Direct Labor***

Direct labor cost includes salaries, wages, bonuses and other payments to our employees in the PRC who are involved in the production of our products. The main factors affecting our direct labor cost are CPI, the changes of any government policies or laws and the demand and supply of skilled labor.

### ***Operating Expenses***

Our operating expenses comprise of administrative expenses, distribution expenses and other operating expense.

Our administrative expenses comprise mainly of administrative staff salaries and related welfare costs, research and development expenses, depreciation charges of office equipment, furniture and fixtures, amortization charges relating to land use rights, allowance for doubtful trade receivables, professional fees, government duties and fees, insurance expenses, rental expenses, travel expenses, entertainment expenses, office expenses and miscellaneous expenses.

Our distribution expenses comprise mainly of freight costs, travel expenses, marketing and promotion expenses as well as salaries and commission paid to our sales and marketing personnel.



Other operating expenses comprise mainly of loss on disposal of property, plant and equipment and miscellaneous expenses.

### ***Finance Costs***

Finance costs comprise mainly of interest expense relating to our loans, capital lease obligations, exchange deficit and bank charge.

### ***Income Tax Expense***

For the period from January 28, 2003 to December 31, 2004, Shandong Fuwei was granted certain tax relief under which it was exempted from PRC income tax. As of January 2005, Shandong Fuwei has been a wholly foreign-owned enterprise under the laws of the PRC. Accordingly, Shandong Fuwei is entitled to tax concessions whereby the profit for the first two financial years beginning with the first profit-making year (after setting off tax losses carried forward from prior years) is exempt from income tax in the PRC and the profit for each of the subsequent three financial years is taxed at 50% of the prevailing tax rates set by the relevant tax authorities.

On March 16, 2007, the National People's Congress of the PRC passed the Enterprise Income Tax Law of the People's Republic of China, which law took effect on January 1, 2008 (the "New Tax Law"). Under the New Tax Law, domestic enterprises and foreign-invested enterprises will generally become subject to a unified enterprise income tax rate of 25%, except that enterprises incorporated prior to March 16, 2007 may continue to enjoy existing preferential tax treatments until January 1, 2013. In addition, certain qualifying "High Technology Enterprises" may still benefit from a preferential tax rate of 15% under the New Tax Law if they meet the definition of "Government Advocated High Technology Enterprise" to be set forth in the more detailed implementing rules when they become adopted. Shandong Fuwei was designated as a High-and-New Tech Enterprise in December 2008 and will retain its status as a high-tech enterprise for three years commencing from 2011 enjoying a favorable corporate tax rate of 15% during the term from January 1, 2011 to December 31, 2013 pursuant to Enterprise Income Tax Law.

The US entity, Fuwei Films USA, LLC, is headquartered in South Carolina. As of December 31, 2013, the income tax rate is 39%, including 34% of federal income tax rate and 5% of state income tax rate.

### **Inflation**

According to the National Bureau of Statistics of China, the change in the consumer price index in China was 2.6%, 2.6% and 5.4% in 2013, 2012 and 2011, respectively.

## Critical Accounting Policies

The SEC defines critical accounting policies as those that are, in management's view, most important to the portrayal of our financial condition and results of operations and those that require significant judgments and estimates. We prepare our financial statements in accordance with the U.S. GAAP, which requires us to make estimates and assumptions that affect the reported amounts of our assets and liabilities, to disclose contingent assets and liabilities on the date of the financial statements, and to disclose the reported amounts of revenues and expenses incurred during the financial reporting period. We continue to evaluate these estimates and assumptions based on the most recently available information, our own historical experience and various other assumptions that we believe to be reasonable under the circumstances. We rely on these evaluations as the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Since the use of estimates is an integral component of the financial reporting process, actual results could differ from those estimates. Some of our accounting policies require higher degrees of judgment than others in their application. We consider the policies discussed below to be critical to an understanding of our financial statements as their application assists management in making their business decisions.

**Goodwill Impairment** Goodwill represents the excess of purchase price and related costs over the value assigned to the net tangible and identifiable intangible assets of businesses acquired. Goodwill is not amortized but is tested for impairment annually, or when circumstances indicate a possible impairment may exist. Impairment testing is performed at a reporting unit level. An impairment loss generally would be recognized when the carrying amount of the reporting unit exceeds the fair value of the reporting unit, with the fair value of the reporting unit determined using a discounted cash flow (DCF) analysis. A number of significant assumptions and estimates are involved in the application of the DCF analysis to forecast operating cash flows, including the discount rate, the internal rate of return, and projections of realizations and costs to produce. Management considers historical experience and all available information at the time the fair values of its reporting units are estimated.

**Collectibility of Accounts Receivable** Our management has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis. Credit evaluations are performed on all customers requiring credit over a certain amount. Generally, we offer our customers in the PRC credit terms of up to 30-45 days. Our international sales are settled through telegraphic transfer and letters of credit, which generally have payment terms of between 30 and 60 days.

We offer different credit terms to our customers based on criteria such as working relationship, payment history, creditworthiness and their financial position. All credit terms are to be approved by our finance department, in consultation with our sales and marketing department. For extension of larger credit limits, approvals have to be sought from our credit committee which is made up of members from our finance department, sales department and CFO. Our finance department and sales department review our outstanding debt account on a monthly basis and follow up with customers when payments are due. We do not impose interest charges on overdue account receivable.

As of December 31, 2013, our largest trade debtor was Eternal Electronic Material (Guangzhou) Co., Ltd, a company based in China, The balance of trade receivables from Eternal Electronic Material (Guangzhou) Co., Ltd, was RMB2.9 million.

We make specific allowance for doubtful trade receivables when our management takes the view (taking into account the aging of trade receivables and in consultation with our sales department) that we will not be able to collect the amounts due. Our customers pay by installments, creating long accounts receivable cycles. We provide for an allowance for doubtful accounts based on our best estimate of the amount of losses that could result from the inability or intention of our existing customers not to make the required payments. We generally review the allowance by taking into account factors such as historical experience, age of the accounts receivable balances and economic conditions.

Specific write-off of trade receivables is made when the outstanding trade receivables have been due for more than two years.

The analysis of the allowance for doubtful amounts for 2013, 2012 and 2011 is as follows (in thousands):

|                              | December 31,2013 |       | December 31,2012 | December 31,2011 |
|------------------------------|------------------|-------|------------------|------------------|
|                              | RMB              | US\$  | RMB              | RMB              |
| Balance at beginning of year | 1,196            | 197   | 1,785            | 2,140            |
| Bad debt expense(recovery)   | (401 )           | (66 ) | (589 )           | (355 )           |
| Write-offs                   | -                | -     | -                | -                |
| Balance at end of year       | 795              | 131   | 1,196            | 1,785            |

***Impairment of Long-lived Assets***

The Company recognizes an impairment loss when circumstances indicate that the carrying value of long-lived assets with finite lives may not be recoverable. Management's policy in determining whether an impairment indicator exists, a triggering event, comprises measurable operating performance criteria at an asset group level as well as qualitative measures. If an analysis is necessitated by the occurrence of a triggering event, the Company uses assumptions, which are predominately identified from the Company's strategic long-range plans, in determining the impairment amount. In the calculation of the fair value of long-lived assets, the Company compares the carrying amount of the asset group with the estimated future cash flows expected to result from the use of the assets. If the carrying amount of the asset group exceeds the estimated expected undiscounted future cash flows, the Company measures the amount of the impairment by comparing the carrying amount of the asset group with their estimated fair value. We estimate the fair value of assets based on market prices (i.e., the amount for which the asset could be bought by or sold to a third party), when available. When market prices are not available, we estimate the fair value of the asset group using discounted expected future cash flows at the Company's weighted-average cost of capital. Management believes its policy is reasonable and is consistently applied. Future expected cash flows are based upon estimates that, if not achieved, may result in significantly different results.

**Results of Operations**

The following discussion of our results of operations is based upon our audited consolidated financial statements beginning on page F-1 of this Annual Report.

The table below sets forth certain line items from our Statement of Income as a percentage of revenues:

|                          | For the year ended<br>December 31, |        |        |
|--------------------------|------------------------------------|--------|--------|
|                          | 2013                               | 2012   | 2011   |
|                          | (% of Total Revenue)               |        |        |
| Gross profit             | (5.1 )                             | (0.8 ) | 15.9   |
| Operating expenses       | (16.1)                             | (16.3) | (10.2) |
| Other expense            | (1.5 )                             | 0.5    | (1.1 ) |
| Income tax benefit(loss) | 3.3                                | 2.1    | (0.7 ) |
| Net income(loss)         | (19.3)                             | (14.6) | 3.9    |

**Fiscal year ended 2013 compared to fiscal year ended 2012**

**Revenues**

Our revenue can be analyzed as follows (in thousands):

|                                  | For the year ended December 31, |        |               |         |               |  |
|----------------------------------|---------------------------------|--------|---------------|---------|---------------|--|
|                                  | 2013                            |        |               | 2012    |               |  |
|                                  | RMB                             | US\$   | % of<br>Total | RMB     | % of<br>Total |  |
| Stamping and transfer film       | 142,309                         | 23,508 | 46.7 %        | 202,029 | 54.2 %        |  |
| Printing film                    | 27,852                          | 4,601  | 9.1 %         | 42,449  | 11.3 %        |  |
| Metallized film                  | 17,686                          | 2,922  | 5.8 %         | 18,886  | 5.1 %         |  |
| Specialty film                   | 89,382                          | 14,764 | 29.3 %        | 92,536  | 24.8 %        |  |
| Base film for other applications | 27,721                          | 4,579  | 9.1 %         | 16,966  | 4.5 %         |  |
|                                  | 304,950                         | 50,374 | 100.0%        | 372,866 | 100 %         |  |

During the fiscal year ended December 31, 2013, net revenues were RMB305.0 million (US\$50.3 million), compared to RMB372.9 million during the same period in 2012, representing a decrease of RMB67.9 million or 18.2%, mainly due to the reduction of average sales price by 4.9% and total sales volumes by 14.0%. For further analysis of the factors causing revenue decrease, the reduction of average sales price caused a decrease of RMB15.6 million and sales volume factor made a decrease of RMB52.3 million.

In 2013, sales of specialty films were RMB89.4 million (US\$14.8 million) or 29.3% of our total revenues as compared to RMB92.5 million or 24.8% in 2012, which was a decrease of RMB3.1 million, or 3.4%, as compared to the same period in 2012. For further analysis of the factors causing specialty films revenue decrease, the reduction of average sales price caused a decrease of RMB5.6 million and sales volume factor made an increase of RMB2.5 million. The decrease was largely attributable to the decrease in sales prices for films in electronics and high-end packaging.

Overseas sales were RMB41.9 million or US\$6.9 million, or 13.7% of total revenues, compared with RMB70.6 million or 18.9% of total revenues in 2012. For further analysis of the factors causing overseas sales decrease, the increase of average sales price caused an increase of RMB1.6 million and sales volume factor made a decrease of RMB30.3 million. The decrease in overseas sales was mainly due to the slow growth in demand from enhanced competition as well as anti-dumping measures taken by the USA and South Korea, which led to decrease in orders from the overseas market compared to the same period of 2012.

The following is a breakdown of domestic versus overseas sales for the periods ended December 31, 2013 and 2012 (amounts in thousands):

|                          | For the year ended December 31, |        |            |           |            |   |  |
|--------------------------|---------------------------------|--------|------------|-----------|------------|---|--|
|                          | 2013                            |        |            | 2012      |            |   |  |
|                          | RMB                             | US\$   | % of Total | RMB       | % of Total |   |  |
| Sales in China           | 263,076                         | 43,457 | 86.3       | % 302,290 | 81.1       | % |  |
| Sales in other countries | 41,874                          | 6,917  | 13.7       | % 70,576  | 18.9       | % |  |
|                          | 304,950                         | 50,374 | 100.0      | % 372,866 | 100.0      | % |  |

### ***Cost of Goods Sold***

Cost of goods sold during the year of 2013 totaled RMB320.4million (US\$52.9 million) as compared to RMB376.0 million in the prior year. This was RMB55.6 million or 14.8% lower than the same period in 2012, mainly due to the decreased sales volume of 14.0% in 2013 compared to the same period in 2012. For further analysis of the factors causing cost of goods sold decrease, the reduction of unit cost of goods sold caused a decrease of RMB2.9 million and sales volume factor made a decrease of RMB52.7 million.

### ***Gross (Loss) Profit***

Our gross loss was RMB15.4 million (US\$2.5 million) for the year of 2013, representing a gross margin of (5.0)%, as compared to a gross margin of (0.8)% in 2012. Gross margin decreased by 4.2 percentage points compared to the same period in 2012. Our average unit sales price decreased by 4.9% compared to last year due to the excess capacity and stronger competition in the market. In addition, the main raw materials used in our production of BOPET films, polyethylene terephthalate (or PET) resin and additives, comprised approximately 71.4% of our total costs of goods sold and their prices were greatly influenced by price fluctuation in crude oil. Our main raw material costs, PET resin, were reduced by 3.0% compared to last year. Moreover, the remaining costs except raw materials comprising approximately 28.6% of our total cost of goods sold increased by 1.1% compared to that in 2012. Consequently, the decrease in product sales price exceeded that in cost of goods sold per unit during 2013 compared with 2012, which contributed to the significant decrease in our gross profit.

***Operating Expenses***

Our operating expenses during the year ended December 31, 2013 were RMB49.0 million, a decrease of RMB11.9 million, or 19.6%, as compared to 2012. The decrease was mainly due to no goodwill impairment for the year ended December 31, 2013.

***Other Expense***

Total other expense is a combination result of interest income, interest expense and others income (expense). Total other expense during the year ended December 31, 2013 was RMB4.6 million (US\$0.8 million), compared to total other income of RMB1.8 million in 2012. Total other expense of 2013 increased comparing to that of 2012, which was mainly due to the fact that most of interests were expensed in current year while all interest payments were capitalized in 2012. Interest payments totaled RMB12.2 million (US\$2.0 million) during 2013, RMB1.0 million or 8.9% higher than that in 2012, which was mainly due to higher interest payment associated with capital lease obligations.

***Income Tax Benefit (Expense)***

Income tax benefit during the year ended December 31, 2013 was RMB10.0 million (US\$1.7 million) compared to an income tax benefit of RMB7.7 million during 2012, which was mainly attributable to tax effect of changes in deferred tax during 2013.



**Fiscal year ended 2012 compared to fiscal year ended 2011****Revenues**

Our revenue can be analyzed as follows (in thousands):

|                                  | For the year ended December 31, |        |            |      |         |            |
|----------------------------------|---------------------------------|--------|------------|------|---------|------------|
|                                  | 2012                            |        |            | 2011 |         |            |
|                                  | RMB                             | US\$   | % of Total |      | RMB     | % of Total |
| Stamping and transfer film       | 202,029                         | 32,428 | 54.2       | %    | 293,768 | 54.6       |
| Printing film                    | 42,449                          | 6,814  | 11.3       | %    | 55,218  | 10.3       |
| Metallized film                  | 18,886                          | 3,031  | 5.1        | %    | 28,205  | 5.3        |
| Specialty film                   | 92,536                          | 14,853 | 24.8       | %    | 140,491 | 26.1       |
| Base film for other applications | 16,966                          | 2,723  | 4.5        | %    | 19,963  | 3.7        |
|                                  | 372,866                         | 59,849 | 100        | %    | 537,645 | 100        |

During the fiscal year ended December 31, 2012, net revenues were RMB372.9 million (US\$59.8 million), compared to RMB537.6 million during the same period in 2011, representing a decrease of RMB164.7 million or 30.6%, mainly due to the reduction of average sales price by 30.6% and total sales volumes by 0.7%. Additional factors causing a decrease in revenue include the reduction of average sales price causing a decrease of RMB160.8 million and a decrease of RMB4.0 million in our sales volume.

In 2012, sales of specialty films were RMB92.5 million (US\$14.9 million) or 24.8% of our total revenues as compared to RMB140.5 million or 26.1% in 2011, which was a decrease of RMB48.0 million, or 34.1%, as compared to the same period in 2011. Additional factors causing a decrease in revenue of specialty films include, the reduction of average sales price causing a decrease of RMB23.2 million and a decrease of RMB24.8 million in our sales volume. The decrease was largely attributable to the decrease in demand and sales prices for films in electronics and high-end packaging.

Overseas sales were RMB70.6 million or US\$11.3 million, or 18.9% of total revenues, compared with RMB145.5 million or 27.1% of total revenues in 2011. Additional factors causing a decrease in overseas sales include the reduction of average sales price causing a decrease of RMB47.9 million and a decrease of RMB27.0 million in sales volume. The decrease in overseas sales was mainly due to the slow growth in demand from international market and enhanced competition as well as anti-dumping measures taken by the USA and South Korea, which led to decrease in orders from the overseas market and a significant decrease of the sales prices compared to the same period of 2011.

The following is a breakdown of domestic versus overseas sales for the periods ended December 31, 2012 and 2011 (amounts in thousands):

|                          | <b>For the year ended December 31,</b> |        |            |           |            |   |  |
|--------------------------|--|--------|------------|-----------|------------|---|--|
|                          | 2012                                   |        |            | 2011      |            |   |  |
|                          | RMB                                    | US\$   | % of Total | RMB       | % of Total |   |  |
| Sales in China           | 302,290                                | 48,521 | 81.1       | % 392,195 | 72.9       | % |  |
| Sales in other countries | 70,576                                 | 11,328 | 18.9       | % 145,450 | 27.1       | % |  |
|                          | 372,866                                | 59,849 | 100.0      | % 537,645 | 100.0      | % |  |

### ***Cost of Goods Sold***

Cost of goods sold during the year of 2012 totaled RMB376.0 million (US\$60.3 million) as compared to RMB452.2 million in the prior year. This was RMB76.2 million or 16.9% lower than the same period in 2011, mainly due to the decreased price of 14.7% of main raw materials in 2012 compared to the same period in 2011. Additional factors causing a decrease in cost of goods sold include the reduction of unit cost of goods sold causing a decrease of RMB72.8 million and a decrease of RMB3.4 million in sales volume.

### ***Gross (Loss) Profit***

Our gross loss was RMB3.1 million (US\$0.5 million) for the year of 2012, representing a gross margin of (0.8)%, as compared to a gross margin of 15.9% in 2011. Gross margin decreased by 16.7 percentage points compared to the same period in 2011. Our average unit sales price decreased by 30.6% compared to last year due to the excess capacity and stronger competition in the market. In addition, the main raw materials used in our production of BOPET films, polyethylene terephthalate (or PET) resin and additives, comprised approximately 73.0% of our total costs of goods sold and their prices were greatly influenced by price fluctuation in crude oil. Our main raw materials costs, PET resin, were reduced by 14.7% compared to last year. Consequently, the decrease in product sales price largely exceeded that in main raw material costs during 2012 compared with 2011, which contributed to a significant decrease in our gross profit.

### ***Operating Expenses***

Our operating expenses during the year ended December 31, 2012 were RMB60.9 million, an increase of RMB6.1 million, or 11.2%, as compared to 2011. The increase was mainly due to goodwill impairment for the year ended December 31, 2012.

### ***Other Expense***

Total other expense is a combination result of interest income, interest expense and others income (expense). Total other income during the year ended December 31, 2012 was RMB1.8 million (US\$0.3 million), compared to total other expense of RMB5.7 million in 2011, which mainly attributed to interest capitalization of RMB11.2 million (US\$1.8 million) related to the third production line project in 2012. Interest payments totaled RMB11.2 million (US\$1.8 million) during 2012, RMB1.0 million or 9.3% higher than that in 2011, which was mainly due to higher interest rates on bank loans.

### ***Income Tax Benefit (Expense)***

Income tax benefit during the year ended December 31, 2012 was RMB7.7 million (US\$1.2 million) compared to an income tax expense of RMB4.0 million during 2011, which was mainly attributable to tax effect of changes in deferred tax during 2012.

### *Liquidity and Capital Resources*

Since inception, our sources of cash were mainly from cash generated from our operations and borrowings from financial institutions and capital contributed by our shareholders.

Our capital expenditures in 2013 have been primarily financed through short-term borrowings from financial institutions. The interest rates of short-term borrowings from financial institutions during the three-year period from 2011 to 2013 ranged from 0% to 7.87%, and these borrowings may not be paid prior to maturity.

Since inception, we have utilized significant amounts of secured short-term financing to fund our acquisition of Brückner, DMT and Dornier production lines and working capital needs. As of December 31, 2013, we had borrowings of RMB115.0 million from two financial institutions in the PRC.

Each of the related loan agreements contains provisions regarding collateral, covenants prohibiting us from engaging in certain activities (including selling, mortgaging or otherwise disposing of or encumbering all or substantially all of our assets or before any merger, acquisition, spin-off, or other transaction resulting in a change in our corporate structure) without the lenders consent and acceleration (and setoff) provisions in the event of default in payment or failure to comply with such covenants.

We paid off four short-term loans totaling RMB110.0 million (US\$18.2million) to Bank of Communications Co., Ltd. in April 2013 and then obtained five new short-term loans from Bank of Communications Co., Ltd. in April and May 2013 for a total amount of RMB105.0 million (US\$17.3million), including: (i) RMB20.0 million (US\$3.3 million) on April 18, 2013, maturing on April 2, 2014; (ii) RMB20.0 million (US\$3.3 million) on April 19, 2013, maturing on April 11, 2014; (iii) RMB25.0 million (US\$4.1 million) on April 23, 2013, maturing on April 16, 2014; (iv) RMB20.0 million (US\$3.3 million) on April 25, 2013, maturing on April 18, 2014; and (v) RMB20.0million (US\$3.3 million) on May 2, 2013, maturing on April 24, 2014. The annual interest rate of these bank loans is 7.2%. As of December 31, 2013, the balance of short-term loans is RMB105.0 million (US\$17.3 million).

On November 20, 2009, we signed a long-term loan agreement of RMB10.0 million (US\$1.7 million) with Weifang Dongfang State-owned Assets Management Co., Ltd., with an eight-year loan term, which became effective on October 19, 2009 and will expire on October 18, 2017. From 2015 to 2016, the Company will make principal installment payments of RMB3.35 million (US\$0.6 million) per year with the remaining principal balance of RMB3.3 million (US\$0.5 million) due in 2017. The annual interest rate for the loan is the benchmark interest rate for over five-year loans announced by the People's Bank of China reduced by 10% and the applicable annual interest rate for the period ended December 31, 2013 is 6.12%. The loan is guaranteed by Shandong Deqin Investment & Guarantee Co., Ltd. and is used for our projects.

We believe that, after taking into consideration our present and future banking facilities, existing cash and the expected cash flows to be generated from our operations, we have adequate sources of liquidity to meet our short-term obligations and our working capital.

A summary of our cash flows for 2013, 2012 and 2011 is as follows (in thousands):

|   | 2013     |         | 2012     |     | 2011      |      |   |
|---|----------|---------|----------|-----|-----------|------|---|
|   | RMB      | US\$    | RMB      |     | RMB       |      |   |
| Net cash provided by (used in) operating activities | 3,090    | 510     | 46,451   |     | (14,018   | )    |   |
| Net cash (used in) provided by investing activities | (32,069) | (5,296) | (85,389) |     | (119,325) |      |   |
| Net cash provided by (used in) financing activities | 35,568   | 5,875   | (202     | )   | 6,501     |      |   |
| Effect of foreign exchange rate changes             | (17      | )       | 20       | (26 | )         | (213 | ) |
| Net increase (decrease) in cash and cash equivalent | 6,572    | 1,109   | (39,166) |     | (127,055) |      |   |
| Cash and cash equivalent                            |          |         |          |     |           |      |   |
| At beginning of the year                            | 5,006    | 804     | 44,172   |     | 171,227   |      |   |
| At end of the year                                  | 11,578   | 1,913   | 5,006    |     | 44,172    |      |   |

### *Operating Activities*

Net cash provided by operating activities was RMB3.1 million for the year ended December 31, 2013 as compared to net cash provided by operating activities of RMB46.5 million for the year ended December 31, 2012. This decrease in cash flows from operating activities was attributable primarily to the increased operating loss in current year.

Net cash provided by operating activities was RMB46.5 million for the year ended December 31, 2012 as compared to net cash used in operating activities of RMB14.0 million for the year ended December 31, 2011. This increase in cash flows from operating activities was attributable primarily to the decrease in accounts receivables. We have started taking actions to collect overdue invoices from our customers, which resulted in an increase in cash flows.

Net cash used in operating activities was RMB14.0 million for the year ended December 31, 2011 as compared to net cash provided from operating activities of RMB98.6 million for the year ended December 31, 2010. The decrease of net cash provided from operating activities of RMB112.6 million was mainly due to the increase of receivables from clients and other receivables and reduced advance from our customers.

### *Investing Activities*

Net cash used in investing activities was RMB32.1 million in 2013 mainly due to investment in the third production line project.

Net cash used in investing activities was RMB85.4 million in 2012 due to equipment purchase from Dornier.

Net cash used in investing activities was RMB119.3 million in 2011 due to the deposit for the Letter of Credit for Dornier equipment and the advance of the equipment.

### ***Financing Activities***

Net cash provided by financing activities was RMB35.6 million for the year ended December 31, 2013, which was mainly due to increase in Bank's Acceptance Bill.

Net cash used in financing activities was RMB0.2 million for the year ended December 31, 2012, which was mainly due to repayment of bank loans.

Net cash generated from financing activities was RMB6.5 million for the year ended December 31, 2011, which was mainly due to increased bank loans.

### **Foreign Exchange Exposure**

#### ***Translations***

Our reporting currency is RMB. The functional currency of our operating subsidiary in the PRC is RMB and our operating subsidiary also maintains its books and records in RMB. Accordingly, we are not exposed to any material foreign currency translation effects.

### ***Transactions***

We are, to a certain extent, exposed to transaction foreign currency exposure arising from our operations in the PRC.

We began conducting part of our sales in foreign currency in 2004 with the commencement of our overseas sales business. During 2013, 2012 and 2011, approximately 86.3%, 81.1% and 72.9% respectively, of our revenue was denominated in RMB and the remainder was in US dollar. The proportion of raw materials we purchased within the PRC during 2013, 2012 and 2011 were 98.0%, 88.3% and 84.9%, respectively. The remainder was purchased in US dollars.

Our foreign currency exchange risk arises mainly from this mismatch between the currency of our sales, purchases and operating expenses. We may, therefore, be susceptible to foreign exchange exposure.

In addition, we also maintain US dollar accounts with financial institutions for our US dollar receipts and US dollar payments. We may also incur foreign exchange gains or losses when we convert the US dollar balances into RMB.

Currently, we do not have a formal foreign currency hedging policy as our foreign exchange gains and losses in 2013, 2012 and 2011 were insignificant. Our management believes that it is more efficient for us to assess the hedging need of each transaction on a case-by-case basis. We will continue to monitor our foreign exchange exposure in the future and will consider hedging any material foreign exchange exposure should such need arise.

### **Capital Expenditures and Contractual Commitments**

#### ***Capital Expenditures***

Our capital expenditures in 2013, 2012 and 2011 were as follows (in thousands):

| For the year ended December 31, |      |      |
|---------------------------------|------|------|
| 2013                            | 2012 | 2011 |
| RMB                             | RMB  | RMB  |



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|  |        |         |        |
|--|--------|---------|--------|
| Buildings                                | -      | -       | -      |
| Plant and equipment                      | 1,667  | 6,106   | 33,195 |
| Motor vehicles                           | -      | -       | 914    |
| Assets under construction                | 10,172 | 138,811 | 36,305 |
| Others (computer and furniture fittings) | 356    | 70      | 2,173  |
| Total                                    | 12,195 | 144,987 | 72,587 |

The following table summarizes our contractual commitments as of December 31, 2013 and the effects caused by those commitments are expected to have on our liquidity and cash flow in future periods:

| Contractual Commitments              | Total              | Less<br>than 1<br>Total<br>Year | 1-3<br>Years | 3-5<br>Years | More<br>than<br>5<br>Years |
|--------------------------------------|--------------------|---------------------------------|--------------|--------------|----------------------------|
|                                      | (RMB in thousands) |                                 |              |              |                            |
| Equipment Purchase Contract(i)       | 12,019             | 12,019                          | -            | -            | -                          |
| Bank loans(ii)                       |                    |                                 |              |              |                            |
| -Principal                           | 115,000            | 105,000                         | 6,700        | 3,300        | -                          |
| -Interest(iii)                       | 3,807              | 2,893                           | 814          | 100          | -                          |
| Obligations under capital lease(iv)  |                    |                                 |              |              |                            |
| -Carrying amount of lease obligation | 16,876             | 8,314                           | 8,562        | -            | -                          |
| -Interest on unpaid obligation       | 1,150              | 852                             | 298          | -            | -                          |
| Operating leases(v)                  | 369                | 369                             | -            | -            | -                          |
| Total                                | 149,221            | 129,447                         | 16,374       | 3,400        | -                          |

- (i) The purchase of equipment will be financed by the sale of our ordinary shares or by bank borrowings or by funds generated from business operations.  
We have secured short-term loans of RMB105.0 million on December 31, 2013 that are due on different dates in 2013. We also have long-term loans for RMB10.0 million. Our obligations under our existing loans have been mainly met through the cash flow from our operations and financing activities. In the past, cash flow from operations has been sufficient to meet payment obligations and/or we have been able to extend our borrowings. In the event that our cash flows are insufficient to satisfy these obligations, we may consider additional bank loans, issuing bonds, or other forms of financing to satisfy our capital requirements.
- (ii) The interest expenses are estimated based on the interest rate of borrowings adopted by the People's Bank of China on December 31, 2013 plus an estimated risk premium on borrowing.
- (iii) The Group has commitments under capital lease agreements as for a part of new third production line and related equipment. The lease has terms of 3 years expiring by the end of December 2015.  
The operating leases mainly relate to our rental of staff dorms and offices. The term of these leases typically ranges from 1 year to two years, and are renewable subject to renegotiation of terms upon expiration. We intend to finance these operating leases from our cash flows from operations.
- (v)

### **Off-Balance Sheet Arrangements and Contingent Liabilities**

We do not have any off-balance sheet guarantees, any outstanding derivative financial instruments, interest rate swap transactions or foreign currency forward contracts.

### **Inflation**

According to the National Bureau of Statistics of China, the change in the consumer price index in China was 2.6%, 2.6% and 5.4% in 2013, 2012 and 2011, respectively.

### **Recent Accounting Pronouncements**

In July 2013, the Financial Accounting Standards Board, or FASB, issued a new accounting standard which will require the presentation of certain unrecognized tax benefits as reductions to deferred tax assets rather than as liabilities in the consolidated balance sheets when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. The new standard requires adoption on a prospective basis in the first quarter of 2015; however, early adoption is permitted. We do not expect the adoption will have a significant impact on our consolidated financial statements.

In February 2013, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2013-02, which requires entities to present information about significant items reclassified out of accumulated other comprehensive income (loss) by component either on the face of the statement where net income is presented or as a separate disclosure in the notes to the financial statements. This ASU is effective for the Company in the first quarter of fiscal 2014. We do not expect the adoption will have a significant impact on our consolidated financial statements.

In July 2012, the FASB issued ASU 2012-02, which amends how companies test for impairment of indefinite-lived intangible assets. The new guidance permits a company to assess qualitative factors to determine whether it is more likely than not that the fair value of an indefinite-lived intangible asset is less than its carrying amount as a basis for determining whether it is necessary to perform the annual impairment test. The ASU is effective for the Company in the first quarter of fiscal 2014. We do not expect the adoption will have a significant impact on our consolidated financial statements.

Other pronouncements issued by the FASB or other authoritative accounting standards group with future effective dates are either not applicable or not significant to the consolidated financial statements of the Company.

#### **Research and Development, Patents and Licenses**

We rely on copyright, patent, trademark and other intellectual property law, nondisclosure agreement and technical know-how to protect our intellectual property and proprietary rights. We enter into confidentiality and licensing agreements with the relevant employees. Our senior employees and employees who work in our research and development department and other technical departments have signed agreements acknowledging that we own the rights to all technology, inventions, trade secrets, works of authorship, developments and other processes generated in connection with their employment with us or their use of our resources or relating to our business or our property and that they must assign any ownership rights that they may claim in those works to us. As most of our business is currently conducted in mainland China, we have not taken any action outside mainland China to protect our intellectual property.

As of the date of this Annual Report, we have received 21 patents from, and have 12 patent applications pending with the PRC authorities.

We currently sell our products in the PRC with the registered trademark of “Fuwei Films”. Our ability to compete in our markets and to achieve future revenue growth will depend, in significant part, on our ability to protect our proprietary technology and operate without infringing upon the intellectual property rights of others. An infringement upon these rights may reduce or eliminate any competitive advantage we have developed, causing us to lose sales or otherwise harm our business. We are not aware of any infringement or unauthorized use of our intellectual property rights. We will take appropriate legal actions to protect our rights if there is any unauthorized use or infringement of our rights in the future. To date, we have not been sued for infringement of intellectual property rights by any third party.

### **Trend Information**

Since the second half of 2011, the international capacity of BOPET films surged especially in countries such as India and China which attributed to more supply than demand and reduced prices in the market. We expect this trend to continue in 2014, which will result in fiercer price competition. We expect that in the next two to three years, the global BOPET production capacity will continue to increase while supply will continue to surpass demand in the market.

In addition, aiming at the rapidly developed thick films market (with applications in high value-added electronics, electrical, solar energy and other industries), giants including Mitsubishi Plastics, Inc., SKC, Inc. and China Lucky Film Corporation invested in and built production lines in China, which will bring challenges and fiercer competition to our thick film project.

Other than as disclosed elsewhere in this Annual Report, we are not aware of any trends, uncertainties, demands, commitments or events that are reasonably likely to have a material effect on our net sales, profitability, liquidity or capital resources, or that caused the disclosed financial information to not necessarily be indicative of future operating results or financial conditions.

## **Item 6. Directors, Senior Management and Employees**

### **A. Directors and senior management.**



The following table sets forth information regarding our directors and executive officers as of the date of this Annual Report on Form 20-F:

### Directors and Executive Officers

| Name                              | Age | Position                                       |
|-----------------------------------|-----|--|
| Xiaoan He                         | 52  | Chairman, Director and Chief Executive Officer |
| Xiuyong Zhang                     | 44  | Chief Financial Officer and Director           |
| Tee Chuang Khoo <sup>(1)(2)</sup> | 68  | Independent Director                           |
| Changrong Ji <sup>(1)(2)(3)</sup> | 68  | Independent Director                           |
| Shan Jiang <sup>(1)</sup>         | 67  | Independent Director                           |
| Yong Jiang                        | 40  | Board Secretary                                |
| Xiaoming Wang                     | 54  | Vice President of Shandong Fuwei               |

(1) Member of the Audit Committee.

(2) Member of the Compensation Committee.

(3) Member of the Corporate Governance and Nominating Committee.

**Xiaoan He** has been the Chairman of the Board of Directors and Chief Executive Officer of our Company since 2005 and is responsible for the formulation and implementation of our business strategies and management of our business operations. Mr. He has more than fifteen years of management experience in the plastics and packaging industries in the PRC. From June 2004 to January 2005, Mr. He was our General Manager responsible for our daily operation and management. Prior to joining us as the General Manager in June 2004, Mr. He was the general manager of Suzhou Broadway Plastic Packaging Co., Ltd from 1996 to 2003. From 1990 to 1996, he was the vice general manager at Suzhou Xiangxuehai Freezer Co., Ltd and from 1983 to 1990, he was the vice general manager at Suzhou Marine Machinery Co., Ltd. Mr. He obtained his EMBA from China Europe International Business School in 2003 and Bachelor in Engineering from Shanghai Jiaotong University in 1983.

***Xiuyong Zhang*** has been a director of our Company since November 2007. He began serving as our Chief Financial Officer on April 11, 2008. He had accumulated more than 10 years of experience in investment, accounting and financial fields. He is responsible for day-to-day management of our investment, financing, accounting and auditing matters in the Company and financing, financial and taxation matters for its subsidiary. Prior to joining us as a director of the Company, Mr. Zhang has also been the director of Shandong Fuwei since July 2004, and the Vice President since January 2005. Mr. Zhang was the vice-head of an audit firm, Shandong Zhengyuan Hexin Auditors, Weifang branch from 1999 to 2004. From 1991 to 1999, he was an accounting supervisor at the main office of Weifang City Local Products Company. Mr. Zhang was jointly certified as a Public Valuer by the Ministry of Personnel and Ministry of Finance in the PRC in 2004. He was certified as the Chinese Certified Public Accountant by the Ministry of Finance of the PRC in 1997. He received the Professional Certification in Law from China University of Political Science and Law and China Central Radio and TV University in 2005. He received the Certification of Financial Accounting from Shandong Television University in 1996.

***Tee Chuang Khoo*** has been a director of our Company since November 2007. Mr. Khoo was a Senior Partner in Management Consulting at DENE Management Consulting Co., Ltd. (“DENCE”) in Shanghai from October 2005 to October 2007. From November 2000 to September 2005, Mr. Khoo was a Senior Partner at Improve Management Consulting Services in Malaysia where he was responsible for reducing manufacturing costs and process improvement. Mr. Khoo was an Executive Director at JPK (M) Sdn Bhd, a Malaysian-listed company, from October 1998 to September 2000, where he assisted the Managing Director with the entire operation of the company. From November 1996 to August 1998, he was the General Manager of Broadway Group’s (a Singapore-listed company) product factories in Johor Baru, Malaysia, and in China. He also held managerial positions at the Malaysian conglomerate, The Lion Group, and he was a Human Resources Manager at Metal Box Singapore Ltd, a Singapore-listed company owned by the British Metal Box Group. Mr. Khoo received a Bachelor of Arts in Finance & Management from the University of Oregon (USA), a Masters in Business Administration (MBA) from University of Southern California (USA) and a diploma in Accounting from the Association of International Accountants from the United Kingdom.

***Changrong Ji*** has been a director of our Company since March 2007. Mr. Ji is currently the Investigation Officer of the People’s Bank of China, Weifang city central branch and has been since 2004. Mr. Ji was the president of People’s Bank of China, Weifang City central branch from 2001 to 2004 and was the president of People’s Bank of China, Weihai City central branch from 1999 to 2001. From 1989 to 1997, Mr. Ji was the vice-president of People’s Bank of China, Weifang city central branch. He joined the State Administration of Foreign Exchange, Weifang branch as its deputy director from 1989 to 1997 and was appointed as the director of the State Administration of Foreign Exchange, Weihai branch from 1999 to 2001. Mr. Ji was the director of the State Administration of Foreign Exchange, Weifang branch from 2001 to 2004. Mr. Ji obtained his Master’s degree in Economics in 1999 from Shanghai Fudan University and his bachelor’s degree in international economics in 1993 from East China Normal University.

***Shan Jiang*** has been a director of our Company since August 2010. He is a Partner of C&I Partners Legal Firm in Beijing since 1995. Prior to that, he worked in Legal Affairs Center of China from 1986 to 1995; and he worked in maritime court office in Ministry of Communications from 1982 to 1986. Mr. Shan Jiang graduated from Renmin University of China majored in Economic Law in 1985.

**Yong Jiang** has been the Board Secretary since April 2011. He is also assistant President of Fuwei Films (Shandong) Co., Ltd. since 2007. From 2003 to 2006, he served as assistant manager, deputy manager and manager of the marketing department for Shandong Fuwei. In 1998, he joined Weifang Neoluck Plastic Co., Ltd. where he was responsible for overseas sales and production planning. Since 2010, Mr. Jiang has been studying to obtain his EMBA degree in Nankai University. In 1998, he received his bachelor's degree in Information Management and Information System from Shandong University.

**Xiaoming Wang** has been Vice President of Shandong Fuwei since January 2005 and is responsible for the management of our production facilities, production planning and engineering. Prior to joining us, Mr. Wang was the vice manager of Weifang Engine Manufacturing Co. from 1986 to 1998 and the deputy general manager of Shandong Neo-Luck from 1998 to 2003. Mr. Wang was the deputy general manager of Shandong Fuwei during 2004. Mr. Wang was certified as a professional economist by the Shandong Province Human Resources Committee in 2001 and obtained a certificate in Economics Management awarded by the PRC Central Party Learning Institute and obtained a certificate in Business Enterprises Operational Management from the Shandong Television University in 1986.

None of our directors or officers is related to each other. To the best of our knowledge and belief, there are no arrangements or understandings with any of our principal shareholders, customers, suppliers, or any other person, pursuant to which any of our directors or executive officers were appointed.

The business address of our directors and executive officers is No. 387 Dongming Road, Weifang Shandong, People's Republic of China, Postal Code: 261061.



## Board Committees

Our Board of Directors has established an Audit Committee, Compensation Committee and a Corporate Governance and Nominating Committee, and adopted charters for each of these committees. We have appointed independent directors to each of our committees.

Nasdaq Rule 5605(b)(1) requires that the Board be comprised of a majority of Independent Directors as such term is defined in Rule 5605(a)(2). The Company provided Nasdaq with a notice on December 25, 2007 stating that as a “Controlled Company”, it is exempt from the requirements of Rule 5605(b)(1). Pursuant to Rule 5615(c)(1), a “Controlled Company” is a Company of which more than 50% of the voting power for the election of directors is held by an individual, a group or another company. As of December 31, 2012, Weifang State-Owned Assets Operation Administration Company, a wholly-owned subsidiary of Weifang State-owned Asset Management and Supervision Committee, controlled 65.45% of the outstanding ordinary shares of Fuwei. As a result, Fuwei is considered to be a Controlled Company and relied upon the exemption from December 25, 2007.

## Audit Committee

Our Audit Committee currently consists of Tee Chuang Khoo, Changrong Ji and Jiang Shan. On August 4, 2010, the board of directors appointed Mr. Shan Jiang to be a director and a member of the Audit Committee of the Company. The Audit Committee will oversee our accounting and financial reporting processes and the audits of our financial statements. The audit Committee is responsible for, among other things:

- selecting the independent auditors and pre-approving all auditing and non-auditing services permitted to be performed by the independent auditors;
- reviewing and approving all proposed related-party transactions;
- discussing the annual audited financial statements with management and the independent auditors;
- annually reviewing and reassessing the adequacy of our audit committee charter;
- meeting separately and periodically with management and the independent auditors;

- reviewing such other matters that are specifically delegated to our audit committee by our board of directors from time to time; and
- reporting regularly to the full board of directors.

### **Compensation Committee**

Our Compensation Committee currently consists of Tee Chuang Khoo and Changrong Ji. The Compensation Committee is responsible for, among other things:

- reviewing and determining the compensation package for our senior executives;
- reviewing and making recommendations to our board with respect to the compensation of our directors;
- reviewing and approving officer and director indemnification and insurance matters;
- reviewing and approving any employee loan in an amount equal to or greater than RMB100,000; and
- reviewing periodically and approving any long-term incentive compensation or equity plans, programs or similar arrangements, annual bonuses, employee pension and welfare benefit plans.

### **Corporate Governance and Nominating Committee**

Mr. Changrong Ji is the sole member of our Corporate Governance and Nominating Committee. The Corporate Governance and Nominating Committee is responsible for, among other things:

- identifying and recommending to the board nominees for election or re-election to the board;
- making appointments to fill any vacancy on our board;
- reviewing annually with the board the current composition of the board in light of the characteristics of independence, age, skills, experience and availability of service to us;



· identifying and recommending to the board any director to serve as a member of the board's committees;

· advising the board periodically with respect to significant developments in the law and practice of corporate governance as well as our compliance with applicable laws and regulations, and making recommendations to the board on all matters of corporate governance and on any corrective action to be taken; and

· monitoring compliance with our code of business conduct and ethics, including reviewing the adequacy and effectiveness of our procedures to ensure proper compliance.

### **Duties of Directors**

Under Cayman Islands laws, our directors have a common law duty of loyalty to act honestly in good faith with a view to our best interests. Our directors also have a duty to exercise the skill they actually possess and such care and diligence that a reasonably prudent person would exercise in comparable circumstances. In fulfilling their duty of care to us, our directors must ensure compliance with our memorandum and articles of association. A shareholder has the right to seek damages if a duty owed by our directors is breached. You should read "Information - Differences in Corporate Law" for a more complete discussion of these matters.

### **B. Compensation**

#### **Compensation of Directors and Executive Officers**

All directors receive reimbursements from us for expenses which are necessary and reasonably incurred by them for providing services to us or in the performance of their duties. Our directors who are also our employees receive compensation in the form of salaries, housing allowances, other allowances and benefits in kind in their capacity as our employees. Our directors do not receive any compensation in their capacity as directors in addition to their salaries and other remunerations as members of our management team. We pay their expenses related to attending board meetings.

The aggregate cash compensation and benefits that we paid to our directors and executive officers, a group of 7 persons for the year ended December 31, 2013 was approximately RMB1.6 million. No executive officer is entitled to any severance benefits upon termination of his or her employment with the Company.

## Employment and Service Agreements

### *Executive Officers*

We have entered into a Service Agreement dated April 27, 2005, with Mr. Xiaohan He for the position of Chief Executive Officer for a term of three years, effective December 25, 2006. On December 26, 2009, we extended the Service Agreement with Mr. He for three years to December 25, 2012. Additionally, on December 26, 2012, Mr. He's Service Agreement was extended for three years to December 25, 2015. Under this Service Agreement, Mr. He's annual basic salary is RMB500,000 and is eligible for a discretionary bonus.

We have also entered into a Service Agreement with Mr. Xiuyong Zhang, our Chief Financial Officer. The initial term of his Service Agreement began from March 1, 2006 to March 1, 2009. Upon the expiration of his Service Agreement, we extended the term of his Service Agreement for another three years to March 1, 2012. Mr. Zhang's Service Agreement was further renewed for a term of three years to February 28, 2015. Under the term of his initial Service Agreement, Mr. Zhang was entitled to an annual basic salary of RMB300,000. As approved by the board of directors, Mr. Zhang's annual salary was adjusted to RMB 350,000 effective as of January 1, 2011. Mr. Zhang can terminate his Service Agreement upon three months prior written notice or by paying the Company a sum equaling to three months salary in lieu of such notice. The Service Agreement may also be terminated by either party pursuant to the applicable provisions of the China Labor Law.

We have also entered into Service Agreements with our other executive officers. Mr. Yong Jiang renewed his service agreement with the Company in December 2011 with an unspecified term. The initial term of Mr. Xiaoming Wang's Service Agreement was three years commencing from April 2, 2007. Upon expiration of his Service Agreement, it was renewed for two years to December 31, 2011. Mr. Wang's Service Agreement was further renewed in December 2011 with an unspecified term.

We may only terminate the Service Agreement prior to the expiry (except by mutual agreement and except as provided in the Service Agreement) upon the occurrence of certain events including, without limitation, for cause, disability or personal bankruptcy. The term of service of each of our executive officers will be renewed for successive periods of one year each after the expiration of the initial period. The Service Agreement may be terminated by not less than three months' notice in writing served by either party to the Service Agreements. We have the option to pay the executive officer salary in lieu of any required period of notice of termination.

Under the terms of their respective Service Agreements, Mr. Xiaoming Wang and Mr. Yong Jiang are entitled to an annual basic salary of RMB276,000 and RMB204,000, respectively, effective January 1, 2012. Their annual salaries may be revised at the discretion of the Compensation Committee. We may pay them discretionary management bonuses for any financial year, the payment and the amount of which are subject to the approval of the Compensation Committee. Except for the payment in lieu of notice described above, there are no provisions for benefits for termination of employment of our executive officers under the Service Agreements.

### **Share Option Plan**

We plan to adopt a share option plan that is a share incentive plan, the purpose of which is to recognize and acknowledge the contributions the eligible participants had or may have made to our company. The share option plan will provide the eligible participants an opportunity to have a personal stake in our company with the view to achieving the following objectives:

- motivate the eligible participants to optimize their performance efficiency for the benefit of our company; and
- attract and retain or otherwise maintain an on-going business relationship with the eligible participants whose contributions are or will be beneficial to our long-term growth.

### **Indemnification**

Cayman Islands law does not limit the extent to which a company's articles of association may provide for indemnification of officers and directors, except to the extent any such provision may be held by the Cayman Islands courts to be contrary to public policy, such as to provide indemnification against civil fraud or the consequences of committing a crime. Pursuant to our memorandum and articles of association, our directors and officers, as well as any liquidator or trustee for the time being acting in relation to our affairs, will be indemnified and secured harmless out of our assets and profits from and against all actions, costs, charges, losses, damages and expenses that any of them or any of their heirs, executors or administrators may incur or sustain by reason of any act done, concurred in or omitted in or about the execution of their duties in their respective offices or trusts. Accordingly, none of these indemnified persons will be answerable for the acts, receipts, neglects or defaults of each other; neither will they be answerable for joining in any receipts for the sake of conformity, or for any bankers or other persons with whom any moneys or effects belonging to us may have been lodged or deposited for safe custody, or for insufficiency or deficiency of any security upon which any moneys of or belonging to us may be placed out or invested, or for any other loss, misfortune or damage which may happen in the execution of their respective offices or trusts. This indemnity will not, however, extend to any fraud or dishonesty that may attach to any of said persons.

Insofar as indemnification for liabilities arising under the Securities Act may be permitted to directors, officers or persons controlling us pursuant to the foregoing provisions, we have been informed that in the opinion of the Securities and Exchange Commission such indemnification is against public policy as expressed in the Securities Act and is therefore unenforceable.

### **C. Board practices**

Our Articles provide that our board of directors will consist of not less than two directors. At each annual general meeting, one-third of the directors (or, if their number is not a multiple of three, the number nearest to but not greater than one-third) shall retire from office by rotation except that the chairman of the board and/or the managing director of our company shall not be required to retire whilst holding such office nor be taken into account in determining the number of directors to retire in each year. A director who is appointed by the board must retire at our next annual general meeting of the shareholders following his or her appointment. A retiring director is eligible for re-election.

### **D. Employees**

As of December 31, 2013, our total staff consisted of 259 employees.

We do not have any collective bargaining agreements with our employees. We have never experienced any material labor disruptions and are unaware of any current efforts or plans to organize employees. We believe we have good relationships with our employees.

## **Item 7. Major Shareholders and Related Party Transactions**

### **A. Major shareholders.**

The following table sets forth information with respect to the beneficial ownership, within the meaning of Rule 13d-3 under the Exchange Act, of our ordinary shares, as of April 11, 2014, for:

- each person known to us to own beneficially more than 5% of our ordinary shares; and
- each of our directors and executive officers who beneficially own our ordinary shares.

Beneficial ownership includes voting or investment power with respect to the securities. Except as indicated below, and subject to applicable community property laws, the persons named in the table have or share the voting and investment power with respect to all ordinary shares shown as beneficially owned by them. The number of our ordinary shares used in calculating the percentage for each listed person includes any options exercisable by such person within 60 days after the date of this Annual Report. Percentage of beneficial ownership is based on 13,062,500 ordinary shares outstanding as of April 11, 2014. Unless otherwise indicated, the address of such individual is c/o No. 387 Dongming Road, Weifang Shandong People's Republic of China, Postal Code: 261061.

|  | Shares Beneficially Owned |     |         |   |
|--|---------------------------|-----|---------|---|
|  | Number                    |     | Percent |   |
| Executive Officers and Directors:  |                           |     |         |   |
| Xiaoan He  | 65,520                    | (1) | 0.5     | % |
| Xiuyong Zhang  | 46,800                    | (2) | 0.4     | % |
| Tee Chuang Khoo  | —                         |     | —       |   |
| Changrong Ji   | —                         |     | —       |   |
| Xiaoming Wang  | 37,440                    | (3) | 0.3     | % |
| Shan Jiang   | —                         |     | —       |   |
| Yong Jiang   | 18,720                    | (4) | 0.1     | % |
| All directors and executive officers as a group (7 persons)  | 187,200                   |     | 1.1     | % |
| 5% Shareholders:   |                           |     |         |   |
| Weifang State-Owned Assets Management and Supervision Committee 439 Wenhua Road, Weifang 261031, China | 1,637,497                 | (5) | 12.55   | % |
| Shandong SNTON Group Co., Ltd.   | 6,912,503                 | (6) | 52.9    | % |

Owned by Everise Investment Management Co., Ltd., a Hong Kong corporation (“Everise Investment”). 187,200 shares of ordinary shares of the Company are held of record by Everise Investment and Mr. He shares voting and (1)dispositive control with Messrs. Jiang Yong, Xiuyong Zhang, Xuehua Li and Xiaoming Wang over the shares held by Everise Investment. Mr. He disclaims beneficial ownership in 187,200 shares of ordinary shares except to the extent of his pecuniary interest in 65,520 shares of ordinary shares.

Owned by Everise Investment. 187,200 shares of ordinary shares of the Company are held of record by Everise (2)Investment and Mr. Zhang shares voting and dispositive control with Messrs. Jiang Yong, Xiaoan He, Xuehua Li and Xiaoming Wang over the shares held by Everise Investment. Mr. Zhang disclaims beneficial ownership in 187,200 shares of ordinary shares except to the extent of his pecuniary interest in 46,800 shares of ordinary shares.



(3) Owned by Everise Investment. 187,200 shares of ordinary shares of the Company are held of record by Everise Investment and Mr. Wang shares voting and dispositive control with Messrs. Jiang Yong, Xiaohan He, Xuehua Li and Xiuyong Zhang over the shares held by Everise Investment. Mr. Wang disclaims beneficial ownership in 187,200 shares of ordinary shares except to the extent of his pecuniary interest in 37,440 shares of ordinary shares.

(4) Owned by Everise Investment. 187,200 shares of ordinary shares of the Company are held of record by Everise Investment and Mr. Jiang shares voting and dispositive control with Messrs. Xiaohan He, Xuehua Li, Xiaoming Wang and Xiuyong Zhang over the shares held by Everise Investment. Mr. Jiang disclaims beneficial ownership in 187,200 shares of ordinary shares except to the extent of his pecuniary interest in 18,720 shares of ordinary shares.

(5) According to the notification dated May 9, 2011 from the Weifang State-owned Assets Operation Administration Company, a wholly-owned subsidiary of Weifang State-owned Asset Management and Supervision Committee (the "Administration Company"), the former controlling shareholders of the Company, Messrs. Jun Yin, Duo Wang and Tong Ju Zhou, had transferred their entire ownership in several intermediate holding companies to the Administration Company, Ms. Qing Liu and Mr. Zhixin Han. 52.9% of its outstanding ordinary shares were controlled indirectly by the Administration Company and 12.55% of its outstanding ordinary shares are jointly controlled indirectly by Ms. Liu and Mr. Han. According to the Second Notification dated May 17, 2011 from the Administration Company, Ms. Qing Liu and Mr. Zhixin Han have transferred their entire ownership in the intermediate holding company, Easebright Investments Limited, to the Administration Company. As a result of the transfer, and based on the information provided by the Administration Company, the Company believed that 65.45% of its outstanding ordinary shares were controlled indirectly by the Administration Company and the sole director of each of the intermediate holding companies, Mr. Zheng Min. Subsequently, on March 25, 2014, beneficial ownership of 6,912,503 ordinary shares of the Company previously owned by the Administration Company through Apex Glory Holdings Limited, a British Virgin Islands corporation, was transferred to Shandong SNTON Optical Materials Technology Co., Ltd., a PRC entity ("Shandong Optical") through a public auction. The transfer process is expected to be completed by the end of April 2014.

(6) Shandong Optical is the indirect beneficial owner of 6,912,503 Ordinary Shares of the Company, which are held directly by its wholly-owned subsidiary Apex Glory Holdings Limited, a British Virgin Islands corporation ("Apex Glory"). Shandong Optical beneficially owns 52.90% of the Ordinary Shares of the Company. Apex Glory is the owner of 6,912,503 Ordinary Shares of the Company representing 52.90% beneficial ownership. Shandong Optical controls the power to vote and dispose of 6,912,503 ordinary shares of the Company. Apex Glory shares the power to vote and dispose of 6,912,503 Ordinary Shares of the Company. Shandong Optical and Apex Glory are located at Xinxing Road 377, Kenli Economic Development Zone, Dongying City, Shandong Province, PRC. Mr. Zhongmin Wang is the Director and representative of Shandong Optical.

Except as disclosed below, there were no related party transactions with major shareholders during the period commencing January 1, 2011 and ending December 31, 2013.

## **B. Related Party Transactions.**

### **Our Related-Party Transaction Policies**

We have conducted our related-party transactions on normal commercial terms that we believe are fair and reasonable and in the interests of our shareholders as a whole. We believe that the terms of our related-party transactions are comparable to the terms we could obtain from independent third parties. Our related-party transactions are subject to the review and approval of the Audit Committee of our board of directors.

The transactions and balances with related parties are analyzed as follows:

#### **(a) Transactions with Related Parties**

During the years ended 2013, 2012 and 2011, we paid approximately RMB163,690 (USD\$27,040), RMB152,905 and RMB120,317, respectively, to Fuhua Industrial Material Management Co., Ltd. as rental payments in connection with living quarters for our staff.

As of December 31, 2013, the balance due from Joyinn Hotel Investment & Management Co., Ltd. was RMB21.0 million(US\$3.5 million). The background of the long term deposit is disclosed in Note 10.

Obligations under sale-leaseback transaction amounting to RMB16.9 million (US\$2.8 million) were guaranteed by Weifang State-Owned Assets Operation Administration Company, Beijing Shiweitong Technology Development Co., Ltd., Fuwei Films (Holdings) Co., Ltd., and Fuwei Films (BVI) Co., Ltd., respectively.

## **C. Interests of Experts and Counsel.**

Not applicable.

## **Item 8. Financial Information**

### **A. Consolidated Statements and Other Financial Information.**

Our consolidated financial statements are included herein under Item 18.

We have not paid any dividends on our ordinary shares. The payment of dividends in the future, if any, is within the discretion of our Board of Directors and will depend upon our earnings, capital requirements and financial condition and other relevant factors. We do not anticipate declaring or paying any dividends in the foreseeable future.

### **Legal Proceedings.**

Shandong Fuwei is currently a party to five legal proceedings in China. From time to time, we may be subject to legal actions and other claims arising in the ordinary course of business.

On July 9, 2012, a client (the "Plaintiff") filed a lawsuit against Shandong Fuwei over the execution of the Procurement Contract between them in Beijing Daxing District People's Court. Shandong Fuwei raised a jurisdictional objection when filing the pleading and Beijing Daxing District People's Court overruled the objection. Shandong Fuwei filed an appeal against the judgment in the First Intermediate People's Court of Beijing. The appeal was then dismissed on January 23, 2013 and the lawsuit will be heard by Beijing Daxing District People's Court with a claim at RMB953,113 plus its interest. On May 15, 2013, Beijing Daxing District People's Court heard the case and then adjourned the hearing due to the fact that plaintiff failed to provide sufficient evidence. On June 25, 2013, the case was heard in Beijing Daxing District again but it was also adjourned due to Plaintiff's failure to provide sufficient evidence. The case was then scheduled to be heard on August 7, 2013. However, on the day prior to reopening, Fuwei was informed by Beijing Daxing District People's Court that the hearing was adjourned again for the same reason that Plaintiff failed to provide sufficient evidence. To date, Shandong Fuwei is still waiting for a court reopening notice from the Beijing Daxing District People's Court.

On October 29, 2012, another client of Shandong Fuwei (the "Plaintiff") filed a lawsuit against Shandong Fuwei over the execution of the Procurement Contract between them in Zhejiang Haining People's Court. Shandong Fuwei raised a jurisdictional objection when filing the pleading and Zhejiang Haining People's Court sustained the objection and decided that the lawsuit be heard by Weifang High-Tech District People's Court. The Plaintiff filed an appeal against the judgment in Zhejiang Jiaxing People's Court. The appeal was then dismissed and the plaintiff withdrew its charges against Shandong Fuwei on March 5, 2013. Soon afterwards, on March 20, 2013, the court unfroze an amount of RMB770,000 of Shandong Fuwei's savings, which had been frozen during the hearing of the lawsuit. In early May 2013, this client filed a lawsuit against Shandong Fuwei over the product liability in Zhejiang Haining People's Court. Pursuant to a court order, an amount of RMB770,000 of Shandong Fuwei's savings was frozen. Shandong Fuwei then raised a jurisdictional objection which was overruled. Shandong Fuwei filed an appeal against this judgment. The appeal was then dismissed as a final decision. On October 21, 2013, the Plaintiff and Shandong Fuwei reached a settlement to compensate the Plaintiff by RMB160,000 or products valued at RMB160,000 from Shandong Fuwei and the case was closed.

On May 31, 2013, a supplier of Shandong Fuwei (the "Plaintiff") filed a lawsuit against Shandong Fuwei over the execution of the Construction Contract between them in Weifang High-Tech District People's Court with a claim at RMB870,000. On July 8, 2013, Weifang High-Tech District People's Court heard the case and the Plaintiff offered a settlement. Afterwards, the Plaintiff and Shandong Fuwei failed to reach a settlement. On December 18, 2013, Weifang High-Tech District People's Court issued a civil judgment that Shandong Fuwei paid the claim at RMB870,000 to the Plaintiff. On December 28, 2013, Shandong Fuwei filed an appeal against the judgment in the Intermediate People's Court of Weifang and the case was heard on February 26, 2014. To date, the case is still in the process of hearing.

On June 5, 2013, a supplier (the "Plaintiff") filed a lawsuit against Shandong Fuwei over the execution of the Procurement Contract between them in Zhangjiagang People's Court, claiming that the quality guaranteed deposit of RMB208,000 set aside from the total contract payable should be refunded by Shandong Fuwei. Shandong Fuwei declined its claim for the reason of quality problem related to the supplied equipment. On March 7, 2014, Zhangjiagang People's Court heard the case and supported the Plaintiff's claim. Shandong Fuwei filed an appeal against the judgment in the Intermediate People's Court of Suzhou. To date, the case is still in the process of hearing.

On January 21, 2014, an Hong Kong citizen (the "Plaintiff") filed a lawsuit against Shandong Fuwei in the Intermediate People's Court of Weifang to claim a refund of US\$500,000 (approximately RMB4,138,250) and related interest of RMB2,331,784. The plaintiff alleged that according to an oral agreement of purchasing intention for stocks of Fuwei Films (Holdings) Co., Ltd. (the "Fuwei Holdings") between the Plaintiff and Shandong Fuwei in June 2005, the Plaintiff transferred US\$500,000 to Wellplus Investments Limited, a company registered in Hong Kong, for acquiring stocks of Fuwei Holdings. However, the Plaintiff has not received any stocks of Fuwei Holdings till now. Shandong Fuwei believes that there was not any engagement or agreement about stock purchase between Shandong Fuwei and the Plaintiff and did not be aware of the fact of fund transfer between the Plaintiff and Wellplus Investments Limited. The case was heard by the Intermediate People's Court of Weifang on April 3, 2014. To date, the case is still in the process of hearing.

**B. Significant Changes.**

No significant changes have occurred since the date of the consolidated financial statements.

**Item 9. The Offer and Listing.**

**A. Offer and listing details.**

We have authorized capital of 20,000,000 ordinary shares, par value US\$0.129752 per share. As of April 11, 2014, 13,062,500 ordinary shares were issued and outstanding.

The annual high and low market prices of our ordinary shares for the three most recent full financial years and subsequent period are as set forth below:

Ordinary Shares

| (Year Ended)     | High   | Low    |
|------------------|--------|--------|
| December 31,2011 | \$6.55 | \$1.07 |
| December 31,2012 | \$2.48 | \$0.80 |
| December 31,2013 | \$4.00 | \$0.91 |

The high and low market prices of our ordinary shares for each financial quarter over the two most recent full financial years and subsequent period are as set forth below:

Ordinary Shares

| (Quarter Ended)    | High   | Low    |
|--------------------|--------|--------|
| March 31, 2012     | \$2.00 | \$1.16 |
| June 30, 2012      | \$2.48 | \$0.80 |
| September 30, 2012 | \$1.50 | \$1.07 |
| December 31, 2012  | \$1.46 | \$1.14 |
| March 31, 2013     | \$1.95 | \$1.27 |
| June 30, 2013      | \$1.40 | \$0.91 |
| September 30, 2013 | \$4.00 | \$0.97 |
| December 31, 2013  | \$1.55 | \$1.01 |

For the most recent six months, the high and low market prices of our ordinary shares are as set forth below:

Ordinary Shares

| (Month Ended)                   | High   | Low    |
|---------------------------------|--------|--------|
| November 30, 2013               | \$1.27 | \$1.03 |
| December 31, 2013               | \$1.21 | \$1.01 |
| January 31, 2014                | \$1.49 | \$1.11 |
| February 28, 2014               | \$1.29 | \$1.13 |
| March 31, 2014                  | \$2.24 | \$1.11 |
| April 1, 2014 (through April 9) | \$1.84 | \$1.48 |

**B. Plan of Distribution.**

Not applicable.

**C. Markets.**

Our ordinary shares were included for quotation on the Nasdaq Global Market on December 18, 2006 under the symbol "FFHL".

**D. Selling Shareholders.**

Not applicable.

**E. Dilution.**

Not applicable.

**F. Expenses of the Issue.**

Not applicable.

**Item 10. Additional Information.**

**A. Share Capital.**

Not applicable.

**B. Memorandum and Articles of Association.**

We are a Cayman Islands company and our affairs are governed by our memorandum and articles of association and the Companies Law, Cap.22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands, or the Companies Law. We have filed copies of our complete Memorandum and Articles of Association as exhibits to our Annual Report on Form 20-F for the year ended 2006 filed with the SEC on April 2, 2007.

As of the date of this Annual Report, our authorized share capital consisted of 20,000,000 ordinary shares, par value US\$0.129752 per share. As of the date of this Annual Report, 13,062,500 ordinary shares were issued and

outstanding, and no preference shares were issued and outstanding.



## **Ordinary Shares**

We were incorporated under the laws of the Cayman Islands as an exempted company. A Cayman Islands exempted company:

- is a company that conducts its business outside the Cayman Islands;
- is exempted from certain requirements of the Companies Law, including the filing of any annual return of its shareholders with the Registrar of Companies or the Immigration Board;
- does not have to make its register of shareholders open to inspection; and
- may obtain an undertaking against the imposition of any future taxation.

The following summarizes the terms and provisions of our share capital, as well as the material applicable laws of the Cayman Islands. This summary is not complete, and you should read our amended and restated memorandum and articles of association, filed as exhibits to this Annual Report.

The following discussion primarily concerns ordinary shares and the rights of holders of ordinary shares.

## **Protection of Minority Shareholders**

The Grand Court of the Cayman Islands may, on the application of shareholders holding not less than one fifth of our shares in issue, appoint an inspector to examine our affairs and report thereon in a manner as the Grand Court shall direct.

Any shareholder may petition the Grand Court of the Cayman Islands which may make a winding up order, if the court is of the opinion that it is just and equitable that we should be wound up. Where any such petition has been presented by our shareholders, the Grand Court is permitted to make alternative order to a winding-up order including orders regulating the conduct of our affairs in the future, requiring us to refrain from doing an act complained of by the petitioner or for the purchase of our shares by us or another shareholder.

Claims against us by our shareholders must, as a general rule, be based on the general laws of contract or tort applicable in the Cayman Islands or their individual rights as shareholders as established by our amended and restated memorandum and articles of association.

The Cayman Islands courts ordinarily would be expected to follow English case law precedents which permit a minority shareholder to commence a representative action against, or derivative actions in our name to challenge:

- an act which is ultra vires or illegal;
- an act which constitutes a fraud against the minority shareholder and the wrongdoers are themselves in control of us; and
- an irregularity in the passing of a resolution which requires a qualified (or special) majority.

### **Pre-emption Rights**

There are no pre-emption rights applicable to the issue of new shares under either Cayman Islands law or our amended and restated memorandum and articles of association.

### **Modification of Rights**

Except with respect to share capital (as described below) alterations to our amended and restated memorandum and articles of association may only be made by special resolution of no less than two-thirds of votes cast at a meeting of the shareholders.

Subject to the Companies Law, all or any of the special rights attached to shares of any class (unless otherwise provided for by the terms of issue of the shares of that class) may be varied, modified or abrogated with the sanction of a special resolution passed at a separate general meeting of the holders of the shares of that class.

The provisions of our amended and restated articles of association relating to general meetings shall apply similarly to every such separate general meeting, but the quorum for the purposes of any such separate general meeting or at its adjourned meeting shall be a person or persons together holding (or represented by proxy) not less than one third in nominal value of the issued shares of that class. Every holder of shares of the class shall be entitled on a poll to one vote for every such share held by such holder and that any holder of shares of that class present in person or by proxy may demand a poll.

The special rights conferred upon the holders of any class of shares shall not, unless otherwise expressly provided in the rights attaching to or the terms of issue of such shares, be deemed to be varied by the creation or issue of further shares ranking pari passu therewith.

### **Alteration of Capital**

We may from time to time by ordinary resolution:

- increase our capital by such sum, to be divided into shares of such amounts, as the resolution shall prescribe;
- consolidate and divide all or any of our share capital into shares of larger amount than our existing shares;
- cancel any shares which at the date of the passing of the resolution have not been taken or agreed to be taken by any person, and diminish the amount of our share capital by the amount of the shares so cancelled subject to the provisions of the Companies Law;
- sub-divide our shares or any of them into shares of smaller amount than is fixed by our amended and restated memorandum and articles of association, subject nevertheless to the Companies Law, and so that the resolution whereby any share is subdivided may determine that, as between the holders of the share resulting from such subdivision, one or more of the shares may have any such preference or other special rights, or may have such deferred rights or be subject to any such restrictions as compared with, the others as we have power to attach to unissued or new shares; and
- divide shares into several classes and without prejudice to any special rights previously conferred on the holders of existing shares, attach to the shares respectively as preferential, deferred, qualified or special rights, privileges, conditions or such restrictions which, in the absence of any such determination in a general meeting, may be determined by our directors.

We may, by special resolution, subject to any confirmation or consent required by the Companies Law, reduce our share capital or any capital redemption reserve in any manner authorized by law.

### **Transfer of Shares**

Subject to any applicable restrictions set forth in our amended and restated memorandum and articles of association, any of our shareholders may transfer all or any of his or her shares by an instrument of transfer in the usual or common form or in any form prescribed by the NASDAQ Global Market or in any other form which our directors may approve. You should note that, under Cayman Islands law, a person whose name is entered on the register of members will be deemed to be a member or shareholder of our company. We have designated American Stock Transfer and Trust Company as our share registrar. Under Cayman Islands law, a share certificate constitutes admissible evidence as proof of title of its holder to the shares specified on such certificate.

Our directors may decline to register any transfer of any share which is not paid up or on which we have a lien. Our directors may also decline to register any transfer of any share unless:

- the instrument of transfer is lodged with us accompanied by the certificate for the shares to which it relates and such other evidence as our directors may reasonably require to show the right of the transferor to make the transfer;
- the instrument of transfer is in respect of only one class of shares;
- the instrument of transfer is properly stamped (in circumstances where stamping is required);
- in the case of a transfer to joint holders, the number of joint holders to whom the share is to be transferred does not exceed four; and
- a fee of such maximum sum as the NASDAQ Global Market may at any time determine to be payable or such lesser sum as our directors may from time to time require is paid to us in respect thereof.

If our directors refuse to register a transfer, they shall, within two months after the date on which the instrument of transfer was lodged, send to each of the transferor and the transferee notice of such refusal.

The registration of transfers may, on notice being given by advertisement in such one or more newspapers or by any other means in accordance with any requirements of the NASDAQ Global Market, be suspended and the register closed at such times and for such periods as our directors may from time to time determine; provided, however, that the registration of transfers shall not be suspended nor the register closed for more than 30 days in any year as our directors may determine.

### **Share Repurchase**

We are empowered by the Companies Law and our amended and restated memorandum and articles of association to purchase our own shares, subject to certain restrictions. Our directors may only exercise this power on our behalf, subject to the Companies Law, our amended and restated memorandum and articles of association and to any applicable requirements imposed from time to time by the U.S. Securities and Exchange Commission, the NASDAQ Global Market, or by any recognized stock exchange on which our securities are listed.

## **Dividends**

Subject to the Companies Law, we may declare dividends in any currency to be paid to our shareholders. Dividends may be declared and paid out of our profits, realized or unrealized, or from any reserve set aside from profits which our directors determine is no longer needed. Our board of directors may also declare and pay dividends out of the share premium account or any other fund or account which can be authorized for this purpose in accordance with the Companies Law.

Except in so far as the rights attaching to, or the terms of issue of, any share otherwise provides (1) all dividends shall be declared and paid according to the amounts paid up on the shares in respect of which the dividend is paid, but no amount paid up on a share in advance of calls shall be treated for this purpose as paid up on that share and (2) all dividends shall be apportioned and paid pro rata according to the amounts paid upon the shares during any portion or portions of the period in respect of which the dividend is paid.

Our directors may also pay any dividend that is payable on any shares semi-annually or on any other dates, whenever our financial position, in the opinion of our directors, justifies such payment.

Our directors may deduct from any dividend or other money payable to any shareholder all sums of money (if any) presently payable by such shareholder to us on account of calls or otherwise.

No dividend or other money payable by us on or in respect of any share shall bear interest against us.

In respect of any dividend proposed to be paid or declared on our share capital, our directors may resolve and direct that (1) such dividend be satisfied wholly or in part in the form of an allotment of shares credited as fully paid up, provided that our shareholders entitled thereto will be entitled to elect to receive such dividend (or part thereof if our directors so determine) in cash in lieu of such allotment, or (2) the shareholders entitled to such dividend will be entitled to elect to receive an allotment of shares credited as fully paid up in lieu of the whole or such part of the dividend as our directors may think fit. We may also, on the recommendation of our directors, resolve in respect of any particular dividend that, notwithstanding the foregoing, it may be satisfied wholly in the form of an allotment of shares credited as fully paid up without offering any right of shareholders to elect to receive such dividend in cash in lieu of such allotment.

Any dividend, interest or other sum payable in cash to any shareholder may be paid by check or warrant sent by mail addressed to the shareholder at his registered address, or addressed to such person and at such addresses as the

shareholder may direct. Every check or warrant shall, unless the shareholder or joint shareholders otherwise direct, be made payable to the order of the shareholder or, in the case of joint shareholders, to the order of the shareholder whose name stands first on the register in respect of such shares, and shall be sent at their risk and payment of the check or warrant by the bank on which it is drawn shall constitute a good discharge to us.

All dividends unclaimed by shareholders for one year after having been declared may be invested or otherwise made use of by our board of directors for the benefit of our company until claimed. Any dividend unclaimed by shareholders after a period of six years from the date of declaration of such dividend may be forfeited and, if so forfeited, shall revert to us.

Whenever our directors have resolved that a dividend be paid or declared, our directors may further resolve that such dividend be satisfied wholly or in part by the distribution of specific assets of any kind, and in particular of paid up shares, debentures or warrants to subscribe for our securities or securities of any other company. Where any difficulty arises with regard to such distribution, our directors may settle it as they think expedient. In particular, our directors may issue fractional certificates, ignore fractions altogether or round the same up or down, fix the value for distribution purposes of any such specific assets, determine that cash payments shall be made to any of our shareholders upon the footing of the value so fixed in order to adjust the rights of the parties, vest any such specific assets in trustees as may seem expedient to our directors, and appoint any person to sign any requisite instruments of transfer and other documents on behalf of a person entitled to the dividend, which appointment shall be effective and binding on our shareholders.

### **Untraceable Shareholders**

We are entitled to sell any shares of a shareholder who is untraceable, provided that:

all checks or warrants in respect of dividends of such shares, not being less than three in number, for any sums payable in cash to the holder of such shares have remained uncashed for a period of twelve years prior to the publication of the advertisement and during the three months referred to in the third bullet point below;

we have not during that time received any indication of the whereabouts or existence of the shareholder or person entitled to such shares by death, bankruptcy or operation of law; and

we have caused an advertisement to be published in newspapers in the manner stipulated by our amended and restated memorandum and articles of association, giving notice of our intention to sell these shares, and a period of three months has elapsed since such advertisement and the NASDAQ Global Market has been notified of such intention.

The net proceeds of any such sale shall belong to us, and when we receive these net proceeds we shall become indebted to the former shareholder for an amount equal to such net proceeds.

### **Issuance of Additional Ordinary Shares or Preference Shares**

Subject to the Companies Law and the rules of the NASDAQ Global Market and without prejudice to any special rights or restrictions for the time being attached to any shares or any class of shares, our board of directors may issue additional ordinary shares from time to time as our board of directors determines, to the extent of available authorized but unissued shares and establish from time to time one or more series of preference shares and to determine, with respect to any series of preference shares, the terms and rights of that series, including:

- the designation of the series;
- the number of shares of the series;
- the dividend rights, conversion rights, voting rights; and
- the rights and terms of redemption and liquidation preferences.

Subject to the foregoing, our board of directors may issue series of preference shares without action by our shareholders to the extent authorized but unissued. Accordingly, the issuance of preference shares may adversely affect the rights of the holders of the ordinary shares. In addition, the issuance of preference shares may be used as an anti-takeover device without further action on the part of the shareholders. Issuance of preference shares may dilute the voting power of holders of ordinary shares.

Subject to applicable regulatory requirements, our board of directors may issue additional ordinary shares without action by our shareholders to the extent of available authorized but unissued shares. The issuance of additional ordinary shares may be used as an anti-takeover device without further action on the part of the shareholders. Such issuance may dilute the voting power of existing holders of ordinary shares.

Our ordinary shares are listed on the NASDAQ Global Market under the symbol “FFHL”.

### **Committees of Board of Directors**

Pursuant to our amended and restated articles of association, our board of directors, we have established an audit committee, a compensation committee and a corporate governance and nominating committee.

## **Differences in Corporate Law**

The Companies Law is modeled after similar laws in the United Kingdom but does not follow recent changes in United Kingdom laws. In addition, the Companies Law differs from laws applicable to United States corporations and their shareholders. Set forth below is a summary of the significant differences between the provisions of the Companies Law applicable to us and the laws applicable to companies incorporated in the United States, such as in the State of Delaware.

### ***Duties and Directors***

Under Cayman Islands law, at common law, members of a board of directors owe a fiduciary duty to the company to act in good faith in their dealings with or on behalf of the company and exercise their powers and fulfill the duties of their office honestly. This duty has four essential elements:

- a duty to act in good faith in the best interests of the company;
- a duty not to personally profit from opportunities that arise from the office of director;
- a duty to avoid conflicts of interest; and
- a duty to exercise powers for the purpose for which such powers were intended.

In general, the Companies Law imposes various duties on officers of a company with respect to certain matters of management and administration of the company. The Companies Law contains provisions, which impose default fines on persons who fail to satisfy those requirements. However, in many circumstances, an individual is only liable if he knowingly is guilty of the default or knowingly and willfully authorizes or permits the default.

In comparison, under Delaware law, the business and affairs of a corporation are managed by or under the direction of its board of directors. In exercising their powers, directors are charged with a fiduciary duty of care to protect the interests of the corporation and a fiduciary duty of loyalty to act in the best interests of its shareholders. The duty of care requires that directors act in an informed and deliberative manner and inform themselves, prior to making a business decision, of all material information reasonably available to them. The duty of care also requires that directors exercise care in overseeing and investigating the conduct of the corporation's employees. The duty of loyalty may be summarized as the duty to act in good faith, not out of self-interest, and in a manner which the director reasonably believes to be in the best interests of the shareholders.



Under Delaware law, a party challenging the propriety of a decision of a board of directors bears the burden of rebutting the applicability of the presumptions afforded to directors by the “business judgment rule”. If the presumption is not rebutted, the business judgment rule protects the directors and their decisions, and their business judgments will not be second guessed. Where, however, the presumption is rebutted, the directors bear the burden of demonstrating the entire fairness of the relevant transaction. Notwithstanding the foregoing, Delaware courts subject directors’ conduct to enhanced scrutiny in respect of defensive actions taken in response to a threat to corporate control and approval of a transaction resulting in a sale of control of the corporation.

### ***Interested Directors***

There are no provisions under the Companies Law that require a director who is interested in a transaction entered into by a Cayman Islands company to disclose his interest. However, under our amended and restated memorandum and articles of association, our directors are required to do so, and in the event that they do not do so it may render such director liable to such company for any profit realized pursuant to such transaction.

In comparison, under Delaware law, such a transaction would not be voidable if (a) the material facts as to such interested director’s relationship or interests are disclosed or are known to the board of directors and the board in good faith authorizes the transaction by the affirmative vote of a majority of the disinterested directors, even though the disinterested directors are less than a quorum, (b) such material facts are disclosed or are known to the shareholders entitled to vote on such transaction and the transaction is specifically approved in good faith by vote of the shareholders, or (c) the transaction is fair as to the corporation as of the time it is authorized, approved or ratified. Under Delaware law, a director could be held liable for any transaction in which such director derived an improper personal benefit.

### ***Voting Rights and Quorum Requirements***

Under Cayman Islands law, the voting rights of shareholders are regulated by the company’s articles of association and, in certain circumstances, the Companies Law. The articles of association will govern matters such as quorum for the transaction of business, rights of shares, and majority votes required to approve any action or resolution at a meeting of the shareholders or board of directors. Under Cayman Islands law, certain matters must be approved by a special resolution which is defined as two-thirds of the votes cast by shareholders present at a meeting and entitled to vote or such higher majority as is specified in the articles of association; otherwise, unless the articles of association otherwise provide, the majority is usually a simple majority of votes cast.

In comparison, under Delaware law, unless otherwise provided in the corporation’s certificate of incorporation, each shareholder is entitled to one vote for each share of stock held by the shareholder. Unless otherwise provided in the

corporation's certificate of incorporation or bylaws, a majority of the shares entitled to vote, present in person or represented by proxy, constitutes a quorum at a meeting of shareholders. In matters other than the election of directors, with the exception of special voting requirements related to extraordinary transactions, the affirmative vote of a majority of shares present in person or represented by proxy at the meeting and entitled to vote is required for shareholder action, and the affirmative vote of a plurality of shares is required for the election of directors.

### *Mergers and Similar Arrangements*

A merger of two or more constituent companies under Cayman Islands law requires a plan of merger or consolidation to be approved by the directors of each constituent company and authorization by (a) a majority in number representing seventy-five percent (75%) in value of the shareholders voting together as one class and (b) if the shares to be issued to each shareholder in the surviving company are to have the same rights and economic value as the shares held in the constituent company, a special resolution of the shareholders voting together as one class.

A merger between a Cayman parent company and its Cayman subsidiary or subsidiaries does not require authorization by a resolution of shareholders. For this purpose a subsidiary is a company of which at least ninety percent (90%) of the issued shares entitled to vote are owned by the parent company.

The consent of each holder of a fixed or floating security interest over a constituent company is required unless this requirement is waived by a court in the Cayman Islands.

**Save in certain circumstances, a dissentient shareholder of a Cayman constituent company is entitled to payment of the fair value of his shares upon dissenting to a merger or consolidation. The exercise of appraisal rights will preclude the exercise of any other rights save for the right to seek relief on the grounds that the merger or consolidation is void or unlawful.**

There are statutory provisions that facilitate the reconstruction and amalgamation of companies, provided that the arrangement in question is approved by a majority in number of each class of shareholders and creditors with whom the arrangement is to be made, and who must in addition represent three fourths in value of each such class of shareholders or creditors, as the case may be, that are present and voting either in person or by proxy at a meeting, or meetings convened for that purpose.

The convening of the meetings and subsequently the arrangement must be sanctioned by the Grand Court of the Cayman Islands. While a dissenting shareholder would have the right to express to the court the view that the transaction should not be approved, the court can be expected to approve the arrangement if it satisfies itself that:

- the company is not proposing to act illegally or ultra vires and the statutory provisions as to majority vote have been complied with;
- the shareholders have been fairly represented at the meeting in question;
- the arrangement is such as a businessman would reasonably approve; and
- the arrangement is not one that would more properly be sanctioned under some other provision of the Companies Law or that would amount to a “fraud on the minority”.

When a takeover offer is made and accepted by holders of 90% of the shares within four months, the offerer may, within a two-month period, require the holders of the remaining shares to transfer such shares on the terms of the offer. An objection may be made to the Grand Court of the Cayman Islands but is unlikely to succeed unless there is evidence of fraud, bad faith or collusion.

Cayman Islands laws do not require that shareholders approve sales of all or substantially all of a company’s assets as is commonly adopted by U.S. corporations.

If the arrangement and reconstruction are thus approved, any dissenting shareholders would have no rights comparable to appraisal rights, which would otherwise ordinarily be available to dissenting shareholders of United States corporations, providing rights to receive payment in cash for the judicially determined value of the shares.

### ***Shareholders’ Suits***

Derivative actions have been brought under Cayman Islands law but were unsuccessful for technical reasons. In principle, we will normally be the proper plaintiff and a derivative action may not be brought by a minority shareholder. However, based on English authorities, who would in all likelihood be of persuasive authority in the Cayman Islands, exceptions to the foregoing principle apply in circumstances in which:

- a company is acting or proposing to act illegally or beyond the scope of its authority;
- the act complained of, although not beyond the scope of its authority, could be effected duly if authorized by more than a simple majority vote which has not been obtained; and
- those who control the company are perpetrating a “fraud on the minority.”

Class actions and derivative actions generally are available to shareholders under Delaware law for, among other things, breach of fiduciary duty, corporate waste and actions not taken in accordance with applicable law. In such actions, the court generally has discretion to permit the winning party to recover attorneys' fees incurred in connection with such action.

### *Corporate Governance*

Cayman Islands laws do not restrict transactions with directors, requiring only that directors exercise a duty of care and owe a fiduciary duty to the companies for which they serve. Under our amended and restated memorandum and articles of association, subject to any separate requirement for audit committee approval under the applicable rules of the Nasdaq Stock Market, Inc. or unless disqualified by the chairman of the relevant board meeting, so long as a director discloses the nature of his interest in any contract or arrangement which he is interested in, such a director may vote in respect of any contract or proposed contract or arrangement in which such director is interested and may be counted in the quorum at such meeting.

Cayman Islands law does not limit the extent to which a company's articles of association may provide for indemnification of officers and directors, except to the extent any such provision may be held by the Cayman Islands courts to be contrary to public policy, such as to provide indemnification against civil fraud or the consequences of committing a crime. Our amended and restated memorandum and articles of association provide for the indemnification of our directors, auditors and officers against all losses or liabilities incurred or sustained by him or her as a director, auditor or officer of our company in defending any proceedings, whether civil or criminal, in which judgment is given in his or her favor, or in which he or she is acquitted provided that this indemnity may not extend to any matter in respect of any fraud or dishonesty which may attach to any of these persons.

Insofar as indemnification for liabilities arising under the Securities Act may be permitted to directors, officers or persons controlling us pursuant to the foregoing provisions, we have been advised that in the opinion of the SEC such indemnification is against public policy as expressed in the Securities Act and therefore is unenforceable.

We are managed by our board of directors. Our amended and restated memorandum and articles of association provide that the number of our directors shall not be less than two and there shall be no maximum number of our directors unless our shareholders in the general meeting otherwise determine a maximum number. Initially we have set our board of directors to have 4 directors. Any director on our board may be removed by way of an ordinary resolution of shareholders. At each annual general meeting, one third of our directors for the time being (or, if their number is not a multiple of three, the number nearest to but not greater than one-third) shall retire from office by rotation provided that the chairman of the Board and/or the managing director of the Company shall not, whilst holding such office, be subject to retirement by rotation.. Any vacancies on our board of directors or additions to the existing board of directors can be filled by an ordinary resolution of our shareholders or the affirmative vote of a majority of the remaining directors, although this may be less than a quorum where the number of remaining directors falls below the minimum number fixed by our board of directors. Our directors are not required to hold any of our shares to be qualified to serve on our board of directors.

Meetings of our board of directors may be convened at any time deemed necessary by any one of our directors. Advance notice of a meeting is not required if each director entitled to attend consents to the holding of such meeting.

A meeting of our board of directors at which a quorum is present shall be competent to make lawful and binding decisions. At any meeting of our directors, each director is entitled to one vote.

Questions arising at a meeting of our board of directors are required to be decided by simple majority votes of the members of our board of directors present or represented at the meeting. In the case of a tie vote, the chairman of the meeting shall have a second or deciding vote. Our board of directors may also pass resolutions without a meeting by unanimous written consent.

Insofar as indemnification for liabilities arising under the Securities Act may be permitted to directors, officers or persons controlling us pursuant to the foregoing provisions, we have been advised that in the opinion of the SEC such indemnification is against public policy as expressed in the Securities Act and therefore is unenforceable.

### ***Inspection of Corporate Records***

Shareholders of a Cayman Islands company have no general right under Cayman Islands law to inspect or obtain copies of a list of shareholders or other corporate records of the company. However, these rights may be provided in the articles of association.

In comparison, under Delaware law, shareholders of a Delaware corporation have the right during normal business hours to inspect for any proper purpose, and to obtain copies of list(s) of shareholders and other books and records of the corporation and its subsidiaries, if any, to the extent the books and records of such subsidiaries are available to the corporation.

### ***Shareholder Proposals***

The Companies Law does not provide shareholders any right to bring business before a meeting or requisition a general meeting. However, these rights may be provided in the articles of association.

Unless provided in the corporation's certificate of incorporation or bylaws, Delaware law does not include a provision restricting the manner in which shareholders may bring business before a meeting.

### ***Approval of Corporate Matters by Written Consent***

The Companies Law allows a special resolution to be passed in writing if signed by all the shareholders and authorized by the articles of association.

In comparison, Delaware law permits shareholders to take action by written consent signed by the holders of outstanding stock having not less than the minimum number of votes that would be necessary to authorize or take such action at a meeting of shareholders.

### ***Calling of Special Shareholders Meetings***

The Companies Law does not have provisions governing the proceedings of shareholders meetings that are usually provided in the articles of association.

In comparison, Delaware law permits the board of directors or any person who is authorized under a corporation's certificate of incorporation or bylaws to call a special meeting of shareholders.

### ***Staggered Board of Directors***

The Companies Law does not contain statutory provisions that require staggered board arrangements for a Cayman Islands company. Such provisions, however, may validly be provided for in the articles of association.

In comparison, Delaware law permits corporations to have a staggered board of directors.

### ***Anti-takeover Provisions***

Neither Cayman Islands nor Delaware law prevents companies from adopting a wide range of defensive measures, such as staggered boards, blank check preferred, and removal of directors only for cause and provisions that restrict the rights of shareholders to call meetings, act by written consent and submit shareholder proposals.

## **C. Material Contracts.**

### **1) Loan Contract**

We entered into five short-term loans contracts with Bank of Communications Co., Ltd. in April and May 2013 for a total amount of RMB105.0 million (US\$17.3million), including: (i) RMB20.0 million (US\$3.3 million) on April 18, 2013, maturing on April 2, 2014; (ii) RMB20.0 million (US\$3.3 million) on April 19, 2013, maturing on April 11, 2014; (iii) RMB25.0 million (US\$4.1 million) on April 23, 2013, maturing on April 16, 2014; (iv) RMB20.0 million (US\$3.3 million) on April 25, 2013, maturing on April 18, 2014; and (v) RMB20.0million (US\$3.3 million) on May 2, 2013, maturing on April 24, 2014. The annual interest rate of these bank loans is 7.2%, which was the rate increased by 20% compared with the benchmark interest rate announced by the People's Bank of China on the date when the loan was credited to our bank account. As of December 31, 2013, the balance of short-term loans is RMB105.0 million (US\$17.3 million).

On November 20, 2009, we signed a long-term loan contract of RMB10 million with Weifang Dongfang State-owned Assets Management Co., Ltd. for a term of eight years effective October 19, 2009, which will expire on October 18, 2017. The loan is guaranteed by Shandong Deqin Investment & Guarantee Co., Ltd. and is used for the Company's key projects.

### **2) Sale-Leaseback Contract**

On December 21, 2012, Shandong Fuwei signed a sale-leaseback contract with International Far Eastern Leasing Co., Ltd. ("Far Eastern Leasing"). Far Eastern Leasing purchased certain equipment included in the third production line, and simultaneously leased them back to Shandong Fuwei. Shandong Fuwei will pay rent totaling RMB21.95 million (including interest) to Far Eastern Leasing for 36 months beginning on December 26, 2012 until December 26, 2015. In March 2013, Shandong Fuwei signed another sale-leaseback contract with Far Eastern Leasing, pursuant to which



it has agreed to pay total rent of RMB5.49 million (including interest) to Far Eastern Leasing for 36 months beginning on March 27, 2013 until March 27, 2016. The financed equipment mentioned above is covered by an insurance policy, the premium of which will be paid by Shandong Fuwei. The contract was guaranteed by the following entities: Weifang State-owned Assets Operation Administration Company, Fuwei Films (Holdings) Co., Ltd, Fuwei (BVI) Co., Ltd., and Beijing Shiweitong Science and Technology Co., Ltd.

### **3)Ownership of Property Transfer Agreement under Sale-Leaseback Contract**

On December 21, 2012, Shandong Fuwei signed an ownership of property transfer agreement under sale-leaseback contract with Far Eastern Leasing. According to relevant laws and regulations, through a sale-leaseback, Shandong Fuwei transferred a portion of the third line equipment which was valued at RMB20.26 million to Far Eastern Leasing for RMB20.0 million. Pursuant to the terms of the agreement, Far Eastern Leasing will make a payment of RMB20.0 million to Shandong Fuwei within 7 business days upon effective date of the agreement. The payment was received by Shandong Fuwei on December 26, 2012.

In addition, on March 26, 2013, Shandong Fuwei signed an ownership of property transfer agreement under sale-leaseback contract with Far Eastern Leasing. According to relevant laws and regulations, through a sale-leaseback, Shandong Fuwei transferred a portion of the third line equipment which was valued at RMB18.1 million to Far Eastern Leasing for RMB5.0 million. Pursuant to the terms of the agreement, Far Eastern Leasing will make a payment of RMB5.0 million to Shandong Fuwei within 7 business days upon effective date of the agreement. The payment was received by Shandong Fuwei on March 27, 2013.

### **D. Exchange Controls.**

Chinese government imposes control over the convertibility of RMB into foreign currencies. Under the current unified floating exchange rate system, the People's Bank of China publishes a daily exchange rate for RMB, or the PBOC Exchange Rate, based on the previous day's dealings in the inter-bank foreign exchange market. Financial institutions authorized to deal in foreign currency may enter into foreign exchange transactions at exchange rates within an authorized range above or below the PBOC Exchange Rate according to market conditions.

Pursuant to the Foreign Exchange Control Regulations issued by the State Council on January 29, 1996 and effective as of April 1, 1996 (and amended on January 14, 1997) and the Administration of Settlement, Sale and Payment of Foreign Exchange Regulations which came into effect on July 1, 1996 regarding foreign exchange control, or the Regulations, conversion of Renminbi into foreign exchange by foreign investment enterprises for current account items, including the distribution of dividends and profits to foreign investors of joint ventures, is permissible upon the proper production of qualified commercial vouchers or legal documents as required by the Regulations. Foreign investment enterprises are permitted to remit foreign exchange from their foreign exchange bank account in China upon the proper production of, inter alia, the board resolutions declaring the distribution of the dividend and payment of profits. Conversion of RMB into foreign currencies and remittance of foreign currencies for capital account items, including direct investment, loans, security investment, is still subject to the approval of the State Administration of Foreign Exchange, or SAFE, in each such transaction. On January 14, 1997, the State Council amended the Foreign Exchange Control Regulations and added, among other things, an important provision, as Article 5 provides that the State shall not impose restrictions on recurring international payments and transfers.

Under the Regulations, foreign investment enterprises are required to open and maintain separate foreign exchange accounts for capital account items (but not for other items). In addition, foreign investment enterprises may only buy, sell and/or remit foreign currencies at those banks authorized to conduct foreign exchange business upon the production of valid commercial documents and, in the case of capital account item transactions, document approval from SAFE.

Currently, foreign investment enterprises are required to apply to SAFE for “foreign exchange registration certificates for foreign investment enterprises”. With such foreign exchange registration certificates (which are granted to foreign investment enterprises, upon fulfilling specified conditions and which are subject to review and renewal by SAFE on an annual basis) or with the foreign exchange sales notices from the SAFE (which are obtained on a transaction-by-transaction basis), foreign-invested enterprises may enter into foreign exchange transactions at banks authorized to conduct foreign exchange business to obtain foreign exchange for their needs.

## **E. Taxation.**

### **United States Federal Income Taxation**

#### **General**

The following is a summary of the material U.S. federal income tax consequences of the acquisition, ownership, and disposition of our ordinary shares, based upon laws and relevant interpretations thereof in effect as of the date of this Annual Report on Form 20-F, all of which are subject to change. This summary does not deal with all possible tax

consequences relating to an investment in our ordinary shares, such as the tax consequences under state, local or other tax laws.

The discussion below of the U.S. federal income tax consequences to “U.S. Holders” will apply to a beneficial owner of our ordinary shares that is for U.S. federal income tax purposes:

- an individual citizen or resident of the United States;
- a corporation (or other entity treated as a corporation) that is created or organized (or treated as created or organized) in or under the laws of the United States, any state thereof or the District of Columbia;
- an estate whose income is includible in gross income for U.S. federal income tax purposes regardless of its source; or
- a trust if (i) a U.S. court can exercise primary supervision over the trust’s administration and one or more U.S. persons are authorized to control all substantial decisions of the trust, or (ii) it has a valid election in effect under applicable U.S. Treasury regulations to be treated as a U.S. person.

A beneficial owner of our ordinary shares that is described above is referred to herein as a “U.S. Holder”. If a beneficial owner of our ordinary shares is not described as a U.S. Holder and is not an entity treated as a partnership or other pass-through entity for U.S. federal income tax purposes, such owner will be considered a “Non-U.S. Holder”. The material U.S. federal income tax consequences applicable specifically to Non-U.S. Holders of owning and disposing of our ordinary shares are described below under the heading “Non-U.S. Holders”.

This summary is based on the Internal Revenue Code of 1986, as amended, or the Code, its legislative history, Treasury regulations promulgated there under, published rulings and court decisions, all as currently in effect. These authorities are subject to change or differing interpretations, possibly on a retroactive basis.

This discussion does not address all aspects of U.S. federal income taxation that may be relevant to any particular holder based on such holder’s individual circumstances. In particular, this discussion considers only holders that own and hold our ordinary shares as capital assets within the meaning of Section 1221 of the Code, and does not address the potential application of the alternative minimum tax. In addition, this discussion does not address the U.S. federal income tax consequences to holders that are subject to special rules, including:

- financial institutions or financial services entities;
- broker-dealers;
- persons that are subject to the mark-to-market accounting rules under Section 475 of the Code;
- tax-exempt entities;
- governments or agencies or instrumentalities thereof;
- insurance companies;
- regulated investment companies;
- real estate investment trusts;
- certain expatriates or former long-term residents of the United States;
- persons that actually or constructively own 5% or more of our voting shares;
  - persons that acquired our ordinary shares pursuant to an exercise of employee options, in connection with employee incentive plans or otherwise as compensation;
  - persons that hold our ordinary shares as part of a straddle, constructive sale, hedging, conversion or other integrated transaction;
- persons whose functional currency is not the U.S. dollar;
- controlled foreign corporations; or
- passive foreign investment companies.

This discussion does not address any aspect of U.S. federal non-income tax laws, such as gift or estate tax laws, or state, local or non-U.S. tax laws or, except as discussed herein, any tax reporting obligations applicable to a holder of our ordinary shares. Additionally, this discussion does not consider the tax treatment of partnerships or other pass-through entities or persons who hold our ordinary shares through such entities. If a partnership (or other entity classified as a partnership for U.S. federal income tax purposes) is the beneficial owner of our ordinary shares, the U.S. federal income tax treatment of a partner in the partnership will generally depend on the status of the partner and the activities of the partnership. This discussion also assumes that any distribution made (or deemed made) by us on our ordinary shares and any consideration received (or deemed received) by a holder in consideration for the sale or other disposition of our ordinary shares will be in U.S. dollars.

We have not sought, and will not seek, a ruling from the Internal Revenue Service (“IRS”) or an opinion of counsel as to any U.S. federal income tax consequence described herein. The IRS may disagree with the description herein, and its determination may be upheld by a court. Moreover, there can be no assurance that future legislation, regulations, administrative rulings or court decisions will not adversely affect the accuracy of the statements in this discussion.

**THIS DISCUSSION IS ONLY A SUMMARY OF THE MATERIAL U.S. FEDERAL INCOME TAX CONSEQUENCES OF THE ACQUISITION, OWNERSHIP AND DISPOSITION OF OUR ORDINARY SHARES. IT IS NOT TAX ADVICE. EACH HOLDER OF OUR ORDINARY SHARES IS URGED TO CONSULT ITS OWN TAX ADVISOR IN RESPECT TO THE PARTICULAR TAX CONSEQUENCES TO SUCH HOLDER OF THE ACQUISITION, OWNERSHIP AND DISPOSITION OF OUR ORDINARY SHARES, INCLUDING THE APPLICABILITY AND EFFECT OF ANY STATE, LOCAL, AND NON-U.S. TAX LAWS, AS WELL AS U.S. FEDERAL TAX LAWS AND ANY APPLICABLE TAX TREATIES.**

## U.S. Holders

### *Taxation of Cash Distributions Paid on Ordinary Shares*

Subject to the passive foreign investment company (PFIC) rules discussed below, a U.S. Holder generally will be required to include in gross income as ordinary income the amount of any cash dividend paid on our ordinary shares. A cash distribution on our ordinary shares generally will be treated as a dividend for U.S. federal income tax purposes to the extent paid out of our current or accumulated earnings and profits (as determined under U.S. federal income tax principles). Such dividend generally will not be eligible for the dividends-received deduction generally allowed to domestic corporations in respect of dividends received from other domestic corporations. The portion of such distribution, if any, in excess of such earnings and profits generally will constitute a return of capital that will be applied against and reduce (but not below zero) the U.S. Holder's adjusted tax basis in our ordinary shares. Any remaining excess generally will be treated as gain from the sale or other taxable disposition of such ordinary shares and will be treated as described under "*Taxation on the Disposition of Ordinary Shares*" below.

With respect to non-corporate U.S. Holders, such cash dividends may be subject to U.S. federal income tax at the lower applicable regular long term capital gains tax rate (see "*Taxation on the Disposition of Ordinary Shares*" below) provided that (a) our ordinary shares are readily tradable on an established securities market in the United States or, in the event we are deemed to be a PRC "resident enterprise" under the relevant PRC tax laws, we are eligible for the benefits of the Agreement between the Government of the United States of America and the Government of the People's Republic of China for the Avoidance of Double Taxation and the Prevention of Tax Evasion with Respect to Taxes on Income, or the U.S.-PRC Tax Treaty, (b) we are not a PFIC, as discussed below, for either the taxable year in which the dividend was paid or the preceding taxable year, and (c) certain holding period requirements are met. Under published IRS authority, shares are considered for purposes of clause (a) above to be readily tradable on an established securities market in the United States only if they are listed on certain exchanges, which presently include the NASDAQ Global Market. Although our ordinary shares are currently listed and traded on the NASDAQ Global Market, U.S. Holders nonetheless should consult their own tax advisors regarding the availability of the lower rate for any cash dividends paid in respect to our ordinary shares.

If a PRC income tax applies to any cash dividends paid to a U.S. Holder on our ordinary shares, such tax maybe treated as a foreign tax eligible for a deduction from such holder's U.S. federal taxable income or a foreign tax credit against such holder's U.S. federal income tax liability (subject to applicable conditions and limitations). In addition, if such PRC tax applies to any such dividends, a U.S. Holder may be entitled to certain benefits under the U.S.-PRC Tax Treaty if such holder is considered a resident of the United States for purposes of, and otherwise meets the requirements of, the U.S.-PRC Tax Treaty. U.S. Holders should consult their own tax advisors regarding the deduction or credit for any such PRC tax and their eligibility for the benefits of the U.S.-PRC Tax Treaty.

### ***Taxation on the Disposition of Ordinary Shares***

Upon a sale or other taxable disposition of our ordinary shares, and subject to the PFIC rules discussed below, a U.S. Holder generally will recognize capital gain or loss in an amount equal to the difference between the amount realized and the U.S. Holder's adjusted tax basis in the ordinary shares.

The regular U.S. federal income tax rate on capital gains recognized by U.S. Holders generally is the same as the regular U.S. federal income tax rate on ordinary income, except that long-term capital gains recognized by non-corporate U.S. Holders generally are subject to U.S. federal income tax at a maximum regular rate of 20%. Capital gain or loss will constitute long-term capital gain or loss if the U.S. Holder's holding period for our ordinary shares exceeds one year. The deductibility of capital losses is subject to various limitations.

If a PRC income tax applies to any gain from the disposition of our ordinary shares by a U.S. Holder, such tax maybe treated as a foreign tax eligible for a deduction from such holder's U.S. federal taxable income or a foreign tax credit against such holder's U.S. federal income tax liability (subject to applicable conditions and limitations). In addition, if such PRC tax applies to any gain, such U.S. Holder maybe entitled to certain benefits under the U.S.-PRC Tax Treaty if such holder is considered a resident of the United States for purposes of, and otherwise meets the requirements of, the U.S.-PRC Tax Treaty. U.S. Holders should consult their own tax advisors regarding the deduction or credit for any such PRC tax and their eligibility for the benefits of the U.S.-PRC Tax Treaty.

### ***Passive Foreign Investment Company Rules***

A foreign (i.e., non-U.S.) corporation will be a PFIC if at least 75% of its gross income in a taxable year of the foreign corporation, including its pro rata share of the gross income of any corporation in which it is considered to own at least 25% of the shares by value, is passive income. Alternatively, a foreign corporation will be a PFIC if at least 50% of its assets in a taxable year of the foreign corporation, ordinarily determined based on fair market value and averaged quarterly over the year, including its pro rata share of the assets of any corporation in which it is considered to own at least 25% of the shares by value, are held for the production of, or produce, passive income. Passive income

generally includes dividends, interest, rents and royalties (other than certain rents or royalties derived from the active conduct of a trade or business), and gains from the disposition of passive assets.

Based on the composition (and estimated values) of our assets and the nature of the income and our subsidiaries for our 2013 taxable year, we do not believe that we will be treated as a PFIC for such year. However, because we have not performed a definitive analysis as to our PFIC status for our 2013 taxable year, there can be no assurance in respect to our PFIC status for such taxable year. There also can be no assurance with respect to our status as a PFIC for our current taxable year (2014) or any future taxable year. The determination of whether we are or have been a PFIC is primarily factual, and there is little administrative or judicial authority on which to rely to make a determination of PFIC status. Accordingly, the IRS or a court considering the matter may not agree with our analysis of whether we are or were a PFIC during any particular year.

If we are determined to be a PFIC for any taxable year (or portion thereof) that is included in the holding period of a U.S. Holder of our ordinary shares, and, in the case of our ordinary shares, the U.S. Holder did not make either a timely qualified electing fund, or QEF, election for our first taxable year as a PFIC in which the U.S. Holder held (or was deemed to hold) our ordinary shares, or a mark-to-market election, each as described below, such holder generally will be subject to special rules for regular U.S. federal income tax purposes with respect to:

· any gain recognized by the U.S. Holder on the sale or other disposition of our ordinary shares; and

any “excess distribution” made to the U.S. Holder (generally, any distributions to such U.S. Holder during a taxable year of the U.S. Holder that are greater than 125% of the average annual distributions received by such U.S. Holder in respect of the ordinary shares during the three preceding taxable years of such U.S. Holder or, if shorter, such U.S. Holder’s holding period for the ordinary shares).

Under these rules,

the U.S. Holder's gain or excess distribution will be allocated ratably over the U.S. Holder's holding period for the ordinary shares;

the amount allocated to the U.S. Holder's taxable year in which the U.S. Holder recognized the gain or received the excess distribution, or to the period in the U.S. Holder's holding period before the first day of our first taxable year in which we are a PFIC, will be taxed as ordinary income;

the amount allocated to other taxable years (or portions thereof) of the U.S. Holder and included in its holding period will be taxed at the highest tax rate in effect for that year and applicable to the U.S. Holder; and

the interest charge generally applicable to underpayments of tax will be imposed in respect of the tax attributable to each such other taxable year of the U.S. Holder.

In general, if we are determined to be a PFIC, a U.S. Holder may avoid the PFIC tax consequences described above in respect to our ordinary shares by making a timely QEF election (or a QEF election along with a purging election). Pursuant to the QEF election, a U.S. Holder will be required to include in income its pro rata share of our net capital gains (as long-term capital gain) and other earnings and profits (as ordinary income), on a current basis, in each case whether or not distributed in the taxable year of the U.S. Holder in which or with which our taxable year ends. However, a U.S. Holder may make a QEF election only if we agree to provide certain tax information to such holder annually. At this time, we do not intend to provide U.S. Holders with such information as may be required to make a QEF election effective.

Alternatively, if a U.S. Holder, at the close of its taxable year, owns ordinary shares in a PFIC that are treated as marketable stock, the U.S. Holder may make a mark-to-market election in respect to such ordinary shares for such taxable year. If the U.S. Holder makes a valid mark-to-market election for the first taxable year of the U.S. Holder in which the U.S. Holder holds (or is deemed to hold) ordinary shares and for which we are determined to be PFIC, such holder generally will not be subject to the PFIC rules described above in respect to its ordinary shares. Instead, in general, the U.S. Holder will include as ordinary income each year the excess, if any, of the fair market value of its ordinary shares at the end of its taxable year over the adjusted tax basis in its ordinary shares. The U.S. Holder also will be allowed to take an ordinary loss in respect of the excess, if any, of the adjusted tax basis of its ordinary shares over the fair market value of such shares at the end of its taxable year (but only to the extent of the net amount of previously included income as a result of the mark-to-market election). The U.S. Holder's adjusted tax basis in its ordinary shares will be adjusted to reflect any such income or loss amounts, and any further gain recognized on a sale or other taxable disposition of the ordinary shares will be treated as ordinary income.



The mark-to-market election is available only for stock that is regularly traded on a national securities exchange that is registered with the Securities and Exchange Commission, including the NASDAQ Global Market, or on a foreign exchange or market that the IRS determines has rules sufficient to ensure that the market price represents a legitimate and sound fair market value. While our ordinary shares currently are listed and traded on the NASDAQ Global Market, U.S. Holders nonetheless should consult their own tax advisors regarding the availability and tax consequences of a mark-to-market election in respect to our shares under their particular circumstances.

If we are a PFIC and, at any time, have a foreign subsidiary that is classified as a PFIC, a U.S. Holder of our ordinary shares should be deemed to own a portion of the shares of such lower-tier PFIC, and could incur liability for the deferred tax and interest charge described above if we receive a distribution from, or dispose of all or part of our interest in, or the U.S. Holder were otherwise deemed to have disposed of an interest in, the lower-tier PFIC. U.S. Holders are urged to consult their own tax advisors regarding the tax issues raised by lower-tier PFICs.

A U.S. Holder that owns (or is deemed to own) ordinary shares in a PFIC during any taxable year of the U.S. Holder may have to file an IRS Form 8621 (whether or not a market-to-market election is or has been made) with such U.S. Holder's U.S. federal income tax return and provide such other information as may be required by the U.S. Treasury Department.

The rules dealing with PFICs and with the QEF and mark-to-market elections are very complex and are affected by various factors in addition to those described above. Accordingly, U.S. Holders of our ordinary shares should consult their own tax advisors concerning the application of the PFIC rules to our ordinary shares under their particular circumstances.

### ***Additional Taxes***

U.S. Holders that are individuals, estates or trusts and whose income exceeds certain thresholds generally will be subject to a 3.8% Medicare contribution tax on unearned income, including, without limitation, dividends on, and gains from the sale or other taxable disposition of, our ordinary shares, subject to certain limitations and exceptions. U.S. Holders should consult their own tax advisors regarding the effect, if any, of such tax on their ownership and disposition of our ordinary shares.

## **Non-U.S. Holders**

Cash-dividends paid to a Non-U.S. Holder in respect to our ordinary shares generally will not be subject to U.S. federal income tax, unless such dividends are effectively connected with the Non-U.S. Holder's conduct of a trade or business within the United States (and, if required by an applicable income tax treaty, are attributable to a permanent establishment or fixed base that such holder maintains or maintained in the United States).

In addition, a Non-U.S. Holder generally will not be subject to U.S. federal income tax on any gain attributable to a sale or other taxable disposition of our ordinary shares unless such gain is effectively connected with its conduct of a trade or business in the United States (and, if required by an applicable income tax treaty, is attributable to a permanent establishment or fixed base that such holder maintains or maintained in the United States) or the Non-U.S. Holder is an individual who is present in the United States for 183 days or more in the taxable year of sale or other disposition and certain other conditions are met (in which case such gain from U.S. sources generally is subject to U.S. federal income tax at a 30% rate or a lower applicable tax treaty rate).

Cash dividends and gains that are effectively connected with the Non-U.S. Holder's conduct of a trade or business in the United States (and, if required by an applicable income tax treaty, are attributable to a permanent establishment or fixed base that such holder maintains or maintained in the United States) generally will be subject to regular U.S. federal income tax at the same regular U.S. federal income tax rates applicable to a comparable U.S. Holder and, in the case of a Non-U.S. Holder that is a corporation for U.S. federal income tax purposes, may also be subject to an additional branch profits tax at a 30% rate or a lower applicable tax treaty rate.

## **Backup Withholding and Information Reporting**

In general, information reporting for U.S. federal income tax purposes should apply to cash distributions made on our ordinary shares within the United States to a U.S. Holder (other than an exempt recipient) and to the proceeds from sales and other dispositions of our ordinary shares by a U.S. Holder (other than an exempt recipient) to or through a U.S. office of a broker. Payments made (and sales and other dispositions effected at an office) outside the United States will be subject to information reporting in limited circumstances. In addition, certain information concerning a U.S. Holder's adjusted tax basis in its ordinary shares and adjustments to that tax basis and whether any gain or loss with respect to such ordinary shares is long-term or short-term also may be required to be reported to the IRS, and certain holders may be required to file an IRS Form 8938 (Statement of Specified Foreign Financial Assets) to report their interest in our ordinary shares.

Moreover, backup withholding of U.S. federal income tax, at a rate of 28%, generally will apply to cash dividends paid on our ordinary shares to a U.S. Holder (other than an exempt recipient) and the proceeds from sales and other

dispositions of our ordinary shares by a U.S. Holder (other than an exempt recipient), in each case who:

- fails to provide an accurate taxpayer identification number;
- is notified by the IRS that backup withholding is required; or
- in certain circumstances fails to comply with applicable certification requirements.

A Non-U.S. Holder generally may eliminate the requirement for information reporting and backup withholding by providing certification of its foreign status, under penalties of perjury, on a duly executed applicable IRS Form W-8 or by otherwise establishing an exemption.

Backup withholding is not an additional tax. Rather, the amount of any backup withholding will be allowed as a credit against a U.S. Holder's or a Non-U.S. Holder's U.S. federal income tax liability and may entitle such holder to a refund, provided that certain required information is timely furnished to the IRS. Holders are urged to consult their own tax advisors regarding the application of backup withholding and the availability of and procedures for obtaining an exemption from backup withholding in their particular circumstances.

#### **Other Non-United States Taxation Treatment**

The following discussion is a summary of certain anticipated PRC and Cayman Islands tax consequences of an investment in our ordinary shares. The discussion does not deal with all possible tax consequences relating to an investment in our ordinary shares and does not purport to deal with the tax consequences applicable to all categories of investors, some of which (such as dealers in securities, insurance companies and tax-exempt entities) may be subject to special rules. In particular, the discussion does not address the tax consequences under state, local and other national tax laws. Accordingly, each prospective investor should consult its own tax advisor regarding the particular tax consequences to it of an investment in our ordinary shares. The following discussion is based upon laws and relevant interpretations thereof in effect as of the date of this Annual Report, all of which are subject to change.

## China Taxation

There are significant uncertainties under the new corporate income tax law of the PRC, or the New Tax Law, which became effective on January 1, 2008, regarding our PRC enterprise income tax liabilities, such as a tax on any dividends paid to us by our PRC subsidiary. The New Tax Law also contains uncertainties regarding possible PRC withholding tax on dividends we pay to our overseas shareholders and gains realized from the transfer of our shares by our overseas shareholders.

We are a holding company incorporated in the Cayman Islands, which indirectly holds, through Fuwei (BVI), our equity interest in Shandong Fuwei, our subsidiary and actual operating body in the PRC. Our business operations are principally conducted through Shandong Fuwei.

Under the New Tax Law, enterprises established under the laws of jurisdictions outside China with their “de facto management bodies” located within China may be considered to be PRC tax resident enterprises for tax purposes and subjected to the tax obligations of a PRC tax resident. If we or Fuwei (BVI) is considered as a PRC tax resident enterprise under the New Tax Law, then our global income will be subject to PRC enterprise income tax at the rate of 25%.

On April 22, 2009, the State Administration of Taxation issued a Notice Regarding Recognition of Overseas Incorporated Enterprises Controlled by PRC Domestic Enterprises as PRC Resident Enterprises Based on the De Facto Management Body Criteria (the “Tax Residency Notice”). Under the Tax Residency Notice, which was retroactively effective as of January 1, 2008, an overseas enterprise will be deemed to be a PRC resident enterprise and thus subject to Enterprise Income Tax of 25% on its global income if it satisfies four conditions: (i) the company’s management team responsible for daily operations are located in China, or the location where the management team carries out their responsibilities is in China; (ii) finance and personnel decisions are made or need approval by institutions or people in China; (iii) the company’s major property, accounting ledger, company seal and minutes of board meetings and shareholder meetings are kept in China; and (iv) at least half of the members of the board of directors with voting rights or the management team habitually live in China.

Although Tax Residency Notice applies only to overseas registered enterprises controlled by PRC enterprises, not to those controlled by PRC individuals, the determining criteria set forth in Tax Residency Notice may reflect the State Administration of Taxation’s general position on how the “de facto management body” test should be applied in determining the tax resident status of offshore enterprises, regardless of whether they are controlled by PRC enterprises or individuals. If we are deemed a PRC resident enterprise, we may be subject to the Enterprise Income Tax at 25% on our global income. If we are considered a resident enterprise and earn income other than dividends from our PRC subsidiaries, a 25% Enterprise Income Tax on our global income could significantly increase our tax burden and materially and adversely affect our cash flow and profitability.

However, China-sourced income of foreign enterprises, such as dividends paid by a PRC subsidiary to its overseas parent, will normally be subject to PRC tax.

Furthermore, the implementation rules of the New Tax Law provide that (i) if the enterprise that distributes the dividends is domiciled in the PRC, or (ii) if gains are realized from transferring equity interests of enterprises domiciled in the PRC, then such dividends or capital gains are treated as China-sourced income. It is not clear how “domicile” may be interpreted under the New Tax Law, and it may be interpreted as the jurisdiction where the enterprise is a tax resident. Therefore, if we are considered as a PRC resident enterprise for PRC tax purposes, any dividends we pay to our overseas shareholders as well as gains realized by such shareholders from the transfer of our shares may be regarded as China-sourced income and, thus, may be subject to PRC tax.

As the New Tax Law and the implementation rules have only recently taken effect, it is uncertain as to how they will be implemented by the relevant PRC tax authorities. If dividend payments from Shandong Fuwei and from Fuwei (BVI) to us are subject to PRC withholding tax, our financial condition, results of operations and the amount of dividends available to pay our shareholders may be adversely affected. Also, if dividends we pay to our overseas shareholders or gains realized by such shareholders from the transfer of our shares are subject to PRC tax, it may materially and adversely affect your investment return and the value of your investment in us. There is an income tax treaty in effect between the United States and China, so U.S. shareholders may be entitled to certain benefits under such treaty.

### **Cayman Island Taxation**

The Cayman Islands currently has no exchange control restrictions. The Cayman Islands currently levies no taxes on individuals or corporations based upon profits, income, gains or appreciation and there is no taxation in the nature of inheritance tax or estate duty. There are no other taxes likely to be material to the Company levied by the government of the Cayman Islands, save certain stamp duties which may be applicable, from time to time, on certain instruments executed in or brought within the jurisdiction of the Cayman Islands. The Cayman Islands is not a party to any double tax treaties.

Pursuant to section 6 of the Tax Concessions Law (1999 Revision) of the Cayman Islands, the Company has obtained an undertaking from the Governor in Cabinet:

- (a) that no law which is enacted in the Cayman Islands imposing any tax to be levied on profits or income or gains or appreciation shall apply to the Company or its operations; and
- (b) in addition, that no tax is levied on profits, income, gains or appreciation or no tax which is in the nature of estate duty or inheritance tax shall be payable by the Company:



- (i) on or in respect of the shares, debentures or other obligations of the Company; or
- (ii) by way of withholding in whole or in part of any relevant payment as defined in section 6(3) of the Tax Concession Law (1999 Revision).

The undertaking is for a period of 20 years from 24 August, 2004.

#### **F. Dividends and Paying Agents.**

Not applicable.

#### **G. Statement by Experts.**

Not applicable.

#### **H. Documents on Display**

We are subject to the periodic reporting and other informational requirements of the Securities Exchange Act of 1934, as amended, or the Exchange Act. Under the Exchange Act, we are required to file reports and other information with the Securities and Exchange Commission. Specially, we are required to file annually a Form 20-F no later than six month after the close of each fiscal year, which is December 31. Copies of reports and other information, when so filed, may be inspected without charge and may be obtained at prescribed rates at the public reference facilities maintained by the Securities and Exchange Commission at Judiciary Plaza, 100 F. Street, N.E., Washington, D.C. 20549. The public may obtain information regarding the Washington, D.C. Public Reference Room by calling the Commission at 1-800-SEC-0330. The SEC also maintains a Web site at [www.sec.gov](http://www.sec.gov) that contains reports, proxy and information statements, and other information regarding registrants that make electronic filings with the SEC using its EDGAR system.

As a foreign private issuer, we are exempt from the rules under the Exchange Act prescribing the furnishing and content of quarterly reports and proxy statements, and officers, directors and principal shareholders are exempt from the reporting requirements pursuant to Section 16 of the Exchange Act.

Documents concerning the Company that are referred to in this document may also be inspected at our office, which is at No. 387 Dongming Road, Weifang Shandong 261061, People's Republic of China.

## **I. Subsidiary Information.**

Not applicable.

## **Item 11. Quantitative and Qualitative Disclosures about Market Risk.**

### **Foreign exchange risk**

We are exposed to the risk of foreign currency exchange rate fluctuation. We have never used derivative instruments to hedge our exchange rate risks, do not plan to do so, and may not be successful should we attempt to do so in the future. Nevertheless, we believe such risk is low as no foreign currency liabilities are incurred and the principal operations are limited mainly to the market in China.

Our operating subsidiary, Shandong Fuwei's, functional currency is Renminbi while our functional currency is Hong Kong Dollars. Transactions in other currencies are recorded in Renminbi at the rates of exchange prevailing when the transactions occur. Monetary assets and liabilities denominated in other currencies are converted into Renminbi at rates of exchange in effect at the balance sheet dates. Exchange gains and losses are recorded in our statements of operations as a component of current period earnings.

The China State Administration for Foreign Exchange, under the authority of the People's Bank of China, controls the conversion of Renminbi into foreign currencies. The principal regulation governing foreign currency exchange in China is the Foreign Currency Administration Rules (1996), as amended. Under the Rules, once various procedural requirements are met, Renminbi is convertible for current account transactions, including trade and services, but not for capital account transactions, including direct investment, loan or investment in securities outside China, unless the prior approval of the State Administration of Foreign Exchange of China is obtained. Although the Chinese government regulations now allow greater convertibility of Renminbi for current account transactions, significant restrictions still remain. Currently, we are not involved in foreign exchange transactions as all transactions are conducted in China are in Renminbi and all exporting business is completed in U.S. dollars.



The value of the Renminbi is subject to changes in China's central government policies and to international economic and political developments affecting supply and demand in the China Foreign Exchange Trading System market. Since 1994, the conversion of Renminbi into foreign currencies, including U.S. dollars, has been based on rates set by the People's Bank of China, which are set daily based on the previous day's interbank foreign exchange market rates and current exchange rates on the world financial markets. Since 1994, the official exchange rate generally has been stable. The official exchange rate for the conversion of Renminbi into U.S. dollars remained stable until Renminbi was revalued in July 2005 and allowed to fluctuate by reference to a basket of foreign currencies, including the U.S. dollar. Under the new policy, Renminbi is permitted to fluctuate within a band against a basket of foreign currencies.

We conduct substantially all of our operations through Shandong Fuwei, and its financial performance and position are measured in terms of Renminbi. Any appreciation of the Renminbi against the United States dollar would consequently have an adverse effect on our financial performance and asset values when measured in terms of United States dollar. Our solutions are primarily procured, sold and delivered in China for Renminbi. The majority of our revenues are denominated in Renminbi. Should the Renminbi appreciate against United States dollar, such appreciation could have a material adverse effect on our profits and the foreign currency equivalent of such profits repatriated by the Chinese entities to us.

### **Interest rate risk**

We are exposed to interest rate risk arising from having short-term variable rate borrowings from time to time. Our future interest expense would fluctuate in line with any change in our borrowing rates. We do not have any derivative financial instruments and believe our exposure to interest rate risk and other relevant market risks is not material.

### **Inflation**

According to the National Bureau of Statistics of China, the change in Consumer Price Index in China was 2.6%, 2.6% and 5.4% in 2013, 2012 and 2011 respectively.

### **Credit and liquidity risks**

We adopt a risk assessment model to our customer credit management system, and we offer different credit terms to our customers based on criteria such as working relationship, payment history, creditworthiness and their financial position. All credit terms are approved by our finance department, in consultation with our sales department. For extension of larger credit limits, approvals have to be sought from our credit committee which is made up of members

from our finance department, sales department and the CFO. Our finance department and sales department review our outstanding debtor balances on a monthly basis and follow up with customers when payments are due. We believe that there would not material impact risk to our operations in our credit and liquidity risk from sales and customers and other relevant market risks.

**Item 12. Description of Securities Other than Equity Securities**

Not applicable.

**PART II**

**Item 13. Default, Dividend Arrearages and Delinquencies**

None.

**Item 14. Material Modifications to the Rights of Security Holders and Use of Proceeds**

Not applicable.

**Item 15. Controls and Procedures**

(a) Disclosure Controls and Procedures.

Under the supervision and with the participation of our management, including the principal executive officer and the principal accounting officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as of the end of the period covered by this report (the "Evaluation Date"). Based on this evaluation, our principal executive officer and principal accounting officer concluded as of the Evaluation Date that our disclosure controls and procedures were effective such that the material information required to be included in our Securities and Exchange Commission ("SEC") reports is accumulated and communicated to management (including such officers) as appropriate to allow timely decisions regarding required disclosure and recorded, processed, summarized and reported within the

time periods specified in SEC rules and forms relating to us, including our consolidated subsidiaries. Additionally, there were no changes in our internal control over financial reporting that during the period covered by this Annual Report on Form 20-F has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

(b) Management's annual report on internal control over financial reporting.

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f) and 15d-15(f). Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting. In making its assessment of the effectiveness of the Company's internal control over financial reporting, management used the criteria issued by the Committee of Sponsoring Organizations of the Treadway Commission in Internal Control-Integrated Framework. Based on our evaluation, our principal executive officer and principal financial officer have concluded as of the Evaluation Date, our internal controls over financial reporting were ineffective as of December 31, 2013 due to the material weakness described below.

The Public Company Accounting Oversight Board defines a material weakness as a deficiency, or combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control over financial reporting that is less severe than a material weakness, yet important enough to merit attention by those responsible for oversight of our financial reporting. A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A deficiency in design exists when:

- a control necessary to meet the control objective is missing; or
- an existing control is not properly designed such that, even if the control operates as designed, the control objective is not always met.

A deficiency in operation exists when a properly designed control does not operate as designed, or when the person performing the control does not possess the necessary authority or qualifications to perform the control effectively.

The material weaknesses identified result from inadequate technical accounting staff with knowledge of and experience with US generally accepted accounting principles, pursuant to which we prepare our consolidated financial statements, to support stand-alone external financial reporting under public company or SEC requirements.

We are in the process of developing and implementing a remediation plan to address the deficiencies in the areas of personnel with knowledge of and experience with US generally accepted accounting principles. However, additional measures may be necessary, and the measures we expect to take to improve our internal controls may not be sufficient

to address the issues identified, to ensure that our internal controls are effective or to ensure that such material weakness or other material weaknesses would not result in a material misstatement of our annual or interim financial statements. In addition, other material weaknesses or significant deficiencies may be identified in the future. If we are unable to correct deficiencies in internal controls in a timely manner, our ability to record, process, summarize and report financial information accurately and within the time periods specified in the rules and forms of the SEC will be adversely affected. This failure could negatively affect the market price and trading liquidity of our common stock, cause investors to lose confidence in our reported financial information, subject us to civil and criminal investigations and penalties, and generally materially and adversely impact our business and financial condition.

All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can only provide reasonable assurances with respect to financial statement preparation and presentation. In addition, any evaluation of effectiveness for future periods is subject to the risk that controls may become inadequate because of changes in conditions in the future.

The Company's independent auditor, Kabani & Company, Inc., has audited the consolidated financial statements of the Company for the fiscal year ended December 31, 2013.

(c) Attestation report of the registered public accounting firm.

This Annual Report on Form 20-F does not include an attestation report of the Company's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's registered public accounting firm pursuant to the rules of the Securities and Exchange Commission that permit the company to provide only management's report in this Annual Report.

(d) Changes in internal control over financial reporting.

There were no changes in our internal control over financial reporting (as defined in Rule 13a-15(f) of the Exchange Act) that occurred during the year ended December 31, 2013 that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting. It should be noted that while our management believes that our disclosure controls and procedures provide a reasonable level of assurance; our management does not expect that our disclosure controls and procedures or internal financial controls will prevent all errors or fraud. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

**Item 16 [Reserved]**

**Item 16A. Audit Committee Financial Expert**

Our Board of Directors has nominated Tee Chuang Khoo, Changrong Ji, and Shan Jiang as members of the Audit Committee, all of whom are “independent” under the rules of Nasdaq Marketplace Rule 4200(a)(15). In addition, Tee Chuang Khoo qualifies as an audit committee as the financial expert as defined under the applicable rules of the SEC issued pursuant to Section 407 of the Sarbanes-Oxley Act of 2002.

**Item 16B. Code of Ethics**

The Code of Ethics for the members of our Board of Directors and Officers was approved by our Board of Directors on March 27, 2007.

**Item 16C. Principal Accountant Fees and Services**

**Audit Fees**

The audit fees of Kabani & Company, Inc. (“Kabani”), our independent registered public accounting firm, in connection with review and audit fee for 2013 and 2012 was US\$149,000 and US\$150,000, respectively.

### **Audit-Related Fees**

The audit related fee of Kabani including expenses for responding to SEC comments and out-of-pocket expenses, such as traveling and lodging, for the fiscal years ended December 31, 2013 and 2012 amounted to US\$5,151 and US\$3,017, respectively.

### **All Other Fees**

Not applicable.

### **Policy on Pre-Approval of Audit and Permissible Non-Audit Services of Independent Auditors**

The policy of our directors who perform the functions customarily performed by an audit committee is to pre-approve all audit and permissible non-audit services provided by the independent auditors. These services may include audit services and other services.

### **Audit of Financial Statements**

Kabani is responsible for the annual audit of financial statements for the years beginning 2007.

### **Item 16D. Exemptions from the Listing Standards for Audit Committee**

Not applicable.

### **Item 16E. Purchase of Equity Securities by the Issuer and Affiliated Purchasers**

None.

**Item 16F. Change in Registrant's Certifying Accountant.**

Not applicable.

**Item 16G. Significant Differences in Corporate Governance Practices.**

**NASDAQ Marketplace Rules and Home Country Practices**

Pursuant to NASDAQ Listing Rule 5615(a)(3), as a foreign private issuer the Company may follow home country corporate governance practices in lieu of the requirements of the Rule 5600 series, provided that the Company (i) complies with certain mandatory sections of the Rule 5600 series, (ii) discloses each requirement of Rule 5600 that it does not follow and describes the home country practice followed in lieu of such other requirement and (iii) delivers a letter to NASDAQ from the Company's Cayman Islands counsel certifying that the corporate governance practices that the Company does follow are not prohibited by Cayman Islands law. The Company's independent Cayman Islands counsel has certified to NASDAQ that the Company's corporate governance practices are not prohibited by Cayman Islands law.



**Item 16H. Mine Safety Disclosure**

Not applicable.

**Part III**

**Item 17. Financial Statements**

The Company has elected to provide Financial Statements pursuant to Item 18 (see below).

**Item 18. Financial Statements**

The following documents are filed as Attachment A hereto and are included as part of this Annual report on Form 20-F.

**Audited Consolidated Financial Statements of Fuwei Films (Holdings) Co., Ltd and Subsidiaries**

Report of Independent Registered Public Accounting Firm.

Consolidated Statements of Operations and Comprehensive Income (Loss) for the year ended December 31, 2013, 2012 and 2011.

Consolidated Balance Sheets as of December 31, 2013 and 2012.

Consolidated Statements of Cash Flows for the year ended December 31, 2013, 2012 and 2011.

Consolidated Statements of Equity for the year ended December 31, 2013, 2012 and 2011.

Notes to Consolidated Financial Statements.



**Item 19. Exhibits.**

The following exhibits are filed as part of this Annual Report:

No. Description

- 1.2 Form of Amended Memorandum of Association of Fuwei Films (Holdings) Co., Ltd. (2)
- 1.3 Articles of Association Fuwei Films (Holdings) Co., Ltd. (3)
- 4.1 Form of Underwriting Agreement. (1)
- 4.2 Loan Agreement between Bank of Communications and Fuwei Films (Shandong) Co., Ltd. dated January 15, 2007(3)
- 4.3 Loan Agreement between Bank of Communications and Fuwei Films (Shandong) Co., Ltd. dated January 15, 2007(3)
- 4.4 Asset Purchase Agreement between Fuwei Plastics and Shandong Weifang Auction Firm dated October 9, 2003 (2)
- 4.5 Purchase Agreement between Beijing Baorui and Weifang Jing Cheng Auction Co., Ltd. dated December 17, 2004 (2)
- 4.6 Service Agreement between Fuwei Films (Holdings) Co., Ltd. and Xiaoan He(2)
- 4.7 Employment Agreement between Fuwei Films (Holdings) Co., Ltd. and Xiaoan He (2)
- 4.8 Employment Agreement between Fuwei Films (Holdings) Co., Ltd. and Xiaoming Wang (2)
- 4.9 Employment Agreement between Fuwei Films (Holdings) Co., Ltd. and Xiuyong Zhang (2)
- 4.10 Equipment Contract between Fuwei Films (Holdings) Co., Ltd. and Brückner dated as of June 2005(2)
- 4.11 Credit Letter from Communication Bank of China dated May 8, 2006 (2)
- 4.12 Contract between Fuwei Films (Shandong) Co., Ltd. and Lindauer Dornier GmbH, dated January 20, 2007(4)
- 4.13 Amendment to the Contract of January 20, 2007 between Fuwei Films (Shandong) Co., Ltd. and Lindauer Dornier GmbH, dated February 2, 2007 (4)
- 4.14 Loan Contract between Fuwei Films (Shandong) Co., Ltd. and Bank of Communications, dated July 16, 2008 (4)
- 4.15

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- Loan Contract between Fuwei Films (Shandong) Co., Ltd. and Weifang City Commercial Bank, dated July 18, 2008(4)
- 4.16 Loan Contract between Fuwei Films (Shandong) Co., Ltd. and Weifang City Commercial Bank, dated December 2, 2008 (4)
- 4.17 Loan Contract between Fuwei Films (Shandong) Co., Ltd. and Weifang City Commercial Bank, dated January 13, 2009 (4)
- 4.18 Loan Contract between Fuwei Films (Shandong) Co., Ltd. and Weifang City Commercial Bank, dated January 16, 2009 (4)
- 4.19 Loan Contract between Fuwei Films (Shandong) Co., Ltd. and Bank of Communications, dated June 9, 2009 (5)
- 4.20 Loan Contract between Fuwei Films (Shandong) Co., Ltd. and Bank of Communications, dated June 9, 2009 (5)
- 4.21 Loan Contract between Fuwei Films (Shandong) Co., Ltd. and the Weifang Dongfang State-owned Assets Management Co., Ltd., dated November 20, 2009 (5)
- 4.22 Loan Contract between Fuwei Films (Shandong) Co., Ltd. and Bank of Weifang, dated January 13, 2010 (5)

- 4.23 Loan Contract between Fuwei Films (Shandong) Co., Ltd. and Bank of Communications, dated June 7, 2010 (6)
- 4.24 Loan Contract between Fuwei Films (Shandong) Co., Ltd. and Bank of Communications, dated June 7, 2010 (6)
- 4.25 Loan Contract between Fuwei Films (Shandong) Co., Ltd. and Bank of Communications, dated June 7, 2010 (6)
- 4.26 Contract between Fuwei Films (Shandong) Co., Ltd. and Lindauer Dornier GmbH, dated March 30, 2011(7)
- 4.27 Loan Contract between Fuwei Films (Shandong) Co., Ltd. and Bank of Communications, dated May 25, 2011 (8)
- 4.28 Loan Contract between Fuwei Films (Shandong) Co., Ltd. and Bank of Communications, dated May 25, 2011 (8)
- 4.29 Loan Contract between Fuwei Films (Shandong) Co., Ltd. and Bank of Communications, dated May 25, 2011(8)
- 4.30 Loan Contract between Fuwei Films (Shandong) Co., Ltd. and Bank of Communications, dated May 30, 2011 (8)
- 4.31 Loan Contract between Fuwei Films (Shandong) Co., Ltd. and Bank of Communications, dated April 26, 2011 (8)
- 4.32 Amendment No. 1 to the Contract between Fuwei Films (Shandong) Co., Ltd. and Lindauer Dornier GmbH, dated July 22, 2011 (9)
- 4.33 Entrusted Loan Contract between Fuwei Films (Shandong) Co., Ltd. and Weifang High-Tech Investment Co., Ltd. dated October 28, 2011 (10)
- 4.34 Loan Contract between Fuwei Films (Shandong) Co. Ltd. and Bank of Communications Co., Ltd. dated April 18, 2013. (11)
- 4.35 Loan Contract between Fuwei Films (Shandong) Co. Ltd. and Bank of Communications Co., Ltd. dated April 19, 2013. (11)
- 4.36 Loan Contract between Fuwei Films (Shandong) Co. Ltd. and Bank of Communications Co., Ltd. dated April 25, 2013.(11)
- 4.37 Loan Contract between Fuwei Films (Shandong) Co. Ltd. and Bank of Communications Co., Ltd. dated May 2, 2013. (11)
- 4.38 Loan Contract between Fuwei Films (Shandong) Co. Ltd. and Bank of Communications Co., Ltd. dated April 23, 2013. (11)
- 8.1

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List of the Company's significant subsidiaries, their jurisdiction of incorporation and the names under which they operate business, if different from their name. (3)

- 11.1 Code of Ethics for CEO and Senior Financial Officers. (3)
  - 12.1 Certification of Chief Executive Officer required by Section 302 of the Sarbanes-Oxley Act of 2002. \*
  - 12.2 Certification of Chief Financial Officer required by Section 302 of the Sarbanes-Oxley Act of 2002. \*
  - 13.1 Certification of Chief Executive Officer and Chief Financial Officer required by Section 906 of the Sarbanes-Oxley Act of 2002. \*
  - 101.INS XBRL Instance \*
  - 101.SCH XBRL Taxonomy Extension Schema\*
  - 101.CAL XBRL Taxonomy Extension Calculation\*
  - 101.DEF XBRL Taxonomy Extension Definition\*
  - 101.LAB XBRL Taxonomy Extension Labels\*
  - 101.PRE XBRL Taxonomy Extension Presentation\*
- (1) Filed with the Company's amendment to Registration Statement on Form F-1/A filed with the SEC on December 12, 2006.
  - (2) Filed with the Company's Registration Statement on Form F-1 filed with the SEC on November 24, 2006.
  - (3) Filed with the Company's Annual Report on Form 20-F for the year ended December 31, 2006 filed with the SEC on April 2, 2007.
  - (4) Filed with the Company's Annual Report on Form 20-F for the year December 31, 2008 filed with the SEC on March 30, 2009.

- (5) Filed with the Company's Annual Report on Form 20-F for the year ended December 31, 2009 filed with the SEC on April 21, 2010.
  - (6) Filed with the Company's Quarterly Report on Form 6-k for the quarter ended June 30, 2010 filed with the SEC on August 16, 2010.
  - (7) Filed with the Company's Quarterly Report on Form 6-k for the quarter ended March 31, 2011 filed with the SEC on May 10, 2011.
  - (8) Filed with the Company's Quarterly Report on Form 6-k for the quarter ended June 30, 2011 filed with the SEC on August 10, 2011.
  - (9) Filed with the Amendment No. 2 to the Company's Annual Report on Form 20-F/A for the year ended December 31, 2011 filed with the SEC on September 4, 2012. Certain portions of this Exhibit were omitted based upon a request for confidential treatment and the omitted portions have been separately filed with the Securities and Exchange Commission.
  - (10) Filed with the Company's Annual Report on Form 20-F for the year December 31, 2011 filed with the SEC on April 12, 2012.
  - (11) Filed with the Company's Quarterly Report on Form 6-k for the quarter ended June 30, 2013 filed with the SEC on August 22, 2013.
- \* Filed herewith.

## **SIGNATURES**

The registrant hereby certifies that it meets all of the requirements for filing Form 20-F and has duly caused and authorized the undersigned to sign this Annual Report on its behalf.

### **Fuwei Films (Holdings) Co., Ltd.**

By: /s/ Xiaoan He

Name: Xiaoan He

Title: Chairman, Chief Executive Officer

By: /s/ Xiuyong Zhang

Name: Xiuyong Zhang

Title: Chief Financial Officer

Dated: April 11, 2014



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## Report of Independent Registered Public Accounting Firm

Board of Directors and Stockholders of

Fuwei Films (Holdings) Co., Ltd. and Subsidiaries

We have audited the accompanying consolidated balance sheets of Fuwei Films (Holdings) Co., Ltd. and Subsidiaries (the "Company") as of December 31, 2013 and 2012, and the related consolidated statements of operations and comprehensive income (loss), equity, and cash flows for the years ended December 31, 2013, 2012 and 2011, all expressed in Chinese Yuan (Renminbi or RMB), and US Dollar (USD) expressed only for the year ended December 31, 2013. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Fuwei Films (Holdings) Co., Ltd. and Subsidiaries as of December 31, 2013 and 2012, and the related consolidated statements of operations and comprehensive income (loss), equity, and cash flows for the years ended December 31, 2013, 2012 and 2011 in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. The Company has a working capital deficit of RMB115,587,000 or USD19,094,000 as of December 31, 2013. As more fully described in Note 3(t) to the consolidated financial statements, the Company has incurred a net loss of RMB58,952,000 or USD9,738,000, and the Company may not have sufficient working capital to meet its planned operating activities over the next twelve months. These conditions raise substantial doubt about the Company's ability to continue as a going concern. Management's plans regarding these matters are described in Note 3(t). The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty

/s/ Kabani & Company, Inc.

Certified Public Accountants

Los Angeles, California

April 11, 2014

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**FUWEI FILMS (HOLDINGS) CO., LTD and SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS**

As of December 31, 2013 and 2012

(amounts in thousands, except share and per share data)

|  | Notes | December 31, 2013 |         | December 31,<br>2012 |
|--|-------|-------------------|---------|----------------------|
|  |       | RMB               | US\$    | RMB                  |
| <b>ASSETS</b>                            |       |                   |         |                      |
| Current assets                           |       |                   |         |                      |
| Cash and cash equivalents                |       | 11,578            | 1,913   | 5,006                |
| Restricted cash                          |       | 41,422            | 6,842   | 21,457               |
| Accounts and bills receivable, net       | 4     | 8,373             | 1,383   | 21,587               |
| Inventories                              | 5     | 38,454            | 6,352   | 34,291               |
| Advance to suppliers                     | 9     | 6,977             | 1,153   | 13,543               |
| Prepayments and other receivables        | 6     | 26,107            | 4,313   | 26,174               |
| Deferred tax assets - current            | 20    | 1,702             | 281     | 1,857                |
| Total current assets                     |       | 134,613           | 22,237  | 123,915              |
| Property, plant and equipment, net       |       |                   |         |                      |
| Construction in progress                 | 7     | 524,777           | 86,687  | 233,335              |
| Lease prepayments, net                   | 7     | 632               | 104     | 337,990              |
| Advance to suppliers - long term, net    | 8     | 18,999            | 3,138   | 19,523               |
| Long-term deposit                        | 9     | 2,134             | 353     | 5,299                |
| Other Assets                             | 10    | 16,760            | 2,769   | 16,760               |
| Deferred tax assets - non current        | 11    | 13,244            | 2,188   | 262                  |
|  | 20    | 20,888            | 3,450   | 10,466               |
| Total assets                             |       | 732,047           | 120,926 | 747,550              |
| <b>LIABILITIES AND EQUITY</b>            |       |                   |         |                      |
| Current liabilities                      |       |                   |         |                      |
| Short-term borrowings                    | 12    | 105,000           | 17,345  | 110,000              |
| Accounts payables                        |       | 33,454            | 5,526   | 28,796               |
| Notes payable                            | 13    | 81,990            | 13,544  | 38,299               |
| Advance from customers                   |       | 14,665            | 2,422   | 11,714               |
| Accrued expenses and other payables      | 14    | 6,777             | 1,119   | 6,831                |
| Obligations under capital leases-current | 15    | 8,314             | 1,373   | 6,282                |
| Total current liabilities                |       | 250,200           | 41,329  | 201,922              |
| Obligations under capital leases         | 15    | 8,563             | 1,415   | 13,718               |
| Long-term loan                           | 12    | 10,000            | 1,652   | 10,000               |
| Deferred tax liabilities                 | 20    | 3,736             | 617     | 3,476                |

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|  |         |         |         |
|--|---------|---------|---------|
| Total liabilities  | 272,499 | 45,013  | 229,116 |
| Equity   |         |         |         |
| Shareholders' equity   |         |         |         |
| Registered capital(of US\$0.129752 par value; 20,000,000 shares authorized; 13,062,500 issued and outstanding) | 13,323  | 2,201   | 13,323  |
| Additional paid-in capital   | 311,907 | 51,523  | 311,907 |
| Statutory reserve  | 37,441  | 6,185   | 37,441  |
| Retained earnings  | 96,370  | 15,919  | 155,341 |
| Cumulative translation adjustment  | 1,266   | 210     | 1,222   |
| Total shareholders' equity   | 460,307 | 76,038  | 519,234 |
| Non-controlling interest   | (759 )  | (125 )  | (800 )  |
| Total equity   | 459,548 | 75,913  | 518,434 |
| Total liabilities and equity   | 732,047 | 120,926 | 747,550 |

See accompanying notes to the consolidated financial statements.

**FUWEI FILMS (HOLDINGS) CO., LTD and SUBSIDIARIES****CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)**

For the Years Ended December 31, 2013, 2012 and 2011

(amounts in thousands, except share and per share data)

|  | Notes | The Year Ended December 31, |           |             |             |
|--|-------|-----------------------------|-----------|-------------|-------------|
|  |       | 2013<br>RMB                 | US\$      | 2012<br>RMB | 2011<br>RMB |
| Net sales  | 16    | 304,950                     | 50,374    | 372,866     | 537,645     |
| Cost of sales  | 17,18 | 320,375                     | 52,922    | 375,973     | 452,173     |
| Gross (loss) margin  |       | (15,425 )                   | (2,548 )  | (3,107 )    | 85,472      |
| Operating expenses:  |       |                             |           |             |             |
| Selling expenses   | 17,18 | 16,839                      | 2,782     | 18,212      | 19,930      |
| Administrative expenses  |       | 32,130                      | 5,307     | 32,389      | 34,806      |
| Goodwill impairment  |       | -                           | -         | 10,276      | -           |
| Total operating expenses   |       | 48,969                      | 8,089     | 60,877      | 54,736      |
| Operating (loss) income  |       | (64,394 )                   | (10,637 ) | (63,984 )   | 30,736      |
| Other income (expense):  |       |                             |           |             |             |
| - Interest income  |       | 1,024                       | 169       | 1,022       | 2,612       |
| - Interest expense   | 19    | (10,094 )                   | (1,667 )  | -           | (10,227 )   |
| - Others income (expense), net   |       | 4,505                       | 744       | 798         | 1,872       |
| Total other income (expense)   |       | (4,565 )                    | (754 )    | 1,820       | (5,743 )    |
| (Loss) Income before provision for income taxes                                    |       | (68,959 )                   | (11,391 ) | (62,164 )   | 24,993      |
| Income tax benefit (expense)   | 20    | 10,007                      | 1,653     | 7,727       | (3,955 )    |
| Net (Loss) income  |       | (58,952 )                   | (9,738 )  | (54,437 )   | 21,038      |
| Net income (Loss) attributable to noncontrolling interests                         | 19    | 3                           |           | (10 )       | (43 )       |
| Net (loss) income attributable to the Company                                      |       | (58,971 )                   | (9,741 )  | (54,427 )   | 21,081      |
| Other comprehensive income (loss):   |       |                             |           |             |             |
| - Foreign currency translation adjustments attributable to noncontrolling interest | 22    | 4                           |           | 8           | 39          |
| - Foreign currency translation adjustments attributable to the Company             | 44    | 7                           |           | (8 )        | 44          |

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|  |            |            |            |            |            |            |        |
|--|------------|------------|------------|------------|------------|------------|--------|
| Comprehensive income (loss) attributable to non-controlling interest | 41         | 7          | (2         | )          | (4         | )          |        |
| Comprehensive (loss) income attribute to the Company                 | (58,927    | )          | (9,734     | )          | (54,435    | ) 21,125   |        |
| (Loss) Earnings per share, Basic and diluted                         | 26         | (4.51      | )          | (0.74      | )          | (4.17      | ) 1.61 |
| Weighted average number ordinary shares, Basic and diluted           | 13,062,500 | 13,062,500 | 13,062,500 | 13,062,500 | 13,062,500 | 13,062,500 |        |

See accompanying notes to the consolidated financial statements.

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**FUWEI FILMS (HOLDINGS) CO., LTD and SUBSIDIARIES****CONSOLIDATED STATEMENTS OF EQUITY**

For the Years Ended December 31, 2013, 2012 and 2011

(amounts in thousands, except share data)

|  | Ordinary Shares     |               | Additional<br>paid-in<br>capital | Statutory<br>reserve | Retained<br>earnings | Accumulated<br>other<br>comprehensive<br>income | Total<br>shareholders'<br>equity | Non-controlling<br>interest | Total<br>equity |
|--|---------------------|---------------|----------------------------------|----------------------|----------------------|---|----------------------------------|-----------------------------|-----------------|
|  | Number of<br>shares | Amount<br>RMB |                                  |                      |                      |   |                                  |                             |                 |
| Balance as of<br>December 31,<br>2010            | 13,062,500          | 13,323        | 311,907                          | 35,195               | 190,933              | 1,186   | 552,544                          | (794 )                      | 551,750         |
| Net income<br>(loss)                             | -                   | -             | -                                | -                    | 21,081               | -   | 21,081                           | (43 )                       | 21,038          |
| Transfer to<br>statutory<br>reserve              | -                   | -             | -                                | 2,246                | (2,246 )             | -   | -                                | -                           | -               |
| Foreign<br>currency<br>translation<br>adjustment | -                   | -             | -                                | -                    | -                    | 44  | 44                               | 39                          | 83              |
| Balance as of<br>December 31,<br>2011            | 13,062,500          | 13,323        | 311,907                          | 37,441               | 209,768              | 1,230   | 573,669                          | (798 )                      | 572,871         |
| Net income<br>(loss)                             | -                   | -             | -                                | -                    | (54,427 )            | -   | (54,427 )                        | (10 )                       | (54,437 )       |
| Foreign<br>currency<br>translation<br>adjustment | -                   | -             | -                                | -                    | -                    | (8 )  | (8 )                             | 8                           | -               |
| Balance as of<br>December 31,<br>2012            | 13,062,500          | 13,323        | 311,907                          | 37,441               | 155,341              | 1,222   | 519,234                          | (800 )                      | 518,434         |



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|   |            |        |         |        |           |       |           |        |           |
|---|------------|--------|---------|--------|-----------|-------|-----------|--------|-----------|
| Net income (loss)                       | -          | -      | -       | -      | (58,971 ) | -     | (58,971 ) | 19     | (58,952 ) |
| Foreign currency translation adjustment | -          | -      | -       | -      | -         | 44    | 44        | 22     | 66        |
| Balance as of December 31, 2013         | 13,062,500 | 13,323 | 311,907 | 37,441 | 96,370    | 1,266 | 460,307   | (759 ) | 459,548   |
| Balance as of December 31, 2013 US\$    | 13,062,500 | 2,201  | 51,523  | 6,185  | 15,919    | 210   | 76,038    | (125 ) | 75,913    |

See accompanying notes to the consolidated financial statements.

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**FUWEI FILMS (HOLDINGS) CO., LTD and SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS**

For the Years Ended December 31, 2013, 2012 and 2011

|  | The Years Ended December 31, |          |             |             |
|--|------------------------------|----------|-------------|-------------|
|  | 2013<br>RMB                  | US\$     | 2012<br>RMB | 2011<br>RMB |
| Cash flow from operating activities  |                              |          |             |             |
| Net (loss) income  | (58,952 )                    | (9,738 ) | (54,437 )   | 21,038      |
| Adjustments to reconcile net (loss) income to net cash provided by(used in) operating activities |                              |          |             |             |
| - Loss on disposal of property, plant and equipment  | 33                           | 5        | 10          | -           |
| - Loss on goodwill impairment  | -                            | -        | 10,276      | -           |
| - Depreciation of property, plant and equipment  | 48,161                       | 7,956    | 48,709      | 43,783      |
| - Amortization of intangible assets  | 524                          | 87       | 524         | 454         |
| - Deferred income taxes  | (10,007 )                    | (1,653 ) | (7,727 )    | 165         |
| - Bad debt (recovery) expense  | (1,744 )                     | (288 )   | 1,026       | (354 )      |
| - Inventory provision  | -                            | -        | -           | 3,533       |
| Changes in operating assets and liabilities  |                              |          |             |             |
| - Accounts and bills receivable  | 13,615                       | 2,249    | 31,460      | (26,620 )   |
| - Inventories  | (4,164 )                     | (688 )   | 7,483       | 7,270       |
| - Advance to suppliers   | 7,909                        | 1,306    | (6,351 )    | 2,167       |
| - Prepaid expenses and other current assets  | (398 )                       | (66 )    | 29,192      | (30,180 )   |
| - Accounts payable   | 4,658                        | 769      | 9,579       | 5,021       |
| - Accrued expenses and other payables  | 38                           | 6        | 789         | (7,185 )    |
| - Advance from customers   | 2,952                        | 488      | (162 )      | (25,415 )   |
| - Tax payable  | 465                          | 77       | (23,920 )   | (7,695 )    |
| Net cash provided by (used in) operating activities  | 3,090                        | 510      | 46,451      | (14,018 )   |
| Cash flow from investing activities  |                              |          |             |             |
| Purchases of property, plant and equipment   | (4,416 )                     | (729 )   | (5,285 )    | (35,943 )   |
| Restricted cash related to trade finance   | (19,974 )                    | (3,299 ) | 80,752      | (100,915)   |
| Advanced to suppliers - non current  | 3,165                        | 523      | 57,500      | (273 )      |
| Amount change in construction in progress  | (8,785 )                     | (1,451 ) | (207,432)   | 17,806      |
| Interest capitalization related to CIP   | (2,059 )                     | (340 )   | (11,174 )   | -           |
| Proceeds from sale of property, plant and equipment  | -                            | -        | 250         | -           |
| Net cash used in investing activities  | (32,069 )                    | (5,296 ) | (85,389 )   | (119,325)   |
| Cash flow from financing activities  |                              |          |             |             |
| Principal payments of short-term bank loans  | (110,000)                    | (18,171) | (168,501)   | (142,000)   |
| Proceeds from short-term bank loans  | 105,000                      | 17,345   | 110,000     | 148,501     |
| Payment of capital lease obligation  | (8,123 )                     | (1,342 ) | -           | -           |

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|   |        |       |           |           |
|---|--------|-------|-----------|-----------|
| Change in notes payable   | 43,691 | 7,217 | 38,299    | -         |
| Proceeds from sale-leaseback equipment                                | 5,000  | 826   | 20,000    | -         |
| Net cash (used in) provided by financing activities                   | 35,568 | 5,875 | (202 )    | 6,501     |
| Effect of foreign exchange rate changes                               | (17 )  | 20    | (26 )     | (213 )    |
| Net increase(decrease) in cash and cash equivalent                    | 6,572  | 1,109 | (39,166 ) | (127,055) |
| Cash and cash equivalent  |        |       |           |           |
| At beginning of period/year   | 5,006  | 804   | 44,172    | 171,227   |
| At end of period/year   | 11,578 | 1,913 | 5,006     | 44,172    |
| SUPPLEMENTARY DISCLOSURE:   |        |       |           |           |
| Interest paid   | 12,153 | 2,008 | 11,174    | 10,227    |
| Income tax paid   | -      | -     | -         | 9,654     |
| SUPPLEMENTARY SCHEDULE OF NONCASH INVESTING AND FINANCIAL ACTIVITIES: |        |       |           |           |
| Account payable for plant and equipment:                              | 7,466  | 1,233 | 6,003     | 1,730     |
| Obligations for acquired equipment under capital lease:               | 16,877 | 2,788 | 20,000    | -         |

See accompanying notes to the consolidated financial statements

## **FUWEI FILMS (HOLDINGS) CO., LTD and SUBSIDIARIES**

### **Notes to Consolidated Financial Statements**

(amounts in thousands, except per share data)

#### **(1) Principal Activities and Reorganization**

Fuwei Films (Holdings) Co., Ltd and its subsidiaries (the “Company” or the “Group”) are principally engaged in the production and distribution of BOPET film, a high quality plastic film widely used in packaging, imaging, electronics, electrical and magnetic products in the People’s Republic of China (the “PRC”). The Company is a holding company incorporated in the Cayman Islands, established on August 9, 2004 under the Cayman Islands Companies Law as an exempted company with limited liability. The Company was established for the purpose of acquiring shares in Fuwei (BVI) Co., Ltd (“Fuwei (BVI)”), an intermediate holding company established for the purpose of acquiring all of the ownership interest in Fuwei Films (Shandong) Co., Ltd.

On April 23, 2009, Fuwei Films USA, LLC was set up and co-invested by Fuwei Films (Holdings) Co., Ltd. and Newell Finance Management Co., Ltd. Fuwei Films USA, LLC has a registered capital of US\$10 and total investment amount of US\$100. Fuwei Films (Holdings) Co., Ltd. and Newell Finance Management Co., Ltd. own 60% and 40% of the total shares of Fuwei Films USA, LLC, respectively.

On May 9 and 17, 2011, the Company received two notifications from the Weifang State-Owned Assets Operation Administration Company, a wholly-owned subsidiary of Weifang State-Owned Asset Management and Supervision Committee (the “Administration Company”), regarding the transfer of the Company stock previously controlled by the Company’s major shareholders. As a result of the transfer, and based on information provided by the Administration Company, the Company believes that 65.45% of its outstanding ordinary shares are controlled indirectly by the Administration Company and the sole director of each of the intermediate holding companies, Mr. Zheng Min.

#### **(2) Basis of Presentation**

The Group’s consolidated financial statements are presented in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”).

This basis of accounting differs in certain material respects from that used in the preparation of the books of account of Shandong Fuwei, the Company's principal subsidiary, which are prepared in accordance with the accounting principles and the relevant financial regulations applicable to enterprises limited by shares as established by the Ministry of Finance of the PRC ("PRC GAAP"), the accounting standards used in the country of its domicile. The accompanying consolidated financial statements reflect necessary adjustments not recorded in the books of account of the Company's subsidiaries to present them in conformity with U.S. GAAP.

### **(3) Summary of Significant Accounting Policies and Practices**

#### ***(a) Principles of Consolidation***

The consolidated financial statements include the financial statements of the Company and its three subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

#### ***(b) Foreign Currency Transactions***

The Group's reporting currency is the Chinese Yuan ("Renminbi" or "RMB").

The Company and Fuwei (BVI) operate in Hong Kong as investment holding companies and their financial records are maintained in Hong Kong dollars, being the functional currency of these two entities. Fuwei US company, the wholly owned subsidiaries of the company, their financial records are maintained in US dollars. Assets and liabilities are translated into RMB at the exchange rates at the balance sheet date, equity accounts are translated at historical exchange rates and income, expenses, and cash flow items are translated using the average rate for the period. The translation adjustments are recorded in accumulated other comprehensive income in the statements of equity.

Transactions denominated in currencies other than RMB are translated into RMB at the exchange rates quoted by the People's Bank of China (the "PBOC") prevailing at the dates of transactions. Monetary assets and liabilities denominated in foreign currencies are translated into RMB using the applicable exchange rates quoted by the PBOC at the balance sheet dates. The resulting exchange differences are recorded in the statements of operations.

Commencing from July 21, 2005, the PRC government moved the RMB into a managed floating exchange rate regime based on market supply and demand with reference to a basket of currencies.



For the convenience of the readers, the RMB amounts for the year of 2013 included in the accompanying consolidated financial statements in our annual report has been translated into U.S. dollars at the rate of US\$1.00 = RMB 6.0537, being the noon buy rate for U.S. dollars in effect on December 31, 2013 in the City of New York for cable transfer in RMB per U.S. dollar as certified for custom purposes by the Federal Reserve Bank. No representation is made that the RMB amounts could have been, or could be, converted into U.S. dollar at that rate or at any other certain rate on December 31, 2013, or at any other date.

RMB is not fully convertible into foreign currencies. All foreign exchange transactions involving RMB must take place either through the PBOC or other institutions authorized to buy and sell foreign currency. The exchange rate adopted for the foreign exchange transactions are the rates of exchange quoted by the PBOC which are determined largely by supply and demand.

***(c) Cash and Cash Equivalents and Restricted Cash***

For statements of cash flow purposes, the Company considers all cash on hand and in banks, including accounts in book overdraft positions, certificates of deposit and other highly-liquid investments with maturities of three months or less, when purchased, to be cash and cash equivalents.

As of December 31, 2013 and 2012, there were cash and cash equivalents of RMB11,578 (US\$1,913) and RMB5,006, respectively.

As of December 31, 2013 and 2012, there were restricted cash of RMB41,422 (US\$6,842) and RMB21,457, respectively, as deposit in bank for letters of credit and banker's acceptance bill.

***(d) Trade Accounts Receivable***

Trade accounts receivable are recorded at the invoiced amount after deduction of trade discounts, value added taxes and allowances, if any, and do not bear interest. The allowance for doubtful accounts is the Group's best estimate of the amount of probable credit losses in the Group's existing accounts receivable. The Group determines the allowance based on historical write-off experience, customer specific facts and economic conditions.

The Group reviews its allowance for doubtful accounts monthly. Past due balances over 90 days and over a specified amount are reviewed individually for collectibility. All other balances are reviewed on a pooled basis by aging of such balances. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote.

***(e) Inventories***

Inventories are stated at the lower of cost or market value as of balance sheet date. Inventory valuation and cost-flow is determined using Moving Weighted Average Method basis. The Group estimates excess and slow moving inventory based upon assumptions of future demands and market conditions. If actual market conditions are less favorable than projected by management, additional inventory write-downs may be required. Cost of work in progress and finished goods comprises direct material, direct production cost and an allocated portion of production overheads based on normal operating capacity.

***(f) Property, Plant and Equipment***

Property, plant and equipment are stated at cost less accumulated depreciation.

Depreciation on property, plant and equipment is calculated on the straight-line method (after taking into account their respective estimated residual values) over the estimated useful lives of the assets as follows:

|                            | Years   |
|----------------------------|---------|
| Buildings and improvements | 25 – 30 |
| Plant and equipment        | 10 – 15 |
| Computer equipment         | 5       |
| Furniture and fixtures     | 5       |
| Motor vehicles             | 5       |

Depreciation related to abnormal amounts from idle capacity is charged to cost of goods sold for the period incurred. Total depreciations for the years ended December 31, 2013, 2012 and 2011 were RMB48,161 (US\$7,956), RMB48,709 and RMB43,783 respectively, of which 86.7%, 86.1% and 84.6% was recorded in cost of goods sold and 13.3%, 13.9% and 15.4% was recorded in administrative and selling expenses, respectively.

Construction in progress represented capital expenditure in respect of the BOPET productions line. No depreciation is provided in respect of construction in progress.



F-8

*(g) Leased Assets*

An arrangement, comprising a transaction or a series of transactions, is or contains a lease if the Group determines that the arrangement conveys a right to use a specific asset or assets for an agreed period of time in return for a payment or a series of payments. Such a determination is made based on an evaluation of the substance of the arrangement and is regardless of whether the arrangement takes the legal form of a lease.

Classification of assets leased to the Group. Assets that are held by the Group under leases which transfer to the Group substantially all the risks and rewards of ownership are classified as being held under capital leases. Leases which do not transfer substantially all the risks and rewards of ownership to the Group are classified as operating leases.

Assets acquired under capital leases. Where the Group acquires the use of assets under capital leases, the amounts representing the fair value of the leased asset, or, if lower, the present value of the minimum lease payments, of such assets are included in property, plant and equipment and the corresponding liabilities, net of finance charges, are recorded as obligations under capital leases. Depreciation is provided at rates which write off the cost or valuation of the assets over the term of the relevant lease or, where it is likely the Group will obtain ownership of the asset, the life of the asset. Finance charges implicit in the lease payments are charged to the consolidated income statement over the period of the leases so as to produce an approximately constant periodic rate of charge on the remaining balance of the obligations for each accounting period. Contingent rentals are charged to the consolidated income statement in the accounting period in which they are incurred.

Operating lease charges. Where the Group has the use of assets held under operating leases, payments made under the leases are charged to the consolidated income statement in equal installments over the accounting periods covered by the lease term, except where an alternative basis is more representative of the pattern of benefits to be derived from the leased asset. Lease incentives received are recognized in the consolidated income statement as an integral part of the aggregate net lease payments made. Contingent rentals are charged to the consolidated income statement in the accounting period in which they are incurred.

Sale and leaseback transactions. Gains or losses on equipment sale and leaseback transactions which result in capital leases are deferred and amortized over the terms of the related leases. Gains or losses on equipment sale and leaseback transactions which result in operating leases are recognized immediately if the transactions are established at fair value. Any loss on the sale perceived to be a real economic loss is recognized immediately. However, if a loss is compensated for by future rentals at a below-market price, then the artificial loss is deferred and amortized over the period that the equipment is expected to be used. If the sale price is above fair value, then any gain is deferred and amortized over the useful life of the assets.

***(h) Lease Prepayments***

Lease prepayments represent the costs of land use rights in the PRC. Land use rights are carried at cost and charged to expense on a straight-line basis over the respective periods of rights of 30 years. The current portion of lease prepayments has been included in prepayments and other receivables in the balance sheet.

***(i) Goodwill***

Goodwill represents the excess of purchase price and related costs over the value assigned to the net tangible and identifiable intangible assets of businesses acquired. Goodwill is not amortized but is tested for impairment annually, or when circumstances indicate a possible impairment may exist. Impairment testing is performed at a reporting unit level. An impairment loss generally would be recognized when the carrying amount of the reporting unit exceeds the fair value of the reporting unit, with the fair value of the reporting unit determined using a discounted cash flow (DCF) analysis. A number of significant assumptions and estimates are involved in the application of the DCF analysis to forecast operating cash flows, including the discount rate, the internal rate of return, and projections of realizations and costs to produce. Management considers historical experience and all available information at the time the fair values of its reporting units are estimated. Goodwill was determined to be fully impaired during the year ended December 31, 2012.

***(j) Impairment of Long-lived Assets***

The Company recognizes an impairment loss when circumstances indicate that the carrying value of long-lived assets with finite lives may not be recoverable. Management's policy in determining whether an impairment indicator exists, a triggering event, comprises measurable operating performance criteria at an asset group level as well as qualitative measures. If an analysis is necessitated by the occurrence of a triggering event, the Company uses assumptions, which are predominately identified from the Company's strategic long-range plans, in determining the impairment amount. In the calculation of the fair value of long-lived assets, the Company compares the carrying amount of the asset group with the estimated future cash flows expected to result from the use of the assets. If the carrying amount of the asset group exceeds the estimated expected undiscounted future cash flows, the Company measures the amount of the impairment by comparing the carrying amount of the asset group with their estimated fair value. We estimate the fair value of assets based on market prices (i.e., the amount for which the asset could be bought by or sold to a third party), when available. When market prices are not available, we estimate the fair value of the asset group using discounted expected future cash flows at the Company's weighted-average cost of capital. Management believes its policy is reasonable and is consistently applied. Future expected cash flows are based upon estimates that, if not achieved, may result in significantly different results. No impairment was determined to exist as of December 31, 2013 and 2012.

***(k) Revenue Recognition***

Sales of plastic flexible packaging materials are reported, net of value added taxes (“VAT”), sales returns, trade discounts. The standard terms and conditions under which the Group generally delivers allow a customer the right to return product for refund only if the product does not conform to product specifications; the non-conforming product is initially identified by customer, and the customer notifies the Group about the situation. After receiving the Group’s permission, the non-conforming product may be returned for replacement or refund. The Group recognizes revenue when products are delivered and the customer takes ownership and assumes risk of loss, collection of the relevant receivable is probable, persuasive evidence of an arrangement exists and the sale price is fixed or determinable.

In the PRC, VAT of 17% on invoice amount is collected in respect of the sales of goods on behalf of tax authorities. The VAT collected is not revenue of the Group; instead, the amount is recorded as a liability on the consolidated balance sheet until such VAT is paid to the authorities.

***(l) Research and Development Costs***

Research and development expenditures are expensed as incurred. Research and development costs amounted to RMB10,906(US\$1,802), RMB9,617and RMB10,159 for the year ended December 31, 2013, 2012 and 2011and such costs were recorded in administrative expenses.

***(m) Income Taxes***

Income taxes are accounted for under the asset and liability method. Under guidance contained in FASB ASC 740-10, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. We follow the recognition and disclosure provisions under guidance contained in FASB ASC 740-10-25. Under this guidance, tax positions are evaluated for recognition using a more-likely-than-not threshold, and those tax positions requiring recognition are measured as the largest amount of tax benefit that is greater than fifty percent likely of being realized upon ultimate settlement with a taxing authority that has full knowledge of all relevant information. Our policy is to record interest and penalties relating to uncertain tax positions in income tax expense.

***(n) Earnings (loss) per Share***

Basic earnings (loss) per share is computed by dividing net earnings (loss) by the weighted average number of ordinary shares outstanding during the year. Diluted earnings (loss) per share is calculated by dividing net earnings (loss) by the weighted average number of ordinary and dilutive potential ordinary shares outstanding during the year. Diluted potential ordinary shares consist of shares issuable pursuant to stock option plan.

***(o) Use of Estimates***

The preparation of the consolidated financial statements in accordance with U.S. GAAP requires management of the Group to make a number of estimates and assumptions relating to the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. On an ongoing basis, management reviews its estimates and assumptions including those related to the recoverability of the carrying amount and the estimated useful lives of long-lived assets, valuation allowances for accounts receivable and realizable values for inventories. Changes in facts and circumstances may result in revised estimates.

***(p) Noncontrolling interest***

Non-controlling interest represents the portion of equity that is not attributable to the Company. The net income (loss) attributable to noncontrolling interests are separately presented in the accompanying statements of income and other comprehensive income. Losses attributable to noncontrolling interests in a subsidiary may exceed the interest in the subsidiary's equity. The related noncontrolling interest continues to be attributed its share of losses even if that attribution results in a deficit of the noncontrolling interest balance.

***(q) Segment Reporting***

The Group uses the “management approach” in determining reportable operating segments. The management approach considers the internal organization and reporting used by the Group’s chief operating decision maker for making operating decisions and assessing performance as the source for determining the Group’s reportable segments. Management, including the chief operating decision maker, reviews operating results solely by monthly revenue of BOPET film (but not by sub-product type or geographic area) and operating results of Shandong Fuwei, the operating subsidiary in the PRC. As such, the Group has determined that the Group has a single operating segment.

***(r) Contingencies***

In the normal course of business, the Group is subject to contingencies, including legal proceedings and claims arising out of the business that relate to a wide range of matters, including among others, product liability. The Group recognizes a liability for such contingency if it determines it is probable that a loss has occurred and a reasonable estimate of the loss can be made. The Group may consider many factors in making these assessments including past history and the specifics of each matter. As of December 31, 2013 and 2012, the balance of predicted liability was RMB200 (US\$33) and RMB830, respectively, which was estimated liability related to our defective products and included in accrued expenses and other payables as current liabilities on balance sheets.

***(s) Reclassification***

Certain reclassifications have been made to the fiscal year 2013 and 2012 consolidated financial statements to conform to the fiscal 2013 consolidated financial statement presentation. These reclassifications had no effect on net loss or cash flows as previously reported.

***(t) Going Concern Matters***

The accompanying consolidated financial statements have been prepared in conformity with generally accepted accounting principles which contemplate continuation of the company as a going concern. However, as of December 31, 2013, the Company had a working capital deficiency of RMB115,587 (US\$19,094) and accumulated deficit of RMB58,952 (US\$9,738) from net losses incurred during the year of 2013. Confronted with the fierce competition in the BOPET industry in China, the Company may still witness losses over the next twelve months. The ability of the Company to operate as a going concern depends upon its ability to obtain outside sources of working capital and/or generate positive cash flow from operations. The Company accordingly has developed an outside financing plan to

meet the need of working capital for our operation or debts. At the same time, the Company will continue implementing cost reductions on both manufacturing costs and operating expenses to improve profit margins. The accompanying consolidated financial statements do not include any adjustments relating to the recoverability and classification of asset carrying amounts or the amount and classification of liabilities that might result should the Company be unable to continue as a going concern.

***(u) Recently Issued Accounting Standards***

In July 2013, the Financial Accounting Standards Board, or FASB, issued a new accounting standard which will require the presentation of certain unrecognized tax benefits as reductions to deferred tax assets rather than as liabilities in the consolidated balance sheets when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. The new standard requires adoption on a prospective basis in the first quarter of 2015; however, early adoption is permitted. We do not expect the adoption will have a significant impact on our consolidated financial statements

In February 2013, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2013-02, which requires entities to present information about significant items reclassified out of accumulated other comprehensive income (loss) by component either on the face of the statement where net income is presented or as a separate disclosure in the notes to the financial statements. This ASU is effective for the Company in the first quarter of fiscal 2014. We do not expect the adoption will have a significant impact on our consolidated financial statements

In July 2012, the FASB issued ASU 2012-02, which amends how companies test for impairment of indefinite-lived intangible assets. The new guidance permits a company to assess qualitative factors to determine whether it is more likely than not that the fair value of an indefinite-lived intangible asset is less than its carrying amount as a basis for determining whether it is necessary to perform the annual impairment test. The ASU is effective for the Company in the first quarter of fiscal 2014. We do not expect the adoption will have a significant impact on our consolidated financial statements

Other pronouncements issued by the FASB or other authoritative accounting standards group with future effective dates are either not applicable or not significant to the consolidated financial statements of the Company.

**(4) Accounts and Bills Receivable, net**

Accounts receivable consisted of the following:

|                                       | December 31, 2013 |        | December 31, 2012 |  |
|---------------------------------------|-------------------|--------|-------------------|--|
|                                       | RMB               | US\$   | RMB               |  |
| Accounts receivable                   | 6,868             | 1,134  | 11,943            |  |
| Less: Allowance for doubtful accounts | (795 )            | (131 ) | (1,196 )          |  |
|                                       | 6,073             | 1,003  | 10,747            |  |
| <br>                                  |                   |        |                   |  |
| Bills receivable                      | 2,300             | 380    | 10,840            |  |
|                                       | 8,373             | 1,383  | 21,587            |  |

An analysis of the allowance for doubtful accounts for 2013, 2012 and 2011 is as follows:

|                              | December 31, 2013 |       | December 31, 2012 |  | December 31, 2011 |  |
|------------------------------|-------------------|-------|-------------------|--|-------------------|--|
|                              | RMB               | US\$  | RMB               |  | RMB               |  |
| Balance at beginning of year | 1,196             | 197   | 1,785             |  | 2,140             |  |
| Bad debt (recovery)expense   | (401 )            | (66 ) | (589 )            |  | (355 )            |  |
| Write-offs                   | -                 | -     | -                 |  | -                 |  |
| <br>                         |                   |       |                   |  |                   |  |
| Balance at end of year       | 795               | 131   | 1,196             |  | 1,785             |  |

The Group has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis. Credit evaluations are performed on all customers requiring credit over a certain amount. These receivables are due within 7 to 90 days from the date of billing. Normally, the Group does not obtain collateral from customers.

**(5) Inventories**

Inventories consisted of the following:

|               | December 31, 2013 |       | December 31, 2012 |  |
|---------------|-------------------|-------|-------------------|--|
|               | RMB               | US\$  | RMB               |  |
| Raw materials | 16,322            | 2,696 | 19,081            |  |



|                             |          |          |          |  |
|-----------------------------|----------|----------|----------|--|
| Work-in-progress            | 3,436    | 568      | 3,095    |  |
| Finished goods              | 24,114   | 3,983    | 17,507   |  |
| Consumables and spare parts | 693      | 114      | 719      |  |
| Allowance for obsolescence  | (6,111 ) | (1,009 ) | (6,111 ) |  |
|                             | 38,454   | 6,352    | 34,291   |  |

**(6) Prepayments and Other Receivables**

Prepayments and other receivables consisted of the following:

|                   | December 31, 2013 |       | December 31, 2012 |
|-------------------|-------------------|-------|-------------------|
|                   | RMB               | US\$  | RMB               |
| Prepayments       | 593               | 98    | 627               |
| Other receivables | 25,514            | 4,215 | 25,547            |
|                   | 26,107            | 4,313 | 26,174            |

**(7) Property, Plant and Equipment**

Property, plant and equipment consisted of the following:

|                                | December 31, 2013 |          | December 31, 2012 |
|--------------------------------|-------------------|----------|-------------------|
|                                | RMB               | US\$     | RMB               |
| Buildings                      | 101,027           | 16,688   | 46,280            |
| Plant and equipment            | 735,831           | 121,551  | 453,518           |
| Computer equipment             | 2,367             | 391      | 2,056             |
| Furniture and fixtures         | 12,201            | 2,015    | 9,027             |
| Motor vehicles                 | 2,093             | 346      | 2,094             |
|                                | 853,519           | 140,991  | 512,975           |
| Less: accumulated depreciation | (328,742)         | (54,304) | (279,640)         |
|                                | 524,777           | 86,687   | 233,335           |

All of the Group's buildings are located in the PRC. As of December 31, 2013 and 2012, property, plant and equipment plus land use rights with carrying value totaling RMB262,809 (US\$43,413) and RMB231,501 respectively were pledged to banks as collateral for short-term bank loans and credit limits (see Note 12).

Construction-in-progress represents capital expenditure in respect of the BOPET production line. The interest capitalization was RMB2,059 and RMB11,174 during the years ended December 31, 2013 and 2012, respectively.

**(8) Lease Prepayments**

The balance represents the lease prepayments of land use rights of the Group as follows:

|   | December 31, 2013 |       | December 31, 2012 |
|---|-------------------|-------|-------------------|
|   | RMB               | US\$  | RMB               |
| Non-current portion                                   | 18,999            | 3,138 | 19,523            |
| Current portion - amount charged to expense next year | 454               | 75    | 454               |
|   | 19,453            | 3,213 | 19,977            |

As of December 31, 2013, total prepaid land use rights were pledged to banks as collateral for short-term bank loans and credit limit in bank (see Note 12).

Land use rights amortization for the year ended December 31, 2013, 2012 and 2011 were RMB454 (US\$75), RMB454 and RMB454, respectively.

As of December 31, 2013, prepaid land use rights of the Group included certain parcels of land located in Weifang City, Shandong Province, the PRC, with a net book value of RMB19,453 (US\$3,213). The land use rights for land with area of approximately 43,878 square meters, 5,279 square meters and 25,094 square meters will expire in November 2050, May 2053 and February 2055, respectively.

### **(9) Advance to suppliers**

Historically, we have significant working capital commitments because suppliers of PET resin and additives -based raw materials require us to make prepayments in advance of shipment. Besides, we may make prepayments related to some equipment purchases based on arrangement of contract. Our prepayments to suppliers were recorded either as advances to suppliers, if they are expected to be utilized within 12 months as of balance sheet date, or as long-term prepayments, which was included in the line item “advance to suppliers –long term” in our consolidated balance sheet, if they represented the portion expected to be utilized after 12 months. As of December 12, 2013 and 2012, the current portion of advance to suppliers was RMB6,977 (US\$1,153) and RMB13,543, respectively. The noncurrent portion of advance to suppliers was RMB2,134 (US\$353) and RMB5,299, net of allowance for bad debts of RMB272 (US\$45) and RMB1,616, respectively, as of December 31, 2013 and 2012.

### **(10) Long-term Deposit**

On January 20, 2008, Shandong Fuwei signed a “Letter of Intent of Joyinn Capital Increase and Share Expansion”(“LOI”) with Joyinn Hotel Investment & Management Co., Ltd. (“Joyinn”) and the Shareholder of Joyinn. Joyinn is a legal company of limited liability that registered on May 19, 2006 in Beijing, with registered capital of RMB50,000 (US\$6,236).

According to the LOI, Shandong Fuwei deposited RMB 26,000 (half of the would-be added register capital of RMB52,000), to Joyinn as the prepayment as of June 30, 2008. The prepayment to Joyinn will be regarded as investment payment after all parties enter into the final capital increase and shares expansion agreement during the effective term of this LOI. A share pledging agreement was entered into subsequently on April 9, 2008 between Shandong Fuwei and Shandong Xinmeng Investment Co., Ltd (“Pledger”), which holds 97.6% shares of Joyinn. The Pledger agreed to pledge its 52% interest in Joyinn, as a guarantee to the prepayment on the newly increased register capital made by Shandong Fuwei to Joyinn. Based on the mutual supplementary agreement signed in June 2008, the prepayment was decreased by RMB5,000 and returned to the Company on June 18, 2008.



On June 23, 2009, Shandong Fuwei and the Pledger, the major shareholder of Joyinn, agreed that the Pledger would pledge another 19% of its interest in Joyinn in addition to the previous pledge of 52% interest in Joyinn as a guarantee to the prepayment on the newly increased register capital made by Shandong Fuwei to Joyinn. As a result, the Pledger's percentage of pledged interest in Joyinn increased from 52% to 71%. In the year 2010, the Company impaired the deposit amount by RMB4,240 (US\$681). The impairment was determined based on an independent appraisal study.

On July 14, 2009, Shandong Fuwei and Joyinn signed "Supplementary Agreement of Letter of Intent of Joyinn Capital Increase and Share Expansion" which extends the duration of former agreement to two (2) years that is, Fuwei has the option right to determine to continue or withdraw the investment prior to January 14, 2010, the expiration date of the agreement.

Upon the expiration of the Supplementary Agreement on January 14, 2010, Shandong Fuwei and the Pledger entered into an agreement pursuant to which the Pledger agreed to transfer a 71% interest in Joyinn to Shandong Fuwei. The transaction is subject to the approval of the authority body of both parties.

On March 9, 2012, Shandong Fuwei and the Pledger agreed that prior to the approval of the foregoing share transfer, all the related agreements and share pledge terms and conditions will remain in full force and effect.

The Pledger's percentage of Joyinn was transferred to Weifang State-Owned Assets Operation Administration Company (the "Administration Company") according to the court order. On December 10, 2012, Shandong Fuwei entered into a Share Pledge Agreement with the major shareholder of Joyinn – the Administration Company, in which the Administration Company agreed all the terms and conditions in LOI and its Supplementary Agreement. The Administration Company, as the new Pledger, agreed to increase the pledged interest by 16.8% to 87.8%.

As of December 31, 2013 and 2012 the total amount of the deposit was RMB16,760 (US\$2,769) and RMB16,760, respectively.

#### **(11) Other assets**

Other assets represent loss on sale-leaseback arrangement with International Far Eastern Leasing Co., Ltd. The loss is treated as compensation for the future rentals paid by Shandong Fuwei at a below-market price. The artificial loss should be deferred and amortized in proportion to the amortization of the related leased assets. As of December 31, 2013 and 2012, the total amount of the other assets was RMB13,244 (US\$2,188) and RMB262, respectively.

**(12) Short-term and Long-term Bank Loans**

| Lender   | Interest<br>rate per<br>annum | 12-31-2013 |          | 12-31-2012 |
|--|-------------------------------|------------|----------|------------|
|  |                               | RMB        | US\$     | RMB        |
| <b>SHORT-TERM LOANS</b>                                  |                               |            |          |            |
| Bank of Communications Co., Ltd.                         |                               |            |          |            |
| - May 11, 2012 to May 7, 2013                            | 7.87 %                        | -          | -        | 10,000     |
| - May 8, 2012 to April 5, 2013                           | 7.87 %                        | -          | -        | 30,000     |
| - May 9, 2012 to April 15, 2013                          | 7.87 %                        | -          | -        | 35,000     |
| - May 9, 2012 to April 26, 2013                          | 7.87 %                        | -          | -        | 35,000     |
| - April 18, 2013 to April 2, 2014                        | 7.20 %                        | 20,000     | 3,304    | -          |
| - April 19, 2013 to April 11, 2014                       | 7.20 %                        | 20,000     | 3,304    | -          |
| - April 23, 2013 to April 16, 2014                       | 7.20 %                        | 25,000     | 4,129    | -          |
| - April 25, 2013 to April 18, 2014                       | 7.20 %                        | 20,000     | 3,304    | -          |
| - May 2, 2013 to April 24, 2014                          | 7.20 %                        | 20,000     | 3,304    | -          |
| <b>LONG-TERM LOANS</b>                                   |                               |            |          |            |
| Weifang Dongfang State-owned Assets Management Co., Ltd. |                               |            |          |            |
| - October 19, 2009 to October 18, 2017                   | 6.12 %                        | 10,000     | 1,652    | 10,000     |
|  |                               | 115,000    | 18,997   | 120,000    |
| Less amounts classified as short-term                    |                               | (105,000)  | (17,345) | (110,000 ) |
|  |                               | 10,000     | 1,652    | 10,000     |

## Notes:

The Company has entered into six loan agreements with commercial banks to finance its working capital, R&D investment and construction. The weighted average interest rate of short-term bank loans outstanding as of December 31, 2013 and 2012 was 7.42% and 7.66% per annum, respectively.

The principal amounts of the above short-term loans are repayable at the end of the loan period.

The Company paid off four short-term loans totaling RMB110,000 (US\$18,171) to Bank of Communications Co., Ltd. in April 2013 and then obtained five new short-term loans from Bank of Communications Co., Ltd. in April and May 2013 for a total amount of RMB105,000 (US\$17,345), including: (i) RMB20,000 (US\$3,304) on April 18, 2013, maturing on April 2, 2014; (ii) RMB20,000 (US\$3,304) on April 19, 2013, maturing on April 11, 2014; (iii) RMB25,000 (US\$4,129) on April 23, 2013, maturing on April 16, 2014; (iv) RMB20,000 (US\$3,304) on April 25, 2013, maturing on April 18, 2014; and (v) RMB20,000 (US\$3,304) on May 2, 2013, maturing on April 24, 2014. The annual interest rate of these bank loans is 7.20%. As of December 31, 2013 and 2012, the balance of short-term loans was RMB105,000 (US\$17,345) and RMB110,000, respectively.

On November 20, 2009, we signed a long-term loan agreement of RMB10,000 (US\$1,652) with Weifang Dongfang State-owned Assets Management Co., Ltd., with an eight-year loan term, which became effective on October 19, 2009 and will expire on October 18, 2017. From 2015 to 2016, the Company will make principal installment payments of RMB3,350 (US\$553) per year with the remaining principal balance of RMB3,300 (US\$545) due in 2017. The annual interest rate for the loan is the benchmark interest rate for over five-year loans announced by the People's Bank of China reduced by 10% and the applicable annual interest rate for the period ended December 31, 2013 is 6.12%. The loan is guaranteed by Shandong Deqin Investment & Guarantee Co., Ltd. and is used for our projects.

Bank loans outstanding, which are all denominated in Renminbi, are secured and guaranteed as follows:

|  | December 31, 2013 |        | December 31, 2012 | December 31, 2011 |
|--|-------------------|--------|-------------------|-------------------|
|  | RMB               | US\$   | RMB               | RMB               |
| Secured by:                                  |                   |        |                   |                   |
| Property plant and equipment, Land use right | 105,000           | 17,345 | 110,000           | 150,000           |
| Bills receivable                             | -                 | -      | -                 | -                 |
| Guarantee company                            | 10,000            | 1,652  | 10,000            | 10,000            |
| Restricted cash                              | -                 | -      | -                 | 18,501            |
|  | 115,000           | 18,997 | 120,000           | 178,501           |

Long-term bank loans maturity for the next five years after December 31, 2013 are as follows:

|             | RMB   | US\$ |
|-------------|-------|------|
| Fiscal 2014 | -     | -    |
| Fiscal 2015 | 3,350 | 553  |
| Fiscal 2016 | 3,350 | 553  |
| Fiscal 2017 | 3,300 | 546  |
| Fiscal 2018 | -     | -    |

**(13) Notes Payable**

As of December 31, 2013, Shandong Fuwei had banker's acceptances opened with a maturity from three to six months totaling RMB81,990 (US\$13,544) for payment in connection with raw materials on a total deposits of RMB40,998 (US\$6,772) at SPD Bank.

Notes payable consisted of the following:

| Issuing bank | December 31, 2013 |        | December 31, 2012 |
|--------------|-------------------|--------|-------------------|
|              | RMB               | US\$   | RMB               |
| SPD Bank     | 81,990            | 13,544 | 38,299            |
|              | 81,990            | 13,544 | 38,299            |



**(14) Accrued Expenses and Other Payables**

Accrued expenses and other payables consisted of the following:

|                     | December 31, 2013 |       | December 31, 2012 |
|---------------------|-------------------|-------|-------------------|
|                     | RMB               | US\$  | RMB               |
| Other payables      | 6,577             | 1,087 | 6,001             |
| Predicted liability | 200               | 32    | 830               |
|                     | 6,777             | 1,119 | 6,831             |

As of December 31, 2013 and 2012, the balance of predicted liability was RMB200 (US\$32) and RMB830, respectively, which was estimated liability related to our defective products.

**(15) Obligations under capital leases**

The Group has commitments under capital lease agreements as for a part of new third production line and associated equipment. The lease has terms of 3 years expiring by the end of December, 2015. As of December 31, 2013, future payments under these capital leases are as follows:

|   | December 31, 2013                           |         |                              |       | December 31, 2012 |      |   |                              |          |
|---|---|---------|------------------------------|-------|-------------------|------|---|------------------------------|----------|
|   | RMB   | US\$    | RMB                          | US\$  | RMB               | US\$ | RMB   | RMB                          | RMB      |
|   | Present value of the minimum lease payments |         | Total minimum lease payments |       | Interest          |      | Present value of the minimum lease payments | Total minimum lease payments | Interest |
| Within 1 year   | 8,314                                       | 1,373   | 9,166                        | 1,514 | 852               | 141  | 6,282                                       | 7,287                        | 1,005    |
| After 1 year but within 2 years                                     | 8,259                                       | 1,364   | 8,555                        | 1,413 | 296               | 49   | 6,637                                       | 7,333                        | 696      |
| After 2 years but within 3 years                                    | 304   | 51      | 306                          | 51    | 2                 | -    | 7,081                                       | 7,332                        | 251      |
| After 3 years   | -   | -       | -                            | -     | -                 | -    | -   | -                            | -        |
|   | 16,877                                      | 2,788   | 18,027                       | 2,978 | 1,150             | 190  | 20,000                                      | 21,952                       | 1,952    |
| Less: balance due within one year classified as current liabilities | (8,314)                                     | (1,373) |                              |       |                   |      | (6,282)                                     |                              |          |

|       |       |        |
|-------|-------|--------|
| 8,563 | 1,415 | 13,718 |
|-------|-------|--------|

Details of obligations under capital leases are as follows:

|  | December 31, 2013<br>RMB | December 31, 2012<br>RMB |
|--|--------------------------|--------------------------|
| RMB denominated obligations                                    |                          |                          |
| Fixed interest rate of 6.49% per annum as of December 31, 2013 | 16,877                   | 20,000                   |
|  | 16,877                   | 20,000                   |

Guarantee deposit of RMB800 (US\$132) over the capital leased assets concerned and relevant insurance policies were provided to the lessors as collateral and security. In addition, as is customary in the case of capital leases, the Group's obligations are secured by four related parties (see Notes 21).

#### **(16) Revenues**

The Company's revenue is primarily derived from the manufacture and sale of plastic flexible packaging materials.

During the fiscal year ended December 31, 2013, net revenues were RMB304,950 (US\$50,374), compared to RMB372,866 during the same period in 2012, representing a decrease of RMB67,916 or 18.2%, mainly due to the reduction of average sales price by 4.9% and total sales volumes by 14.0%. For further analysis of the factors causing revenue decrease, the reduction of average sales price caused a decrease of RMB15,660 and sales volume factor made a decrease of RMB52,256.

The following table shows the distribution of the Company's revenue by the geographical location of customers, whereas all the Company's assets are located in the PRC:

|   | December 31, 2013 |        | December 31,<br>2012 | December 31,<br>2011 |
|---|-------------------|--------|----------------------|----------------------|
|   | RMB               | US\$   | RMB                  | RMB                  |
| Sales in China  | 263,076           | 43,457 | 302,290              | 392,195              |
| Sales in other countries (principally Europe, Asia and North America) | 41,874            | 6,917  | 70,576               | 145,450              |
|   | 304,950           | 50,374 | 372,866              | 537,645              |

Overseas sales were RMB41,874 (US\$6,917) or 13.7% of total revenues, compared with RMB70,576 or 18.9% of total revenues in 2012. The decrease in overseas sales was mainly due to enhanced competition as well as anti-dumping measures taken by the USA and South Korea, which led to decrease in orders from the overseas market compared to the same period of 2012.

The Company's revenue by significant types of films for 2013, 2012 and 2011 was as follows:

|                                  | December 31, 2013 |        |            | December<br>31, 2012 |            | December<br>31, 2011 |            |   |
|----------------------------------|-------------------|--------|------------|----------------------|------------|----------------------|------------|---|
|                                  | RMB               | US\$   | % of Total | RMB                  | % of Total | RMB                  | % of Total |   |
| Stamping and transfer film       | 142,309           | 23,508 | 46.7 %     | 202,029              | 54.2 %     | 293,768              | 54.6 %     | % |
| Printing film                    | 27,852            | 4,601  | 9.1 %      | 42,449               | 11.4 %     | 55,218               | 10.3 %     | % |
| Metallized film                  | 17,686            | 2,922  | 5.8 %      | 18,886               | 5.1 %      | 28,205               | 5.3 %      | % |
| Specialty film                   | 89,382            | 14,764 | 29.3 %     | 92,536               | 24.8 %     | 140,491              | 26.1 %     | % |
| Base film for other applications | 27,721            | 4,579  | 9.1 %      | 16,966               | 4.5 %      | 19,963               | 3.7 %      | % |
|                                  | 304,950           | 50,374 | 100.0 %    | 372,866              | 100.0 %    | 537,645              | 100.0 %    | % |

In 2013, sales of specialty films were RMB89,382 (US\$14,764) and 29.3% of our total revenues as compared to RMB92,536 and 24.8% in 2012, which was a decrease of RMB3,154, or 3.4%, as compared to the same period in 2012. The decrease was largely attributable to the decrease in sales prices for films in electronics and high-end packaging.

#### (17) Depreciation and Amortization

Depreciation of property, plant and equipment and amortization of intangible asset is included in the following captions:

|                         | December 31, 2013 |       | December 31, 2012 | December 31, 2011 |
|-------------------------|-------------------|-------|-------------------|-------------------|
|                         | RMB               | US\$  | RMB               | RMB               |
| Cost of goods sold      | 41,771            | 6,900 | 41,918            | 36,988            |
| Selling expenses        | 33                | 5     | 59                | 53                |
| Administrative expenses | 6,357             | 1,051 | 6,732             | 6,742             |
|                         | 48,161            | 7,956 | 48,709            | 43,783            |

### (18) Freight Costs

The Group records freight costs related to the transporting of the raw materials to the Group's warehouse in cost of raw materials and all other outbound freight costs in selling expenses. For the year ended December 31, 2013, 2012 and 2011, freight costs included in cost of goods sold were RMB3,738 (US\$617), RMB2,527 and RMB2,147, respectively, and RMB11,770 (US\$1,944), RMB10,534 and RMB9,771, respectively, were included in selling expenses.

**(19) Interest Expense**

The Group capitalizes interest expense as a component of the cost of construction in progress. The following is a summary of interest cost incurred during the year ended December 31, 2013, 2012 and 2011:

|                                  | December 31, 2013 |       | December 31, 2012 | December 31, 2011 |
|----------------------------------|-------------------|-------|-------------------|-------------------|
|                                  | RMB               | US\$  | RMB               | RMB               |
| Interest cost capitalized        | 2,059             | 341   | 11,174            | -                 |
| Interest cost charged to expense | 10,094            | 1,667 | -                 | 10,227            |
|                                  | 12,153            | 2,008 | 11,174            | 10,227            |

**(20) Income Taxes**

## Cayman Islands Tax

Under the current Cayman Island laws, the Company is not subject to tax on income or capital gain. In addition, upon payments of dividends by the Company to its shareholders, no Cayman Islands withholding tax is imposed.

## PRC Tax

Shandong Fuwei, being a Hi-Tech Enterprise in the Weifang Hi-Tech Industrial Zone in Shandong, the PRC, has been granted preferential tax treatments by the Tax Bureau of the PRC. According to the PRC Income Tax Law and various approval documents issued by the Tax Bureau, Shandong Fuwei's profit was taxed at a rate of 15%.

If our subsidiary Shandong Fuwei was not entitled to a reduced enterprise income tax, or EIT, rate of 15% for the year ended December 31, 2013, 2012 and 2011, it would have had an EIT rate of 25%, net income and basic and diluted earnings per share would be reduced by the following amounts:

|            | 2013 | 2012 | 2011    |
|------------|------|------|---------|
|            | RMB  | US\$ | RMB     |
| Net income | -    | -    | (2,499) |

|                    |   |   |   |         |
|--------------------|---|---|---|---------|
| Earnings per share |   |   |   |         |
| - Basic            | - | - | - | (0.19 ) |
| - Diluted          | - | - | - | (0.19 ) |

The Group had minimal operations in jurisdictions other than the PRC. Net (loss) income before income taxes consists of:

|                        | 2013     |          | 2012     |          | 2011     |
|------------------------|----------|----------|----------|----------|----------|
|                        | RMB      | US\$     | RMB      | RMB      | RMB      |
| Cayman Islands         | (2,144 ) | (354 )   | (2,482 ) | (2,183 ) | (2,183 ) |
| British Virgin Islands | (3 )     | (1 )     | (3 )     | (2 )     | (2 )     |
| PRC                    | (66,860) | (11,045) | (59,655) | 27,285   | 27,285   |
| U.S.A                  | 48       | 8        | (25 )    | (107 )   | (107 )   |
|                        | (68,959) | (11,391) | (62,164) | 24,993   | 24,993   |

The Company has no material unrecognized tax benefit which would favorably affect the income taxes in future periods and does not believe there will be any significant increases or decreases within the next twelve months. As of December 31, 2013, we do not have any accrued liability for uncertain tax positions.

Shandong Fuwei was designated as a High-and-New Tech Enterprise in December 2008 and retained its status as a high-tech enterprise for three years commencing from 2011 enjoying a favorable corporate tax rate during the term from January 1, 2011 to December 31, 2013 pursuant to the Enterprise Income Tax Law. Accordingly, the deferred taxes as of December 31, 2013 have been calculated employing the statutory rate of Shandong Fuwei of 15%.

Income tax benefit (expense) consists of:

|                                    | Current  | Deferred | Total    |
|------------------------------------|----------|----------|----------|
|                                    | RMB      | RMB      | RMB      |
| PRC Income tax                     |          |          |          |
| Year ended December 31, 2011       | (3,790 ) | (165 )   | (3,955 ) |
| Year ended December 31, 2012       | -        | 7,727    | 7,727    |
| Year ended December 31, 2013       | -        | 10,007   | 10,007   |
| Year ended December 31, 2013(US\$) | -        | 1,653    | 1,653    |

Income tax expenses reported in the consolidated statements of income differs from the income tax expense amount computed by applying the PRC income tax rate of 15% (the statutory tax rate of the Company's principal subsidiary) for the year ended December 31, 2013, 2012 and 2011 for the following reasons:

|   | 2013     |          | 2012     |          | 2011 |
|---|----------|----------|----------|----------|------|
|   | RMB      | US\$     | RMB      | RMB      | RMB  |
| Income (loss)before income taxes                      | (68,959) | (11,391) | (62,164) | 24,993   |      |
| Computed "expected" tax expense                       | (218 )   | (36 )    | -        | (6,604 ) |      |
| Non-deductible expenses                               | -        | -        | -        | (767 )   |      |
| Non-taxable income                                    | 131      | 22       | -        | 940      |      |
| Tax holiday   | 87       | 14       | -        | 2,641    |      |
| Tax effect of deferred tax and tax rates differential | 10,007   | 1,653    | 7,727    | (165 )   |      |
| Actual income tax benefit (expense)                   | 10,007   | 1,653    | 7,727    | (3,955 ) |      |

Tax effects of temporary differences that give rise to significant portions of the deferred tax assets (liabilities) as of December 31, 2013 and 2012 are presented below.

|   | December 31, 2013 |        | December 31, 2012 |   |
|---|-------------------|--------|-------------------|---|
|   | RMB               | US\$   | RMB               |   |
| Current   |                   |        |                   |   |
| Accounts receivable   | 119               | 20     | 179               |   |
| Other receivables   | 636               | 105    | 636               |   |
| Inventory impairment  | 917               | 151    | 917               |   |
| Estimated Loss due to Product Warranty  | 30                | 5      | 125               |   |
|   | 1,702             | 281    | 1,857             |   |
| Non-current   |                   |        |                   |   |
| Property, plant and equipment, principally due to differences in depreciation | 1,340             | 221    | 1,481             |   |
| Construction in progress, principally due to capitalized interest             | (3,363 )          | (555 ) | (3,093 )          | ) |
| Lease prepayments, principally due to differences in charges                  | (373 )            | (62 )  | (383 )            | ) |
| Allowance for advanced to supplier-long term                                  | 41                | 7      | 242               |   |
| Net loss carryforward   | 19,507            | 3,222  | 8,743             |   |
|   | 17,152            | 2,833  | 6,990             |   |
| Net deferred income tax assets  | 18,854            | 3,114  | 8,847             |   |

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. Considering the level of historical performance of Shandong Fuwei, management believes the deferred tax assets are realizable.

**(21) Related Party Transactions**

| Name of party   | Relationship  |
|---|---|
| Shandong Baorui Investment Co., Ltd<br>("Shandong Baorui")  | Former shareholder (10%) of Shandong Fuwei. Shandong Baorui is 22.1% owned by the Group Founders. |
| Shenghong Group Co., Ltd ("Shenghong Group")                | Former shareholder (90%) of Shandong Fuwei.   |
| Shandong Neo-Luck Plastic Co., Ltd<br>("Shandong Neo-Luck") | The Group Founders' former employer previously engaged in the business of BOPET film production.  |

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|  |   |
|--|---|
| Weifang Neo-Luck (Group) Co., Ltd<br>("Weifang Neo-Luck Group")                                  | Major shareholder (59%) of Shandong Neo-Luck. One of the directors of the Company was the general manager of Weifang Neo-Luck Group prior to joining the Company in April 2005. |
| Weifang State-Owned Assets Operation<br>Administration Company (the<br>"Administration Company") | Shareholder of the Company 65.45%   |
| Everise Investment Management Co., Ltd.  | Owned by the Management of the Company  |
| Beijing Shiweitong Technology Development<br>Co., Ltd.   | Subsidiary of Weifang State-Owned Assets Operation<br>Administration Company  |
| Joyinn Hotel Investment & Management Co., Ltd.   | Subsidiary of Weifang State-Owned Assets Operation<br>Administration Company  |

During the years ended 2013, 2012 and 2011, we paid approximately RMB164 (USD\$27), RMB153 and RMB120, respectively, to Fuhua Industrial Material Management Co., Ltd. as rental payments in connection with living quarters for our staff.

As of December 31, 2013, the balance due from Joyinn Hotel Investment & Management Co., Ltd. was RMB16,760 (US\$2,769) net of impairment of RMB4,240 (US\$700). The background of the long term deposit is disclosed in Note 10.

Obligations under sale-leaseback transaction amounting to RMB16,877 (US\$2,788) were guaranteed by Weifang State-Owned Assets Operation Administration Company, Beijing Shiweitong Technology Development Co., Ltd., Fuwei Films (Holdings) Co., Ltd., and Fuwei Films (BVI) Co., Ltd., respectively.

## **(22) Pension Plan**

Pursuant to the relevant PRC regulations, the Group is required to make contributions at a rate of 20% of employees' salaries and wages to a defined contribution retirement scheme organized by the local Social Bureau in respect of the retirement benefits for the Group's employees in the PRC. The total amount of contributions of RMB1,047 (US\$173), RMB949 and RMB1,003 for the year ended December 31, 2013, 2012 and 2011 respectively, was charged to administrative expenses in the accompanying consolidated statements of income. The Group has no other obligation to make payments in respect of retirement benefits of the employees.

### **(23) Fair Value of Financial Instruments**

Our accounting for Fair Value Measurement and Disclosures, defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. This topic also establishes a fair value hierarchy which requires classification based on observable and unobservable inputs when measuring fair value. The fair value hierarchy distinguishes between assumptions based on market data (observable inputs) and an entity's own assumptions (unobservable inputs). The hierarchy consists of three levels:

Level one — Quoted market prices in active markets for identical assets or liabilities;

Level two — Inputs other than level one inputs that are either directly or indirectly observable; and

Level three — Unobservable inputs developed using estimates and assumptions, which are developed by the reporting entity and reflect those assumptions that a market participant would use.

Determining which category an asset or liability falls within the hierarchy requires significant judgment. The Company evaluates its hierarchy disclosures each quarter. The measurement basis used in the preparation of the consolidated financial statements is the historical cost basis except that the following assets and liabilities are stated at their fair value, such as derivative financial instruments and available-for-sale equity securities. The Company had no assets and liabilities measured at fair value on December 31, 2013.

The carrying amount of cash and cash equivalents, trade accounts receivable, prepayments and other receivables, amounts due from related parties, amounts due to related parties, and accrued liabilities and other payables, approximate their fair values because of the short maturity of these instruments.

The carrying amount of bank loans approximate the fair value based on the borrowing rates currently available for bank loans with similar terms and maturity.

### **(24) Business and Credit Concentrations**

(a) Almost all of the Group's customers are located in the PRC. There is no individual customer with gross revenue more than 10% of total gross revenue during the year ended December 31, 2013, 2012 and 2011.

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Each amount due from the following customers represented more than 10% of the outstanding accounts receivable on December 31, 2013 and 2012.

|   | Percentage of accounts receivable outstanding (%) |   |
|---|---|---|
|   | December 31, 2013                                 |   |
| Eternal Electronic Material (Guangzhou) Co., Ltd. | 39.0  | % |

|   | Percentage of accounts receivable outstanding (%) |   |
|---|---|---|
|   | December 31, 2012                                 |   |
| Eternal Electronic Material (Guangzhou) Co., Ltd. | 29.5  | % |
| Kurz Production(M)SDN BHD MY                      | 11.7  | % |
| Celplast Metallized Products Limited              | 10.6  | % |
| Leonhard Kurz Stiftung &Co. KG                    | 10.4  | % |

(b) The Group purchased a significant portion of PET resin required for the production of BOPET film from Sinopec Yizheng Chemical Fibre Company Limited (“Sinopec Yizheng”) during the year ended December 31, 2013, 2012 and 2011. The Group believes that there are a limited number of suppliers in the PRC with the ability to consistently supply PET resin that meets the Group’s quality standards and requirements. Currently, the Group has an annual supply agreement with Sinopec Yizheng pursuant to which Sinopec Yizheng has agreed to supply fixed quantities of PET resin to the Group on a monthly basis at the prevailing market prices. The terms of such supply agreement are reviewed annually. Although the Group believes that it maintains a good relationship with its major suppliers, there can be no assurance that Sinopec Yizheng will continue to sell to the Group under normal commercial terms as and when needed.

The following are the vendors that supplied 10% or more of our raw materials for each of the year ended December 31, 2013, 2012 and 2011:

| Supplier                                       | Item                    | Percentage of total purchases (%) |      |      |
|--|-------------------------|-----------------------------------|------|------|
|  |                         | 2013                              | 2012 | 2011 |
| Sinopec Yizheng Chemical Fibre Company Limited | PET resin and Additives | 56.7                              | 36.4 | 43.8 |
| Jiangyin Huaxing Compound Co., Ltd.            | PET resin               | 4.1                               | 16.5 | 11.0 |

The balance of advance to supplier to Sinopec Yizheng and Jiangyin Huaxing was RMB1,928 and RMB23 as of December 31, 2013, respectively.

The balance of advance to supplier to Sinopec Yizheng and Jiangyin Huaxing was RMB6,202 and RMB3,069 as of December 31, 2012, respectively.

The balance of advance to supplier to Sinopec Yizheng and Jiangyin Huaxing was RMB1,860 and RMB2,473 as of December 31, 2011, respectively.

## **(25) Commitments and Contingencies**

### **(a) Operating lease commitments**

Future minimum lease payments under non-cancelable operating leases as of December 31, 2013 are as follows:

|                             | December 31, 2013 |      |
|-----------------------------|-------------------|------|
|                             | RMB               | US\$ |
| Operating lease commitments | 369               | \$61 |

The Company leases warehouses, staff quarters and offices under operating leases. The leases duration is typically for one to three years, with an option to renew. None of the leases includes contingent rentals.

For the year ended December 31, 2013, 2012 and 2011, total rental expenses for non-cancelable operating leases were RMB410 (US\$68), RMB383 and RMB606, respectively.

### **(b) Capital commitments**

Capital commitments for purchase of property, plant and equipment as of December 31, 2013 were RMB12,019 (US\$1,985).

### **(c) Outstanding bills receivable discounted**

As of December 31, 2013, the Company had not retained any recourse obligation in respect of bills receivable discounted with and sold to banks.

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**(d) Legal Proceedings**

Shandong Fuwei is currently a party to five legal proceedings in China. From time to time, we may be subject to legal actions and other claims arising in the ordinary course of business.

On July 9, 2012, a client (the “Plaintiff”) filed a lawsuit against Shandong Fuwei over the execution of the Procurement Contract between them in Beijing Daxing District People’s Court. Shandong Fuwei raised a jurisdictional objection when filing the pleading and Beijing Daxing District People’s Court overruled the objection. Shandong Fuwei filed an appeal against the judgment in the First Intermediate People’s Court of Beijing. The appeal was then dismissed on January 23, 2013 and the lawsuit will be heard by Beijing Daxing District People’s Court with a claim at RMB953 plus its interest. On May 15, 2013, Beijing Daxing District People’s Court heard the case and then adjourned the hearing due to the fact that plaintiff who failed to provide sufficient evidences. On June 25, 2013, the case was heard in Beijing Daxing District again but it was also adjourned due to Plaintiff’s failure to provide sufficient evidence. The case was then scheduled to be heard on August 7, 2013. However on the day prior to reopening, Fuwei was informed by Beijing Daxing District People’s Court that the hearing was adjourned again for the same reason that the Plaintiff failed to provide sufficient evidences. To date, Shandong Fuwei is still waiting for a court reopening notice from the Beijing Daxing District People’s Court.

On October 29, 2012, another client of Shandong Fuwei (the “Plaintiff”) filed a lawsuit against Shandong Fuwei over the execution of the Procurement Contract between them in Zhejiang Haining People’s Court. Shandong Fuwei raised a jurisdictional objection when filing the pleading and Zhejiang Haining People’s Court sustained the objection and decided that the lawsuit be heard by Weifang High-Tech District People’s Court. The Plaintiff filed an appeal against the judgment in Zhejiang Jiaxing People’s Court. The appeal was then dismissed and the plaintiff withdrew its charges against Shandong Fuwei on March 5, 2013. Soon afterwards, on March 20, 2013, the court unfroze an amount of RMB770 of Shandong Fuwei’s savings, which had been frozen during the hearing of the lawsuit. In early May 2013, this client filed a lawsuit against Shandong Fuwei over the product liability in Zhejiang Haining People’s Court. Pursuant to a court order, an amount of RMB770 of Shandong Fuwei’s savings was frozen. Shandong Fuwei then raised a jurisdictional objection which was overruled. Shandong Fuwei filed an appeal against this judgment. The appeal was then dismissed as a final decision. On October 21, 2013, the Plaintiff and Shandong Fuwei reached a settlement to compensate the Plaintiff by RMB160 or products valued at RMB160 from Shandong Fuwei and the case was closed.

On May 31, 2013, a supplier of Shandong Fuwei (the “Plaintiff”) filed a lawsuit against Shandong Fuwei over the execution of the Construction Contract between them in Weifang High-Tech District People’s Court with a claim at RMB870. On July 8, 2013, Weifang High-Tech District People’s Court heard the case and the Plaintiff offered a settlement. Afterwards, the Plaintiff and Shandong Fuwei failed to reach a settlement. On December 18, 2013, Weifang High-Tech District People’s Court issued a civil judgment that Shandong Fuwei should pay the claim at RMB870 to the Plaintiff. On December 28, 2013, Shandong Fuwei filed an appeal against the judgment in the Intermediate People’s Court of Weifang and the case was heard on February 26, 2014. To date, the case is still in the process of hearing.

On June 5, 2013, a supplier (the "Plaintiff") filed a lawsuit against Shandong Fuwei over the execution of the Procurement Contract between them in Zhangjiagang People's Court, claiming that the quality guaranteed deposit of RMB208 set aside from the total contract payable should be refunded by Shandong Fuwei. Shandong Fuwei declined its claim for the reason of quality problem related to the supplied equipment. On March 7, 2014, Zhangjiagang People's Court heard the case and supported the Plaintiff's claim. Shandong Fuwei filed an appeal against the judgment in the Intermediate People's Court of Suzhou. To date, the case is still in the process of hearing.

On January 21, 2014, an Hong Kong citizen (the "Plaintiff") filed a lawsuit against Shandong Fuwei in the Intermediate People's Court of Weifang to claim a refund of US\$500 (approximately RMB4,138) and related interest of RMB2,332. The plaintiff alleged that according to an oral agreement of purchasing intention for stocks of Fuwei Films (Holdings) Co., Ltd. (the "Fuwei Holdings") between the Plaintiff and Shandong Fuwei in June 2005, the Plaintiff transferred US\$500 to Wellplus Investments Limited, a company registered in Hong Kong, for acquiring stocks of Fuwei Holdings. However, the Plaintiff has not received any stocks of Fuwei Holdings till now. Shandong Fuwei believes that there was not any engagement or agreement about stock purchase between Shandong Fuwei and the Plaintiff and did not be aware of the fact of fund transfer between the Plaintiff and Wellplus Investments Limited. The case was heard by the Intermediate People's Court of Weifang on April 3, 2014. To date, the case is still in the process of hearing.



**(26) Earnings (Loss) Per Share**

Basic and diluted earnings per share for the period/year ended December 31, 2013, 2012 and 2011 have been calculated as follows:

|  | 2013       |            | 2012       |            | 2011       |
|--|------------|------------|------------|------------|------------|
|  | RMB        | US\$       | RMB        | RMB        | RMB        |
| Net (loss) income available to ordinary shareholders           | (58,971 )  | (9,741 )   | (54,427 )  |            | 21,081     |
| Weighted average number of ordinary shares outstanding         | 13,062,500 | 13,062,500 | 13,062,500 | 13,062,500 | 13,062,500 |
| Dilutive effect of share options                               | -          | -          | -          | -          | -          |
| Diluted weighted average number of ordinary shares outstanding | 13,062,500 | 13,062,500 | 13,062,500 | 13,062,500 | 13,062,500 |
| Basic and diluted earnings (loss)per share                     | (4.51 )    | (0.74 )    | (4.17 )    |            | 1.61       |

**(27) Fuwei Films (Holdings) Co., Ltd (Parent Company)**

Under PRC regulations, the Company's operating subsidiary, Shandong Fuwei may pay dividends only out of its accumulated profits, if any, determined in accordance with the accounting standards and regulations prevailing in the PRC ("PRC GAAP"). In addition, Shandong Fuwei is required to set aside at least 10% of its accumulated profits each year, if any, to fund the statutory general reserve until the balance of the reserve reaches 50% of its registered capital. The statutory general reserve is not distributable in the form of cash dividends to the Company and can be used to make up cumulative prior year losses, if any, and may be converted into share capital by the issue of new shares to shareholders in proportion to their existing shareholdings, or by increasing the par value of the shares currently held by them, provided that the reserve balance after such issue is not less than 25% of the registered capital. Further, Shandong Fuwei is also required to allocate 5% of the profit after tax, determined in accordance with PRC GAAP, to the statutory public welfare fund which is restricted to be used for capital expenditures for staff welfare facilities owned by the Company. The statutory public welfare fund is not available for distribution to equity owners (except in liquidation) and may not be transferred in the form of loans, advances, or cash dividends. As of December 31, 2013, an aggregate amount of RMB37,441 (US\$6,185) has been appropriated from retained earnings and set aside for statutory general reserve and public welfare fund, by Shandong Fuwei.

As of December 31, 2013, the amount of restricted assets of Shandong Fuwei, which may not be transferred to the Company in the form of loans, advances or cash dividends by the subsidiaries without the consent of a third party, was approximately 48% of the Company's consolidated total assets as discussed above. In addition, the current foreign exchange control policies applicable in the PRC also restrict the transfer of assets or dividends outside the PRC.

The following presents condensed unaudited unconsolidated financial information of the Parent Company only.

**Condensed unaudited Balance Sheet as of December 31, 2013 and 2012**

|   | 2013           |               | 2012           |
|---|----------------|---------------|----------------|
|   | RMB            | US\$          | RMB            |
| Cash and cash equivalents                         | 67             | 11            | 65             |
| Other current assets                              | 262,449        | 43,353        | 271,006        |
| Investments in subsidiaries                       | 367            | 61            | 378            |
| <b>Total assets</b>                               | <b>262,882</b> | <b>43,425</b> | <b>271,450</b> |
| Current liabilities                               | 52,325         | 8,643         | 51,842         |
| Total shareholders' equity                        | 210,558        | 34,782        | 219,608        |
| <b>Total liabilities and shareholders' equity</b> | <b>262,882</b> | <b>43,425</b> | <b>271,450</b> |

**Condensed unaudited Statements of Operations (For the years ended December 31, 2013, 2012 and 2011)**

|  | 2013            |                | 2012            | 2011          |
|--|-----------------|----------------|-----------------|---------------|
|  | RMB             | US\$           | RMB             | RMB           |
| Interest income (expenses)                                   | (9 )            | (1 )           | (13 )           | (18 )         |
| General and administrative expenses                          | (2,135 )        | (353 )         | (2,468 )        | (3,281 )      |
| Other income   | -               | -              | -               | 1,116         |
| Loss before equity in undistributed earnings of subsidiaries | (2,144 )        | (354 )         | (2,482 )        | (2,183 )      |
| Equity in earnings of subsidiaries                           | (56,808)        | (9,384)        | (51,956)        | 22,515        |
| <b>Net income</b>  | <b>(58,952)</b> | <b>(9,738)</b> | <b>(54,437)</b> | <b>20,332</b> |

**Condensed unaudited Statement of Cash Flows (For the year ended December 31, 2013, 2012 and 2011)**

|   | 2013     |         | 2012     |     | 2011     |     |
|---|----------|---------|----------|-----|----------|-----|
|   | RMB      | US\$    | RMB      | RMB | RMB      | RMB |
| Cash flow from operating activities   |          |         |          |     |          |     |
| Net income  | (58,952) | (9,738) | (54,437) |     | 20,332   |     |
| Adjustment to reconcile net income(loss) to net cash from operating activities: |          |         |          |     |          |     |
| - Equity in earnings of subsidiaries  | 56,808   | 9,384   | 51,956   |     | (22,515) |     |
| - Foreign exchange gain   | -        | -       | -        |     | -        |     |
| Changes in operating assets and liabilities:                                    |          |         |          |     |          |     |
| - Other current assets  | -        | -       | -        |     | -        |     |
| - Other current liabilities   | (124 )   | (20 )   | 61       |     | (7,277 ) |     |
| Net cash provided by operating activities                                       | (2,268 ) | (375 )  | (2,420 ) |     | (9,460 ) |     |
| Cash flow from financing activities   |          |         |          |     |          |     |
| Payments to related parties   | 2,272    | 375     | 2,365    |     | 9,493    |     |
| Proceeds from related parties   | -        | -       | -        |     | -        |     |
| Effect of exchange  | (2 )     | -       | (1 )     |     | (4 )     |     |
| Net cash provided by(used in) financing activities                              | 2,270    | 375     | 2,364    |     | 9,489    |     |
| Net increase(decrease) in cash  | 2        | 0       | (56 )    |     | 29       |     |
| Cash:   |          |         |          |     |          |     |
| At beginning of year  | 65       | 11      | 121      |     | 92       |     |
| At end of year  | 67       | 11      | 65       |     | 121      |     |

**(28) Unaudited Quarterly Data**

| Quarter Ended Fiscal year | March 31 |         | June 30  |         | September 30 |          | December 31 |        | Total     |          |
|---------------------------|----------|---------|----------|---------|--------------|----------|-------------|--------|-----------|----------|
|                           | RMB      | US\$    | RMB      | US\$    | RMB          | US\$     | RMB         | US\$   | RMB       | US\$     |
| 2013                      |          |         |          |         |              |          |             |        |           |          |
| Revenue                   | 76,577   | 12,330  | 77,401   | 12,611  | 75,890       | 12,400   | 75,082      | 12,403 | 304,950   | 50,374   |
| Gross profit              | (1,191 ) | (191 )  | (2,307 ) | (376 )  | (9,857 )     | (1,611 ) | (2,070 )    | (342 ) | (15,425 ) | (2,548 ) |
| Net income                | (18,076) | (2,909) | (18,190) | (2,964) | (23,203)     | (3,792)  | 499         | 82     | (58,971)  | (9,741)  |

Basic and diluted earnings (1.38 ) (0.22 ) (1.39 ) (0.23 ) (1.78 ) (0.29 ) 0.04 0.01 (4.51 ) (0.74 ) per share

**(29) Subsequent Event**

On March 25, 2014, a public auction was held by the Company's controlling shareholder, the Weifang State-owned Assets Operation Administration Company which is a wholly-owned subsidiary of Weifang State-owned Asset Management and Supervision Committee, in order to sell over 6,912,503 (or 52.9%) of the Company's outstanding ordinary shares it owned. The public auction resulted in the acceptance of a successful bid from an unrelated party, Shandong SNTON Optical Materials Technology Co., Ltd. (the "Bidder"). The Bidder is expected to receive control over 6,912,503 (or 52.9%) of the Company's outstanding ordinary shares at a price of RMB101,800 (approximately US\$16,573) or approximately US\$2.40 per ordinary share.

The Bidder is an optical BOPET film manufacturer established in August 2011 with registered capital of RMB260,000 (approximately US\$42,328). The parent company of the Bidder is Shandong SNTON Group Co., Ltd., which was founded in January 1987, mainly specializes in metal products, fine chemicals, new materials and real estate development.