If you are in any doubt about this circular or as to the action to be taken，you should consult your stockbroker，bank manager， solicitor，professional accountant or other professional adviser．

If you have sold or transferred all your shares in China Literature Limited，you should at once hand this circular to the purchaser or transferee or to the bank，stockbroker or other agent through whom the sale was effected for transmission to the purchaser or transferee．

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# CHINA LITERATURE LIMITED阅文集团 

（Stock Code：772）

# PROPOSAL FOR <br> RENEWAL OF CONTINUING CONNECTED TRANSACTION AND NOTICE OF EXTRAORDINARY GENERAL MEETING 

Independent Financial Adviser to the Independent Board Committee and the Independent Shareholders



## SOMERLEY CAPITAL LIMITED


#### Abstract

A notice convening the extraordinary general meeting of China Literature Limited to be held at Niccolo Room，Level 25，The Murray， Hong Kong，a Niccolo Hotel， 22 Cotton Tree Drive，Central，Hong Kong at 3：00 p．m．on Wednesday，December 9，2020，is set out on pages 36 to 37 of this circular．A form of proxy for use at the extraordinary general meeting is also enclosed．Such form of proxy is also published on the websites of The Stock Exchange of Hong Kong Limited（www．hkexnews．hk）and the Company （http：／／ir．yuewen．com）．Whether or not you are able to attend the extraordinary general meeting，you are requested to complete the form of proxy in accordance with the instructions printed thereon and return it to the Hong Kong share registrar of the Company， Computershare Hong Kong Investor Services Limited，at 17M Floor，Hopewell Centre， 183 Queen＇s Road East，Wanchai，Hong Kong as soon as possible but in any event not less than 48 hours before the time appointed for the holding of the extraordinary general meeting or any adjournment thereof．Completion and return of the form of proxy will not preclude shareholders from attending and voting in person at the extraordinary general meeting（or any adjournment thereof）if they so wish．


## PRECAUTIONARY MEASURES FOR THE EXTRAORDINARY GENERAL MEETING

In order to prevent the spread of COVID－19 pandemic and to safeguard the health and safety of Shareholders，the Company will implement the following precautionary measures at the EGM：
－compulsory body temperature checks
－compulsory wearing of surgical face masks
－no provision of refreshments and corporate gifts
Any person who does not comply with the precautionary measures may，to the extent permitted under applicable laws，be denied entry into the venue of the EGM．All attendees are requested to wear surgical face masks at all times at the venue of the EGM． Shareholders are reminded to exercise their voting rights at the EGM by appointing the chairman of the EGM as proxy to attend and vote on the relevant resolutions at the EGM instead of attending the EGM in person．
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In view of the ongoing COVID-19 pandemic and recent requirements for prevention and control of its spread, the Company will implement the following precautionary measures at the EGM to protect attending Shareholders, staff and other stakeholders from the risk of infection:
(i) compulsory body temperature checks will be conducted on every attending Shareholder, proxy and other attendees at the entrance of the EGM venue. Any person found to be suffering from a fever or otherwise unwell will be denied entry into the EGM venue or be required to leave the EGM venue;
(ii) all attendees are requested to wear surgical face masks at the EGM venue at all times, and to maintain a safe distance with other attendees; and
(iii) no refreshments and corporate gifts will be provided.

To the extent permitted under applicable laws, the Company reserves the right to deny entry into the EGM venue or require any person to leave the EGM venue in order to ensure the safety of the attendees at the EGM.

In the interest of all stakeholders' health and safety and in response to the recent guidelines on prevention and control of COVID-19 pandemic, Shareholders are reminded that physical attendance in person at the EGM is not necessary for the purpose of exercising voting rights. As an alternative, by completing form of proxy in accordance with the instructions printed thereon, Shareholders may appoint the chairman of the EGM as proxy to attend and vote on the relevant resolutions at the EGM instead of attending the EGM in person.

In this circular, unless the context otherwise requires, the following expressions shall have the following meanings:
$\left.\begin{array}{ll}\text { "2018 Distribution Framework } & \text { an agreement entered into on August 13, 2018, between } \\ \text { Agreement" } & \text { Shanghai Yueting (on behalf of the Group) and Tencent } \\ & \text { Computer (on behalf of the Retained Tencent Group) in }\end{array}\right\}$

## DEFINITIONS

$\left.\begin{array}{ll}\text { "Extraordinary General Meeting" } & \text { the extraordinary general meeting of the Company to be } \\ \text { or "EGM" } \\ & \text { held at Niccolo Room, Level 25, The Murray, Hong } \\ & \text { Kong, a Niccolo Hotel, } 22 \text { Cotton Tree Drive, Central, } \\ & \text { Hong Kong at } 3: 00 \text { p.m. on Wednesday, December 9, } \\ & 2020 \text { or any adjournment thereof and notice of which is }\end{array}\right\}$

## DEFINITIONS

| ＂Listing Rules＂ | the Rules Governing the Listing of Securities on the Stock Exchange，as amended from time to time |
| :---: | :---: |
| ＂PRC＂ | the People＇s Republic of China，but for the purposes of this circular only，excludes Hong Kong，Macau Special Administrative Region and Taiwan |
| ＂Retained Tencent Group＂ | Tencent and its subsidiaries，excluding the Group |
| ＂RMB＂ | Renminbi，the lawful currency of the PRC |
| ＂SFO＂ | Securities and Futures Ordinance，Chapter 571 of the Laws of Hong Kong，as amended from time to time |
| ＂Shanghai Yueting＂ | Yueting Information Technology（Shanghai）Co．，Ltd． （閲霆信息技術（上海）有限公司）（previously known as Shengting Information Technology（Shanghai）Co．，Ltd．）， a company established in the PRC on May 27，2008，and the indirectly wholly－owned subsidiary of the Company |
| ＂Share（s）＂ | ordinary share（s）of nominal value of US\＄0．0001 each in the capital of the Company |
| ＂Shareholder（s）＂ | the holder（s）of the Share（s） |
| ＂Stock Exchange＂ | The Stock Exchange of Hong Kong Limited |
| ＂subsidiary（ies）＂ | has the meaning ascribed to it under the Listing Rules |
| ＂Tencent＂ | Tencent Holdings Limited，one of the controlling shareholders of the Company，a limited liability company organized and existing under the laws of the Cayman Islands and the shares of which are listed on the main board of the Stock Exchange（stock code：700），and the controlling shareholder of the Company |
| ＂Tencent Computer＂ | Shenzhen Tencent Computer Systems Company Limited（深圳市騰訊計算機系統有限公司），a company established in the PRC on November 11， 1998 and a wholly－owned subsidiary of Tencent |
| ＂\％＂ | per cent |

## 阅文集团 ${ }^{\text {T }}$

## CHINA LITERATURE LIMITED <br> 阅文集团 <br> （Incorporated in the Cayman Islands with limited liability）

（Stock Code：772）

Executive Directors：
Mr．Cheng Wu
Mr．Hou Xiaonan

Non－Executive Directors：
Mr．James Gordon Mitchell
Mr．Wu Wenhui
Mr．Cao Huayi
Mr．Cheng Yun Ming Matthew

Independent Non－Executive Directors：
Ms．Yu Chor Woon Carol
Ms．Leung Sau Ting Miranda
Mr．Liu Junmin

Registered office：
The offices of Maples Corporate Services Limited
PO Box 309，Ugland House
Grand Cayman KY1－1104
Cayman Islands

Head office and principal place of business in China：
Block 6，No． 690 Bi Bo Road
Pudong XinQu
Shanghai
People＇s Republic of China

Principal place of business in Hong Kong：
Room 1503－04，ICBC Tower
3 Garden Road
Central
Hong Kong

November 10， 2020

To the Shareholders

Dear Sir or Madam

## PROPOSAL FOR <br> RENEWAL OF CONTINUING CONNECTED TRANSACTION <br> AND <br> NOTICE OF EXTRAORDINARY GENERAL MEETING

## INTRODUCTION

The purpose of this circular is to give you the notice of the Extraordinary General Meeting and the proposal to be put forward at the Extraordinary General Meeting：the renewal of the continuing connected transaction contemplated under the 2021 Distribution Framework Agreement．

## RENEWAL OF CONTINUING CONNECTED TRANSACTION

Reference is made to the announcement of the Company dated August 11, 2020 in respect of the renewal of the 2021 Distribution Framework Agreement. For further details of the 2018 Distribution Framework Agreement, please see the announcement of the Company dated August 13, 2018 and the circular of the Company dated September 28, 2018.

The 2018 Distribution Framework Agreement shall expire on December 31, 2020. As the Group intends to continue carrying out the transactions under the 2018 Distribution Framework Agreement in the ordinary and usual course of business of the Group, Shanghai Yueting (on behalf of Group) and Tencent Computer (on behalf of the Retained Tencent Group) agreed to enter into the 2021 Distribution Framework Agreement for a term of three years commencing from January 1, 2021 to December 31, 2023 (both days inclusive), subject to the Shareholders' approval.

## 2021 Distribution Framework Agreement

Principal terms of the 2021 Distribution Framework Agreement are set out as follows:

| Date | $:$ August 11, 2020 |
| :--- | :--- |
| Parties | $: \quad$ (1) Shanghai Yueting (on behalf of the Group), and |

(2) Tencent Computer (on behalf of the Retained Tencent Group)

Terms : From January 1, 2021 to December 31, 2023

Subject matter : The Group shall license the transmission rights (including but not limited to the information network transmission right, the broadcast right and the projection right) and the derivative rights of the film and television contents (including but not limited to the films, television series, and animations) which are legally owned by it, to the Retained Tencent Group.

For the avoidance of doubt, in the event that the Group cooperates with the Retained Tencent Group in the licensing of the information network transmission right of works (including audio works and comics), such transactions will be conducted and carried out under the IP cooperation framework agreement entered into between Shanghai Yueting (on behalf of the Group) and Tencent Computer (on behalf of the Retained Tencent Group) dated September 27, 2019. For further details of the IP cooperation framework agreement, please refer to the announcement of the Company dated September 27, 2019 and the circular of the Company dated October 23, 2019.


#### Abstract

Fee arrangements : The Retained Tencent Group shall pay licensing fees in one or more of the following manners, depending on the specific project and form of cooperation agreed between the relevant parties:


(1) fixed fee,
(2) revenue/profit sharing, or
(3) a mix of the above fee arrangements.


#### Abstract

Payment and : The scope of the licensing and payment and settlement terms settlement terms under the 2021 Distribution Framework Agreement shall be agreed separately between the relevant parties in implementation agreements, which will be entered into under the 2021 Distribution Framework Agreement.


## Pricing Policy

The licensing fees payable and/or the percentage of the revenue/profit to be shared by the Retained Tencent Group to the Group shall be determined after arm's length negotiation between the parties with reference to the prevailing market price and considering and various related commercial factors, including the nature, popularity, quantity, quality and commercial potential of the films, television series, and animations. The pricing policies are subject to the nature of the film and television contents, the transmission rights of which will be licensed under the 2021 Distribution Framework Agreement.

In respect of the television series and the animations, the Retained Tencent Group shall pay the Group fixed licensing fees, which are determined taking account into: (i) the popularity and commercial potential of the television series or the animations, (ii) the track record of revenue per episode and pricing trend of the Group, and (iii) the prevailing market price of premium series and the animations. Meanwhile, as the demands for the premium content consumption in the PRC increased significantly in the past few years and are expected to increase, the licensing fees of premium series and the animations are expected to grow in line with the market trend.

In respect of the web films, the Retained Tencent Group shall share the revenue/profit with the Group at a sharing rate ranging from $50 \%$ to $70 \%$, which is subject to the market performance of the web films.

As at the Latest Practicable Date, the licensing fees payable by the Retained Tencent Group to the Group have been determined on fixed licensing fee basis or revenue/profit sharing basis. The Group might explore in the future fee arrangements in the forms of the mixture of a fixed licensing fee and revenue/profit sharing in order to capture potential upside. The determination of the percentage of revenue/profit sharing in the future may also take into account the factors including the proposed licensing fees, the existing relationship, the expected commercial value of the film and television contents, among others, and will be determined based on arm's length negotiations.

Before entering into any distribution agreement pursuant to the 2021 Distribution Framework Agreement, we will assess our business needs and compare the licensing fees or the sharing rates proposed by the Tencent Group with the licensing fees or the sharing rates offered by at least two other comparable independent platform operators in the film and television contents distribution industry. If no comparable independent third party is available, the business department is required to explain the reasonableness and necessity of cooperation with related parties and why it is in the interests of the Group as a whole, in terms of the background of the cooperation, cooperation considerations and reasonableness of pricing. The Group will only enter into a distribution agreement with the Retained Tencent Group when the agreement is in the best interests of the Company and the Shareholders as a whole.

## Historical Amounts

The historical amounts of the licensing fees paid by the Retained Tencent Group to the Group under the 2018 Distribution Framework Agreement for the two years ended December 31, 2019 and the six months ended June 30, 2020 are set out as follows:

| For the |  |
| :---: | ---: |
| For the year ended | six months <br> ended |
| December 31, | June 30, |
| $\mathbf{2 0 1 8}$ | $\mathbf{2 0 1 9}$ |
| $\left(R M B^{\prime} 000\right)$ | $\left(R M B^{\prime} 000\right)$ |
|  | (RMB <br>  <br> ( unaudited) |

Aggregate amounts of the licensing fees
paid by the Retained Tencent Group
to the Group

In respect of the year 2018, as the Group completed the acquisition of New Classics Media Holdings Limited ("NCM") which is the principal entity engaged in the transactions under the Distribution Framework Agreement in late October 2018, there were no transactions with the Retained Tencent Group under the 2018 Distribution Framework Agreement in last two months of 2018.

In respect of the year 2019, there was a profound adjustment faced by the media industry in the PRC, leading to the slow broadcast approval process for drama series on television and internet video platforms and a decline in the number of project filings, productions and releases. Therefore, the actual number of television series and films distributed through the Retained Tencent Group was less than expected at the time when the caps were determined.

In respect of the first half of the year 2020, the above adjustment continuously affected the production and licensing of television series and films. Meanwhile, the outbreak of the COVID-19 also negatively impacted the Group's production and release cycle for media projects has been affected significantly, leading to a substantial drop in both the number and fee of licensing transactions between the Group and the Retained Tencent Group.

## Annual Caps and Basis of Determination

The proposed annual caps for the licensing fees payable by the Retained Tencent Group to the Group under the 2021 Distribution Framework Agreement for the three years ending December 31, 2023 are set out as follows:

| For the year ending December 31, |  |  |
| :---: | :---: | ---: |
| $\mathbf{2 0 2 1}$ | $\mathbf{2 0 2 2}$ | $\mathbf{2 0 2 3}$ |
| $\left(R M B^{\prime} 000\right)$ | $\left(R M B^{\prime} 000\right)$ | $\left(R M B^{\prime} 000\right)$ |

Aggregate amounts of licensing fees
payable by the Retained Tencent
Group to the Group $\quad 1,550,000 \quad 2,000,000 \quad 2,400,000$

The above annual caps for the three years ending December 31, 2023 were determined with reference to (i) the historical amounts of the licensing fees paid by the Retained Tencent Group under the 2018 Distribution Framework Agreement for the year ended December 31, 2019, (ii) the expected resumption of the cooperation under the 2021 Distribution Framework Agreement for the year ending December 31, 2021 to the extent comparable to that for the year ended December 31, 2019, (iii) the estimated annual growth of the scale of the films, television series, and animations project pipelines invested by the Group for the three years ending December 31, 2023 as a result of the closer cooperation relationship between the Group and the Retained Tencent Group, (iv) based on the current negotiation with the Retained Tencent Group, (a) the Group and the Retained Tencent Group's intention to cooperate on three to four television series and nine animations for the year ending December 31, 2021, with each television series estimated to generate licensing fee for the Group at approximately RMB250 million to RMB400 million and each animation estimated to generate licensing fee for the Group ranging from RMB20 million to RMB 155.5 million depending on the nature, popularity and commercial potential of the television series and animations, and (b) the estimated annual increase of one to two television series and one to two animations for the two years ending December 31, 2023, (v) the estimated costs of the films, television series, and animations project pipelines invested by the Group, (vi) the limited number of players in the films, television series, and animations distribution industry, and (vii) the anticipated number of active users and estimated revenue in each of the Retained Tencent Group's platforms.

## Reasons and Benefits for Entering into the 2021 Distribution Framework Agreement

Through entering into the 2021 Distribution Framework Agreement, the films, television series and animations produced by the Group could be widely distributed, thereby enhancing the popularity of the Group's contents, and fully unleashing the monetization potential of the Group's intellectual property. It is also expected that the cooperation will be complementary and mutually beneficial as the Group's adaptation works will broaden the user base of the Group and the Retained Tencent Group, thereby enhancing the popularity of the Group's platforms, products and services.

## INTERNAL CONTROL MEASURES

The Group's Business Development Team will seek to solicit cooperation with other Independent Third Parties to the extent commercially practicable, and will compare the commercial terms offered by the Independent Third Parties with those offered by the Retained Tencent Group in respect of all the continuing connected transactions of the Group respectively entered into with the Retained Tencent Group. For instance, the Group will assess its business needs and compare the licensing fees proposed by the Retained Tencent Group with the licensing fees offered by at least two other comparable platform operators in the PRC media industry.

In making the decision as to whether the Group will cooperate with the Retained Tencent Group, the Business Development Team will also consider other commercial factors, such as the potential of the intellectual properties, the prevailing market pricing, the prospects of the intellectual property cooperation, with a view to maximizing the commercial value of the relevant intellectual properties. In respect of the selection of the platform operators, the Group will also consider other factors, including (i) the breadth of user base and traffic of various online video platforms, (ii) the user demographics of different online video platforms, (iii) the existing cooperation with various platforms, and (iv) the rates of licensing fees proposed by the online video platforms. The Business Development Team is required to comply with the pricing policies for the continuing connected transactions with the Retained Tencent Group as set out above, and the internal control team of the Company will regularly monitor the compliance of such pricing policies.

The growth in the aggregate amount of the continuing connected transactions between the Group and the Retained Tencent Group is in line with the revenue growth of the Company. The amount of existing connected transactions as a percentage of the Company's total revenue has remained relatively stable. The Company does not expect the increase in the annual cap to raise further reliance and dependency concerns. Meanwhile, the executive Directors will supervise the implementation of such internal procedures on a regular basis (e.g. holding regular meetings with different departments and inquiries into the transactions undertaken pursuant to the 2021 Distribution Framework Agreement), and the Board will also conduct the regular review of the transactions underlying the 2021 Distribution Framework Agreement.

Furthermore, regardless of the party the Group may cooperate with (whether it is the Retained Tencent Group or any Independent Third Party), the Company has established a standard procedure to examine cooperation and its underlying agreement by taking into account various commercial factors. Before entering into an agreement, legal affairs department and finance department of the Company will conduct feasibility study and separate review of the cooperation and consider the benefits and risks of such cooperation on a case-by-case basis. The Group will only enter into an individual distribution agreement with the Retained Tencent Group if (i) the licensing fees and quality of distribution are no less favorable than those from other independent third-party provider; and (ii) it is in the best interest of the Company and the Shareholders. The Group will solicit more players for pricing comparison should the landscape of the online video distribution industry evolves.

## INFORMATION ON THE PARTIES

The Group is principally engaged in online literature business, and is a pioneer of China's online literature market and operates the leading online literature platforms. Shanghai Yueting is an indirectly wholly-owned subsidiary of the Company which is principally engaged in the business of the development in computer hardware and software, the design and production of computer products, providing technical services and the marketing planning services.

Tencent and its subsidiaries are principally engaged in the provision of Internet value-added services including digital entertainment, FinTech, cloud services and online advertising. Tencent Computer is principally engaged in the provision of Internet value-added services and online advertising in the PRC.

## LISTING RULES IMPLICATIONS

As of the Latest Practicable Date, Tencent is the controlling Shareholder, and Tencent Computer is a wholly-owned subsidiary of Tencent. Accordingly, Tencent Computer is a connected person of the Company and the transactions contemplated under the 2021 Distribution Framework Agreement constitute continuing connected transactions of the Company pursuant to Chapter 14A of the Listing Rules.

As the highest applicable percentage ratio in respect of the proposed revised annual caps for the 2021 Distribution Framework Agreement is more than 5\%, the transactions contemplated thereunder are therefore subject to reporting, announcement, annual review and independent Shareholders' approval under Chapter 14A of the Listing Rules.

# LETTER FROM THE BOARD 

## GENERAL

Your attention is drawn to the letter from the Independent Board Committee set out on pages 15 to 16 of this circular, which contains its recommendation to the Independent Shareholders in relation to the 2021 Distribution Framework Agreement and the transactions contemplated thereunder (including the proposed annual caps for each of the three years ending December 31, 2023). Your attention is also drawn to the letter of advice from the Independent Financial Adviser set out on pages 17 to 29 of this circular, which contains its advice to the Independent Board Committee and the Independent Shareholders in relation to the 2021 Distribution Framework Agreement and the transactions contemplated thereunder (including the proposed annual caps for each of the three years ending December 31, 2023), and the principal factors and reasons taken into account in arriving at its recommendation.

## NOTICE OF EXTRAORDINARY GENERAL MEETING

Set out on pages 36 to 37 of this circular is the notice of the Extraordinary General Meeting at which, inter alia, ordinary resolutions will be proposed to Shareholders to consider and approve the 2021 Distribution Framework Agreement.

## FORM OF PROXY

A form of proxy is enclosed for use at the Extraordinary General Meeting. Such form of proxy is also published on the websites of the Stock Exchange (www.hkexnews.hk) and the Company (http://ir.yuewen.com). Whether or not you intend to attend the Extraordinary General Meeting, you are requested to complete the form of proxy in accordance with the instructions printed thereon and return it to the Hong Kong share registrar of the Company, Computershare Hong Kong Investor Services Limited, at 17M Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong not less than 48 hours before the time fixed for holding the Extraordinary General Meeting or any adjournment thereof. Completion and delivery of the form of proxy shall not preclude a Shareholder from attending and voting in person at the Extraordinary General Meeting if they so wish and in such event the form of proxy shall be deemed to be revoked. In view of the outbreak of COVID-19 pandemic, you are strongly encouraged to appoint the chairman of the Extraordinary General Meeting as proxy to attend and vote on your behalf at the Extraordinary General Meeting.

## VOTING BY POLL

Tencent and its associates, namely THL A13 Limited (directly holding 292,083,460 Shares), Qinghai Lake Investment Limited (directly holding 230,705,634 Shares), and Tencent Mobility Limited (directly holding 78,337,470), are required under the Listing Rules to abstain from voting on the resolutions on approving the 2021 Distribution Framework Agreement at the Extraordinary General Meeting. Please refer to Appendix I to this circular for further details. Save as disclosed above, the Board is not aware of any other Shareholder who has any material interest that is required under the Listing Rules to abstain from voting on the aforementioned resolution.

Pursuant to Rule 13.39(4) of the Listing Rules and article 13.6 of the Articles of Association, any resolution put to the vote of the Shareholders at a general meeting shall be decided on a poll except where the chairman of the Extraordinary General Meeting, in good faith, decides to allow a resolution which relates purely to a procedural or administrative matter to be voted on by a show of hands. Accordingly, each of the resolutions set out in the notice will be taken by way of poll.

On a poll, every Shareholder present in person or by proxy or, in the case of a Shareholder being a corporation, by its duly authorized representative, shall have one vote for every fully paid Share of which he/she is the holder. A Shareholder entitled to more than one vote needs not use all his/her votes or cast all the votes he/she uses in the same way.

## OPINION FROM THE BOARD

The Directors (excluding the independent non-executive Directors whose view have been included in the section headed "Letter from the Independent Board Committee" of this circular) are of the view that the terms of the 2021 Distribution Framework Agreement were determined after arm's length negotiation, and the transactions contemplated thereunder (including the proposed annual caps for the three years ending December 31, 2023) are conducted in the ordinary and usual business of the Company and are on normal commercial terms, fair and reasonable and in the interests of the Company and the Shareholders as a whole.

The independent non-executive Directors have formed the Independent Board Committee for the purposes of advising the independent Shareholders in respect of the 2021 Distribution Framework Agreement and the transactions contemplated thereunder (including the proposed annual caps for the three years ending December 31, 2023) and whose views and recommendation have been included in the section headed "Letter from the Independent Board Committee" of this circular.

Mr. James Gordon Mitchell, Mr. Cheng Yun Ming Matthew, Mr. Cheng Wu and Mr. Hou Xiaonan, are employees of Tencent, and have therefore abstained from voting on the relevant Board resolutions approving the 2021 Distribution Framework Agreement and the transactions contemplated thereunder. Save as disclosed above, none of the other Directors has material interests in the transactions contemplated under the 2021 Distribution Framework Agreement. Save as disclosed above, none of the other Directors have abstained from voting on the relevant resolutions at the Board meeting.

## RECOMMENDATION

The Directors consider that the proposed resolutions for the 2021 Distribution Framework Agreement are in the interests of the Group and the Shareholders as a whole. The Directors therefore recommend the Shareholders to vote in favor of all the resolutions to be proposed at the Extraordinary General Meeting.

The Independent Board Committee, having taken into account the advice of Somerley, consider that the 2021 Distribution Framework Agreement and the transactions contemplated thereunder (including the proposed annual caps for the three years ending December 31, 2023 thereunder) are on normal commercial terms, are fair and reasonable so far as the Independent Shareholders are concerned, in the ordinary and usual course of the business of the Group, and in the interests of the Company and the Shareholders as a whole. Accordingly, the Independent Board Committee recommends the Independent Shareholders to vote in favor of the ordinary resolution in respect of the 2021 Distribution Framework Agreement and the transactions contemplated thereunder (including the proposed annual caps for the three years ending December 31, 2023 thereunder) at the Extraordinary General Meeting.

Yours faithfully<br>By order of the Board<br>CHINA LITERATURE LIMITED<br>Mr. James Gordon Mitchell<br>Chairman of the Board and Non-executive Director

## LETTER FROM THE INDEPENDENT BOARD COMMITTEE

The following is the text of a letter from the Independent Board Committee setting out its recommendation to the Independent Shareholders in relation to the 2021 Distribution Framework Agreement．

# CHINA LITERATURE LIMITED <br> 阅文集团 

（Incorporated in the Cayman Islands with limited liability）
（Stock Code：772）

November 10， 2020

To the Independent Shareholders

Dear Sirs or Madams，

## THE 2021 DISTRIBUTION FRAMEWORK AGREEMENT

We refer to the circular dated November 10， 2020 issued by the Company to the Shareholders（the＂Circular＂），of which this letter forms part．Terms defined in this circular shall have the same meanings herein unless the context otherwise requires．

We have been appointed by the Board as members of the Independent Board Committee to advise the Independent Shareholders as to whether the 2021 Distribution Framework Agreement and the transactions contemplated thereunder are entered into by the Group in its ordinary and usual course of business，on normal commercial terms，in the interests of the Company and the Shareholders as a whole and are fair and reasonable so far as the Independent Shareholders are concerned．Somerley has been appointed as the Independent Financial Adviser to advise the Independent Board Committee and the Independent Shareholders in this regard．

After taking into account the advice of Somerley as set out in this circular，we consider that the 2021 Distribution Framework Agreement and the transactions contemplated thereunder （including the proposed annual caps for the three years ending December 31， 2023 thereunder） are on normal commercial terms and are fair and reasonable so far as the Independent Shareholders are concerned．We further consider that the entering into of the 2021 Distribution Framework Agreement（including the proposed annual caps for the three years ending December 31， 2023 thereunder）is in the ordinary and usual course of the business of the Group，and in the interests of the Company and the Shareholders as a whole．

## LETTER FROM THE INDEPENDENT BOARD COMMITTEE

Accordingly, we recommend the Independent Shareholders to vote in favour of the ordinary resolutions to be proposed at the Extraordinary General Meeting to approve the 2021 Distribution Framework Agreement and the transaction contemplated thereunder (including the proposed annual caps for the three years ending December 31, 2023).

Yours faithfully,
The Independent Board Committee
Ms. YU Chor Woon Carol Ms. LEUNG Sau Ting Miranda Mr. LIU Junmin
Independent non-executive Directors

## LETTER FROM THE INDEPENDENT FINANCIAL ADVISER

The following is the full text of a letter of advice from Somerley to the Independent Board Committee and the Independent Shareholders, which has been prepared for the purpose of inclusion in the Circular.

SOMERLEY CAPITAL LIMITED
20th Floor
China Building
29 Queen's Road Central
Hong Kong

November 10, 2020

## To: the Independent Board Committee and the independent Shareholders

Dear Sirs,

## RENEWAL OF CONTINUING CONNECTED TRANSACTION

## INTRODUCTION

We refer to our appointment to advise the Independent Board Committee and the Independent Shareholders in relation to the 2021 Distribution Framework Agreement and the transactions contemplated thereunder (the "Continuing Connected Transactions") (including the proposed annual caps for the three years ending December 31, 2023 (the "Annual Caps")), details of which are contained in the letter from the Board in the circular issued by the Company to the Shareholders dated November 10, 2020 (the "Circular"), of which this letter forms a part. Unless the context otherwise requires, capitalised terms used in this letter shall have the same meanings as those defined in the Circular.

As at the Latest Practicable Date, Tencent is the controlling shareholder of the Company, and Tencent Computer is a wholly-owned subsidiary of Tencent. Accordingly, Tencent Computer is a connected person of the Company and the transactions contemplated under the 2021 Distribution Framework Agreement constitute continuing connected transactions of the Company pursuant to Chapter 14A of the Listing Rules.

As the highest applicable percentage ratio in respect of the Annual Caps is more than 5\%, the 2021 Distribution Framework Agreement and the transactions contemplated thereunder (including the Annual Caps) are therefore subject to reporting, announcement, annual review, circular (including independent financial advice) and independent Shareholders' approval requirements under Chapter 14A of the Listing Rules.

In view of Tencent's interests in the 2021 Distribution Framework Agreement, Tencent and its associates are required under the Listing Rules to abstain from voting on the resolution to be proposed at the Extraordinary General Meeting to approve the 2021 Distribution Framework Agreement and the transactions contemplated thereunder (including the Annual Caps).

The Independent Board Committee, comprising all the independent non-executive Directors, namely Ms. Yu Chor Woon Carol, Ms. Leung Sau Ting Miranda and Mr. Liu Junmin, has been established to advise the Independent Shareholders in respect of the 2021 Distribution Framework Agreement and the transactions contemplated thereunder (including the Annual Caps) are fair and reasonable so far as the Independent Shareholders are concerned, and in the interests of the Company and the Shareholders as a whole. We, Somerley, have been appointed to advise the Independent Board Committee and the Independent Shareholders in this regard.

During the past two years, we have acted as the independent financial adviser to the independent board committee and the independent shareholders of the Company in relation to certain connected transactions, details of which were set out in the circular of the Company dated April 9, 2019 and October 23, 2019. In addition, we are currently acting as the independent financial adviser to the Company in relation to a proposed major and connected transaction, as detailed in the announcement of the Company dated August 27, 2020. The above engagements were/are limited to providing independent advisory services to the independent board committee and the independent shareholders of the Company pursuant to the Listing Rules. Under the above engagements, we received or will receive normal professional fees from the Company. Notwithstanding the above engagements, as at the Latest Practicable Date, there were no relationships or interests between (a) Somerley, and (b) the Group, the Retained Tencent Group and their respective subsidiaries and associates that could reasonably be regarded as a hindrance to our independence as defined under Rule 13.84 of the Listing Rules to act as the Independent Finance Adviser.

In formulating our opinion and recommendation, we have relied on the information and facts supplied, and the opinions expressed, by the Directors and management of the Group and have assumed that such information, facts and opinions were true, accurate and complete in all material aspects and will remain so up to the time of the Extraordinary General Meeting. We have reviewed, among others, (i) the 2021 Distribution Framework Agreement, (ii) the annual report of the Company for the year ended December 31, 2019, (iii) the interim report of the Company for the six months ended June 30, 2020, and (iv) other information contained in the Circular. We have also sought and received confirmation from the Directors that all material relevant information has been supplied to us and no material facts have been omitted from the information supplied and opinions expressed to us. We have no reason to believe that any material information has been omitted or withheld from us, or to doubt the truth, accuracy or completeness of the information provided. We have relied on such information and consider that the information we have received is sufficient for us to reach an informed view. We have, however, not conducted any independent investigation into the business, affairs and financial position of the Group, the Retained Tencent Group and their respective subsidiaries or associates, nor have we carried out any independent verification of the information supplied.

## LETTER FROM THE INDEPENDENT FINANCIAL ADVISER

## PRINCIPAL FACTORS AND REASONS CONSIDERED

In arriving at our opinion and recommendation with regard to the Continuing Connected Transactions (including the Annual Caps), we have taken into account the following principal factors and reasons:

## 1. Information on the parties

## The Group

The Group is principally engaged in online literature business and is a pioneer of China's online literature market and operates the leading online literature platforms. Shares of the Company have been listed on the Stock Exchange since November 2017 and the Company had a market capitalisation of approximately HK $\$ 65.2$ billion as at the Latest Practicable Date.

In recent years, the Group continued to strengthen its content offering and increase the number of high-quality literary works and writers on its platforms. Further, the Group has been exploring ways to fully realise the potential value of its intellectual property. Against this background, in October 2018, the Group acquired New Classics Media Holdings Limited ("NCM") (which is primarily engaged in television series, web series and film production and distribution in China) in order to, among others, facilitate the adaptation process of the Group's literary contents into other entertainment formats (including television series, films and animations), strengthen its licensing business, and bring in additional revenue streams to the Group.

The Group recorded total revenues of approximately RMB8.3 billion in 2019, representing an increase of approximately $66.0 \%$ from approximately RMB5.0 billion in 2018. Such increase was primarily driven by the increase in revenues from intellectual property operations (mainly comprising licensing and distribution of television series and film), reflecting the Group's increasing participation in the intellectual property adaptation businesses. Total revenues of the Group increased by approximately $9.7 \%$ year-over-year to approximately RMB3.3 billion in the first half of 2020, mainly due to the increase in revenue from its online business as a result of the expansion of the Group's distribution channels and the users' growing willingness to pay for the Group's reading content.

## Tencent

Tencent is a leading player in the internet, social media and entertainment industries in the PRC with an extensive network coverage and a vast user base. It is principally engaged in the provision of Internet value-added services including digital entertainment, FinTech, cloud services and online advertising. According to Tencent's 2019 annual report, the total member subscriptions of Tencent's major video platforms, including Tencent Video, reached 106 million as at December 31, 2019 and Tencent remained the clear industry leader in terms of content, users and financial metrics. As disclosed in Tencent's 2020 interim report, the video content subscriptions increased to approximately 114 million.

## LETTER FROM THE INDEPENDENT FINANCIAL ADVISER

## 2. Background to and reasons for the Continuing Connected Transactions

The Group has been partnering with Tencent to distribute its works through the Retained Tencent Group's portfolio of leading internet products, including Mobile QQ, Weixin Reading and Tencent Video. Such cooperation in the distribution has, since late 2018, been extended to cover not only the literary contents, but also other entertainment forms, including television series, films and animations after the acquisition of NCM.

The existing cooperation between two groups are governed by the 2018 Distribution Framework Agreement as approved by the then independent shareholders of the Company at an extraordinary general meeting held on October 19, 2018. The 2018 Distribution Framework Agreement has a term commencing from October 19, 2018 and expiring on December 31, 2020. In light of the expiry of the 2018 Distribution Framework Agreement, on August 11, 2020, Shanghai Yueting (on behalf of the Group) and Tencent Computer (on behalf of the Retained Tencent Group) entered into the 2021 Distribution Framework Agreement in order to continue the cooperation in the distribution of television series, films and animations in the coming three years.

The Directors stated in its letter that through entering into the 2021 Distribution Framework Agreement, the literary works provided by the Group could be widely distributed through the adaptation into television series, films and animations, thereby enhancing the popularity of the Group's literary contents and fully unleashing the monetization potential of the Group's intellectual property. It is also expected that the cooperation will be complementary and mutually beneficial as the Group's adaptation works will broaden the user base of the Group and the Retained Tencent Group, which in turn enhance the popularity of the Group's platforms, products and services.

## 3. Principal terms of the 2021 Distribution Framework Agreement

The following is a summary of the principal terms of the 2021 Distribution Framework Agreement, and for further details, please refer to the section headed " 2021 Distribution Framework Agreement" in the letter from the Board.

## Subject matter

Pursuant to 2021 Distribution Framework Agreement, the Group shall license the transmission rights (including the information network transmission right, the broadcast right and the projection right) and the derivative rights of the Group's television and film contents (including television series, films and animations) to the Retained Tencent Group, and the Retained Tencent Group shall pay licensing fees to the Group in return.

## LETTER FROM THE INDEPENDENT FINANCIAL ADVISER

The relevant parties shall enter into implementation agreement(s) for each transaction contemplated under the 2021 Distribution Framework Agreement, in order to agree on the scope of licensing and other terms.

## Term

Subject to approval of the Independent Shareholders at the Extraordinary General Meeting, the 2021 Distribution Framework Agreement has a term of three years, from January 1, 2021 to December 31, 2023.

## Fee arrangements

The fee arrangements relating to the 2021 Distribution Framework Agreement shall be depending on the specific project and form of cooperation agreed between the relevant parties and as follows:
(1) fixed fee,
(2) revenue/profit sharing, or
(3) a mix of the above fee arrangements.

## Pricing policies

The licensing fees payable and/or the percentage of the revenue/profit to be shared by the Retained Tencent Group to the Group shall be determined after arm's length negotiation between the parties with reference to the prevailing market price and taking into account various related commercial factors, including the nature, popularity, quantity, quality and commercial potential of television series, films and animations. The pricing policies vary depending on the nature of the television and film contents.

In respect of the television series and the animations, the Retained Tencent Group shall pay the Group fixed licensing fees, which are determined after taking account into: (i) the popularity and commercial potential of the television series or the animations, (ii) the track record of revenue per episode and pricing trend of the Group, and (iii) the prevailing market price of premium series and the animations.

In respect of the web films, the Retained Tencent Group is expected to share the revenue/profit with the Group at a sharing rate ranging from $50 \%$ to $70 \%$, which is subject to the market performance of the web films.

## LETTER FROM THE INDEPENDENT FINANCIAL ADVISER

The Group might explore in the future fee arrangements in the forms of the mixture of a fixed licensing fee and revenue/profit sharing in order to capture potential upside. When determining the percentage of revenue/profit sharing in the future, the parties may also take into account the factors, among others, the proposed licensing fees, the existing relationship, and the expected commercial value of the film and television contents.

Based on our discussion with the management of the Group, the Group will only enter into an individual implementation agreement with the Retained Tencent Group when the licensing fees or the revenue/profit sharing rates offered by the Retained Tencent Group are in line with or higher than the market prices and such agreement is in the best interests of the Company and the Shareholders as a whole. As set out in the letter from the Board, the Group will compare the licensing fees or the revenue/profit sharing rates proposed by the Retained Tencent Group with those offered by at least two other comparable independent platform operators in the film and television contents distribution industry. If no comparable independent third party is available, the business department of the Group is required to explain the reasonableness and necessity of cooperation with the Retained Tencent Group and why it is in the interests of the Group as a whole, in terms of the background of the cooperation, cooperation considerations and reasonableness of pricing. In other words, if the licensing fees or the revenue/profit sharing rates offered by the Retained Tencent Group in the individual distribution agreement are lower than the market price, the Group has the discretion not to enter into such agreement with the Retained Tencent Group to ensure that the arrangement will not be detrimental to the interests of the Group.

## Payment and settlement terms

The relevant parties shall enter into implementation agreements under the 2021 Distribution Framework Agreement to specify the payment and settlement terms.

## Comparison of terms with Independent Third Parties

We have discussed with the management of the Group the pricing policies of the 2018 Distribution Framework Agreement as set out above. We have also reviewed a list of the transactions contemplated under the 2018 Distribution Framework Agreement and the sample contracts (the "Sample Contracts"), which were selected on a random basis from all executed contracts that are effective during the period from October 19, 2018 to June 30, 2020. Management of the Group has confirmed to us that there were no licensing of web films between the Retained Tencent Group and the Group during the period from October 19, 2018 to June 30, 2020, and that they have provided to us an exhaustive list of contracts for the above transactions and time period.

## LETTER FROM THE INDEPENDENT FINANCIAL ADVISER

Based on our review, all the Sample Contracts followed the fixed fee arrangement, to be settled on a monthly or quarterly basis upon the transfer of transmission and derivatives rights of the relevant television series and animations. We further note that the agreed licensing fees for a particular television series and animation varied widely ranging, from approximately RMB100 million to RMB700 million in respect of television series, and from approximately RMB10 million to RMB30 million in respect of animations. Based on our discussion with the management of the Group, the relevant licensing fee and the pricing model for each project depends on various commercial and other factors, as stated in the term section above, as such, the variety of fee arrangements as structured in the 2018 Distribution Framework Agreement is to allow the Group a degree of flexibility to determine the optimal pricing model and to maximize the monetary potential of the Group's media contents.

For the purpose of analysing the pricing policies, we have obtained sample contracts for similar licensing arrangements between the Group and independent third parties, selected on a random basis from the transaction list covering the period from October 19, 2018 to June 30, 2020. We note that the pricing models and payment terms with independent third parties are consistent with those stated in the 2018 Distribution Framework Agreement and/or the Sample Contracts reviewed by us. Similar to the Sample Contracts, the licensing fee of each project with an independent third party varied widely, and it was agreed after arm's length negotiations and taking into account various commercial factors.

As informed by the management of the Group, the exact terms of the underlying transactions will only be agreed upon the entering into of the implementation agreements, and that the fee arrangements under the 2021 Distribution Framework shall be consistent with the historical and the prevailing commercial practices with other independent third parties, and subject to the internal control measures, including comparison of commercial terms with independent third parties and internal review procedures, details of which are further discussed below.

## 4. Internal control measures

As set out in the letter from the Board, the Group's Business Development Team, comprising personnel responsible for overseeing its intellectual property operations, will seek to solicit cooperation with other independent third parties to the extent commercially practicable, and will compare the commercial terms offered by the independent third parties with those offered by the Retained Tencent Group in respect of the Continuing Connected Transactions. For instance, the Group will assess its business needs and compare the licensing fees proposed by the Retained Tencent Group with the licensing fees offered by at least two other comparable platform operators in the PRC media industry.

## LETTER FROM THE INDEPENDENT FINANCIAL ADVISER

In making the decision as to whether the Group will cooperate with the Retained Tencent Group, the Business Development Team will also consider other commercial factors, such as the potential of the intellectual properties, the prevailing market pricing, the prospects of the intellectual property cooperation, with a view to maximizing the commercial value of the relevant intellectual properties. In respect of the selection of the platform operators, the Group will also consider other factors, including (i) the breadth of user base and traffic of various online video platforms; (ii) the user demographics of different online video platforms; (iii) the existing cooperation with various platforms and (iv) the rates of licensing fees proposed by the online video platforms. The Business Development Team is required to comply with the pricing policy for the Continuing Connected Transactions as set out above, and the internal control team of the Company will regularly monitor the compliance of such pricing policy.

The executive Directors will supervise the implementation of such internal procedures on a regular basis (e.g. holding regular meetings with different departments and inquiries into the transactions undertaken pursuant to the 2021 Distribution Framework Agreement), and the Board will also conduct the regular review of the transactions underlying the 2021 Distribution Framework Agreement.

In addition, as part of the Group's standard procedures, regardless of the party the Group may cooperate with (whether it is the Retained Tencent Group or any independent third party), the legal affairs department and financial department of the Company will conduct a feasibility study and a separate review of the cooperation and consider the benefits and risks of such cooperation on a case-by-case basis before entering into an agreement. As set out in the letter from the Board, the Group will only enter into an individual implementation agreement with the Retained Tencent Group if (i) the licensing fees and quality of distribution are no less favorable than those from other independent third-party provider; and (ii) it is in the best interest of the Company and the Shareholders. The Group shall solicit more players for pricing comparison should the landscape of the online video distribution industry evolves.

In our view, the above internal control procedures are important for the conduct of the Continuing Connected Transactions, since exact terms of the transactions will only be agreed upon the entering into of the individual implementation agreements. In these circumstances, we concur that the solicitation of cooperation with other independent third parties, and comparison of the terms with those offered by the Retained Tencent Group, will help the Group to ensure that the underlying transactions pursuant to the 2021 Distribution Framework Agreement are on terms no less favourable to the Group and in the interests of the Company and the Shareholders as a whole. Further, the independent non-executive Directors and auditors of the Company will review the Continuing Connected Transactions each year, details of which are set out in the section below headed "Reporting requirements and conditions".

## LETTER FROM THE INDEPENDENT FINANCIAL ADVISER

## 5．The Annual Caps

## Review of historical transactions

Set out below are the historical transaction amounts and the relevant caps under the 2018 Distribution Framework Agreement for the two years ended December 31， 2018 and 2019，and for the six months ended June 30，2020：

|  | For the six <br> months ended |  |
| ---: | ---: | ---: |
| For the year ended December 31， | June 30， |  |
| 2018 | $\mathbf{2 0 1 9}$ | 2020 |
| $R M B$ million | RMB million | RMB million |


| Aggregate amounts of the |
| :--- |
| licensing fees received by |
| the Group from the |
| Retained Tencent Group |
| Relevant annual caps |
| Utilisation rate | 1,400

Note：Based on the relevant six－month transaction amount and pro rata annual cap amount

As mentioned in the earlier section，the Group completed the acquisition of NCM in October 2018 and since then commenced the licensing of transmission rights and derivative rights of its television series，films and animations to the Retained Tencent Group under the 2018 Distribution Framework Agreement．We are advised by the management of the Group that although there were no licensing transactions with the Retained Tencent Group under the 2018 Distribution Framework Agreement in last two months of 2018，NCM licensed in total three television and web series to the Retained Tencent Group in the earlier months of 2018， generating licensing fees of approximately RMB1，587 million．

In 2019，NCM distributed four television and web series on the platforms of the Retained Tencent Group，including Memories of Peking（芝麻胡同）and Joy of Life（慶餘年），which ranked top in terms of viewership during their respective broadcast time slots，according to the Company＇s 2019 annual report．In addition to television and web series，the Group also released a number of animations on the Retained Tencent Group＇s video platforms，such as Galaxy Devastator（崩壞星河）and Battle Through the Heavens（斗破蒼穹），which generated a substantial number of views．

From the financial respective, the Group received aggregate licensing fees of approximately RMB1,008 million from the Retained Tencent Group in 2019, utilising approximately $48.0 \%$ of annual cap. As advised by the management of the Group, the low utilisation rate was mainly a result of the actual number of television series and films distributed through the Retained Tencent Group was less than expected at the time when the caps were determined, which in turn was mainly due to the profound adjustment faced by the television and film industry in the PRC, leading to the slow broadcast approval process for television series on television channels and online video platforms and a decline in the number of project filings, productions and releases.

In addition to the above industry-wide adjustment that continued to affect the production and licensing of television series and films of the Group in the first half of 2020, the outbreak of COVID-19 negatively impacted the macro-economy in the PRC. As a result, the Group's production and release cycle for media projects has been affected significantly, leading to a substantial drop in both the number and fee of licensing transactions between the Group and the Retained Tencent Group, amounting to approximately RMB12 million.

## Assessment of the Annual Caps

The Annual Caps under the 2020 Distribution Framework Agreement for the three years ending December 31, 2021, 2022 and 2023 are RMB1,550 million, RMB2,000 million and RMB2,400 million, respectively. We note that the Annual Cap estimated for the year 2021 is significantly lower than the annual caps for 2019 and 2020, as a result of the lower-thanexpected historical utilisation due to the industry headwind and COVID-19 as described above, before increasing back in 2022 and 2023 to a level comparable to the annual caps for 2019 and 2020.

As set out in the letter from the Board, the Annual Caps were determined with reference to, among others, (i) the historical amounts of the licensing fees paid by the Retained Tencent Group under the 2018 Distribution Framework Agreement for the year ended December 31, 2019, (ii) the expected resumption of the cooperation under the 2021 Distribution Framework Agreement for the year ending December 31, 2021 to the extent comparable to that for the year ended December 31, 2019, and (iii) the estimated annual growth of the scale of the television series, films and animations project pipelines invested by the Group for the three years ending December 31, 2023 as a result of the closer cooperation relationship between the Group and the Retained Tencent Group.

In assessing the reasonableness of the Annual Caps, we have obtained the underlying projections of the Annual Caps in the coming years, and have discussed with the Group the bases and assumptions underlying such projections. We note that the licensing transactions in relation to television series for each of the years 2021, 2022 and 2023 represent over $80 \%$ of the Annual Caps. As advised by the management of the Group, given the licensing fees for films payable by the Retained Tencent Group to the Group is expected to be immaterial as compared to those for television series, it has not been taken into consideration when determining the Annual Caps.

As advised by the management of the Group, despite the production and release cycle of NCM's media projects being affected by the macro changes in the television and film industry in the PRC and the impact arising from the outbreak of COVID-19, the broadcast approval process for television series on television channels and online video platforms by the relevant PRC authorities has been gradually resuming to normal. Given that the outbreak of COVID-19 in the PRC is under control, and that movie theatres in the PRC are allowed to begin the reopening process starting from July 2020 with the execution of prevention and control measures regarding COVID-19, the Company expects that there will not be a large scale outbreak of COVID-19 in the PRC in the near future. The Company further expects that NCM will gradually resume the production and distribution of television series and films and the total number of projects available for licensing will grow steadily and release as scheduled between 2021 and 2023. It is assumed that NCM will license three to four television series to the Retained Tencent Group in 2021, which is in line with historical records in past two years, and there will be two or three more television series to be licensed to the Retained Tencent Group in 2022 and 2023.

In addition, we observe that the estimated licensing fees for a particular television series is estimated by the Company with reference to the historical amounts for similar genres of television series. A fixed fee model is assumed, with licensing fees ranging from approximately RMB250 million to RMB400 million for each television series, which fall within the range of those fees set out in the Sample Contracts reviewed by us.

As set out in the 2020 interim report of the Company, the Group intends to take major steps to speed up cross sector development and establish a stronger connection between the Group's products and the Retained Tencent Group's portfolio. We also note from Tencent's 2020 first quarter result announcement, stating that with the appointment of a new management team at the Company, Tencent intends to deepen cooperation with the Group in adapting its literature intellectual property into various media formats such as television series and anime, leveraging the Retained Tencent Group's distribution capability to broaden its user reach, as well as exploring product innovation and new technologies to strengthen its content ecosystem. This partly explained the anticipated higher volume of media licensing transactions in the underlying projections of the Annual Caps, as compared to the historical transactions under the 2018 Distribution Framework Agreement.

## Our general view

In general, in our opinion, it is in the interests of the Group and the Shareholders to determine the Annual Caps in a way that can accommodate the potential growth of the Group's business. In particular, the licensing fees for a particular television series varied significantly, ranging from approximately RMB100 million to RMB700 million based on the historical transactions under the 2018 Distribution Agreement. Besides, the macro changes in the PRC television and film industry led to the unpredictable production and release cycle of the Group's media projects. The Group may also choose to cooperate with independent third parties as opposed to the Retained Tencent Group, depending on the particular project in question and the terms being offered by different platforms. These factors made it difficult for the management of the Group to project the exact availability of television series, and hence
the licensing transactions between the Group and the Retained Tencent Group in coming three years. Therefore, we consider it appropriate for the Group to set the Annual Caps that accommodate the wide range of media projects' licensing fee and the intended closer cooperation relationship between two groups. Provided that the Continuing Connected Transactions are subject to annual review by the independent non-executive Directors and auditors of the Company, as required under the Listing Rules and other internal control procedures to safeguard the Group's interest (as summarised in the section above headed "Internal control measures"), the Group would have desirable flexibility in conducting its business if the Annual Caps are tailored to future business activities. In assessing the reasonableness of the Annual Caps, we have discussed with the management of the Group the factors taken into account as stated earlier in this section. We consider it reasonable for the Company to use the above factors in determining the Annual Caps.

## 6. Reporting requirements and conditions

Pursuant to Rules 14 A .55 to 14 A .59 of the Listing Rules, the Continuing Connected Transactions are subject to the following annual review requirements:
(a) the independent non-executive Directors must review the Continuing Connected Transactions every year and confirm in the Company's annual report whether the Continuing Connected Transactions have been entered into:
(i) in the ordinary and usual course of business of the Group;
(ii) on normal commercial terms or better; and
(iii) according to the agreements governing them on terms that are fair and reasonable and in the interests of the Shareholders as a whole;
(b) the Company must engage its auditors to report on the Continuing Connected Transactions every year. The Company's auditors must provide a letter to the Board (with a copy to be provided to the Stock Exchange at least ten business days before the bulk printing of the Company's annual report) confirming whether anything has come to their attention that causes them to believe that the Continuing Connected Transactions:
(i) have not been approved by the Board;
(ii) were not, in all material respects, in accordance with the pricing policies of the Group if the Continuing Connected Transactions involve the provision of goods or services by the Group;
(iii) were not entered into, in all material respects, in accordance with the relevant agreements governing the Continuing Connected Transactions; and
(iv) have exceeded the Annual Caps;

## LETTER FROM THE INDEPENDENT FINANCIAL ADVISER

(c) the Company must allow, and ensure that the counterparties to the Continuing Connected Transactions allow, the Company's auditors sufficient access to their records for the purpose of the reporting on the Continuing Connected Transactions as set out in paragraph (b);
(d) the Company must promptly notify the Stock Exchange and publish an announcement if the independent non-executive Directors and/or auditors of the Company cannot confirm the matters as required.

In light of the reporting requirements and conditions attached to the Continuing Connected Transactions, in particular, (i) the restriction of the value of the Continuing Connected Transactions by way of the Annual Caps; and (ii) the ongoing review by the independent non-executive Directors and auditors of the Company of the terms of the Continuing Connected Transactions (including the Annual Caps) not being exceeded, and given the Company's internal safeguards in place, we are of the view that appropriate measures will be in place to monitor the conduct of the Continuing Connected Transactions and assist in safeguarding the interests of the Shareholders.

## OPINION AND RECOMMENDATION

Having taken into account the principal factors and reasons set out above, we consider that the Continuing Connected Transactions (including the Revised Annual Caps) are on normal commercial terms, fair and reasonable so far as the Independent Shareholders are concerned, in the ordinary and usual course of business of the Group and in the interests of the Company and the Shareholders as a whole.

Accordingly, we recommend that the Independent Board Committee to advise, and we ourselves recommend, the Independent Shareholders to vote in favour of the resolution to be proposed at the Extraordinary General Meeting to approve the 2021 Distribution Framework Agreement (including the Annual Caps).

# Yours faithfully, for and on behalf of <br> SOMERLEY CAPITAL LIMITED <br> John Wong <br> Director 

[^0]
## 1. RESPONSIBILITY STATEMENT

This circular, for which the Directors collectively and individually accept full responsibility, includes particulars given in compliance with the Listing Rules for the purpose of giving information with regard to the Group. The Directors having made all reasonable enquiries, confirm that to the best of their knowledge and belief the information contained in this circular is accurate and complete in all material respects and not misleading or deceptive, and there are no other matters the omission of which would make any statement herein or this circular misleading.

## 2. SHARE CAPITAL

As at the Latest Practicable Date, the number of issued Shares was $1,015,781,716$ Shares of nominal value of US $\$ 0.0001$ each which have been fully paid.

## 3. EXPERT AND CONSENTS

The following are the qualification of the expert who has given opinions and advice contained in this circular:

Name Qualification

Somerley a licensed corporation to carry out type 1 (dealing in securities) and type 6 (advising on corporate finance) regulated activities as defined under the Securities and Futures Ordinance

As at the Latest Practicable Date, Somerley:
(a) has given and has not withdrawn its written consent to the issue of this circular with the inclusion of its letter and references to its name, in the form and context in which it appears.
(b) neither had any shareholding in any member of the Group nor had any right (whether legally enforceable or not) to subscribe for or nominate persons to subscribe for any securities in any member of the Group.
(c) did not have any direct or indirect interest in any assets which have been acquired or disposed of by, or leased to any member of the Group, or were proposed to be acquired or disposed of by, or leased to any member of the Group since December 31,2019 , being the date to which the latest published audited consolidated financial statements of the Company were made up.

## 4. NO MATERIAL ADVERSE CHANGE

The Directors are not aware of any material adverse change in the financial or trading position of the Group since December 31, 2019, being the date to which the latest published audited annual financial statements of the Company were made up.

## 5. SERVICE CONTRACTS OF DIRECTORS

Each of the executive Directors has entered into a service contract with the Company for a term of three years commencing from August 1, 2020 and is subject to retirement by rotation and re-election in accordance with the Articles of Association as a replacement of the service contract entered into between the Company and the executive Directors on April 27, 2020, and is subject to termination as provided in the service contract.

Each of Mr. James Gordon Mitchell, Mr. Cao Huayi and Mr. Cheng Yun Ming Matthew, as the non-executive Director, has entered into an appointment letter with the Company on October 19, 2017, May 17, 2019 and November 22, 2019, respectively, for an initial term of three years commencing from the date of their respective appointment letter, subject to retirement by rotation and re-election in accordance with the Articles of Association and is subject to termination as provided in the appointment letter. Mr. Wu Wenhui, a non-executive Director, has entered into an appointment letter with the Company for an initial term of one year commencing from April 27, 2020.

Each of the independent non-executive Directors has entered into an appointment letter with the Company on October 19, 2017 for an initial term of three years, subject to re-election in accordance with the Articles of Association and is subject to termination as provided in the appointment letter.

None of the Directors has a service contract which is not determinable by the Group within one year without payment of compensation (other than statutory compensation).

## 6. DISCLOSURE OF INTERESTS

As at the Latest Practicable Date, the interests and short positions of the Directors and the chief executives of the Company in the Shares, underlying Shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) which have been notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they were taken or deemed to have taken under such provisions of the SFO), or which were recorded in the register required to be kept pursuant to section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code as set out in Appendix 10 of the Listing Rules were as follows:

## Interests of Directors and Chief Executives of the Company

| Name | Capacity/Nature of Interest | Number of Shares | Long/short position | Approximate Percentage of Shareholding in the Company ${ }^{(1)}$ |
| :---: | :---: | :---: | :---: | :---: |
| Mr. Wu Wenhui ${ }^{(2)}$ | Interest in controlled corporations | 5,100,626 | Long position | 0.50\% |
|  | Interest in controlled corporations | 9,485,220 | Short position | 0.93\% |


| Name | Capacity/Nature of Interest | Number of Shares | Long/short position | Approximate Percentage of Shareholding in the Company ${ }^{(1)}$ |
| :---: | :---: | :---: | :---: | :---: |
| Mr. James Gordon Mitchell | Beneficial owner | 281,352 | Long position | 0.03\% |
| Mr. Cao Huayi ${ }^{(3)}$ | Interest in controlled corporations | 40,850,722 | Long position | 4.02\% |
| Mr. Cheng Yun Ming Matthew | Beneficial owner | 3,092 | Long position | 0.00\% |
| Mr. Cheng Wu | Beneficial owner | 1,304,400 | Long position | 0.13\% |
| Mr. Hou Xiaonan | Beneficial owner | 112,072 | Long Position | 0.01\% |

Interests of Directors and Chief Executives in associated corporations of the Company

|  | Name of |
| :--- | :--- | :--- | ---: | :--- |
| associated |  |
| corporations |  |$\quad$| Capacity/Nature |
| :---: |
| of Interest |$\quad$| Number of |
| ---: |
| Shares |$\quad$| Approximate <br> Percentage of <br> Shareholding <br> in the |
| ---: |
| associated |
| corporation ${ }^{(1)}$ |


| Name | Name of associated corporations | Capacity/Nature of Interest | Number of Shares | Approximate <br> Percentage of Shareholding in the associated corporation |
| :---: | :---: | :---: | :---: | :---: |
| Mr. Cheng Wu | Tencent <br> Holdings <br> Limited | Beneficial owner | 284,925 ${ }^{(6)}$ | 0.00\% |
| Mr. Hou Xiaonan | Tencent <br> Holdings <br> Limited | Beneficial owner | $111,833^{(7)}$ | 0.00\% |
| Mr. Wu Wenhui ${ }^{(8)}$ | Tencent <br> Holdings Limited | Interest of controlled corporation | 300,000 | 0.00\% |
| Mr. Wu Wenhui ${ }^{(9)}$ | Shanghai <br> Hongwen <br> Networking <br> Technology Co., Ltd. | Interest of controlled corporation | 3,462,000 | 34.62\% |
| Mr. Wu Wenhui ${ }^{(9)}$ | Shanghai <br> Yuewen <br> Information Technology Co., Ltd. | Interest of controlled corporation | 3,462,000 | 34.62\% |

Notes:
(1) The calculation is based on the total number of $1,015,781,716$ Shares in issue as of Latest Practicable Date.
(2) Mr. Wu Wenhui holds the entire share capital of Grand Profits Worldwide Limited. Hence, Mr. Wu Wenhui is deemed to be interested in (i) the 5,100,626 Shares held by Grand Profits Worldwide Limited, and (ii) the derivatives held by Grand Profits Worldwide Limited, representing 9,485,220 underlying Shares.
(3) Mr. Cao Huayi is interested in $100 \%$ and $43.63 \%$ of C-Hero Limited and X-Poem Limited respectively and is therefore deemed to be interested in the $34,230,324$ Shares and $6,620,398$ Shares interested in by C-Hero Limited and X-Poem Limited pursuant to the share purchase agreement dated August 13, 2018 entered into among the Company and the vendors including C-Hero and X-Poem in relation to the acquisition of the entire equity interest of New Classics Media Holdings Limited (the "2018 NCM Share Purchase Agreement"), without taking into account the supplemental deed entered into among the Company and the vendors including C-Hero and X-Poem in relation to the amendment of the 2018 NCM Share Purchase Agreement dated August 27, 2020, which is subject to the Shareholders' approval at the EGM, respectively.
（4）These interests comprise（i） $2,172,136$ shares of Tencent，（ii） 55,396 shares underlying Tencent in respect of the awarded shares granted to Mr．James Gordon Mitchell under share award schemes of Tencent，and（iii） $6,741,770$ shares underlying Tencent in respect of the options granted to Mr．James Gordon Mitchell under share option schemes of Tencent．Tencent is the controlling shareholder of the Company and thus is an associated corporation of the Company．
（5）These interests comprise（i） 340,237 shares of Tencent，（ii） 27,273 shares underlying Tencent in respect of the awarded shares granted to Mr．Cheng Yun Ming Matthew under share award schemes of Tencent，and（iii） 66,723 shares underlying Tencent in respect of the options granted to Mr．Cheng Yun Ming Matthew under share option schemes of Tencent．Tencent is the controlling shareholder of the Company and thus is an associated corporation of the Company．
（6）These interests comprise（i） 22,208 shares of Tencent，（ii） 579 shares underlying Tencent in respect of the awarded shares granted to Mr．Cheng Wu under share award schemes of Tencent，and（iii） 262,138 shares underlying Tencent in respect of the options granted to Mr．Cheng Wu under share option schemes of Tencent． Tencent is the controlling shareholder of the Company and thus is an associated corporation of the Company．
（7）These interests comprise（i） 64,508 shares of Tencent，（ii） 21,196 shares underlying Tencent in respect of the awarded shares granted to Mr．Hou Xiaonan under share award schemes of Tencent，and（iii）26，129 shares underlying Tencent in respect of the options granted to Mr．Hou Xiaonan under share option schemes of Tencent．Tencent is the controlling shareholder of the Company and thus is an associated corporation of the Company．
（8）Mr．Wu Wenhui holds the entire share capital of Grand Profits Worldwide Limited and therefore is deemed to be interested in the 300,000 shares of Tencent held by Grand Profits Worldwide Limited．
（9）Each of Shanghai Hongwen Networking Technology Co．，Ltd．（上海宏文網絡科技有限公司，＂Shanghai Hongwen＂and Shanghai Yuewen Information Technology Co．，Ltd．（上海閲文信息技術有限公司，＂Shanghai Yuewen＂are owned as to $34.62 \%$ by Ningbo Meishan Bonded Port Area Yuebao Investment Co．，Ltd．（寧波梅山保税港區閲寶投資有限公司），which in turn is held as to $83.88 \%$ by Mr．Wu Wenhui．Under the SFO， Shanghai Hongwen and Shanghai Yuewen are associated corporations of the Company．

Save as disclosed above，as at the Latest Practicable Date，none of the Directors or the chief executive of the Company had or was deemed to have any interest or short position in the shares，underlying shares or debentures of the Company or its associated corporations （within the meaning of Part XV of the SFO）that was required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO（including interests and short positions which they were taken or deemed to have taken under such provisions of the SFO），or required to be recorded in the register required to be kept under Section 352 of the SFO，or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code．

Save as disclosed herein，as at the Latest Practicable Date，none of the Directors，directly or indirectly，has had any interest in any assets which had since December 31， 2019 （being the date to which the latest published audited financial statements of the Company were made up） been acquired or disposed of by or leased to any member of the Group，or were proposed to be acquired or disposed of by or leased to any member of the Group．

Save as disclosed in this circular，there was no contract or arrangement subsisting as at the Latest Practicable Date，in which any of the Directors or proposed directors was materially interested and which was significant in relation to the businesses of the Group．

## 7. COMPETING INTERESTS

As at the Latest Practicable Date, none of the Directors, proposed directors and any of their associate(s) had interest in a business which competes or may compete with the business of the Group, or may have any conflicts of interest with the Group pursuant to Rule 8.10 of the Listing Rules.

## 8. DOCUMENTS AVAILABLE FOR INSPECTION

Copies of the following documents will be available for inspection at the office of the Company during normal business hours from the date of this circular up to November 25, 2020 (both days inclusive):
(a) the 2021 Distribution Framework Agreement,
(b) letter from the Independent Board Committee,
(c) letter from the Independent Financial Adviser,
(d) the service contracts of the Directors, and
(e) letter of consent from Somerley.

# 阅文集团 ${ }^{\text {T }}$ CHINA LITERATURE LIMITED <br> 阅文集团 <br> （Incorporated in the Cayman Islands with limited liability） 

（Stock Code：772）

## NOTICE OF EXTRAORDINARY GENERAL MEETING

NOTICE IS HEREBY GIVEN THAT the Extraordinary General Meeting of China Literature Limited（the＂Company＂）will be held at Niccolo Room，Level 25，The Murray， Hong Kong，a Niccolo Hotel， 22 Cotton Tree Drive，Central，Hong Kong at 3：00 p．m．on Wednesday，December 9， 2020 for the purposes of considering and，if thought fit，passing with or without modifications，the following resolutions as ordinary resolutions．

Unless otherwise specified，capitalized terms used in this notice and the following resolutions shall have the same meanings as those defined in the circular of the Company dated November 10， 2020 （the＂Circular＂）．

## Ordinary Resolution

1．To consider and，if thought fit，pass with or without modification the following resolutions as ordinary resolutions：
＂That：
（a）the 2021 Distribution Framework Agreement and the transactions contemplated thereunder，details of which are more particularly described in the circular of the Company dated November 10， 2020 （the＂Circular＂），be and is hereby approved，ratified and confirmed；
（b）the proposed annual caps for the continuing connected transactions contemplated under the 2021 Distribution Framework Agreement for the three years ending December 31， 2023 as set out in the Circular be and are hereby approved，ratified and confirmed；and
(c) any one executive Director be and is hereby authorized for and on behalf of the Company to execute, and where required, to affix the common seal of the Company to, any documents, instruments or agreements, and to do any acts and things deemed by him or her to be necessary, expedient or appropriate in order to give effect to and implement the transactions contemplated under the 2021 Distribution Framework Agreement (including the proposed annual caps thereunder for the three years ending December 31, 2023).

By order of the Board<br>CHINA LITERATURE LIMITED<br>Mr. James Gordon Mitchell<br>Chairman of the Board and Non-executive Director

Hong Kong, November 10, 2020

Registered office:
The offices of Maples Corporate Services Limited PO Box 309, Ugland House
Grand Cayman KY1-1104
Cayman Islands

Head office and principal place of business in China:
Block 6, No. 690 Bi Bo Road
Pudong XinQu, Shanghai
People's Republic of China

## Principal place of business in Hong Kong:

Room 1503-04, ICBC Tower, 3 Garden Road, Central Hong Kong

Notes:
(i) A shareholder entitled to attend and vote at the above meeting is entitled to appoint one or more proxies to attend, speak and vote in his/her stead. The proxy does not need to be a shareholder of the Company.
(ii) Where there are joint registered holders of any shares, any one of such persons may vote at the above meeting (or at any adjournment of it), either personally or by proxy, in respect of such shares as if he/she were solely entitled thereto but the vote of the senior holder who tenders a vote, whether in person or by proxy, will be accepted to the exclusion of the vote(s) of the other joint holders and, for this purpose, seniority shall be determined by the order in which the names stand in the register of members of the Company in respect of the relevant joint holding.
(iii) In order to be valid, the completed form of proxy must be deposited at the Hong Kong share registrar of the Company, Computershare Hong Kong Investor Services Limited, at 17M Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong, together with the power of attorney or other authority (if any) under which it is signed or a certified copy of that power of attorney or authority (such certification to be made by either a notary public or a solicitor qualified to practice in Hong Kong), at least 48 hours before the time appointed for holding the above meeting or any adjournment thereof (as the case may be). The completion and return of the form of proxy shall not preclude shareholders of the Company from attending and voting in person at the above meeting (or any adjourned meeting thereof) if they so wish.
(iv) The register of members of the Company will be closed from Friday, December 4, 2020 to Wednesday, December 9, 2020, both days inclusive, in order to determine the eligibility of shareholders to attend the above meeting, during which period no share transfers will be registered. To be eligible to attend the above meeting, all properly completed transfer forms accompanied by the relevant share certificates must be lodged for registration with the Hong Kong share registrar of the Company, Computershare Hong Kong Investor Services Limited, at Shops 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong not later than 4:30 p.m. on Thursday, December 3, 2020.
(viii) Pursuant to Rule 13.39(4) of the Listing Rules, voting for all the resolutions set out in this notice will be taken by poll at the above meeting.


[^0]:    Mr. John Wong is a licensed person registered with the Securities and Futures Commission and a responsible officer of Somerley Capital Limited, which is licensed under the SFO to carry out Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities. He has over ten years of experience in the corporate finance industry.

